STAFF PAPER

May 2014

IASB Meeting

Project	**Comprehensive review of the *IFRS for SMEs***
Paper topic	Feedback from comment letters on the October 2013 ED

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Purpose of this paper

1. This agenda paper summarises the main feedback received from comment letters in response to ED/2013/9 *Proposed amendments to the IFRS for SMEs* (the ED) which was published for public comment in October 2013. The five month comment period ended on 3 March 2014.

2. This agenda paper does not include any staff recommendations. The staff will provide their recommendations, recommendations from the SME Implementation Group (SMEIG) and more detailed feedback from comment letters as the IASB discusses each issue during the redeliberations process.

Structure of this paper

3. This agenda paper is set out as follows:

   (a) Respondents by type and geography

   (b) User outreach

   (c) Method of summarising responses

   (d) Overall feedback and main issues raised by respondents

(e) Responses to individual questions in the Invitation to Comment:

   (i) Definition of 'fiduciary capacity' (Question 1)

   (ii) Accounting for income tax (Questions 2)

   (iii) Other proposed amendments to the *IFRS for SMEs* (Question 3)

   (iv) Other issues raised by respondents (Question 4 and 8)

      1. Specific requirements in the *IFRS for SMEs*
      2. Scope
      3. Alignment with full IFRSs
      4. Accounting policy options
      5. Other general issues

   (v) Transition and effective date (Questions 5-6)

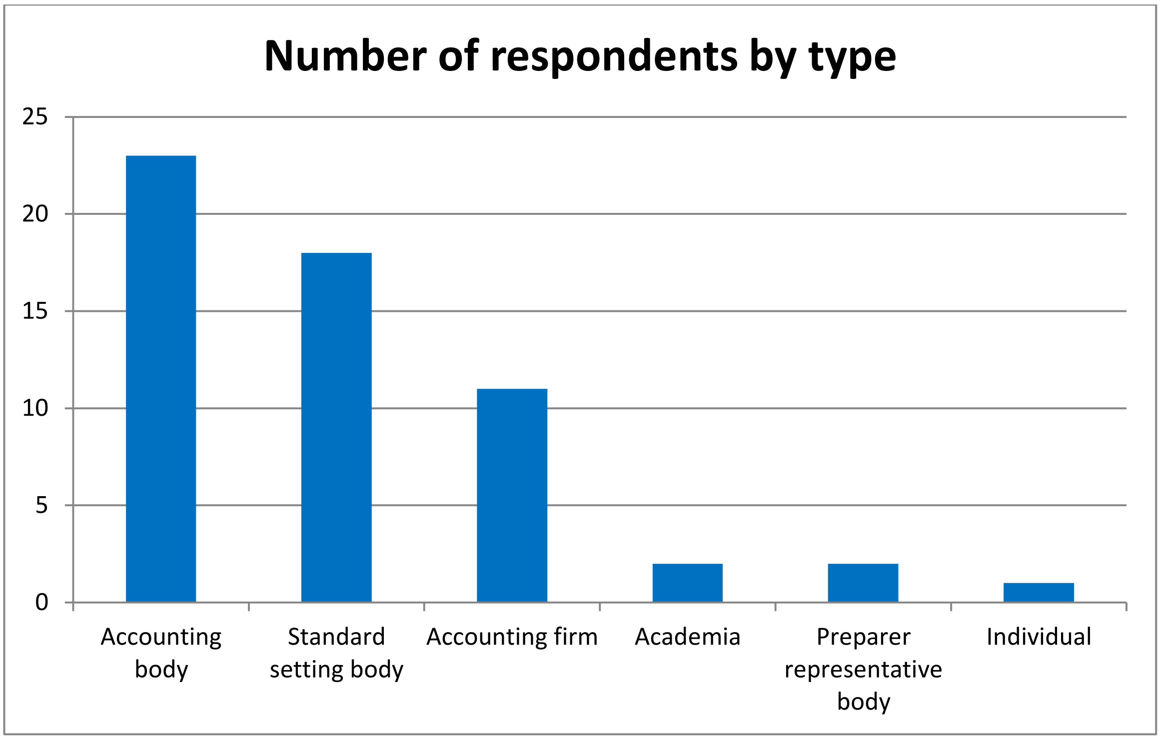
   (vi) Future reviews of the *IFRS for SMEs* (Question 7)

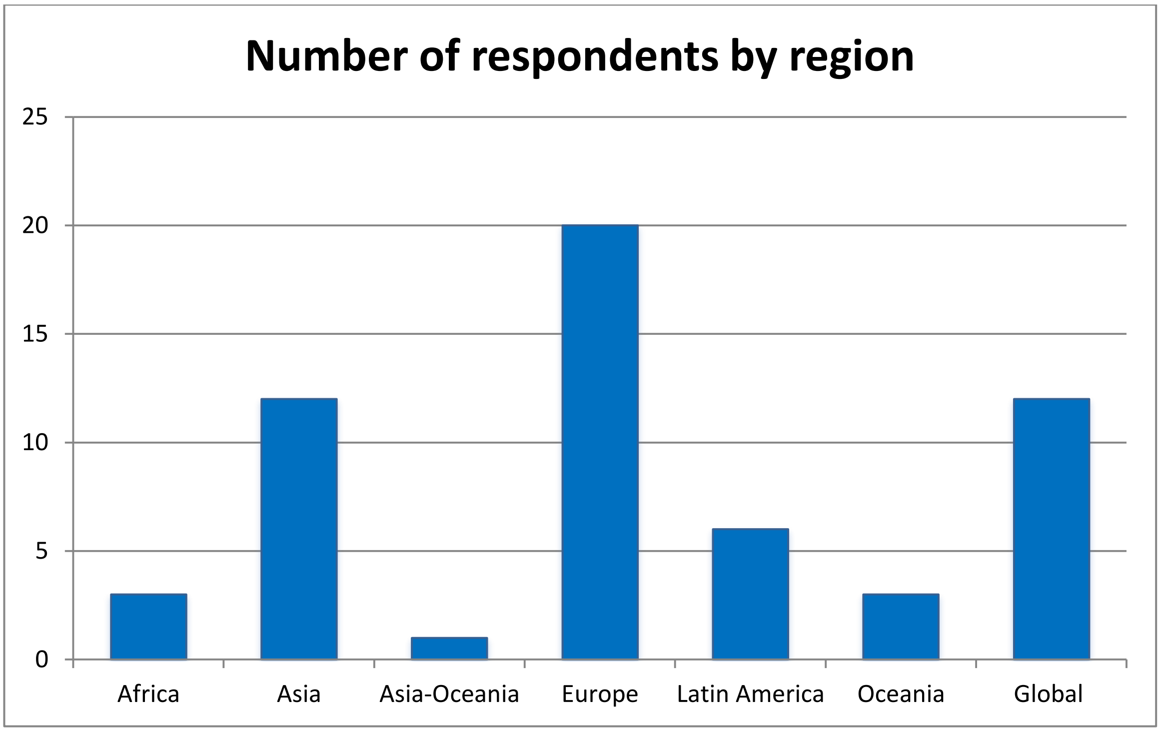
   (vii) Appendix A: Extracts from the comment letter analysis on the RfI–comments on accounting policy option

Respondents by type and geography

4. The IASB received 57 comment letters on the ED. 14 letters came from jurisdictions that currently permit or require some entities to use the *IFRS for SMEs* (this count excludes global firms). The 57 letters are summarised below by type of respondent and geographic region.

