IFRS™

Agenda ref	6B

STAFF PAPER

March 2013

IASB Meeting

Project	**Comprehensive review of the *IFRS for SMEs***		
Paper topic	New and revised IFRSs		
CONTACT(S)	Darrel Scott (Board Advisor)	dscott@ifrs.org	+44 (0) 20 7246 6489
	Michelle Fisher	mfisher@ifrs.org	+44 (0) 20 7246 6918

Purpose of this paper

1. This Agenda Paper 6B asks the IASB to consider the responses received to the questions in the IASB's 2012 Request for Information (RFI) on new and revised IFRSs issued since the *IFRS for SMEs* was published.

2. This Agenda Paper 6B summarises the main comments received from respondents, provides the IASB staff and SMEIG recommendations, and includes a question for the IASB to discuss.

Structure of this paper

3. This Agenda Paper 6B is set out as follows:

    (a) Issue 4: Consideration of new and revised IFRSs

    - (i) Introduction
    - (ii) Summary of the main comments received in response to the questions in the RFI.
    - (iii) Staff comments. Additional information that may be useful to the IASB discussions.

(iv) SMEIG recommendation based on the near final draft of the SMEIG report.

(v) Staff recommendation. This has been updated from the initial recommendation presented in the agenda papers for the SMEIG meeting to reflect further staff thinking in light of discussions at the SMEIG meeting.

(vi) Question for the IASB to discuss.

(b) Appendix containing full extract from the near final draft of the SME Implementation Group (SMEIG) report on Issue 4

Note, issue numbers in Agenda Paper 6B follow the same numbering as in the agenda papers for the SMEIG meeting.

Introduction

4. The RFI contained several questions on how to deal with changes to full IFRSs resulting from new and revised IFRSs issued since the *IFRS for SMEs* was published in 2009.

5. Firstly the RFI asked individual questions on each of the following new and revised IFRSs because these IFRSs are considered to contain the main recognition and measurement changes made to full IFRSs that will also relate to requirements in the *IFRS for SMEs.* The questions in the RFI asked respondents whether the *IFRS for SMEs* should be revised to reflect the main changes to the IFRS, but modified as appropriate to reflect the needs of users of SME financial statements and cost-benefit considerations (the full questions from the RFI have not been repeated here due to their length):

(a) IFRS 10 *Consolidated Financial Statements* (Question S4 in the RFI)

(b) IFRS 13 *Fair Value Measurement* (Question S6)

(c) IFRS 11 *Joint Arrangements* (Question S8)

(d) IFRS 3 (amended 2008) *Business Combinations* (Question S12) [1]

(e) IAS 19 (amended 2011) *Employee Benefits* (Question S15)

(f) IAS 12 (amended 2010) *Income Taxes* (Question S18)

6. Secondly, the RFI asked a separate question (Question G1) on how to deal with minor improvements to IFRSs, ie where amendments clarify guidance and wording, modify definitions or make other relatively minor amendments to full IFRSs to address unintended consequences, conflicts or oversights (eg as part of the IASB's Annual Improvements project). The question in the RFI asked how should the IASB deal with such minor improvements when the *IFRS for SMEs* is based on the old wording from full IFRSs.

7. **Important note:** The RFI did not ask any questions on the current projects on the IASB's agenda that are expected to result in changes to full IFRSs for the following reasons:

(a) Until a final IFRS is issued, the views of the IASB are always tentative and subject to change.

(b) Sometimes, the principles in a final IFRS differ significantly from those examined in a discussion paper or initially proposed in an exposure draft.

(c) In other cases, a final IFRS is not issued at all, or work on a project is suspended for an indefinite period.

The next triennial review of the *IFRS for SMEs* will ask specific questions about any new and revised IFRSs issued after this comprehensive review has been completed.

Responses from comment letters on Issue 4

8. Views on whether or not the *IFRS for SMEs* should be updated during this comprehensive review for new and revised IFRSs issued since the *IFRS for SMEs*

[1] IFRS 3 (2008) was issued shortly before the *IFRS for SMEs* was issued but was not incorporated in the *IFRS for SMEs*.

was published were evenly split, with a slight majority in favour of updating. There were more respondents in favour of adopting the changes to IAS 19(2011) than the other new and revised IFRSs as it was felt it would result in comparability with full IFRSs without increasing complexity. Furthermore, many comment letters in favour of not updating during this review would favour updating the *IFRS for SMEs* for new and revised IFRSs in the future (at the next triennial review), once the changes become established under full IFRSs.

