

AGENDA PAPER

IFRS Foundation Trustees' meeting—Due Process Oversight Committee

London

12-13 April 2012

Agenda ref

3Hi

DPOC: Correspondence with KPMG on IFRS for SMEs

To: IFRS Foundation Due Process Oversight Committee
From: Paul Pacter, Board Member, IASB ppacter@ifrs.org
Re: Letter from KPMG regarding IFRS for SMEs Questions and Answers (Q&As)

KPMG has written to the Trustees of the IFRS Foundation (letter dated 27 January 2012 and also two earlier letters) expressing the concern of the KPMG Network about “the appropriateness of supplementing the IFRS for SMEs by a series of non-binding Q&As and the potential dilution of the power of a single stand-alone standard for SMEs”.

Several other international auditing firms have made similar comments in their letters to the SME Implementation Group commenting on draft Q&As.

The purpose of this memo is to explain the background and status of the Q&As.

The information in this memo is intended to assist the IFRS Foundation’s Due Process Oversight Committee in considering the point raised by KPMG and developing a response.

I am the IASB Board Member responsible for the IFRS for SMEs. Prior to joining the Board in July 2010, I was for seven years the IASB’s Director of Standards for SMEs. In this latter capacity I managed the project that culminated in the Board issuing the IFRS for SMEs.

The IFRS for SMEs has quickly gained worldwide acceptance.

The IFRS for SMEs was issued in July 2009. Over 70 jurisdictions have already adopted it or announced plans to do so. We estimate that in 2012 over 10 million SMEs will use the IFRS for SMEs around the world. In contrast, the total number of listed companies on the 53 stock exchanges that are members of the World Federation of Exchanges is 46,000 (and at least 15,000 of those do not yet use IFRSs).

The IFRS for SMEs is tailored for small companies.

The IFRS for SMEs focuses on the needs of lenders, creditors, and others who look to the financial statements of SMEs for information about cash flows, liquidity, and solvency. And it takes into account the costs to SMEs and the capabilities of SMEs to prepare financial information.

The raison d’être of the IFRS for SMEs is very simple: to help SMEs improve their access to capital by providing financial information that lenders, creditors, and other capital providers understand and have confidence in.

The IFRS for SMEs is much smaller than full IFRSs—it is just 230 pages as compared to over 3,000 pages in full IFRSs. It is organised by topic. And compared with full IFRSs, and many national standards, the IFRS for SMEs is much less complex because it (1) omits topics not relevant to SMEs, (2) eliminates complex options in full IFRS, (3) simplifies many of the recognition and measurement principles in full IFRSs, and (4) reduces the number of required disclosures by roughly 90%.

The IASB and IFRS Foundation are providing comprehensive implementation support.

The IFRS for SMEs has brought a whole new constituency to the IASB—unlisted companies in many countries where, up to now, SMEs have followed a very simple local GAAP. In recognition of this, the Board and the Foundation made a decision to work intensively to

support the smooth and rigorous implementation of the IFRS for SMEs. Historically, the IASB has never provided this degree of implementation support for full IFRSs.

The kinds of implementation support that we are providing for the IFRS for SMEs include:

- Making the entire standard available without charge, including implementation guidance and basis for conclusions (this is different from full IFRSs).
- Issuing illustrative financial statements and a presentation and disclosure checklist along with the standard.
- Translating the entire standard into many languages (18 languages already finished, 6 in process, and 2 more under discussion).
- Developing training materials (self-study materials with hundreds of guidance examples, one module for each of the 35 sections of the IFRS for SMEs, comprising nearly 2,000 pages of materials in all, five languages, free download in PDF format).
- Conducting regional training workshops (22 held so far, 4 others planned, generally three days, 24 classroom hours total, with 1,100 PowerPoint slides in multiple languages available for free download).
- Forming an IFRS for SMEs Implementation Group (SMEIG) to assist in implementation—discussed in more detail below.
- Publishing a free monthly newsletter (13,000 subscribers).
- Designing and maintaining comprehensive and integrated IFRS for SMEs web pages (with many links to download IFRS for SMEs materials for free).
- Publishing an executive briefing booklet (non-technical, aimed at lenders, creditors, owner-managers, and others who use SME financial statements).
- Developing and publishing XBRL tags.

The SME Implementation Group develops Q&As as non-mandatory guidance in applying the IFRS for SMEs.

In September 2010, the Trustees of the IFRS Foundation appointed an SME Implementation Group (SMEIG) following a public call for nominations. Its 22 members were given two responsibilities:

- to develop and publish Q&As as non-mandatory guidance intended to help those who use the IFRS for SMEs to think about specific accounting questions when implementing the IFRS for SMEs.
- to make recommendations to the IASB regarding possible amendments to the IFRS for SMEs as part of a comprehensive post-implementation review of the standard that will get underway in the second half of 2012.