	Africa	Asia	Asia-Oceania	Europe	Latin America	Oceania	Global	Analysis by type
Accounting body	3	6		8	3	1	2	**23**
Standard setting body		6	1	7	3	1		**18**
Accounting firm				2			9	**11**
Academia				1		1		**2**
Preparer representative body				1			1	**2**
Individual				1				**1**
Analysis by region	**3**	**12**	**1**	**20**	**6**	**3**	**12**	**57**


Number of respondents by type
25
20
15
10
5
0
Accounting body
Standard setting body
Accounting firm
Academia
Preparer representative body
Individual


Number of respondents by region
25
20
15
10
5
0
Africa
Asia
Asia-Oceania
Europe
Latin America
Oceania
Global

User outreach

5. Consistent with other outreach on the *IFRS for SMEs*, the vast majority of respondents were accounting organisations, ie standard setters, accounting firms or accounting bodies, with very limited direct participation from preparers themselves. Furthermore, the IASB did not receive any direct responses to the ED from investors, analysts, providers of credit to SMEs or other users of SME financial statements. This in part reflects the relatively limited capacity and resources in both preparer and user organisations that operate within the SME space. Many of the accounting organisations responding to the ED have SME clients and so some feedback from SME preparers has been incorporated in their comment letters. To obtain further feedback from users of SME financial statements the staff is currently performing additional user outreach and this will be presented at a future IASB meeting.

Method of summarising responses

6. The intention of the staff in this agenda paper is to provide a summary of the main comments raised. At a minimum the staff have included those raised by more than two respondents. In addition, the staff have also highlighted some comments raised by only one or two respondents because of the nature of the comment. Staff will provide more detailed feedback from comment letters during the IASB redeliberation process where appropriate.

7. Many respondents provided suggestions for redrafting certain proposed amendments or raised areas where additional guidance would be helpful. Such suggestions are only included in this agenda paper where they are considered to be substantive. However, all suggestions will be considered either for inclusion in future IASB agenda papers when the relevant issues are discussed, or during drafting of the final amendments to the *IFRS for SMEs*.

8. The staff have highlighted geographical trends in the responses given by respondents when the staff think these trends are useful in understanding the

views expressed. A distinction by type of respondent has generally not been provided because most respondents were accounting organisations.

Overall feedback and main issues raised by respondents

9. Most respondents supported the majority of the changes proposed in the ED. The following is a summary of the main issues raised by respondents. The rest of this agenda paper expands on this summary:

    (a) The most common concern raised was the decision of the IASB not to propose accounting policy options for revaluation of property, plant and equipment (PPE) and capitalisation of development/borrowing costs.

    (b) Most respondents commented on the IASB's proposed approach for dealing with new and revised IFRSs. The following were the main issues raised (respondents generally only raised one or two of the following points):

        (i) The criteria for assessing changes to full IFRSs should be expanded and improved.

        (ii) Changes to the *IFRS for SMEs* should not be introduced until sufficient implementation experience exists under full IFRSs.

        (iii) The simplifications under IAS 19 (2011) *Employee Benefits* should be incorporated during this review.

        (iv) The *IFRS for SMEs* should be more closely aligned with full IFRSs.

    (c) Many respondents commented on the scope of the *IFRS for SMEs*. The following were the main views expressed:

        (i) The scope should not be restricted to non-publicly accountable entities.

        (ii) There is a disparity between the scope (all non-publicly accountable entities) and the primary aim of the IASB in developing the *IFRS for SMEs* in paragraph BC29 of the

ED, which is seen to be a focus on smaller/less complex non-publicly accountable entities.

(iii) Better identify the needs of users of SME financial statements.

(iv) The *IFRS for SMEs* is still too complex for small owner managed entities.

(v) Credit unions should be excluded from the definition of ‘publicly accountable’.

(d) Most respondents supported aligning Section 29 *Income Tax* with IAS 12 *Income Taxes*. However, about half of these respondents also suggested simplifications or other modifications to the proposals in Section 29.

(e) Few respondents commented on many of the other proposed amendments. The following were the main proposed amendments that respondents commented on in their order of significance:

(i) Application of ‘undue cost or effort’.

(ii) Definition of basic financial instruments.

(iii) Requirements for estimating the useful life of goodwill/other intangible assets.

(iv) Exemption from requirements for offsetting income tax assets and liabilities.

(v) Consolidation of group entities with different reporting dates.

(vi) Use of ‘undue cost or effort’ exemption in a business combination.

(vii) Accounting for extractive activities.

(viii) Grouping items in other comprehensive income (OCI).

10. Most respondents supported the proposals in the ED for the transition provisions and effective date. However, a significant minority thought that there should be relief from full retrospective application for some or all the proposed amendments, in particular for proposed changes to Section 29.

11. There was a lack of clarity amongst respondents as to what the IASB means by a three-year cycle for future reviews of the *IFRS for SMEs*. However, of those who expressed a clear view, approximately half of respondents support the three-year cycle whilst the rest support a longer cycle.

Responses to individual questions in the Invitation to Comment

Definition of 'fiduciary capacity' (Question 1)

Introduction

12. The *IFRS for SMEs* is intended for entities that do not have public accountability. An entity is considered to have public accountability if its debt or equity instruments are traded, or in the process of being issued for trading, in a public market, or it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses (paragraph 1.3 of the *IFRS for SMEs*)

13. Since issuing the *IFRS for SMEs*, the IASB has received feedback from interested parties that the meaning of 'fiduciary capacity' in the definition of 'public accountability' is unclear as it is a term with different implications across jurisdictions. However, those interested parties generally did not provide examples or suggest alternative wording/guidance. Therefore the IASB asked a question in the ED asking respondents if they are aware of circumstances where the term has created uncertainty or diversity in practice and whether the term needs to be clarified or replaced.

Feedback

14. A substantial majority of respondents who commented on Question 1 said there is no need to clarify or replace the term 'fiduciary capacity'. Furthermore, no respondents provided examples of where the term had resulted in diversity in practice. However, a few respondents noted that the term had created uncertainty on implementation of the Standard in their jurisdictions. The following examples were given where respondents were uncertain if the entities should be considered

to hold assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses:

(a) All banks and building societies (respondents in the UK).

(b) Pension schemes (UK).

(c) Entities in the transport sector (road and air) that manage resources for a large group of people (Brazil)

15. Some standard setting and accountancy bodies in the UK and Australia noted that because of their concerns that the term ‘fiduciary capacity’ would not capture the entities it was intended for, eg some banks, the concept of public accountability was not used when setting the scope of their local Standards.

16. The three most common suggestions made for how the IASB should deal with the uncertainty caused by the term ‘fiduciary capacity’ were:

(a) The IASB should add a definition of fiduciary capacity to the Glossary of the *IFRS for SMEs*. The IASB should also be mindful of how the definition would translate into other languages.

(b) The meaning of 'fiduciary capacity' is a legal concept and should be left to each jurisdiction to provide additional guidance on its interpretation in that jurisdiction. Local legislative and regulatory authorities, and standard setters, in individual jurisdictions are best placed to decide which entities should be permitted to use the *IFRS for SMEs*.

(c) The IASB should provide further guidance. The following points summarise the main suggestions:

(i) Add examples to illustrate the term ‘fiduciary capacity’. Some respondents noted that there are examples in the training material developed by the IFRS Foundation Education Initiative and suggested the IASB could make reference to that training material in, for example, the Preface to the *IFRS for SMEs*.

(ii) State the factors management need to consider in establishing if an entity's fiduciary activities are incidental to its primary business. The rationale behind the examples in paragraph 1.4 of the ED should be explained.

Accounting for income tax (Question 2)

Introduction

17. When the *IFRS for SMEs* was issued in 2009, Section 29 was based on the IASB's Exposure Draft *Income Tax* (the '2009 ED'), which was issued in March 2009. However, the 2009 ED was never finalised by the IASB. Consequently, the ED proposed to align the main recognition and measurement principles of Section 29 with IAS 12 for deferred tax.

