
IASB[®] meeting

Date	January 2024
Project	Second Comprehensive Review of the <i>IFRS for SMEs</i>[®] Accounting Standard
Topic	Section 20 <i>Leases</i> and IFRS 16 <i>Leases</i>
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This paper has been prepared for discussion at a public meeting of the International Accounting Standards Board (IASB). This paper does not represent the views of the IASB or any individual IASB member. Any comments in the paper do not purport to set out what would be an acceptable or unacceptable application of IFRS[®] Accounting Standards or the *IFRS for SMEs*[®] Accounting Standard. The IASB's technical decisions are made in public and are reported in the IASB[®] *Update*.

Purpose of the paper

1. The purpose of this paper is to ask the International Accounting Standards Board (IASB) to:
 - (a) consider the feedback on the Exposure Draft *Third edition of the IFRS for SMEs Accounting Standard* (Exposure Draft) on amending the *IFRS for SMEs Accounting Standard* (the Standard) to align it with IFRS 16 *Leases* in a future review of the Standard, including cost-benefit considerations of aligning the Standard with IFRS 16; and
 - (b) decide whether to consider aligning the Standard with IFRS 16 in the next comprehensive review of the Standard.
2. In this paper, the term SMEs refers to small and medium-sized entities that are eligible to apply the Standard.

Staff recommendation

3. The staff recommend the IASB consider aligning the Standard with IFRS 16 in the next comprehensive review of the Standard.

Structure of this paper

4. This paper is structured as follows:
 - (a) background (paragraphs 5–14);
 - (b) feedback from comment letters (paragraphs 15–24);
 - (c) staff analysis (paragraphs 25–40);
 - (d) staff recommendation and question for the IASB (paragraph 41); and
 - (e) next steps (paragraph 42).

Background

Current requirements

5. Section 20 *Leases* of the Standard is based largely on IAS 17 *Leases*. IFRS 16 superseded IAS 17. A list of the differences between Section 20 and IAS 17 and an overview of the requirements of Section 20 are provided in Appendix A of [Agenda Paper 30B *Summary of feedback on aligning the IFRS for SMEs Standard with IFRS 16*](#) of the November 2021 IASB meeting.

Feedback on the 2020 Request for Information

6. In January 2020, the IASB published the [Request for Information *Comprehensive Review of the IFRS for SMEs Standard*](#) (2020 Request for Information) as a first step in its second comprehensive review.
7. The 2020 Request for Information asked respondents for views on aligning Section 20 of the Standard with IFRS 16, simplifying some of the recognition, measurement and disclosure requirements of IFRS 16 as well as the language. In seeking views, the IASB noted that leases provide an important source of funding to SMEs and that aligning the Standard with IFRS 16 could improve transparency about SMEs' financial leverage and capital employed. In the 2020 Request for Information, the

IASB said financial statements prepared applying Section 20 aligned with IFRS 16 would more faithfully represent SMEs' assets and liabilities and provide useful and relevant information to users.

8. Overall feedback on the 2020 Request for Information about aligning Section 20 of the Standard with IFRS 16 was mixed. Stakeholders generally suggested the IASB assess costs and benefits of proposing amendments to the Standard to reflect the requirements in IFRS 16, even with simplifications, and obtain more information about the experience of entities applying IFRS 16, including via the Post-implementation Review (PIR) of IFRS 16.

Feedback from the SME Implementation Group (SMEIG)

9. At its February 2021 meeting, the SMEIG members were asked for views on aligning Section 20 of the Standard with IFRS 16, with simplifications. Most SMEIG members agreed that the IASB should undertake additional work to understand the practical challenges entities faced or are facing in implementing or applying IFRS 16 before deciding whether to align the Standard with IFRS 16.¹
10. In light of the mixed feedback by respondents on the 2020 Request for Information, at its September 2021 meeting, SMEIG members were asked to discuss three possible approaches to aligning Section 20 of the Standard with IFRS 16:²
- (a) Approach 1—aligning Section 20 with IFRS 16 with possible simplifications (as described in the 2020 Request for Information);
 - (b) Approach 2—aligning Section 20 with the main principle of IFRS 16 by extending the existing accounting for finance leases in the Standard to all leases; and

¹ See February 2021 [SMEIG Report](#).

² See [Agenda Paper 4A Summary of feedback on aligning the IFRS for SMEs Standard with IFRS 16 Leases](#) of the September 2021 SMEIG meeting and the [meeting summary](#).

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- (c) Approach 3—improving disclosure requirements for operating leases without changing the recognition and measurement requirements in the Standard.
11. There was no consensus among SMEIG members on which approach would be best — support was split between Approach 1 and Approach 3.