9. The following points cover the main reasons given by respondents for not revising the *IFRS for SMEs* for new and revised IFRSs during this comprehensive review:

   (a) An automatic requirement to align the *IFRS for SMEs* with full IFRSs would undermine the original purpose of developing a standalone, simplified, set of accounting principles for SMEs.

   (b) SMEs need a stable platform. Frequent changes in requirements, even minor improvements and wording changes, would be burdensome for SMEs and users of their financial statements. The *IFRS for SMEs* should only be changed where there is a demonstrated need for improving SME reporting justified through an assessment of user needs and cost-benefit considerations.

   (c) The IASB should not incorporate requirements into the *IFRS for SMEs* before they are effective under full IFRSs and the post-implementation reviews have been concluded. The implementation experience of entities applying full IFRSs will provide an insight on the suitability of the new requirements for SMEs eg whether they result in an improvement in financial reporting, any unintended consequences or implementation costs, etc. Such experience is particularly important in areas when changes are complex, for example IFRS 10 and 13.

   (d) Changes to full IFRSs should only be implemented in the *IFRS for SMEs* after they have become established under full IFRSs and are unlikely to be amended further. For example the presentation of actuarial gains and losses under full IFRSs is likely to be revisited and so the current accounting policy option in the *IFRS for SMEs* to recognise them in profit or loss should be retained for now.

10. The following points cover the main reasons given by respondents for revising the *IFRS for SMEs* for new and revised IFRSs during the comprehensive review modified as appropriate to reflect the needs of users of SME financial statements and cost-benefit considerations:

    (a) Changes are made to full IFRSs for good reasons, eg to improve the quality of financial reporting, clarify requirements or provide more guidance. Therefore it would be inappropriate for the *IFRS for SMEs* to become out of date with current requirements in full IFRSs and continue to be based on inferior versions of full IFRSs that have been replaced. The *IFRS for SMEs* was developed from full IFRSs and so it is logical that it should generally remain in line with full IFRSs where possible.

    (b) Consistent accounting across companies under the *IFRS for SMEs* and full IFRSs is desirable. Although modifications to the *IFRS for SMEs* may be necessary for the needs of SMEs, they should be kept to a minimum. Where modifications are made, there should be an option for an entity to follow the recognition and measurement requirements of full IFRSs.

    (c) Consistency with full IFRSs facilitates entities transitioning from the *IFRS for SMEs* to full IFRSs. Also, consistency between the recognition, measurement and presentation principles of full IFRSs and the *IFRS for SMEs* is important for subsidiaries that produce full IFRSs information for consolidation purposes.

    (d) Many jurisdictions have adopted both full IFRSs and the *IFRS for SMEs*. It would be confusing for two unrelated sets of standards to be applied in the same jurisdiction. Differences between the *IFRS for SMEs* and full IFRSs could cause confusion for users of financial statements and requires additional education and training of accountants and other parties using both sets of standards.

(e) Having different definitions and terminology in use under full IFRSs and the *IFRS for SMEs* would be confusing. The definitions of control (IFRS 10) and fair value (IFRS 13) are fundamental to the IFRS Framework and so it is important that the revised definitions are incorporated in the *IFRS for SMEs*. Identical transactions should not be accounted for differently under the two sets of standards.

11. Other suggestions made by comment letters include:

(a) The IASB should develop review criteria to be applied when assessing if and how changes to full IFRSs, including minor improvements, should be incorporated into the *IFRS for SMEs*. This would ensure a consistent approach is followed for updates of the *IFRS for SMEs*, would clarify the objective of the *IFRS for SMEs* and its relationship with full IFRSs, and also enable SMEs to plan for changes for effectively.

(b) Changes to full IFRSs should not be incorporated if they are unlikely to have a significant effect on the financial reporting of most SMEs, for example IFRS 10 and IFRS 13. To do so would result in an unnecessary burden as SMEs would still need to read and understand the requirements. However, changes to full IFRSs should be incorporated if they relate to SME transactions, eg IFRS 11, IFRS 3(2008) and IAS 19(2011).

