

BENEFITS AND DRAWBACKS OF SIMPLIFICATIONS IN FINANCIAL REPORTING FOR MICRO AND SMALL ENTERPRISES

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Purpose: The main thesis of this study is that there are significant drawbacks to simplified financial statements dedicated to SMEs which - despite positive cost effects - generate negative informational, decision-making, and social consequences. The literature and practice reveal a multidimensional tension between the need to ease the burden on SMEs and the necessity to maintain the reliability and usefulness of financial statements. This issue is particularly important in light of the growing role of SMEs in job creation and the flexibility of local markets, as well as in the context of the stability of the financial system, where the lack of accurate and comparable information may lead to misallocation decisions and increased agency costs and information asymmetry

Design/methodology/approach: The achievement of the objective involved the critical review of both national and international literature as the primary research method. Methodologically, the paper is based on a critical review of scientific literature and institutional reports, an analysis of legal acts and accounting standards, and an interpretation of empirical research results relating to the quality of financial information, the cost of capital, and the comparability of financial statements.

Findings: In the course of work, it was found: the balance of benefits and costs associated with reporting simplifications for micro, small, and medium-sized enterprises is not clear-cut. On the one hand, they provide administrative relief and lower the direct costs of accounting. On the other hand, they generate numerous drawbacks which, in the longer term, may outweigh short-term savings. It therefore seems necessary to conduct further research and empirical analyses on the impact of simplifications on SMEs' competitiveness, access to financing, and management culture.

Originality/value: Reporting simplifications take various forms: from exemptions from the obligation to prepare full documentation, through a reduction in the scope of disclosures, simplifications in measurement and presentation principles, and even the adoption of separate, less detailed accounting standards. The primary aim of these solutions is to rationalize costs, reduce bureaucratic requirements, and increase formal accessibility for entrepreneurs with limited resources. At the same time, however, simplifications are not epistemically neutral: they modify the scope and quality of information communicated to the market and to authorities, affecting transparency, data comparability, and the mechanisms of control and accountability.

The research objective is to identify and critically analyse, from multiple angles, the drawbacks of reporting simplifications applied to micro and small enterprises. The paper attempts to systematize the negative effects of these solutions, indicate the mechanisms through which they arise, and assess the implications for individual stakeholder groups.

Keywords: Financial reporting, International Financial Reporting Standard for Small and Medium-sized Entities, micro business, small business.

Category of the paper: Research Paper, Viewpoint.

1. Introduction

The article analyses the advantages and disadvantages of simplifications in financial reporting used by micro and small enterprises (SMEs) based on the Accounting Act, i.e. the Polish balance sheet law. Thus, there is no way to compare it with international standards. The main thesis of the research indicates that although these simplifications bring positive cost effects for SMEs, they also generate negative informational, decision-making and social consequences. The paper discusses in detail the legal basis for the classification of enterprises in Poland and the European Union, including the size criteria and regulations contained in the Accounting Act and EU directives, which are aimed at adapting reporting requirements to the resources of smaller entities. The author critically systematizes the negative effects of these simplifications, emphasizing their impact on information asymmetry, limited decision-making usefulness for external stakeholders, as well as a decrease in the comparability of financial data. The whole is based on a critical review of the scientific literature and analysis of legal acts, with the aim of identifying and assessing the implications of simplifications for different stakeholder groups.

Financial reporting plays a central role in the functioning of a market economy (Zarzycka, Krasodomska, 2022). It constitutes the primary source of information on the asset position, financial standing, and performance of enterprises, enabling stakeholders - owners, creditors, investors, contractors, and supervisory bodies - to make rational economic decisions (Bauer, 2025; Dratwińska-Kania, Ferens, Szewieczek, 2021; Wędzki, 2012; Hołda, Micherda, 2007; Chluska, 2016). It is also worth noting the critical view of financial statements as a source of information for broadly understood stakeholder groups (Bauer, 2025; Chen, Chen, Su, 2001; Zimmermann, Yahya-Zadeh, 2001; Parson, 2003). In the context of small enterprises - namely micro, small, and medium-sized enterprises (SMEs) - this reporting has both an economic and administrative dimension: on the one hand, it provides market information on the entity's value and risk; on the other, it is associated with reporting obligations, costs of preparing and storing documentation, and the risk of regulatory infringements. For this reason, many legal systems have introduced simplified solutions intended to reduce the administrative and cost burdens on

SMEs, allowing them to focus resources on their core operating activities (Kuzior, Pfaff, Poniatowska, Rówińska, 2014).