Question in the Exposure Draft

12. At its November 2021 meeting³, the IASB considered feedback on the 2020 Request for Information and from SMEIG members on the possible approaches to aligning Section 20 of the Standard with IFRS 16. The IASB tentatively decided:
- (a) to retain Section 20 of the Standard;
 - (b) not to pursue improving disclosure requirements for operating leases without changing the recognition and measurement requirements in Section 20; and
 - (c) to consider amending Section 20 to align with IFRS 16 during a future review of the Standard.
13. The IASB considered that the improvements to financial reporting introduced by IFRS 16 are relevant to SMEs because leases provide an important source of funding to SMEs. However, the IASB:
- (a) observed that cost is a pervasive constraint on the information that can be provided by financial reporting as set out in the revised Section 2 *Concepts and Pervasive Principles*—that is, reporting financial information imposes costs and it is important that those costs are justified by the benefits to users in reporting that information;
 - (b) observed that the costs and efforts for SMEs to apply an aligned Section 20 (at this stage of IFRS 16’s life cycle) might not be justified by the benefits to users; and

³ See [Agenda Paper 30A Towards an Exposure Draft—IFRS 16 Leases](#) of the November 2021 SMEIG meeting and the [IASB Update](#).

- (c) prioritised timing— that is, allowing for more experience of applying IFRS 16. The IASB noted findings from the projects on its work plan may provide additional information about the costs and benefits of aligning Section 20 with IFRS 16.

See paragraphs BC230–BC246 of the Basis for Conclusions on the Exposure Draft for a more detailed summary of the IASB’s considerations about Section 20.

14. The IASB decided to ask for further information on cost-benefit considerations in the Invitation to Comment on the Exposure Draft, particularly on whether:
 - (a) aligning Section 20 with IFRS 16 at this time imposes a workload on SMEs disproportionate to the benefit to users of their financial statements; and
 - (b) introducing possible simplifications could help to simplify the requirements and reduce the cost of implementing an aligned Section 20 without reducing the usefulness of the reported information.

Feedback from comment letters

15. The question in the Invitation to Comment is reproduced below:

Question 12

Do you agree with the IASB’s decision to consider amending the Standard to align it with IFRS 16 in a future review of the Standard? In responding to this question, please comment on the cost–benefit considerations in paragraphs (a) and (b) [of Question 12].

16. Most respondents who commented on Question 12 agreed with the IASB’s decision to consider aligning Section 20 of the Standard with IFRS 16 in a future review of the Standard.
17. Many respondents who agreed with the IASB’s decision said waiting for the IASB to complete its PIR of IFRS 16 will provide a better understanding of how to align and simplify the requirements of IFRS 16 for SMEs. Some respondents who agreed with the IASB’s decision said this will allow SMEs to focus on the proposed amendments

to the third edition of the Standard without imposing a disproportionate workload on SMEs.

18. Some respondents suggested the IASB should consider amending Section 20 to align with IFRS 16 during an interim review of the Standard, as soon as the PIR of IFRS 16 is completed, rather than waiting for the next comprehensive review of the Standard. A few of these respondents observed that waiting would:
- (a) delay the improvements from alignment with IFRS 16; and
 - (b) result in inconsistencies with the proposed definition of a liability and therefore the proposed revised Section 2 (see paragraph BC243 of the Basis for Conclusions on the Exposure Draft).
19. Some respondents disagreed with the IASB's decision and said the IASB should consider aligning Section 20 with IFRS 16 in this review. Their reasons included:
- (a) the benefits of aligning Section 20 with IFRS 16 (with appropriate simplifications) for both SMEs and users of their financial statements would outweigh the costs and waiting for a future review would delay the potential improvements introduced by IFRS 16; and
 - (b) there has been sufficient time and experience gained since implementation of IFRS 16 and the IASB should be aware of any significant implementation issues.
20. Some respondents said alignment with IFRS 16 should not be considered for SMEs (neither in the current review nor a future review) because the costs of implementing an amended Section 20 aligned with IFRS 16 would outweigh the benefits due to the complexity and the extent of judgement required to apply an aligned Section 20.

Cost-benefit considerations

21. Some respondents provided examples of costs that preparers of financial statements would incur implementing an aligned Section 20. These included costs of purchasing

appropriate accounting software and updating systems, collating information and additional resources to make the required judgements. Some of these respondents said that the ongoing benefits of aligning Section 20 with IFRS 16 would outweigh these one-off costs. A few respondents said the implementation experience of entities applying IFRS 16 would help reduce implementation costs for SMEs because implementation challenges would have been identified and will help the IASB to identify simplifications for SMEs.