(c) If some, but not all, of the changes from an IFRS standard are incorporated in the *IFRS for SMEs*, care is required to avoid ending up with a mixed approach, ie a mixture of 'old and new' IFRSs, as this may result in an incoherent model. For example, IFRS 3(2008) made significant changes to business combination accounting and the model in IFRS 3(2008) should be incorporated in full or not at all.

(d) Future updates of the *IFRS for SMEs* would be simplified if the IASB considered potential implications for the *IFRS for SMEs* at the same time as changes are made to full IFRSs. Any proposed changes to the *IFRS for SMEs* would be accumulated and included in the omnibus exposure draft issued as part of the IASB's review of the *IFRS for SMEs* expected to take place approximately once every three years.

Staff comments on Issue 4

12. Based on responses to the RFI and also the SME discussion at the World Standard-setters Meeting in October 2012 there seems to be several different opinions and also some confusion about the main objective of the *IFRS for SMEs*.

13. Comment letters have highlighted different possible purposes and uses of the *IFRS for SMEs.* These include:

    (a) A standalone standard tailored for the capabilities of smaller businesses without public accountability and for needs of users of their financial statements.

    (b) A standard intended for jurisdictions that do not have a standard for SMEs, for example where full IFRSs is required for all entities.

    (c) A framework upon which local jurisdictions can develop their own local GAAP for SMEs.

    (d) An intermediate standard for a company that expects to transition to full IFRSs in the future.

    (e) A standard useful for non-publicly accountable subsidiaries, joint ventures or associates of an investor/parent applying full IFRSs. In particular the *IFRS for SMEs* reduces the burden of full IFRS disclosure requirements for these entities.

    (f) A standard useful for larger non-publicly accountable entities which wish to have comparability with listed companies applying full IFRSs but also wish to benefit from the reduced disclosure of the *IFRS for SMEs*.

14. Responses to individual questions in the RFI are generally influenced by the respondent's understanding of the purpose of the *IFRS for SMEs* and which entities it should cater for. For example, if a respondent believes the *IFRS for SMEs* should mainly cater for subsidiaries of full IFRS investors, then respondents

would prefer the recognition, measurement and presentation requirements of the *IFRS for SMEs* to be fully aligned with full IFRSs, ideally without any time lag.

15. Based on responses in the comment letters the staff have identified the following ways of dealing with changes in full IFRSs:

    (a) **Not automatic.** The *IFRS for SMEs* is a standalone standard. Changes to full IFRSs should not automatically be incorporated. Plus, changes unrelated to requirements in full IFRSs may be considered (eg including guidance on preparing combined financial statements). All changes to the *IFRS for SMEs* should be considered for incorporation individually based on an assessment of the needs of users of SME financial statements, capabilities of SMEs and cost-benefit considerations.

    (b) **Not automatic and after implementation experience.** Same as (a). Furthermore, in general, changes to full IFRSs should only be considered after they have become established under full IFRSs and implementation experience has been assessed (eg after post-implementations reviews have been performed, where applicable). Under this approach there would be more of a time lag between when changes are adopted under full IFRSs and when they are adopted under the *IFRS for SMEs* (likely to be delayed by at least an extra three years—one triennial review later).

    (c) **Automatic.** The *IFRS for SMEs* is a simplified version of full IFRSs. It is based on full IFRSs and the main principles in the two sets of standards should be aligned where possible. Changes to full IFRSs should automatically be incorporated in the *IFRS for SMEs*. Such changes may need to be modified for the needs of users of SME financial statements and cost-benefit considerations (eg simplifying requirements where appropriate such as expensing development costs, or removal of accounting policy options if they are too complex for SMEs such as revaluation of intangible assets etc). Changes unrelated to requirements in full IFRSs would only be considered in rare cases.

(d) **Automatic but after implementation experience.** Same as (c). However, in general, changes should only be considered after they have become established under full IFRSs and implementation experience has been assessed. Under this approach there would be more of a time lag between when changes are adopted under full IFRSs and when they are adopted under the *IFRS for SMEs*.

(e) **Full alignment.** The main aim of the *IFRS for SMEs* is to provide relief from the disclosures in full IFRSs. Recognition, measurement and presentation requirements should be fully aligned with full IFRSs because SMEs should be entitled to follow the same accounting treatment as entities applying full IFRSs if they wish to do so. Therefore the *IFRS for SMEs* would permit the same accounting policy options as full IFRSs but may offer additional simplified options (eg investments in associates can be accounted for under the equity method or the cost method). Where possible accounting policy options would be contained within the *IFRS for SMEs* (not by cross-reference to full IFRSs). Disclosure requirements should be modified as appropriate to reflect the needs of users of SME financial statements and cost-benefit considerations.