Conducting business activity involves producing material goods and providing services to satisfy general social needs (Mućko, Sokół, 2011). Legal regulations on running a business are reflected in numerous acts such as the Entrepreneurs' Law, the Personal Income Tax Act, the Value Added Tax Act, and the Accounting Act. The general procedures accompanying the commencement, conduct, suspension, and closure of business activity were described in detail in the Act on Freedom of Economic Activity introduced on 2 July 2004 and repealed on 1 March 2018. That act contained the following definition of activity: "economic activity is profit-oriented manufacturing, construction, trade, and service activity, as well as the exploration, recognition, and extraction of minerals from deposits, and professional activity carried out in an organized and continuous manner". In the Entrepreneurs' Law, which replaced the Act on Freedom of Economic Activity, Article 3 defines "economic activity" as organized profit-oriented activity carried out on a continuous basis.

The enterprise is the most common form of economic organization (Urbanowska-Sojkin, Banaszyk, 2009; Gruszecki, 2002). Using the size of the entity as a criterion, P. Drucker divided enterprises into:

- a) micro business - sole proprietorship or partnership operating without employees and without a distinct management structure,
- b) small business - one intermediate level in the form of boss-employee relations,
- c) medium-sized business - multi-level relations, with horizontal relations predominant; their characteristic feature is the presence of a management team,
- d) large business - clear separation between the top manager deciding on company strategy and the team of lower-level managers handling operations,
- e) very large business - where objectives and strategic plans are decided not by the top manager but by the entire team: the management board and supervisory board (Drucker, 2009).

2. Classification of Enterprises

The classification of enterprises is an important determinant defining the rules of conducting economic activity. Belonging to particular classification groups affects whether a given entity will keep only mandatory records aimed at tax settlements or full accounting; it also determines the scope of obligations related to the preparation of financial statements. The size criterion is also used for granting various types of subsidies and public aid and for imposing tax reporting obligations (Tkocz-Wolny, 2015).

A new classification of entities in the Accounting Act was introduced by the amending act of 6 December 2024 on amending the Accounting Act, the Act on Statutory Auditors, Audit Firms and Public Oversight, and certain other acts. The definition of a micro entity was modified. Under the current regulations (Article 3(1)(1a) of the Accounting Act), a micro entity is an entity which, in the financial year for which it prepares financial statements and in the preceding financial year (or, in the case of an entity commencing activity or keeping books under the Act—in the financial year in which it commenced such activity or keeping books), did not exceed at least 2 of the following 3 thresholds:

1. PLN 2,000,000 – balance sheet total at year-end,
2. PLN 4,000,000 – net revenue from sales of goods and products for the financial year,
3. 10 persons - average annual employment in FTEs.

Whereby an entity loses micro status if, in the financial year for which it prepares financial statements and in the preceding financial year, it exceeded at least 2 of these 3 thresholds.

Under the amended definition, micro status is acquired automatically. Meeting the above conditions is sufficient. Thus, an entity obtains micro status solely based on specified threshold values. The decision to adopt reporting simplifications for a micro entity, however, is still taken by the approving body. Pursuant to Article 14(3) of the amending act, the provisions on the new classification of entities in the Accounting Act applied for the first time to financial statements for a financial year beginning after 31 December 2023.

Table 1.
Classification of Enterprises under Legal Regulations

Regulations	Criterion	Micro	Small	Medium
Accounting Act	Average annual employment	10 FTE	50 FTE	-
	Revenue from sales	4 mln PLN	51 mln PLN	-
	Balance sheet total	2 mln PLN	25,5 mln PLN	-
Entrepreneurs' Law or	Average annual employment	10 FTE	50 FTE	250 FTE
	Revenue from sales	2 mln PLN	10 mln PLN	50 mln PLN
	Balance sheet total	2 mln PLN	10 mln PLN	43 mln PLN
EU Directive	Average annual employment (no more than)	10 FTE	50 FTE	250 FTE
	Revenue from sales	0,70 mln EUR	8 mln EUR	40 mln EUR
	Balance sheet total	0,35 mln EUR	4 mln EUR	20 mln EUR

Source: author's own study based on Ustawa z dnia 29 września 1994 r. *o rachunkowości*, Dz.U. z 2021 r. poz. 217, Ustawa z dnia 6 marca 2018 r. *Prawo przedsiębiorcy* Dz.U. z 2021 poz.. 162, Dyrektywa Parlamentu Europejskiego i Rady z dnia 26 czerwca 2013 r. *w sprawie rocznych sprawozdań finansowych, skonsolidowanych sprawozdań finansowych i powiązanych sprawozdań niektórych rodzajów jednostek, zmieniająca dyrektywę Parlamentu Europejskiego i Rady 2006/43/WE oraz uchylająca dyrektywy Rady 78/660/EWG i 83/349/EWG*, Dz. U. UE L 182/19.