22. Some respondents commented on the costs that users of financial statements could incur when information about leases is unavailable. Some respondents explained that lenders and creditors would get better information from the recognition, in the statement of financial position, of the lessee's obligation to make lease payments. However, a few respondents said that the existing disclosure requirements in Section 20 provide users with sufficient information.
23. Some respondents who commented on Question 12 noted improvements to financial reporting that would arise from aligning Section 20 with IFRS 16. Improvements noted by a few respondents included:
 - (a) users would be provided with information about SMEs' lease commitments that will result in greater transparency about SMEs' assets and liabilities. Furthermore, it would allow comparability between entities that borrow to buy assets and those that lease similar assets.
 - (b) lenders would be provided with better information, which would assist SMEs seeking funding.

Possible simplifications

24. Some respondents commented on possible simplifications to the requirements in IFRS 16 to reduce the cost of implementation of an aligned Section 20, without reducing the usefulness of the reported information. Suggestions made by a few respondents included:

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- (a) *Discount rate*—respondents suggested SMEs use a risk-free rate to discount lease payment to their present value.
 - (b) *Reassessment of the lease liability*—respondents suggested reducing frequency of when the lease liability is remeasured and using the originally determined discount rate if the SME is unable to determine a revised discount rate.
 - (c) *Lease term*—respondents suggested simplifying how SMEs determine the lease term compared to entities applying IFRS 16.
 - (d) *Low-value asset exemption*—respondents suggested extending this exemption for SMEs, for example by specifying a percentage of total asset value or right of use asset value, or prescribing a monetary value, in the Standard.
 - (e) *Simplifications in local GAAP for SMEs*—respondents suggested the IASB consider simplifications made for private entities applying US GAAP or the UK Financial Reporting Council’s proposed amendments to FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*.

Staff analysis

25. The staff analysis is set out as follows:
- (a) assessment of relevance to SMEs (paragraphs 26–28);
 - (b) timing of aligning Section 20 with IFRS 16 (paragraphs 29–37); and
 - (c) possible simplifications (paragraphs 38–40).

Assessment of relevance to SMEs

26. The IASB determines relevance to SMEs by assessing whether the problem addressed by a new requirement in full IFRS Accounting Standards would make a difference in the decisions of users of financial statements prepared applying the *IFRS for SMEs* Accounting Standard (see paragraph BC30 of the Basis for Conclusions on the Exposure Draft).

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27. The IASB considered that the improvements to financial reporting introduced by IFRS 16 are relevant to SMEs because leases provide an important source of funding to SMEs (see paragraph BC240 of the Basis for Conclusions on the Exposure Draft).
28. Feedback indicated that respondents generally agreed that the improvements introduced by IFRS 16 are relevant to SMEs, although some respondents said alignment with IFRS 16 should not be considered for SMEs for cost-benefit reasons (see paragraph 20 of this paper). Most respondents agreed that the IASB should consider alignment with IFRS 16 at a future review but had different views on the timing of the review (see paragraph 29 of this paper). Therefore, the feedback supports the IASB's position in the Exposure Draft, that the improvements to financial reporting introduced by IFRS 16 are relevant to SMEs.

Timing of aligning Section 20 with IFRS 16

29. Some respondents said the IASB should consider aligning Section 20 with IFRS 16 in this review. However, most respondents supported aligning Section 20 with IFRS 16 in a future review of the Standard. Overall the feedback supports the IASB's decision not to align Section 20 with IFRS 16 during this comprehensive review.
30. Respondents however had different views on the timing of the future review. Many respondents said waiting for the IASB to complete its PIR of IFRS 16 will provide a better understanding of how to amend Section 20 to align with IFRS 16 for SMEs. Some respondents suggested the IASB should consider amending Section 20 to align with IFRS 16 during an interim review of the Standard, as soon as the PIR of IFRS 16 is completed, rather than wait for the next comprehensive review of the Standard.
31. Paragraph P16 and P18 of the Preface to the Standard state the following regarding maintenance of the Standard:
- (a) the IASB expects to propose amendments to the Standard by publishing an omnibus Exposure Draft periodically, but not more frequently than approximately once every three years.

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- (b) on occasion, the IASB may identify an urgent matter for which amendment of the Standard may need to be considered outside the periodic review process. However, such occasions are expected to be rare.
- (c) the IASB expects that there will be a period of at least one year between when amendments to the Standard are issued and the effective date of those amendments.
32. Paragraph BC264 of the Basis for Conclusions on the Standard states the IASB supported the following as a tentative approach for future reviews of the Standard:
- (a) a comprehensive review of the Standard should commence approximately two years after the effective date of the amendments to the Standard resulting from a previous comprehensive review. This would allow time for SMEs to apply the amendments and for interested parties to identify and comment on any implementation issues or unintended consequences that result from those amendments.
- (b) between comprehensive reviews, the IASB, with input from the SMEIG, would decide whether there is a need for an interim review to consider any new and revised full IFRS Accounting Standards not yet incorporated or any urgent amendments that have been identified.
- (c) this process would mean that amendments to the Standard would not typically be expected to be more frequent than approximately once every three years, to provide SMEs with a stable platform.
33. The IASB expects to publish the third edition of the Standard in 2024. Therefore, the staff think if the IASB decided to perform an interim review, such amendments could be issued on or after 2027, that is, allowing three years to provide SMEs with a stable platform. The IASB will be asked to discuss the timing of the next comprehensive review at a future meeting.
34. The staff have considered the merits of an interim review versus waiting for the next comprehensive review in the following paragraphs.