Feedback on overall approach for income tax

18. A substantial majority of respondents who commented on Question 2 supported aligning the main recognition and measurement principles in Section 29 with IAS 12. However, about half of these respondents noted that the proposals in the ED were too complex for SMEs and users of their financial statements and/or suggested modifications. Some of these respondents said that an SME should be permitted to apply the taxes payable approach with disclosures if it is unable to apply the requirements in Section 29 without undue cost or effort. Other respondents suggested the IASB conduct further outreach to see if SMEs would be better served and users not significantly affected by allowing an 'undue cost or effort' exemption for some or all requirements and to get feedback on a suitable fallback solution if that exemption is used.

19. A few respondents had suggestions for simplifying the presentation and disclosure requirements in Section 29.

    (a) The requirement for tax consequences of transactions to be attributed to discontinued operations, OCI or equity is often complex. Consider requiring all tax effects to be recorded as part of a single tax charge in the income statement.

(b) Australian respondents suggested consideration of the approach adopted by the Australian Accounting Standards Board (AASB) in modifying the disclosure requirements of AASB 112 *Income Taxes*, in their Reduced Disclosure Requirements. The reductions cover deferred tax disclosures about subsidiaries, joint ventures, business combinations, discontinued operations and dividends.

20. Some respondents who commented on Question 2 did not support aligning the main recognition and measurement principles in Section 29 with IAS 12. The following points summarise the main suggestions made by these respondents:

(a) Permit or require a taxes payable approach with disclosures.

(b) The original Section 29 is well understood in practice and should not be changed.

(c) UK respondents suggested consideration of the approach in the UK Standard FRS 102, which is based on the *IFRS for SMEs*, but provides a ‘timing difference plus’ approach for accounting for deferred tax.

Feedback on specific requirements in Section 29

21. Most respondents were happy with the level of detail proposed in the ED. Some of these respondents commented that it was important to keep Section 29 compact and user-friendly, rather than add too much detail from IAS 12.

22. However a significant minority of respondents said Section 29 should incorporate more detail from IAS 12. The following are the main suggestions made by those respondents, with reasoning where given:

(a) Add the scope exclusion from IAS 12 for investment tax credits. These respondents believe that accounting for investment tax credits by analogy to either grants or income taxes depending on the specific facts and circumstances provides more relevant information.

(b) Add the guidance from IAS 12.30 on tax planning opportunities.

(c) Include all of the criteria in IAS 12.36 for assessing the probability that taxable profit will be available against which unused tax losses or credits can be utilised (Section 29 only has some of the criteria). These respondents argued that not including the criterion in IAS 12.36(c) requiring entities to consider whether tax losses result from identifiable causes which are unlikely to recur increases the threshold for recognising deferred tax assets, making Section 29 more restrictive than IAS 12.

(d) Add the requirement in IAS 12.51C that the presumption that the carrying amount of investment property will be recovered through sale is rebutted if the property is depreciable and held within a business model that will consume substantially all of the economic benefits of the investment over time. These respondents said that this would provide more accurate information to users of the financial statements.

(e) Include the requirements in IAS 12.68A-68C specifying the excess of the tax deduction over the related share based payment expense must be recognised in equity to prevent diversity in practice. These respondents noted SMEs may otherwise recognise the excess in profit or loss or OCI.

(f) Add disclosure in IAS 12.82 of the amount of a deferred tax asset and the nature of the evidence supporting its recognition under certain circumstances. These respondents noted that such information would be readily available and useful to users of SME financial statements.

23. A few respondents raised specific comments:

(a) Section 29 should specify that current tax assets and liabilities that include a financing transaction should be recognised on a discounted basis.

(b) Brazilian respondents requested guidance for jurisdictions where income tax is based on revenue, rather than taxable profit.

24. Some respondents recommended including a list of simplifications and other differences from IAS 12 in the Basis for Conclusions issued with the final amendments.

25. Comments on the 'undue cost or effort' exemption for offsetting income tax assets and liabilities are dealt with under Question 3 below.

Other proposed amendments to the *IFRS for SMEs* (Question 3)

Introduction

26. There are 57 proposed amendments to the *IFRS for SMEs*. These are listed on pages 6-12 of the ED. The proposed alignment of Section 29 with IAS 12, is covered by Question 2 above. Of the remaining issues, the main issues raised by respondents are addressed below in their order of significance, based on a consideration both of the number of respondents raising the same issue and the geographical diversity of those respondents.

General feedback

27. Respondents were only asked to comment on those proposed amendments on which they had concerns. Most respondents either raised no issues in response to Question 3 or only commented on a few of the proposed amendments. No more than 10 respondents commented on any particular proposed amendment.

Application of 'undue cost or effort' (Proposed Amendment 3)

28. The ED proposed additional guidance on the 'undue cost or effort' exemption based on SMEIG Q&A 2012/01 *Application of 'undue cost or effort'*. (see paragraphs 2.14A–2.14C of the ED)

29. The feedback below also covers any general comments about 'undue cost or effort' that respondents raised on proposed amendments 12, 17, 25 and 45, which each propose specific 'undue cost or effort' exemptions.

30. Most respondents who commented supported the additional guidance but said that it was not sufficient on its own. The following points summarise the two most common concerns:

(a) The IASB should provide more guidance to prevent diversity in how the exemption is applied in practice. Some respondents asserted it is likely to be viewed as a low hurdle, almost to the extent of creating a de facto accounting policy option.

(b) An entity should be required to disclose when it has used an ‘undue cost or effort’ exemption and also disclose its reasoning for doing so. Some respondents asserted disclosure would help to control the use of the exemption and would provide useful information for users at little cost to SMEs.

31. The following are the main suggestions provided by the respondents in paragraph 30(a) for further guidance:

(a) Clearly explain the difference between 'undue cost or effort' and 'impracticable' and how the terms interact with each other. Some respondents noted that Q&A 2012/01 has guidance on this that was not included in the ED.

(b) Include a definition of ‘undue cost or effort’ in the Glossary.

(c) Clarify interaction with ‘materiality’.

(d) Include a detailed illustration of the application of ‘undue cost or effort’ in a relevant context.

32. Other suggestions included:

(a) Limit the use of ‘undue cost or effort’ exemptions. If the IASB thinks a requirement in the *IFRS for SMEs* will commonly lead to SMEs incurring costs that exceed the benefits to users of their financial statements it would be preferable to select a different accounting treatment.

(b) Extend the ‘undue cost or effort’ exemption to all requirements in the *IFRS for SMEs*. These respondents noted that the balance between benefit and cost is a qualitative characteristic of information in financial statements in Section 2 *Concepts and Pervasive Principles* of the *IFRS for SMEs*.

Definition of basic financial instruments (Proposed Amendment 14)

33. The ED clarified that foreign currency loans and loans with standard loan covenants will usually be basic financial instruments (see paragraphs 11.9(a) and (c) of the ED).

34. Respondents were predominantly either based in the UK or were global accounting firms. These respondents raised concerns that the *IFRS for SMEs* was more onerous than full IFRSs for the measurement of certain 'basic' debt instruments. They asserted that certain financial instruments that would be measured at fair value through profit or loss in accordance with Section 12 *Other Financial Instrument Issues* (because they do not meet the criteria under paragraph 11.9) would be measured at amortised cost under IFRS 9 *Financial Instruments*. Debt instruments with features such as interest rate caps or floors, stepped interest rates or certain prepayment provisions were given as examples.

35. Some of these respondents suggested that the IASB should reconsider paragraph 11.9 in its entirety to ensure that the *IFRS for SMEs* is not more onerous than full IFRS in this area. Some respondents also said that paragraph 11.9 was difficult to understand and the IASB should try and simplify the wording. Other respondents said that the IASB should consider the outcome of the ED issued by the UK Financial Reporting Council (FRC), which proposed to amend paragraph 11.9 in FRS 102, the UK Standard based on the *IFRS for SMEs*, to address this issue.