As shown in Table 1, all the presented legal acts include definitions of micro and small entities. Directive 2013/34/EU also defines medium-sized enterprises. The Entrepreneurs' Law defines medium-sized enterprises but does not contain a typology of large enterprises.

Solutions implemented at the EU level in financial reporting tie the scope of information presented in annual financial statements primarily to the size of the entity. The directive specifies maximum threshold values while allowing Member States to adapt these general guidelines to their individual needs and specific circumstances.

Thus, a large entrepreneur is an entity that does not meet the conditions for a medium-sized entity. The Accounting Act does not distinguish between medium and large enterprises; instead, it differentiates entities subject to mandatory annual audit by a statutory auditor and those not subject to such an obligation. According to Article 64(1)(4) of the Accounting Act, an entity's financial statements are subject to mandatory audit if, in the preceding financial year for which it prepared financial statements, it met at least two of the following conditions:

- a) average annual employment in FTEs of at least 50 persons,
- b) balance sheet total at year-end equal to at least EUR 2,500,000,
- c) net revenue from sales of goods and products and financial operations for the year equal to at least EUR 5,000,000.

The classification of economic entities forms the foundation for many accounting and financial reporting regulations. Determining the category to which a given enterprise belongs directly affects the scope of reporting obligations, including the possibility of using simplifications in financial statements.

When analysing SME definitions, it should be noted that the definition of micro-enterprises in the Accounting Act does not coincide with the definition of a micro-entrepreneur in the Entrepreneurs' Law. The definition in the Accounting Act is more complex. A partial justification for a separate definition of a micro-entity - as compared to a micro-entrepreneur - is the fact that accounting is an information system used also by entities that are not entrepreneurs.

Micro entities, in the Accounting Act, are described as units that (Nowak 2015):

- employ few workers,
- are most often managed by their owners,
- have low or medium levels of revenues and assets,
- do not have investments in subsidiaries, associates, or joint ventures,
- do not hold or issue complex financial instruments,
- do not issue shares or share options.

SMEs are the main engine of the labour market. In Poland, SMEs account for over 60% of private-sector employment. Small and medium-sized firms often operate locally, creating jobs where large corporations may not be present—especially in smaller towns and rural areas. Thus, SMEs help reduce unemployment, particularly in regions with limited job opportunities. Micro and small enterprises significantly affect GDP (Mlaskawa, 2021; Grzywacz, 2015). Although SMEs typically have fewer resources than large corporations, they are often more innovative and flexible. The ability to respond quickly to changing market conditions,

proximity to customers, and less bureaucracy enable faster introduction of new products and services. SMEs often operate in niche markets where larger firms may not perceive profit potential. In this context, SMEs are a key source of innovation that drives economic development. SMEs operate across different sectors—from industry and trade to services and digital markets (Miszczak, 2022; Hejduk, 1998). This diversity makes the SME sector more resilient to economic shocks because problems in one sector do not necessarily translate into the entire economy. With their broad range of activities, SMEs create a dynamic and diversified economic landscape. It is beyond doubt that the SME group also faces many development barriers (Barber, Metcalfe, Porteous, 1998; Kamińska, 2011; Maćkowiak, 2023; Steinerowska-Streb, 2017).

3. Legal Regulations

The legal framework of financial reporting— including for micro, small, and medium-sized enterprises—is a product of many years of development of accounting standards, EU and national regulations, and the practical needs of the economy. Generally, these regulations aim to provide reliable, credible, and comparable financial information while tailoring the scope of reporting obligations to the organizational and financial capacities of each category of enterprise. The regulatory context for SMEs is unique: on the one hand, they form the backbone of the European and Polish economy; on the other, their limited resources necessitate a specific approach to reporting obligations.

National Regulations – the Accounting Act

In Poland, the principal legal act regulating financial reporting is the Accounting Act of 29 September 1994. This act sets the framework for keeping accounting books, principles for measuring assets and liabilities, and the preparation and presentation of financial statements. Since its adoption, the act has been amended numerous times, largely due to the need to align Polish law with EU regulations. Within the Accounting Act, a special role is played by provisions concerning micro and small entities. They allow the application of simplifications both in keeping books and in preparing financial statements. Micro-enterprises are defined using quantitative criteria (including net revenue from sales of goods and services, balance sheet total, and average annual employment). Similar criteria apply to small entities, with proportionally higher thresholds. For both categories, the legislator has provided for the possibility of using simplified versions of the balance sheet and the profit and loss account. Micro-enterprises are also exempted from the obligation to prepare notes (the additional information), which in practice significantly limits the scope of disclosures. Small entities benefit from slightly less far-reaching reliefs but likewise are not obliged to prepare full

financial statements. Instead, they may use shortened variants that reduce the number of reporting items. It should be emphasized that the legislator's intention was above all to reduce administrative and accounting costs, which for many small companies could be a barrier to doing business. At the same time, however, such an approach raises questions about the reliability and transparency of the picture of the financial position—issues discussed later in this paper.