(f) **Permit fallback.** Regardless of approach, SMEs should be permitted to fallback to full IFRSs for recognition, measurement and presentation requirements (this was suggested for subsidiaries producing information for consolidation purposes under full IFRSs). This would mean the *IFRS for SMEs* is not a self-contained standard as it would contain cross references to full IFRSs. This method would mean there was no time lag.

SMEIG recommendation on Issue 4

The SMEIG made the following recommendations:

a) Changes to the *IFRS for SMEs* should be driven in order of priority by:

(i) implementation experience of SMEs, and

(ii) changes to full IFRSs.

b) New or significantly amended IFRSs should not be incorporated until implementation experience has been assessed (after the post-implementation review). Exceptions may be considered, for example where they would help solve a known problem for SMEs, or changes are simplifications and easily understood.

c) Minor amendments to full IFRSs should only be incorporated where there is a known problem for SMEs.

Staff recommendation on Issue 4

16. The staff believe the primary aim when developing the *IFRS for SMEs* was to provide a standalone, simplified, set of accounting principles that are appropriate for entities that do not have public accountability, in particular those that have less complex transactions, do not have the resources to apply full IFRSs and where comparability with their listed peers is not so important. Such entities do not require complex accounting policy options or the detailed guidance in full IFRSs dealing with complex transactions. The staff think that all entities that have complex transactions, favour comparability with publicly accountable entities and have sufficient expertise should really be applying full IFRSs.

17. Therefore staff think the purpose of the *IFRS for SMEs* is mainly to cater for entities in paragraph 13(a) and (b). This aim should not be undermined by trying to cater for the situations in paragraph 13(c)-(f). While the *IFRS for SMEs* may be useful for these purposes, they were not the main reasons for developing the *IFRS for SMEs*.

18. The staff agree with the SMEIG that the main driver for changes to the *IFRS for SMEs* should be the implementation experience of SMEs, including that of users of their financial statements, with changes to full IFRSs being a secondary driver. Furthermore, the staff recommend changes to full IFRSs should be considered for incorporation in the *IFRS for SMEs* using the following principles (this is the approach in paragraph 15(b)):

(a) All changes to full IFRSs should be considered individually. However, they should only be incorporated if they would improve the financial reporting for SMEs based on an assessment of the implementation experience of SMEs, needs of the users of SME financial statements, and cost-benefit considerations.

(b) To avoid unnecessarily increasing the reporting burden for SMEs, minor amendments to full IFRSs to address unintended consequences, conflicts or oversights (eg as part of the IASB's Annual Improvement process) should only be made where there is a known problem for SMEs, ie there should be a rebuttable presumption that changes should not be incorporated in the *IFRS for SMEs.*

19. Regarding when changes to full IFRSs should be considered, staff recommend the following:

(a) Changes to full IFRSs should only be considered for incorporation in the *IFRS for SMEs* after they have become established under full IFRSs and implementation experience has been assessed (eg after the post-implementation review has been performed, where appropriate). Changes may be considered earlier, for example if they respond to an known problem or would result in simplification—however this is expected to be rare.

(b) Any changes proposed to the *IFRS for SMEs* would be issued for public comment as part of the omnibus exposure draft developed during the IASB's triennial review (explained in P16 to P18 of the *IFRS for SMEs*).

20. Overall the staff recommendation is very similar to the SMEIG view except the staff think that changes should only be considered before implementation experience is assessed in rare cases.

Question to the IASB
e) As a matter of policy, how should the *IFRS for SMEs* be updated for new and revised IFRSs and also annual improvements?

Appendix A: Extract from near final draft of the SMEIG (Issue 4)

Issue 4) Consideration of new and revised IFRSs

21. ***As a matter of policy, how should the IFRS for SMEs be updated for new and revised IFRSs and annual improvements?***

The SMEIG made the following recommendations:

a) Changes to the *IFRS for SMEs* should be driven in order of priority by:

(i) implementation experience of SMEs, and

(ii) changes to full IFRSs.

b) New or significantly amended IFRSs should not be incorporated until implementation experience has been assessed (after the post-implementation review). Exceptions may be considered, for example where they would help solve a known problem for SMEs, or changes are simplifications and easily understood.

c) Minor amendments to full IFRSs should only be incorporated where there is a known problem for SMEs.