Useful life of goodwill/other intangible assets (Proposed Amendments 21 and 26)

36. The ED proposed that an entity that is unable to make a reliable estimate of the useful life of goodwill/another intangible asset should be required to use a useful life that does not exceed 10 years. Previously an entity was required to use a fixed life of 10 years if it could not make a reliable estimate (see paragraphs 18.20, 19.23 and 19.26 of the ED).

37. Respondents generally had concerns about permitting management to use its judgement to determine a useful life when a reliable estimate was not possible. Concerns of respondents included a reduction in comparability between entities,

how to verify/audit the best estimate and whether an unreliable estimate provides useful information to users of financial statements.

Offsetting income tax assets and liabilities (Proposed Amendment 45)

38. The ED proposed addition of an 'undue cost or effort' exemption to the requirement to offset income tax assets and liabilities (see paragraph 29.29 of the ED).

39. Respondents said that an entity should be required to offset deferred tax assets and liabilities if they are related to income taxes levied by the same taxation authority on the same taxable entity (a requirement from IAS 12.74(b)(i)). Other respondents said the wording "it is evident without undue cost or effort that it intends" is unclear and should be clarified. Some of these respondents said that the full wording in IAS 12.71 and 12.74 should be used instead.

Group entities with different reporting dates (Proposed Amendment 9)

40. The ED proposed additional guidance on how to prepare consolidated financial statements if group entities have different reporting dates (see paragraph 9.16 of the ED).

41. Respondents thought the additional guidance was helpful. However they were generally concerned that permitting a parent entity to use the subsidiary's most recent financial statements allowed too much flexibility. Some respondents asserted that the ED would permit the financial statements of the subsidiary to be from a previous year or even from several years ago. These respondents commented that if the difference between the reporting date of the subsidiary and the parent was too great, it would not provide relevant, comparable information for users of the parent's consolidated financial statements.

42. Some respondents recommended that the requirement in Paragraph B93 of IFRS 10 *Consolidated Financial Statements* should be added to paragraph 9.16— it would require the difference to be no more than three months and be consistent

each period. Other respondents agreed, but suggested a greater difference than three months be allowed.

Use of 'undue cost or effort' exemption in a business combination (Proposed Amendment 25)

43. The ED proposed addition of an 'undue cost or effort' exemption to the requirement to recognise intangible assets separately in a business combination (see paragraph 19.15 of the ED).

44. Respondents did not raise concerns with this amendment, but noted that identification of contingent liabilities in a business combination is also challenging and said that the exemption should be extended to contingent liabilities.

Accounting for extractive activities (Proposed Amendment 49)

45. The ED proposed clarification of the accounting requirements for extractive activities (see paragraphs 34.11–34.11A of the ED).

46. Most respondents asserted that the proposed requirements were more onerous than the related requirements in full IFRSs. These respondents noted that paragraph 7 of IFRS 6 *Exploration for and Evaluation of Mineral Resources* exempts an entity under full IFRSs from paragraphs 11-12 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* when developing accounting policies for the recognition and measurement of exploration and evaluation assets. These respondents observed that paragraph 34.11 of the ED would require an entity to determine an accounting policy in accordance with the accounting policy hierarchy in paragraphs 10.4-10.6 of the *IFRS for SMEs,* which would require an entity to consider the concepts and principles in Section 2. Respondents suggested providing a similar exemption to full IFRSs in paragraph 34.11.

47. A few respondents said specific guidance should be provided for accounting for impairment of exploration and evaluation assets, rather than requiring entities to follow the general requirements in Section 27 *Impairment of Assets*. Respondents

asserted that developing specific guidance for impairment of exploration and evaluation assets was an important issue in IFRS 6.

Grouping items in OCI (Proposed Amendment 6)

48. The ED proposed incorporating the main change under IAS 1 (2011 amendment) *Presentation of Items of Other Comprehensive Income*, which requires entities to group items presented in OCI on the basis of whether they are potentially reclassifiable to profit or loss (see paragraph 5.5(g) of the ED).

49. Respondents generally did not think the change was useful for users of SME financial statements, given the limited circumstances where it would be applicable. The *IFRS for SMEs* only has one item of OCI for which recycling is required, ie changes in fair value of hedging instruments in a cash flow hedge.

50. Some respondents noted that the IASB had decided not to reconsider use of OCI during this comprehensive review and had also decided not to require actuarial gains and losses to be presented in OCI (see paragraphs BC34(b) and BC86(b) in the ED). These respondents noted that the IASB's main reasoning for this was because it is considering the treatment of OCI as part of its *Conceptual Framework* project, which may result in changes to the requirements for OCI under full IFRSs. These respondents asserted if other changes affecting OCI were not made during this review, it was inconsistent for the ED to propose this change.

Cumulative exchange differences on disposal of a subsidiary (Proposed Amendment 10)

51. The ED proposed to clarify that no cumulative exchange differences from the translation of a foreign subsidiary are recognised in profit or loss on disposal of the subsidiary (see paragraph 9.18 of the ED)

52. Respondents said cumulative exchange differences from the translation of a foreign subsidiary should be recognised in profit or loss on disposal of a subsidiary, consistent with full IFRSs. These respondents said that this was not a complex area and so there was no reason to diverge from full IFRSs. Other respondents noted that if there is no requirement to recycle the exchange gains to

profit or loss on disposal of a subsidiary, an SME should be permitted to recognise those exchange differences in retained earnings either immediately or on disposal otherwise they will remain as a separate component of equity forever.

Disclosure of policy for termination benefits (Proposed Amendment 43)

53. The ED proposed the removal of the requirement to disclose the accounting policy for termination benefits (see paragraph 28.43 of the ED).

54. Respondents disagreed with the IASB's reasoning for removing the disclosure requirement— namely because entities do not have a choice of treatment for termination benefits. These respondents said that an entity should disclose all accounting policies for which disclosure is relevant to an understanding of the financial statements.

Subsidiaries acquired and held for sale (Proposed Amendment 8)

55. The ED proposed to clarify that all subsidiaries acquired with the intention of sale or disposal within one year should be excluded from consolidation (see paragraphs 9.3–9.3A of the ED).

56. Respondents were concerned that the requirements were unclear on:
    (a) whether the time frame of one year begins from the date of acquisition or from the reporting date; and
    (b) how to account for the subsidiary if the parent changes its intentions or if the subsidiary is otherwise not sold or disposed of within one year.

57. A few respondents proposed a requirement to disclosure unconsolidated subsidiaries.

Distribution of non-cash assets (Proposed Amendment 34)

58. The ED proposed to add guidance on accounting for a distribution of non-cash assets (see paragraph 22.18 of the ED).

59. Respondents had concerns that requiring the liability to be measured at the fair value of the assets distributed added unnecessary complexity (note, this requirement was already in paragraph 22.18). Respondents either suggested the IASB remained silent or added an 'undue cost or effort' exemption from fair value measurement.

Best evidence of fair value (Proposed Amendment 15)

60. The ED proposed to clarify in the guidance on fair value measurement that the best evidence of fair value may be a price in a binding sale agreement (see paragraph 11.27 of the ED).

61. Respondents said the term 'binding sale agreement' needed to be explained, eg by providing an indication of how recently the binding sale agreement was made and whether it would be considered if there was a quoted price for an identical asset in an active market.

Classification of spare parts (Proposed Amendment 20)

62. The ED proposed to incorporate *Classification of servicing equipment* (IAS 16) from *Annual Improvements 2009–2011 Cycle*, issued in May 2012, which clarifies the classification of spare parts, stand-by equipment and servicing equipment as PPE or inventory (see paragraph 17.5 of the ED).