The Q&A programme follows comprehensive due process steps.

The terms of reference and operating procedures of the SMEIG were developed and approved by the Trustees. Those terms of reference establish a comprehensive due process for issuing Q&As.

Briefly described, the steps for issuing a Q&A involve:

- Staff identify an issue and prepare a background paper. In some background papers staff recommend issuing a Q&A, and in others staff recommend that a Q&A not be issued.
- All SMEIG members are requested to provide their comments on the paper (via email) about whether to develop a Q&A and, if yes, what the proposed answer should be. Each SMEIG member's views are circulated to other members to encourage debate. A second (or third) round of comments may be required if a simple majority consensus cannot be reached.
- The draft Q&A is sent to IASB Board members. It will be released for public comment unless four or more IASB members object within 30 days. (While the terms of reference require a minimum 30-day public comment period, for every one of the 11 draft Q&As we have provided a public comment period of not fewer than 60 days.)
- Staff prepare an analysis of comments received and make recommendations for changes to the draft Q&A in light of public comments.
- All SMEIG members are requested to provide their comments via email on the revised Q&A. A second round of comments may be required if a simple majority consensus cannot be reached.
- The final Q&A is sent to IASB Board members. It will be posted on IASB's website unless four or more IASB members object within 15 days. Board members have access to all SMEIG comments and papers.

In developing the Q&As to date, the due process steps have been rigorously followed.

The Q&A programme has been quite limited, and with the upcoming comprehensive review of the IFRS for SMEs it is likely to be terminated altogether.

Only three final Q&As are now published (all deal with eligibility to use IFRS for SMEs). Seven additional drafts have been exposed for public comment. Of those seven:

- On four of them, SMEIG recommends finalising the Q&A. Two of those are now before the Board for consideration.
- Staff have recommended not adopting a final Q&A on three.

No additional Q&As are under development by SMEIG. So there will be a maximum of seven Q&As.

We already say on the IASB website:

"When the International Accounting Standards Board (IASB) issued the IFRS for SMEs in 2009, it made a commitment to undertake a post-implementation review of the standard. The IASB expects to initiate the comprehensive review in 2012. The review is expected to include a request for public comments on amendments that should be considered for the IFRS for SMEs. As part of the review, the IASB will also consider incorporating Q&As into the revised IFRS for SMEs. For that reason, the SMEIG does not expect that it will issue many, if any, additional draft Q&As before the start of the comprehensive review."

Small companies and small countries want Q&As and similar implementation guidance.

Understandably, a large international firm like KPMG is likely to look at the Q&As from a background in full IFRSs. But there is another point of view to consider—the small country and small company perspective. We have circulated KPMG’s view on the Q&As to the members of the SMEIG—and similar large-firm views in letters of comment on the Q&As. Set out below is the response of one SMEIG member from a small developing country:

“Respondents have expressed concerns about the volume of Q&A's, but over a period of 18 months we have so far produced a grand total of [3] final Q&A's,

“2 additional final Q&A's are now proposed, and there are 2 draft Q&A's open for comment. This can hardly be considered an excessive body of guidance, compared to the interpretations and directives which firms and practitioners must issue their SME clients almost daily. Several respondents acknowledge that the SMEIG guidance is not binding, but then proceed to completely ignore this in their responses and in their description of the harm that might arise from a large number of Q&A's. Many express concerns about issuing guidance on terms that are already present in full IFRS, but how is this a concern for the vast majority of SMEs that are not expected to be familiar with full IFRS? There are also concerns about creating an excessive rules-based environment despite the fact that the non-mandatory Q&A's have consistently emphasized the need to exercise judgment and consider the specific circumstances.

“Matters that are obvious and well known to the large firms and major national standard-setting bodies (with their significant technical resources) may not be so obvious to a large proportion of the preparers, auditors and users of the financial statements of SMEs. If the purpose of the SMEIG is simply to issue guidance for use by the large firms and national bodies then I have no problem with the number of Q&A's issued. If the SMEIG guidance is intended for a much broader group of constituents then it seems to me that we would have failed at a significant part of our mandate.”

I hope that this background on the Q&As will help the DPOC allay the concerns of the KPMG Network.

6 February 2012

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Dear Mary

Development of Q & As on the IFRS for SMEs

I am writing to you in response to letters KPMG sent the IASB in relation to the Q&A process in the IFRS for SME programme. The matters you raise have potential implications for the consistent application of IFRSs.

Unfortunately, your correspondence has only recently been brought to my attention. We have recently made changes to the way correspondence to the Trustees is processed and it is those changes that highlighted the oversight in acknowledging your concerns.