EU Directives

EU regulations play a key role in shaping national solutions in financial reporting. The most important legal act is Directive 2013/34/EU of the European Parliament and of the Council on annual financial statements, consolidated financial statements and related reports of certain types of undertakings. It replaced the earlier IV and VII directives, simplifying and modernizing the rules and introducing uniform principles across Member States. The Directive provides for a system of categorizing undertakings into micro, small, medium, and large based on balance sheet, revenue, and employment criteria. Its objective was to reduce administrative burdens and thereby improve the competitiveness of European SMEs. The Directive allows for simplifications for the smallest entities, such as exemptions from preparing the cash flow statement or notes (additional information). Small entities may use simplified forms of the balance sheet and profit and loss account. The EU argued that such simplifications are necessary because small enterprises bear relatively higher costs of full accounting compared to large entities. According to European Commission analyses, the cost of preparing full financial statements per unit of revenue or per employee is significantly higher in SMEs than in corporations. Thus, the Directive was intended as a tool to level the playing field and reduce development barriers.

International Solutions – IFRS for SMEs

At the global level, a key initiative is IFRS for SMEs (International Financial Reporting Standard for Small and Medium-sized Entities), developed by the IASB. Adopted in 2009 as a separate set of accounting rules for entities not required to apply full IFRS, IFRS for SMEs covers all major areas of financial reporting but in a much simplified form. It reduces disclosures, limits measurement options, and in many cases introduces uniform solutions where full IFRS offers alternatives. Examples include abandoning the extensive use of fair value and simplifications in consolidation. Although the standard has not been adopted in the European Union as binding, it has been applied in many countries worldwide and serves as a reference point in discussions on SME reporting. Its philosophy is consistent with EU and national approaches: facilitate accounting for smaller entities while maintaining a minimum level of decision-useful information.

4. Characteristics of Micro and Small Enterprises

One of the most important features of SMEs is their flexibility. Smaller firms can adapt more quickly to changing market conditions, make rapid decisions, and introduce innovations without complex decision-making processes (Smolarek, 2015). This flexibility is particularly important in a dynamic economic environment where adaptability often determines a firm's survival (Lachiewicz, Matejun, 2012). SMEs often operate locally and maintain direct contact with customers. This proximity enables a better understanding of customer needs and faster responses. Owners of small firms typically have direct contact with customers, allowing long-term relationships based on trust and loyalty - hard to achieve in large corporations. Due to their structure, small firms tend to have lower operating costs than large enterprises. Less bureaucracy, lower marketing and management outlays, and often more flexible employment approaches help control costs. As a result, SMEs can compete with larger entities, especially in local markets (Maćkowiak, 2022).

4.1. Objectives of SME Activity

The primary objective of micro-enterprises, like other forms of business activity, is to generate profit and maintain profitability. However, in the case of micro-enterprises - small economic entities - their objectives can be more diversified and tailored to their specific functioning and the individual ambitions of owners (Lemańska-Majdzik, 2013; Deakins, Whittam, 2000). They include: generating profits that allow the owner's livelihood and further development of the firm; effective cost management to maintain profitability (Maćkowiak, 2019). Given the small size of the firm, every financial decision directly affects results. For many micro-enterprise owners, a key goal is achieving professional and personal independence. Running one's own business allows autonomous decision-making, shaping strategy, and flexible time management. Owners have full control over operations, giving greater freedom compared to working in larger organizational structures. Due to their small size, micro-enterprises can respond quickly to changing market conditions by introducing new products or services, changing business models, or tailoring their offerings to customer expectations. They often operate in niche markets, offering specialized products or services. Their goal is to meet specific customer needs, building loyalty and stable revenues. Given limited resources, micro-enterprises often focus on survival in difficult market conditions such as competition or a variable economic environment. They frequently operate locally and have close customer relationships. A major goal may be building customer loyalty by delivering high-quality products and services and an individual approach. In micro-enterprises, customer relationships are crucial for stability. Satisfied customers are more likely to return and recommend the firm to others, contributing to growth without costly marketing. For many entrepreneurs, running a business is a way to pursue passions, develop skills, and take on

challenges. Micro-enterprises often reflect the interests and talents of their owners and can build reputation in a given industry or local market, leading to long-term success and stability.