Applying these principles, the SMEIG recommends:

a) Changes to IAS 19 should be incorporated during this review.

b) Changes to IFRS 3, 10, 11, 12 and 13 should wait until implementation experience has been assessed.

SMEIG discussion

Objective of the *IFRS for SMEs*

22. The SMEIG had a general discussion about the objective of the *IFRS for SMEs*. The majority of SMEIG members considered that the main focus of the Standard should be on the users of the financial statements. SMEIG members envisaged entities applying the *IFRS for SMEs* would be those with a limited or closed user

group and where the users are likely to be less distant from the entity. The SMEIG felt this is consistent with the current scope of the *IFRS for SMEs*, which is based on public accountability. A few SMEIG members felt that the Preface to the *IFRS for SMEs* should reflect the objective of the *IFRS for SMEs* more clearly.

23. In line with paragraph 22, the majority of SMEIG members felt the main focus when making changes to the *IFRS for SMEs* should be on the needs of the users of SME financial statements. Other factors such as the size of the entity, the complexity of its transactions and the resources available to it, are secondary factors to consider when making changes to the *IFRS for SMEs*.

24. A few SMEIG members noted that size and complexity of entities using the *IFRS for SMEs* would be self-regulating. For example, entities with a wider range of complex transactions may find that the *IFRS for SMEs* does not cater for their needs and so they would need to apply full IFRSs.

25. The broad view of the SMEIG was that the *IFRS for SMEs* should be maintained as a standalone standard catering for the specific requirements of SMEs. Based on this, the majority of SMEIG members felt that the main driver for changes to the *IFRS for SMEs* should be the implementation experience of SMEs. SMEIG members felt that small and medium sized practices (SMPs) would be the best source of knowledge on this implementation experience. The SMEIG also strongly supported having a stable platform for SMEs and not making frequent changes to the *IFRS for SMEs*.

Changes to full IFRSs

26. SMEIG members argued that changes to full IFRSs are made for good reason, that consistency in principles is desirable, and that entities and individual preparers and users may transition between the *IFRS for SMEs* and full IFRSs. Therefore, the broad view of the SMEIG was that all changes to full IFRSs should be considered individually and changes should be incorporated in the *IFRS for SMEs* if they would result in an improvement in financial reporting for SMEs.

27. To avoid unnecessarily increasing the reporting burden for SMEs, the SMEIG broadly felt minor amendments to full IFRSs to address unintended consequences, conflicts or oversights should only result in a change to the *IFRS for SMEs* where

there is a known problem for SMEs, ie that there should be a rebuttable presumption that changes should not be incorporated in the *IFRS for SMEs.*

Timing

28. The SMEIG generally felt that changes to full IFRSs should only be considered after the changes have been implemented under full IFRSs and are seen to be working well in practice. However it was generally agreed that the approach should be flexible to allow some changes to be adopted earlier if necessary.

29. The SMEIG agreed on the following approach:

    (a) A review of the *IFRS for SMEs* should take place approximately every three years. The timing could vary slightly, to coincide with changes to full IFRSs that are considered important for SMEs or to deal with urgent or time sensitive issues.

    (b) All changes to full IFRSs that are effective at the time of the review of the *IFRS for SMEs* should be considered for inclusion as part of that review. For example, it may be appropriate to incorporate some of the more principle-based or straight forward changes to full IFRSs as soon as they become effective under full IFRSs if they are considered relevant for SMEs and/or would help solve a known problem for SMEs.

    (c) However, most changes to full IFRSs, in particular those that are complex, would not be incorporated until implementation experience has been assessed (eg after the post-implementation review has been performed, where appropriate).

Changes to incorporate during this review

30. Based on the process set out in paragraph 29 the SMEIG recommended incorporating the 2011 revision to IAS 19 to require all actuarial gains and losses to be recognised in other comprehensive income in the period in which they arise. It was generally agreed that this change would be simple to implement. However, the SMEIG decided that changes in IFRS 3, 10, 11, 12 and 13 should not be considered until after the post-implementation reviews of those IFRSs had been carried out due to the complexity of these IFRSs. The SMEIG agreed that the staff

should look at the minor amendments to full IFRSs under the Annual Improvements project individually and adopt those that respond to a known problem for SMEs.