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35. The staff think the following reasons support the IASB considering aligning the Standard with IFRS 16 in the next comprehensive review:
- (a) the IASB aims to provide a stable platform for SMEs by performing periodic reviews. This second comprehensive review is likely to result in significant amendments to the Standard, following which SMEs would benefit from a stable platform. The staff think aligning the Standard with IFRS 16 in the next comprehensive review instead of an interim review would help to provide a stable platform for SMEs.
 - (b) if the IASB performs an interim review to amend the Standard to align with IFRS 16, there could be pressure on the scope of the interim review to consider other amendments to full IFRS Accounting Standards, which could turn the interim review into a mini comprehensive review.
 - (c) once the second comprehensive review is completed, the IASB has committed to either update the *IFRS for SMEs* educational modules that support the second edition of the Standard, or provide similar comprehensive educational material on the third edition of the Standard. This work is expected to take place in 2025/2026 and would require similar resources as the interim review. Therefore, the IASB would need to consider the importance of an interim review with other pipeline projects on full IFRS Accounting Standards on its agenda.
36. The staff think the following reasons would support the IASB considering aligning the Standard with IFRS 16 in an interim review:
- (a) enabling SMEs and users of their financial statements to benefit from the improvements introduced by IFRS 16 sooner than waiting for the issue of amendments from the next comprehensive review.
 - (b) waiting until the next comprehensive review would lead to a longer period of divergence between the Standard and full IFRS Accounting Standards on a matter that is relevant to SMEs.

- (c) at its December 2023 meeting, the IASB tentatively decided that the PIR of IFRS 16 would commence in the second quarter of 2024. Therefore, the staff think the findings from the PIR would be available to consider during an interim review.
- (d) an interim review would allow SMEs to focus on implementing an aligned Section 20 separately from implementing other amendments to be introduced in the next comprehensive review.

Staff view

37. On balance, the staff think considering aligning the Standard with IFRS 16 in the next comprehensive review instead of an interim review provides SMEs with a stable platform. We also think the IASB would serve the SME community better by focussing on providing educational material to support application of the amendments from the second comprehensive review rather than starting an interim review to consider aligning Section 20 with IFRS 16.

Possible simplifications

38. Respondents suggested possible simplifications that could simplify the requirements and reduce the cost of implementing an aligned Section 20 without reducing the usefulness of the reported information. These suggestions have been summarised in paragraph 24 of this paper.
39. When the IASB considers amending Section 20 to align with IFRS 16 during a future review of the Standard, the staff will consider these possible simplifications in proposing requirements for a Section 20 aligned with IFRS 16.
40. The staff will also consider the following sources of information in making recommendations for an amended Section 20 (aligned with IFRS 16):
- (a) *Feedback on the PIR of IFRS 16*—the IASB tentatively decided to begin the PIR of IFRS 16 in the second quarter of 2024.

- (b) *Developments in local GAAP* such as:
- (i) *FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland*⁴—FRED 82 *Draft amendments to The Financial Reporting Standard applicable in the UK and Republic of Ireland* proposed aligning FRS 102 with IFRS 16. The FRC is reconsidering how to ensure that the model is proportionate and understandable for FRS 102 preparers of all sizes. The FRC currently expects to issue the final amendments to FRS 102 in the first half of 2024, with an effective date not before 1 January 2026.
 - (ii) *Topic 842 Leases*—FASB’s Topic 842 provides simplifications for private companies applying the leases Standard.

Staff recommendation and question for the IASB

41. The staff recommend the IASB consider aligning the Standard with IFRS 16 in the next comprehensive review of the Standard.

Question for the IASB

Does the IASB agree with the staff recommendation in paragraph 41 of this paper to consider aligning the *IFRS for SMEs Accounting Standard* with IFRS 16 *Leases* in the next comprehensive review of the Standard?

⁴ FRS 102 is based on the *IFRS for SMEs Accounting Standard* with some amendments made for application in the UK and Republic of Ireland.

Next steps

42. At a future meeting, the staff will bring a paper to the IASB to consider:
- (a) the timing of the third comprehensive review of the *IFRS for SMEs* Accounting Standard; and
 - (b) whether there is a need for an interim review to consider any new and revised full IFRS Accounting Standards not yet incorporated.