The objectives of small enterprises primarily include achieving profit and maintaining financial stability, but these goals may be more diversified and tailored to the firm's specifics and character. Small enterprises, operating on a more limited scale compared to larger entities, also set goals related to growth, maintaining competitiveness, and impact on the local community. Key areas include: profit generation and operating profitability; liquidity, which is crucial not only for small enterprises, as it ensures that current liabilities-such as supplier payments, wages, and other operating costs-are settled. Stable liquidity helps avoid financial problems, which is particularly important for small entities that do not have access to large financial reserves. Small enterprises also pursue growth and expansion, i.e., expanding operations and investing in innovation. They strive for growth by acquiring new customers, developing product or service offerings, and entering new markets (local, regional, and sometimes even international) (Morrison, Breen, Ali, 2003). Introducing new technologies or improvements in production or service processes can increase efficiency and competitiveness - a key strategic objective. As they develop, an important objective becomes building market position and competitive advantage. Small firms often compete in local markets and aim to acquire and retain loyal customers by delivering high quality. They build advantage through innovation, quality, or an individual approach to customers. Offering unique products or services that differentiate the company from competitors also helps build market advantage and generate stable revenues. Another objective is customer satisfaction and relationship building through high-quality service and meeting specific market needs. Small enterprises often place greater emphasis on building long-term, close customer relationships. High-quality service, customer satisfaction, and loyalty are crucial for long-term success. Tailoring the offer to changing customer needs and expectations-especially locally-makes it possible to gain advantage over larger, less flexible competitors. In terms of risk management, small firms must limit risks that could threaten their operations. The objective is to manage finances to minimize the impact of negative factors such as market fluctuations or changing economic conditions. Small enterprises may also seek to diversify income sources to reduce dependence on a single market or customer, increasing stability (Maćkowiak, 2019).

4.2. Objectives and Justifications for Introducing Simplifications

The fundamental objective of simplification regulations is to reduce administrative costs, which can be a significant burden for SMEs. According to European Commission reports, such costs often constitute a significant percentage of a firm's total expenditures, limiting its ability to invest and grow. Moreover, simplifications aim to increase the accessibility of reporting for entities with limited staffing and technology resources, as well as ensure compliance with the principle of proportionality, which requires tailoring regulatory requirements to an entity's scale and importance in the economy. Another justification is the limited number of external

stakeholders who actually use full financial statements for SMEs. Unlike large listed companies, which are accountable to a wide group of investors and supervisory institutions, small enterprises usually communicate primarily with banks, tax authorities, and owners. In this sense, the full scope of disclosures is often considered excessive relative to real information needs. Legal regulations-national, EU, and international-shape the framework of SME financial reporting, determining not only how books are kept and statements prepared, but also affecting enterprises' access to external financing, their ability to cooperate internationally, and their market competitiveness. In practice, this means that simplifications intended as support tools simultaneously become a source of limitations-forming the core subject of the critique discussed in subsequent parts of the paper.

When analysing financial statement simplifications permitted by the Accounting Act, two groups can be identified: „entity-based simplifications“ and „item-based (subject-matter) simplifications.“

Table 2.
Simplifications (Entity-based vs Item-based)

Entity-based simplifications		Item-based simplifications
Micro-entity	Small entity	
simplifications provided for a small entity and additionally: <ul style="list-style-type: none"> • resignation from the prudent principle in the valuation of individual assets and liabilities, i.e. waiver of impairment losses and provisions, • failure to apply fair value and adjusted purchase price to the measurement of assets and liabilities – Article 28 of the Accounting Act. 	Waiver of the determination of deferred tax assets and provisions. Non-application of the Regulation of the Minister of Finance on financial instruments. No elimination of fixed costs of unused normal production capacity from the cost of manufacturing the inventory of products at the end of the year. Withdrawal from the preparation of the activity report Audited entities may resign from preparing a statement of changes in equity and a cash flow statement.	Simplification of depreciation – making collective write-offs for groups of assets similar in type and purpose or one-off write-offs such fixed assets. Valuation of materials and goods at the purchase price. Use of planned costs for product valuation. Valuation of products in progress with a production cycle of no more than 3 months after the partial cost of production.

Source: author's own study based on: Kabalski, 2016.

Micro-entities may use simplifications in keeping books and in preparing financial statements. The approving body of a micro-entity may decide to prepare: a simplified balance sheet (Art. 46(5)(4) of the Accounting Act) and a simplified profit and loss account (Art. 47(4)(4) of the Act) for micro-entities in accordance with Annex 4 to the Accounting Act.

A financial statement under Annex 4 to the Accounting Act is dedicated to micro-entities and to entities referred to in Article 80(4) of the Act (e.g., trade unions, employers' organizations, chambers of commerce). A financial statement prepared under Annex 4 includes:

- General information.
- The balance sheet.
- Supplementary information to the balance sheet.
- The profit and loss account.