The staff will prepare a report for the Trustees' Due Process Oversight Committee (DPOC) addressing the matters you raise. The DPOC will consider that report when it meets in April, and we will send you a draft of that report in advance of the meeting. Following the meeting, David Sidwell, Chair of the DPOC, will send you a more comprehensive reply.

Please note that all correspondence relating to due process matters is made public on our website.

Please accept my apologies for the delay in responding to you.

Yours sincerely,



Tamara Feldman

Assistant Corporate Secretary and Internal Legal Counsel



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Our ref MT/288
Contact Mary Tokar

14 September 2011

Dear Sirs

Development of Q&As on the IFRS for SMEs

We are writing to express our concern about the initiative sponsored by the IFRS Foundation to provide non-mandatory implementation guidance on the International Financial Reporting Standard for Small and Medium-sized Entities (IFRS for SMEs). We believe that this initiative, while well intentioned, is inconsistent with the objective of having a single, stable, stand-alone standard for SMEs. We therefore strongly recommend that the SME Implementation Group stop issuing Q&As and withdraw any that have been issued.

We agree that the SME Implementation Group is a valuable forum for understanding how the standard is being used in practice and what issues are being raised, especially in these early days. We continue to support the existence of the SME Implementation Group. However, we believe that the SME Implementation Group's efforts should be focused on providing a forum for identifying and assessing questions that are being raised by users implementing the IFRS for SMEs, developing educational material as needed and helping plan the first update of that standard.

We believe that a process to supplement the stand-alone standard with a series of Q&As is inappropriate given the objective of the IFRS for SMEs is to have all accounting requirements integrated into a single standard. Further, the IASB decided to focus the SME standard on those items for which it believed consistent practice was critical. The IASB recognised that providing less guidance than in full IFRSs, with no fallback to full IFRSs, meant that it is likely that there will be greater diversity in practice on issues that were not addressed. Trying to remedy this after the fact with non-binding Q&As calls into question the basic design of the standard. We believe that this initiative will dilute the power of a single standard.

Lastly, we also are concerned about this initiative from the perspective of "full" IFRSs. The SME Implementation Group proposed to issue an "interpretation" on a matter that is equally relevant to full IFRSs – refer Draft Q&A 2011/03 on "traded in a public market", which is the same terminology used in IFRS 8 *Operating Segments* and IAS 33 *Earnings per share*. Matters



that are equally relevant to full IFRSs should be escalated to the IASB or IFRS Interpretations Committee and guidance should be issued only after their due process has been completed.

Yours sincerely

KPMG IFRG Limited

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cc. Mr. Hans Hoogervorst
cc. Mr. Ian Mackintosh
cc. Mr. Paul Pacter



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Our ref MT/288
Contact Mary Tokar

27 January 2012

Dear Sirs

Development of Q&As on the IFRS for SMEs

We appreciate the opportunity to respond to the draft Questions & Answers (Q&As) relating to the International Financial Reporting Standard for Small and Medium-sized Entities (IFRS for SMEs). We have consulted within the KPMG network in respect of this letter, which represents the views of the KPMG network.

As expressed in our previous comment letters dated 14 September 2011 and 29 November 2011, we have concerns about the appropriateness of supplementing the IFRS for SMEs by a series of non-binding Q&As and the potential dilution of the power of a single stand-alone standard for SMEs.

We believe that these concerns are particularly relevant for the two draft Q&As on Sections 11 and 30 (covering the fallback to IFRS 9, *Financial Instruments* and the recycling of cumulative exchange differences on disposal of a subsidiary, respectively). We agree that the conclusions in the draft Q&As are appropriate applications of the IFRS for SMEs. However, even if we believed that it was appropriate for the International Accounting Standards Board to provide implementation guidance in the form of Q&As, we would not agree that there is a genuine need for clarification of these issues as, in our view, the answers to the questions are clear in the IFRS for SMEs and hence issuing Q&As on these topics would not be necessary.

Notwithstanding the above, we continue to support the existence of the SME Implementation Group (SMEIG). However, as was also set out in our previous letters, we believe that the SMEIG should focus on identifying and assessing questions that are being raised by developing educational material as needed and helping plan the updates of the IFRS for SMEs.



Please contact Mary Tokar or Jim Tang on +44 (0)20 7694 8871 if you wish to discuss any of the issues raised above.

Yours faithfully

KPMG IFRG Limited

KPMG IFRG Limited

cc. Hans Hoogervorst, Chairman of the IASB
cc. Ian Mackintosh, Vice Chairman of the IASB
cc. Paul Pacter, Chairman of the SMEIG
cc. Haydeé de Chau, member of the SMEIG