63. Respondents asserted that the cost and effort of monitoring and tracking the individual spare parts, stand-by equipment and servicing equipment as either PPE or inventory would not justify the benefits to users. Respondents also noted that the requirements are unlikely to apply to the majority of SMEs.

Other issues raised by respondents (Question 4 and 8)

Specific issues on requirements in the IFRS for SMEs

64. The following points summarise the comments made by respondents about specific requirements in the *IFRS for SMEs* not covered by the proposed

amendments in the ED. Each of these suggestions was made by only a few respondents:

(a) **The title of the *IFRS for SMEs*** should be changed to focus on the entities within its scope.

(b) **OCI should be removed from the *IFRS for SMEs*** because instances where items are presented in OCI are limited.

(c) **There should be an option to use the equity method** to measure investments in associates, joint ventures and subsidiaries in the separate financial statements of the investor, similar to that considered in the IASB's proposed changes to IAS 27 *Consolidated and Separate Financial Statements*. (Respondents from Latin America)

(d) **Fall-back to IFRSs for financial instruments**. Some respondents said SMEs should be permitted to use the recognition and measurement requirements of IFRS 9 when it has been completed. However other respondents said the fallback to IFRSs should be removed completely and the *IFRS for SMEs* should be a self-contained Standard. Other respondents said if the fallback to IAS 39 *Financial Instruments: Recognition and Measurement* remained, it would be important to clarify which version of IAS 39 is being referred to.

(e) **Clarify meaning of 'transaction price'** for initial recognition of financial instruments. Some SMEs have off-market interest-based arrangements with related parties, eg staff loans at less than market rates. Some respondents asserted that there is diversity in practice across countries and some SMEs are interpreting 'transaction price' as the price of the transaction rather than fair value of the financial instrument.

(f) **Guidance on fair value measurements** should be moved into a separate section to make it more accessible and clarify that the guidance applies both to financial instruments and to non-financial items.

(g) **Hedging requirements** are more restrictive than full IFRSs following the release of the new hedging requirements in IFRS 9. Allow more situations in which hedge accounting can be used, consistent with IFRS 9. This will allow SMEs to apply hedge accounting when it reflects their risk management strategies, without onerous conditions. Some respondents said that the IASB should consider the outcome of the ED issued by the UK FRC, which proposed to amend Section 12 in FRS 102 to incorporate requirements based on IFRS 9.

(h) **Accounting for investment property** should allow a choice between the fair value model and cost model like full IFRSs. This would be easier to apply than the 'undue cost or effort' exemption, and avoid confusion for users of the financial statements of potentially having some investment property measured under the fair value model and some measured under the cost model.

(i) **Presentation of investment property** in the statement of financial position should be determined by the nature of the asset, not its measurement basis. Investment property should be presented as investment property, not PPE, regardless of whether it is measured under the cost model or the fair value model

(j) **Accounting for components of PPE** is complex. Respondents suggested either simplifying the accounting or providing further education material. Some respondents suggested allowing SMEs to derecognise component parts at their replacement cost when it is not practicable to determine the carrying amount, a simplification in paragraph 70 of IAS 16 *Property, Plant and Equipment*.

(k) **Share subscription receivables** should be presented as an asset when certain criteria are met.

(l) **Accounting for biological assets** should allow a choice to use the cost model. This is a complex area that requires use of significant judgement.

General issues about the IFRS for SMEs

Scope

Introduction

65. The *IFRS for SMEs* is intended for use by entities that do not have public accountability.

66. Publicly accountable entities are not permitted to state compliance with the *IFRS for SMEs* (paragraph 1.5 of the *IFRS for SMEs*).

67. The June 2012 Request for Information (RfI) asked whether publicly accountable entities should be permitted to apply the *IFRS for SMEs*. The IASB considered the responses to the RfI, and decided not to propose changes to the scope of the *IFRS for SMEs* or to paragraph 1.5. The IASB's reasoning is in paragraphs BC16-BC22 of the ED.

68. Furthermore, the IASB clarified that its primary aim when developing the *IFRS for SMEs* was to provide a standalone, simplified set of accounting principles for entities that do not have public accountability and that typically have less complex transactions, limited resources to apply full IFRSs and that operate in circumstances in which comparability with their publicly accountable peers is not an important consideration (BC29 of the ED).

Feedback

69. Although the ED did not ask a question on the overall scope of the *IFRS for SMEs*, a significant minority of respondents had comments, most of which they had also raised on the RfI. The following is a summary of the main issues raised by respondents:

    (a) **Do not restrict the scope**. Legislative and regulatory authorities and standard-setters in individual jurisdictions are in the best position to decide which entities should be required or permitted to use the *IFRS for SMEs*. Remove paragraph 1.5 that prohibits publicly accountable entities from stating compliance with the *IFRS for SMEs*.

(b) **Concern about the focus on smaller SMEs**. There is a discrepancy between the stated scope 'entities that do not have public accountability' and the IASB's primary aim when developing the *IFRS for SMEs* in paragraph BC29 of the ED (see paragraph 68). If the IASB focuses only on SMEs at the 'smaller' end of the scope of the *IFRS for SMEs*, the reporting needs of many non-publicly accountable entities will not be effectively addressed. Consequently, the IASB may be limiting the ability of jurisdictions to adopt the *IFRS for SMEs*, in particular those with more advanced financial reporting and regulatory frameworks and where large and complex entities fall in the scope.

(c) **Better identify the needs of users of SME financial statements**. The objective of financial statements in paragraph 2.2 of the *IFRS for SMEs* describes users and their needs in a very similar way to full IFRSs. Consequently, it is hard to understand the conceptual basis for differences from full IFRSs. The IASB should more clearly describe the underlying assumptions for developing the *IFRS for SMEs* in the context of preparers and users. This should include explaining why the *IFRS for SMEs* is not suitable for publicly accountable entities. If cost-benefit is a major driver of the difference from full IFRSs, public accountability is not an appropriate criterion.

(d) ***IFRS for SMEs* is still too complex**. Many entities without public accountability are small owner managed entities. (Respondents from Asia)

(e) **Exclude credit unions from the definition of 'publicly accountable'**. Some credit unions, especially smaller institutions and those in developing countries, should be able to state conformity with the *IFRS for SMEs* to limit excessive compliance burdens. Adherence to an international Standard like the *IFRS for SMEs*, scaled to the small size and limited complexity of these financial institutions, has the potential to improve significantly the usefulness of financial reports.

Alignment with full IFRSs

Introduction

70. The *IFRS for SMEs* was developed using full IFRSs as a starting point and considering what modifications are appropriate in the light of users' needs and cost-benefits. Consequently, one of the most significant issues during this comprehensive review was whether the *IFRS for SMEs* should be updated for new and revised IFRSs published since the *IFRS for SMEs* was issued in 2009.

71. The RfI included questions on the five new or revised IFRSs that had the potential to result in the most significant changes to the *IFRS for SMEs*, namely IFRS 3 (2008) *Business Combinations*, IFRS 10, IFRS 11 *Joint Arrangements*, IFRS 13 *Fair Value Measurement* and IAS 19 (2011). On the basis of the IASB's redeliberations, considering the comments received on the RfI and the primary aim of the *IFRS for SMEs* (see paragraph 68), the IASB decided not to propose to incorporate IFRS 3 (2008), 10, 11 and 13, and IAS 19 (2011). The IASB also developed the following principles for dealing with new and revised IFRSs when developing the ED and during future reviews of the *IFRS for SMEs*:

    (a) Each new and revised IFRS, including annual improvements, should be considered individually on a case-by-case basis.

    (b) New and revised IFRSs should not be considered until they have been published. However, it would generally not be necessary to wait until their Post-implementation Reviews (PIRs) have been completed.