According to Article 48(3) of the Accounting Act, a micro-entity may omit the notes (additional information) referred to in paragraph 1, provided it presents the supplementary information to the balance sheet specified in Annex 4. Furthermore, a micro-entity obliged to prepare a management report may omit it provided that, in the notes (additional information), and in the case referred to in Article 48(3), in the supplementary information to the balance sheet, it presents information on the acquisition of its own shares (stock) as specified in Annex 4 (Article 49(4) of the Act). Small and micro entities may omit, in the management report, key non-financial performance indicators related to the entity's activities and information on employee and environmental matters.

Under Article 45(3) of the Accounting Act, a micro-entity's financial statement does not include the statement of changes in equity (fund) or the cash flow statement. Micro-entities may prepare a statement of changes in equity or a cash flow statement voluntarily.

Simplification of financial statements for SMEs is an important issue aimed at lowering costs and reducing administrative burdens for companies while maintaining transparency and reliability of financial information. Such simplifications respond to the need to tailor reporting requirements to the specifics of smaller entities, which often lack advanced financial structures.

On 14 March 2012, a new Directive 2012/6/EU was introduced, amending the Fourth Directive with respect to micro-entities. In July 2013, Directive 2013/34/EU was adopted, replacing the Fourth and Seventh Directives. A key provision is Article 36 "Exemptions for micro-entities" (Kuzior, Pfaff, Poniatowska, Rówińska, 2014). It expresses, inter alia, the postulate that Member States exempt micro-entities from any or all of the following requirements (Maćkowiak, 2019):

- a) presenting "prepayments and accrued income" and "deferred costs and revenues",
- b) preparing notes (additional information) to the financial statements, provided that certain information is disclosed in a balance sheet footnote,
- c) preparing the management report, provided that the required information is disclosed in the notes to the financial statements or in a balance sheet footnote,
- d) publishing annual financial statements, provided that the balance sheet information contained in those statements is duly submitted, under national law, to at least one designated competent authority.

The above simplifications can be grouped into three areas (Chluska, 2016):

- a) Financial reporting.
- b) Measurement principles.
- c) Exemptions from certain provisions.

Simplifying financial statements for SMEs responds to the needs of smaller entities that do not have complex financial structures and can afford to limit reporting formalities. Simplifications reduce costs, increase operational efficiency, and make financial information more accessible to entrepreneurs.

One key area is the structure of the balance sheet. For micro and small entities, the legislator permitted shortened versions of this statement that reduce the number of items on both the asset and liability sides. Categories presented separately in a full balance sheet (e.g., different types of receivables or breakdowns of equity) may be aggregated into single items in the simplified balance sheet. For entrepreneurs, this means less complicated procedures when preparing documents; for readers, it means less detail. The shortened balance sheet allows only a general assessment of the entity's asset position, making it more difficult to perform in-depth analyses of the asset structure and sources of financing. Similar solutions apply to the profit and loss account. Micro-enterprises may prepare highly condensed statements that include only the basic categories of revenues and costs. Small entities may also limit the number of presented items, forgoing many breakdowns obligatory for larger entities. Such simplifications make the profit and loss account a document showing an overall result rather than a full picture of the sources of profitability and costs. For the owner or management of a micro-firm, this may suffice; however, external stakeholders such as banks or investors face significant limitations in assessing performance. A particularly significant simplification is the ability of micro-entities to omit notes (additional information) altogether. In practice, this means giving up commentary, explanations, or additional numerical data that are essential in full statements - e.g., on accounting policies, post-balance-sheet events, or contingent liabilities. Small entities are not entirely exempt from preparing notes but also benefit from a reduced scope of required disclosures. As a result, their financial statements are much less extensive and detailed than those of medium and large entities.

Regulations also allow simplified measurement principles for certain assets. Micro and small entities may, for example, resign from measuring assets at fair value, using historical cost only. For financial instruments—where large entities must apply complex measurement methods - smaller firms may limit themselves to simpler, easier-to-apply solutions, though less informative. Simplifications also concern depreciation. Some regulations allow simplified methods for determining useful life or uniform depreciation rates. While this reduces workload and costs, it flattens the picture of the value of fixed assets and their real consumption.

As noted, micro-enterprises are exempt from preparing the cash flow statement and statement of changes in equity. Consequently, their financial statements are limited to the balance sheet and profit and loss account (often in shortened form), significantly reducing the scope of available information. The absence of a cash flow statement prevents analysis of liquidity and cash-generating capacity - critical for assessing financial stability. Simplifications also affect consolidation obligations. Small and micro entities - even if they are parent entities - may be exempt from preparing consolidated financial statements. Stakeholders then receive no full information about the capital group, only about the parent entity itself. This reduces the reporting burden but limits the transparency of the group's picture.

Although tax simplifications are not formally part of financial accounting regulations, they closely correspond in practice. Micro-enterprises often use simplified tax records such as the revenue and expense ledger (KPiR) or lump-sum tax. This leads to a situation where reporting obligations are minimized and accounting serves primarily a fiscal rather than informational function. Consequently, the financial picture of such entities is significantly reduced and does not meet the standards of decision-useful financial reporting.

A characteristic feature of all these simplifications is their strong cost-minimization orientation. Micro and small enterprises often lack professional accounting departments, and their owners strive to limit administrative obligations. Legislators and international bodies therefore sought solutions enabling formal compliance with reporting obligations with minimal complexity. The consequence, however, is the creation of documents providing only basic - and often insufficient - information. In practice, the emphasis shifts from the informational function of financial statements to their formal-legal function, a process controversial from the standpoint of accounting science and frequently criticized.

Table 3.

Financial reporting simplifications for SMEs

EU Directive 2013/34/EU	<p>The European Union introduced Directive 2013/34/EU to simplify financial statements for micro, small, and medium-sized enterprises. It established size categories and corresponding reporting rules:</p> <ul style="list-style-type: none"> • Micro-enterprises: the simplest form of reporting. They may prepare shortened balance sheets and profit and loss accounts without many additional disclosures. • Small enterprises: slightly more detailed requirements than for micro, but still exempt from many notes. • Medium-sized enterprises: more detailed reporting, but simplified compared to large entities - e.g., fewer requirements for notes.
Accounting Act (Poland)	<p>The Polish Accounting Act allows simplification for SMEs, for example:</p> <ul style="list-style-type: none"> • No obligation to prepare the cash flow statement: small entities are not required to prepare it. • Limited notes: smaller entities may submit limited notes, reducing administrative burden. • Simplified financial reports: small enterprises may submit shortened statements, such as a condensed balance sheet and profit and loss account.
Standard Audit File for Tax (SAF-T / JPK)	<p>The obligation for SMEs to submit the Standard Audit File is another tool that to some extent substitutes for traditional financial statements, as accounting data are transmitted electronically and systematically to the tax administration. SAF-T enables automation of reporting, reducing errors and administrative burden.</p>
IFRS for SMEs	<p>IFRS has developed a special version of standards dedicated to SMEs, which is simpler than full IFRS. It contains simplified rules for:</p> <ul style="list-style-type: none"> • measurement of assets and liabilities, • disclosure of financial information, • reporting financial performance.

Source: author's own study.

5. Drawbacks of Financial Statement Simplifications for Micro and Small Entities

Simplified financial statements, while beneficial in reducing administrative burdens, have limitations. In particular, they provide less detail, which may affect stakeholders' assessment of a company's financial condition (Jonas, 2015).

Several limitations can be identified. First, two issues should be highlighted: limited detail due to the lack of comprehensive notes, since simplified statements usually include fewer notes, which are key to fully understanding certain transactions, methods for measuring assets and liabilities, and the company's accounting policies (Chluska, 2016). Shortened balance sheets and profit and loss accounts present aggregated data that prevent detailed analysis of the asset and performance situation. Without breakdowns by categories of assets or costs, the reader cannot conduct an in-depth assessment of financial structure. This particularly affects analyses of liquidity, indebtedness, or efficiency of specific business areas. While simplified data may suffice for the owner of a small firm, they are far from sufficient for banks, investors, or suppliers. Consequently, simplified statements lose decision-usefulness and become merely formal documents meeting legal requirements while failing in their informational role. Excessive simplification flattens the picture of the enterprise. Resignation from the cash flow statement or notes deprives readers of knowledge about crucial aspects: cash-generating capacity, accounting policies, post-balance-sheet events, or contingent liabilities. As a result, micro and small entities' statements exhibit lower transparency, and their credibility in the eyes of stakeholders is weakened. The lack of details also hinders verification of data reliability, increasing the risk of errors and abuses. Simplified statements often lack information on segments of activity, which may be essential for stakeholders assessing performance by business area. Information on long-term capital investments may be omitted or simplified, making it harder to understand development strategy and future revenue sources. In simplified P&L statements, cost categories may be less detailed, limiting the ability to analyse operating costs and identify areas for optimization.

The second issue is limited information on risks. Full statements usually include details on financial risks (e.g., credit and liquidity risk). In simplified statements, these may be limited or omitted. Small enterprises are often exempt from preparing the cash flow statement, a key document providing information on actual cash inflows and outflows, which makes it more difficult to assess liquidity and the ability to meet obligations.