    (c) Changes to the *IFRS for SMEs* could be considered at the same time that new and revised IFRSs are published. However, the *IFRS for SMEs* would only be updated for those changes at the next three-yearly review to provide a stable platform for SMEs.

    See paragraphs BC27-BC38 of the ED for the IASB's full reasoning of how it considered new and revised IFRSs.

72. Because the RfI had previously solicited feedback about the main changes to full IFRSs since 2009, the ED only asked for feedback where changes resulting from new and revised IFRSs were proposed in the ED (see Question 3 above).

Feedback

73. Most respondents to the ED had general comments on the IASB's approach for dealing with new and revised IFRSs. The following is a summary of the main issues raised by respondents:

(a) **Establish better criteria for assessing changes to full IFRSs**. Some respondents said the IASB should establish a formal framework or clearer principles to determine whether and when changes to full IFRSs should be incorporated in the *IFRS for SMEs*. Respondents asserted that if a clear framework is established, changes can be better evaluated. These respondents noted that the principles developed by the IASB are not clear enough to achieve this. Some respondents provided suggestions to replace those principles. Some respondents said it was not clear why the IASB was proposing to include some but not other new and revised IFRSs during this review. Examples given:

(i) Some changes to full IFRSs that would improve or simplify requirements in the *IFRS for SMEs* have not been incorporated (eg the basis of the calculation of net interest under IAS 19) while others of limited value have been (eg the recent amendments to IAS 1).

(ii) The proposed amendment to group items in OCI is inconsistent with the IASB's decision not to reconsider the use of OCI in the *IFRS for SMEs* (see paragraph 50).

(b) **Wait until sufficient implementation experience/PIRs complete**. Some respondents said the suitability of a significant new or revised IFRS should only be assessed once a track record of its application under full IFRSs has been established and interpretation issues have been resolved. Respondents asserted this would enhance stability and minimise changes to the *IFRS for SMEs*. Most of these respondents said this would generally be once a PIR has been completed.

(c) **Incorporate IAS 19 (2011).** Apart from those supporters of close alignment with full IFRSs (see paragraph (d) below), very few respondents had specific comments on the IASB's decision not to incorporate IFRS 3 (2008), 10, 11 and 13 during this comprehensive review. In contrast, many respondents said that the IASB should reconsider its decision not to incorporation the main changes under IAS 19 (2011). Respondents asserted that many of these changes would simplify the requirements in the *IFRS for SMEs* whist at the same time enhancing consistency with full IFRSs.

(d) **More closely align the recognition and measurement requirements with full IFRSs**. Some respondents said all recent changes to full IFRSs should be incorporated in the *IFRS for SMEs* at each three-yearly review of the *IFRS for SMEs*, subject to the principles underlying the *IFRS for SMEs* (ie cost-benefits and user needs). Consequently these respondents supported incorporation of changes under IFRS 3 (2008), 10, 11, 12 and 13 and IAS 19 (2011) during this comprehensive review. These respondents were concerned that delaying incorporation of changes to full IFRSs would result in too large a gap between the *IFRS for SMEs* and full IFRSs and that this would make the *IFRS for SMEs* less attractive to entities. Some respondents highlighted the importance of the IASB explaining clearly its reasoning in any areas where the IASB decides not to align *IFRS for SMEs* with full IFRSs.

Accounting policy options

Introduction

74. The June 2012 RfI asked whether SMEs should be permitted to use a revaluation model for PPE, and either permitted or required to capitalise borrowing and development costs meeting criteria similar to that in full IFRSs. The IASB considered the comments received on the RfI together with the IASB's original reason for excluding many accounting policy options from the *IFRS for SMEs* and decided not to propose any changes in the ED to incorporate these options. The IASB's reasoning is provided in paragraphs BC39-BC48 of the ED.

Feedback

75. Although the ED did not ask specific questions, a significant minority of respondents said that the IASB should reconsider its decision on accounting policy options. This was the most common concern raised by respondents to the ED. Most of these respondents asked the IASB to include an option for SMEs to revalue their PPE. However, a significant number also asked the IASB to permit SMEs to capitalise borrowing and or development costs meeting certain criteria. Nevertheless, a significant number of respondents agreed with the IASB's decision not to add additional complex accounting policies in the ED.

76. Respondents provided many different reasons for and against additional accounting policy choices. Many of these reasons were raised in response to the specific questions in the RfI, and were covered in the comment letter analysis on the RfI (relevant extracts are included in Appendix A to this paper). The staff have not repeated those comments in the body of this agenda paper. However, a few respondents raised further arguments, ie not raised on the RfI, and therefore not previously considered by the IASB. These are summarised in paragraphs 77-78 below.

77. Respondents in support of including accounting policy options noted that:

    (a) The requirements for accounting for deferred tax under Section 29 make the *IFRS for SMEs* more complex than would the inclusion of the additional accounting policy options. Furthermore, SMEs can always choose to apply the simpler option, whereas Section 29 is mandatory for all SMEs.

    (b) A Standard that does not allow these options is only suitable for very small entities and jurisdictions that do not have a well-established financial reporting background. If the IASB does not permit these options, jurisdictions will need to amend the *IFRS for SMEs* to meet their needs, reducing comparability between SMEs across borders.

78. Respondents who commented against including additional accounting policy options noted that:

(a) It is best to have a simple, core Standard that jurisdictions can either:

   (i) adopt in its current form— eg in jurisdictions where options would be an unnecessary complexity; or

   (ii) use as a starting point and add to it if they deem necessary. It is inevitable jurisdictions will make changes to the Standard to reflect issues specific to them. It would be impossible to cater for all of these jurisdictional requirements in a simple Standard.

(b) Adding options increases the complexity of the Standard and may dissuade small/less developed jurisdictions (which have the most to benefit from the *IFRS for SMEs*) from adopting it. In situations where those jurisdictions have adopted the Standard, it could lead them to revert to their previous local GAAP.

Other general issues

79. The following is a summary of the other general issues about the *IFRS for SMEs* raised by respondents. Each of these was only made by a small number of respondents:

(a) **SMEIG recommendations**. Some respondents expressed concern that some of the recommendations of the SMEIG were not accepted by the IASB. These respondents noted that the IASB should explain why it did not to follow that advice.

(b) **Glossary items**. Some respondents said the IASB should align definitions with full IFRSs. They said where this is not possible terms in the Glossary that are different from those in full IFRSs should be marked to avoid confusion. Some respondents noted that it is important for SMEs to identify these differences because some SMEs may refer to guidance in full IFRSs to help them apply the *IFRS for SMEs*. Some respondents said the IASB should not define terms in the *IFRS for SMEs* that are used but not defined in full IFRSs, eg 'substantively enacted', because this creates a risk entities may apply those definitions under full IFRSs.

(c) **Due process for Q&As**. Some respondents expressed concern that the due process is not sufficient for Q&As and is not consistent with other IFRS Foundation procedures. Some said the number of Q&As issued should be reduced or stopped completely. Some respondents said that the IFRS Interpretations Committee should be involved in the process. Other respondents requested that it be made clearer that Q&As are non-mandatory guidance. Some expressed concern that if non-mandatory Q&As are incorporated into the *IFRS for SMEs* during the three-yearly reviews, new Q&As might be considered de facto authoritative.

(d) **Size dependent relief**. Some respondents noted that the scope of *IFRS for SMEs* includes a wide range of companies, and note that it would be helpful if the *IFRS for SMEs* provided additional relief for smaller companies, in particular from disclosure requirements. Some respondents suggested either the IASB or national regulators/standard setters could define standardised size categories that would be permitted to use the relief.

(e) **Reduce the disclosure requirements**. Respondents noted that the full IFRSs disclosure project may present the opportunity for the IASB to consider disclosure refinements for the *IFRS for SMEs*.

Transition and effective date (Questions 5-6)

Transition provisions (Question 5)

Introduction

80. The ED proposed that the amendments to the *IFRS for SMEs* in Sections 2–34 should be applied retrospectively.

Feedback

81. A majority of respondents that commented on Question 5 supported the transition provisions without modification. Most of these respondents did not provide any further comments. The following points summarise the main comments made in support of the transition provisions:

(a) Retrospective application would not be a significant burden for SMEs because most of the proposed amendments are minor and are unlikely to have a significant impact on SME reporting.

(b) Retrospective application would provide the most comparable and useful information for users of the financial statements.

(c) Some respondents noted that they only supported retrospective application on the basis that the IASB had said that the proposed amendments would not be burdensome to implement. They noted if it turned out that this was not the case for any of the proposed amendments, prospective application should be permitted.

82. A significant minority of respondents that commented on Question 5 did not support the transition provisions. Approximately half of these disagreed because they thought that retrospective application of the proposed amendments to Section 29 *Income Taxes* would be burdensome —some observing that SMEs will need to consider the effect of each individual change to the requirements for recognising, measuring and disclosing deferred tax. Other respondents said that some of the other proposed amendments may also be costly to apply retrospectively and they did not think the benefits of restated information would justify incurring significant costs. The following points summarise the main suggestions made by respondents:

(a) Allow prospective application of the proposed amendments to Section 29 or of all proposed amendments.

(b) Allow an 'undue cost or effort' exemption from the retrospective application of individual proposed amendments.

(c) Allow prospective application of the proposed amendments but require note disclosure of the impact of the changes on the financial statements

(d) If a proposed amendment is based on a similar amendment to full IFRS that was applied prospectively, it should be applied prospectively by SMEs as well.

83. Approximately half of respondents in jurisdictions that have adopted the *IFRS for SMEs* said that full retrospective application of the proposed amendments would be too costly.

Effective date (Question 6)

Introduction

84. The ED proposed that the effective date of the amendments to the *IFRS for SMEs* should be one year after the final amendments are issued. The ED also proposed that early adoption of the amendments should be permitted.

Feedback

85. A substantial majority of respondents who commented on Question 6 supported the proposals without modification because the proposed amendments are minor and are unlikely to have a significant impact on SME reporting.

86. Some respondents said that the implementation time of one year was too short and suggested that a period of 18-24 months was more appropriate. The following points summarise the main comments made by these respondents:

(a) The effective date should be the beginning of the calendar year starting at least a year after the amendments are issued.

(b) SMEs need sufficient time to transition to any new requirements because of resource constraints.

(c) Additional time is required for jurisdictions which have to comply with local endorsement processes to provide sufficient implementation lead time to their SMEs (raised by two jurisdictions that currently apply the *IFRS for SMEs*).

Future reviews of the *IFRS for SMEs* (Question 7)

Introduction

87. When the *IFRS for SMEs* was issued in 2009 the IASB stated that after the initial comprehensive review, the IASB expects to propose amendments to the *IFRS for SMEs* by publishing an omnibus ED approximately once every three years. The IASB stated that it intended this three-year cycle to be a tentative plan, not a firm commitment. It also noted that, on occasion, it may identify a matter for which an amendment to the *IFRS for SMEs* may need to be considered earlier than in the normal three-year cycle; eg to address an urgent issue.

88. Since issue of the *IFRS for SMEs*, the IASB has received feedback that amendments once every three years (three-year cycle) may be too frequent and that a five-year cycle, with the ability for an urgent issue to be addressed earlier, may be more appropriate. Therefore the IASB asked a question in the ED asking respondents if they agreed with the current approach outlined in paragraph 87.

Feedback

89. A slight majority of respondents that commented on Question 7 supported keeping the three-year cycle. Other respondents generally suggested increasing the length of the cycle, with five years being the most common suggestion. However, it was clear from the responses to Question 7 that there were different interpretations as to what the IASB meant by a three-year cycle. Consequently, the staff think there was approximately an even split between respondents that would retain the three-year cycle and respondents that would extend it. For example some respondents thought that a three-year cycle meant that the next review will commence three years after the revised Standard is issued (ie 2018 if the revised Standard is issued in 2015)—this is likely to equate to an ED being issued every five years, or longer if a RfI is issued first. Paragraph P17 in the Preface to the *IFRS for SMEs* clarifies the IASB's intention and states "…the IASB expects to propose amendments to the *IFRS for SMEs* by publishing an omnibus exposure draft approximately once every three years".

90. The following points summarise the main comments made by respondents supporting retaining a three-year cycle:

(a) A three-year cycle strikes an appropriate balance between providing SMEs with a stable platform and the need for requirements in the *IFRS for SMEs* to be kept up to date

(b) A longer cycle would increase the risk of unwarranted inconsistencies between full IFRSs and the *IFRS for SMEs*.

(c) More experience in applying the *IFRS for SMEs* is required before moving to a longer review cycle.

(d) A longer cycle would lead to the need for more frequent 'urgent' amendments making application of the *IFRS for SMEs* more onerous than originally intended.

(e) A longer review cycle could lead to a longer list of amendments that SMEs would have to cope at the same time, which could add undue burden.

91. The following points summarise the main comments made by these respondents supporting increasing the length of the cycle:

(a) SMEs often have limited resources to deal with frequent changes to their accounting policies and systems and evaluate their impact.

(b) A longer cycle would provide the ability to leverage on implementation experience of entities applying full IFRSs before considering incorporating any new requirements.

(c) In practice a three-year cycle will lead to amendments once every five years, because of the due process for amendments—ie the time needed to solicit ideas, issue a discussion paper/RfI/ED, collate responses, issue a new version of the Standard, and allow sufficient implementation time before the changes are effective.

(d) A review that commences two years after the effective date of amendments from the previous review would allow the IASB to consider any implementation issues or unintended consequences that result from those amendments. This approach would be approximately five years (ie three years of lead time and a two year application period).

92. Some global accounting firms and European accounting organisations said that the IASB should develop a clear framework/criteria formalising a procedure for future reviews of the *IFRS for SMEs* to enhance transparency of the review process. They suggested this should cover whether/when changes to full IFRSs should be incorporated (see also paragraph 73(a)), whether and to what extent to allow options from full IFRSs, whether and to what extent the *IFRS for SMEs* should be amended to address specific issues, and clarifying the timescale for the due process steps. Respondents asserted that this framework would assist the IASB in formulating proposed changes to the Standard and constituents in evaluating whether such proposed changes should be implemented.

93. Some respondents said the IASB should consider how changes affect SMEs and users of their financial statements at the same time as new and revised IFRS are published. These respondents said it would benefit SMEs if they could prepare in advance for future changes.

94. Most respondents were supportive of the IASB addressing urgent issues earlier than the normal review cycle. However, some respondents had concerns that urgent issues should only be addressed in rare cases to ensure they do not detract from providing a stable platform for SMEs. Some respondents said that strict criteria should be established to determine when an issue should be regarded as urgent. Some respondents provided suggestions for such criteria.

Appendix A: Extracts from the comment letter analysis on the RfI – comments on accounting policy options

A1. These extracts are taken from Agenda Paper 8D for the April 2013 IASB meeting (paragraphs 5-7 of that paper covered responses to the RfI on the revaluation model for PPE and paragraphs 13-18 covered responses to the RfI on capitalisation of development/borrowing costs)

Revaluation of property, plant and equipment

A2. The following points cover the main reasons given by respondents to the RfI for not adding an accounting policy option to revalue PPE:

(a) There was a lengthy debate on accounting policy options when the *IFRS for SMEs* was being developed. Introducing options makes the *IFRS for SMEs* more complex and reduces comparability between SMEs. Options increase costs for preparers, eg when deciding which option to use and additional costs if they choose the more complex option and for users as they need to examine the different policies chosen and assess their effects.