Simplified statements may also lack detailed information on the structure of equity, including changes in its components or the amount of reserves. This limits understanding of long-term financial stability. Conversely, information on liabilities, such as long-term loans or leases, may be presented in less detail, hindering assessment of debt structure and related risks. Simplified statements may omit future obligations such as guarantees, contingent liabilities,

or lease commitments. Such information is crucial for assessing a company's true financial position but may be omitted or inadequately disclosed. In smaller firms using simplifications, assets may be measured in simplified ways that do not always reflect their fair market value, affecting balance sheet accuracy and potentially leading to under- or overstatement of the company's assets. The literature repeatedly emphasizes that simplifications exacerbate information asymmetry between the enterprise and its stakeholders. Owners or management possess knowledge of the entity's situation that cannot be fully inferred from a simplified statement. External users - creditors, investors, trading partners - make decisions under uncertainty and with incomplete data. This asymmetry results in a higher cost of capital, greater collateral requirements, and more cautious counterparties. These factors weaken a firm's competitiveness by limiting access to external financing and new markets.

A core attribute of good financial reporting is comparability over time and across entities. Simplifications weaken this principle. Shortened forms of the balance sheet and profit and loss account are not directly comparable with full statements of large entities. Differences impede industry and sector analysis and weaken supervisory bodies' ability to monitor the economy. Simplifications also hinder international comparisons. When some companies report under full IFRS and others use national simplifications, obtaining consistent data becomes problematic - creating barriers for SMEs' internationalization and cooperation with foreign partners.

Financial statements have a control function - allowing tax authorities and auditors to assess lawful conduct and tax settlements. Simplifications significantly limit this function. The absence of detailed data in notes or cash flow statements makes it harder to detect irregularities, including potentially unlawful activities. For the tax administration, this implies a higher risk of errors and abuses; for auditors - limited ability to conduct in-depth analysis. Simplifications may thereby lead to an expansion of the shadow economy and undermine trust in the entire financial reporting system. Although simplifications are primarily addressed to external users, enterprises themselves feel the consequences. Abandoning more detailed reporting limits internal analysis and strategic planning. Owners of micro and small firms often rely on simplified statements, which may lead to superficial assessments and misguided managerial decisions. Another drawback is the shift from reporting as an informational tool to its formal-legal function. Micro and small entities prepare statements mainly to meet statutory requirements rather than to provide decision-useful information. Consequently, accounting in this segment plays a more administrative than managerial or analytical role. This weakens accounting's function as the language of business and a tool supporting decision-making. In the long run, it may marginalize the role of financial statements in the SME sector and entrench their perception as a bureaucratic obligation.

6. Conclusion

The analysis of the drawbacks of simplified financial statements for micro, small, and medium-sized enterprises allows several conclusions of both theoretical and practical significance. Although simplifications are introduced to reduce administrative burdens and tailor reporting requirements to the capacity of the smallest entities, their consequences go far beyond reducing the costs of record-keeping and reporting.

Above all, simplifications reduce the decision-usefulness of financial statements. The reduced scope of information presented turns statements from tools supporting economic decision-making into documents of a purely formal nature. This weakens accounting's fundamental function as a source of reliable, complete, and comparable information.

From the perspective of external stakeholders, simplifications generate information asymmetry, leading to higher agency costs, greater caution among creditors and investors, and a worsened negotiating position for the enterprise with counterparties. In practice, this translates into limited access to capital, the need to provide additional collateral, and higher transaction costs.

In a broader context, simplifications weaken market transparency, reduce the possibility of international and sectoral comparisons, and hinder public institutions' monitoring of the economy's condition. A limited scope of statistical and financial data means that economic policy may be based on incomplete premises, increasing the risk of misguided regulatory decisions.

Simplifications also impact accounting culture. Their use reinforces the belief among entrepreneurs that accounting is merely a set of formal requirements rather than a managerial and analytical tool. This hinders the professionalization of financial staff in the SME sector and limits the implementation of modern management tools. In summary, the balance of benefits and costs associated with reporting simplifications for micro, small, and medium-sized enterprises is not clear-cut. On the one hand, they provide administrative relief and lower the direct costs of accounting. On the other hand, they generate numerous drawbacks which, in the longer term, may outweigh short-term savings. It therefore seems necessary to conduct further research and empirical analyses on the impact of simplifications on SMEs' competitiveness, access to financing, and management culture. The results could underpin potential legal modifications to balance the need to reduce costs with ensuring the reliability, transparency, and decision-usefulness of financial statements. From the standpoint of economic policy, a flexible model should be considered - allowing enterprises to choose between simplifications and full reporting depending on their development strategy and financing needs. Such a solution would help build awareness that full accounting is not only an obligation but also an investment in credibility and the enterprise's durability.

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