(b) The cost model for PPE meets the needs of smaller entities.

(c) If a revaluation model is added, more complex requirements will need to be added in other areas of the *IFRS for SMEs*, eg for deferred taxation and impairment requirements.

(d) SMEs do not need to revalue their PPE to improve access to loan financing. Instead, companies can provide revaluation disclosures in the notes to the financial statements or obtain third party valuations of properties. Regardless of the accounting policy chosen, financial institutions often require a separate valuation to be performed before providing loan finance.

(e) Reliable fair values are often unavailable for items of PPE (this is a bigger issues in developing jurisdictions). Revaluation of PPE in the absence of public information on market values introduces subjectivity and reduce the reliability of financial information.

(f) The fair value of a non-financial asset is only relevant to users of the financial statements if the SME is likely to sell the item in the near future. Most PPE is used within the business for its useful life and then scrapped.

A3. The following points cover the main reasons given by respondents to the RfI for permitting an entity to choose, for each major class of PPE, whether to apply the cost model or the revaluation model:

(a) Adding a revaluation option would not add significant preparer complexity to the *IFRS for SMEs* as SMEs can choose the simpler option, ie the cost model.

(b) The revaluation model is not complex and is already commonly applied by small entities in many jurisdictions. Not allowing a revaluation option may be a barrier to adoption of the *IFRS for SMEs* in some jurisdictions, eg where revaluation is compulsory or SMEs commonly revalue their PPE.

(c) Allowing the revaluation model for PPE may improve access to loan financing and enable entities to better comply with debt-equity ratios in loan covenants. If entities are currently applying a revaluation model under local GAAP, a change to a cost model on adoption of the *IFRS for SMEs* may affect borrowing arrangements.

(d) Measuring property at fair value presents a more accurate reflection of financial position. SMEs should not be prohibited from providing users of financial statements with the most up to date and relevant information.

(e) It is important that entities with significant PPE operating in high inflationary economies or in countries with restrictions relating to foreign currency exchange can revalue those items. In high inflationary economies historic cost will be much lower than current cost. Plus, whilst income increases by inflation, depreciation does not unless the PPE is revalued.

(f) Although allowing a revaluation option would reduce comparability between SMEs, the option is currently permitted under full IFRSs. It could be argued comparability between listed companies is more important than SMEs. Also allowing a revaluation option would improve comparability of SMEs with companies applying full IFRSs. Many entities want to revalue PPE to be comparable with entities applying full IFRSs. Plus, banks and lenders want to be able to compare entities across industry segments.

(g) Allowing full IFRS accounting policy options in the *IFRS for SMEs* would enable subsidiaries that need to prepare information for consolidation purposes under full IFRSs to align their accounting policies with those of the group. Options also facilitate entities transitioning from the *IFRS for SMEs* to full IFRSs.

A4. Other suggestions made by respondents to the RfI include:

(a) Companies could provide revaluation disclosures in the notes to the financial statements.

(b) More complex options, eg the revaluation model, could be included in an appendix to the *IFRS for SMEs* or included within a separate box within the sections. This would allow SMEs that do not want to use complex options to easily ignore the additional requirements. The IASB could also signal which is the simpler option by having a default option (eg cost model) and a permitted alternative (eg revaluation model) to ensure entities do not have to spend resources finding the less costly alternative.

(c) If options are inserted in separate boxed sections (or in an appendix), jurisdictions could easily choose to include or exclude them as appropriate when adopting the *IFRS for SMEs*. This would be better than each jurisdiction adapting the *IFRS for SMEs* themselves by writing their own options (eg as has been done in the UK). The IASB could also publish a core *IFRS for SMEs* (ie excluding all the boxed sections) for jurisdictions where complex options are considered not to be required.

Capitalisation of borrowing costs/development costs

A5. Paragraph A2 covers the main reasons provided by respondents to the RfI for not permitting complex options. In particular, that they generally increase complexity and costs for both preparers and users.

A6. The following points cover the main other reasons given by respondents to the RfI for not changing the current requirement to expense all borrowing costs/development costs:

(a) Requirements to capitalise borrowing/development costs under full IFRSs are too complex for SMEs. For example, the judgments and estimates necessary to distinguishing the research phase from the development phase and determine when the criteria for capitalisation of development costs are met are onerous for SMEs. Similarly the judgement and calculations required in determining which borrowing costs to capitalise, and over what period, are complex. Many SMEs do not have sufficient expertise or the systems in place to apply these requirements properly and this would result in poor quality financial information.

(b) Requiring smaller entities to capitalise certain development/borrowing costs would increase costs without adding significant benefits to users of their financial statements. For example capitalising borrowing costs does not provide lenders with information about whether the SME can pay back the related debt.

(c) It is not clear why the IASB is reconsidering its decision to simplify the approach in full IFRSs for SMEs which was made because of concerns over the cost-benefit implications of requiring capitalisation. The RfI does not provide any evidence suggesting these concerns are no longer valid.

(d) Requiring or allowing capitalisation of development/borrowing costs will increase complexity in other areas, for example deferred taxation. Expensing development costs is in line with the income tax treatment in many jurisdictions which adds to its simplicity.

(e) SMEs can disclose additional information about borrowing/development costs expensed in the notes to the financial statements if they believe it would be useful.

(f) If SMEs wish to apply complex accounting requirements, and have the expertise to do so properly, they can apply full IFRSs.

A7. The following points cover the main reasons given by respondents to the RfI for requiring capitalisation of borrowing and development costs meeting criteria for capitalisation in IAS 23/38:

(a) The recognition and measurement requirements of the *IFRS for SMEs* should be aligned with full IFRSs.

(b) Development and borrowing costs are significant costs for some SMEs, eg start-up companies. Requiring them to be expensed can have a major impact on profits and net assets. This may reduce access to loan financing. It also makes these SMEs appear less profitable than other SMEs and puts them at a disadvantage with entities applying full IFRSs. If the *IFRS for SMEs* continues to require these expenditures to be expensed immediately it may discourage further investment needed to grow the business—for example on research and development or using borrowings to build assets, such as manufacturing plants.

A8. The following points cover the main reasons given by respondents to the RfI for adding an accounting policy option for SMEs, rather than a requirement, to capitalise borrowing and development costs meeting criteria for capitalisation in IAS 23/38.

(a) This would have most of the benefits and few of the drawbacks listed in paragraphs A6-A7.

(b) The option would not add significant complexity to the *IFRS for SMEs* as SMEs can choose the simpler option, ie the cost model.

(c) Although allowing options to capitalise borrowing and development costs meeting criteria for capitalisation in IAS 23/38 would reduce comparability between SMEs, it would improve comparability of SMEs with companies applying full IFRSs.

(d) Including options in the *IFRS for SMEs* provides flexibility and makes it easier for jurisdictions to adopt the *IFRS for SMEs*. Many jurisdictions either require or permit a capitalisation approach for borrowing costs/development costs that is similar to full IFRSs. The current expense approach in the IFRS for SME is a deterrent to adoption in those jurisdictions.

(e) If SMEs have the expertise to capitalise borrowing/development costs in accordance with IAS 23/38, they should be allowed to. SMEs should not be prohibited from providing users of financial statements with the most up to date and relevant information.

A9. Other suggestions made by respondents to the RfI include:

(a) Require capitalisation of borrowing and development costs meeting criteria for capitalisation in IAS 23/38 if it would not result in undue cost or effort.

(b) Simplify the criteria in IAS 23/38 for SMEs. Examples given include simplify criteria for when development costs should be capitalised and only capitalise specific borrowing costs, ie not those from a general pool of borrowings.

(c) A number of other suggestions made by comment letters are similar to those summarised in paragraph A4, ie they cover ways of including accounting policy options within the Standard, eg use of separate boxed sections/appendix.