Agenda paper 5A

Preliminary views on selective subjects from the “Request for Information - Comprehensive Review of the IFRS for SMEs Standard”

By: Saudi Organization For Certified Public Accountants (SOCPA)

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Agenda

- (G1A) The Approach: Should the IFRS for SMEs Standard be aligned with full IFRS Standards?
- (G1B) What extent of alignment of the IFRS for SMEs Standard with full IFRS Standards do you consider most useful, and why?
- (G2) The Board decided that in assessing whether and how to consult on aligning the IFRS for SMEs Standard with full IFRS Standards not currently included in the IFRS for SMEs Standard, the Board would apply three principles: (a) relevance to SMEs; (b) simplicity; and (c) faithful representation. In your view, do these principles provide a framework to assist in determining whether and how the IFRS for SMEs Standard should be aligned with full IFRS Standards?
- (S1) Aligning Section 2 Concepts and Pervasive Principles of the IFRS for SMEs Standard with the 2018 Conceptual Framework for Financial Reporting.

(G1A) The Approach: Should the IFRS for SMEs Standard be aligned with full IFRS Standards?

Our view:

- The best way to construct the IFRS for SMEs is to develop it from within the full IFRSs using the process of elimination for the sake of simplification (very close to the Australian method related to *"Australian reduced disclosure requirements"*).
- The process of development includes following steps:
  - First: Considering the Full IFRSs (no change in requirements, either recognition, measurement or disclosure, and no change in language) effective immediately before updating the IFRS for SMEs;
  - Second: Searching for those areas (primarily whole subjects) that are expected to require undue cost or effort if implemented by an SME and determining whether elimination of such areas would reduce the cost and effort of preparation (and audit) without substantial effect on the faithful representation of the financial statements for their intend use; and

- Third: Considering the purposes of financial statements of an SME
  a. Almost, all SMEs prepare general purpose financial statements equally to satisfy:
     i. statutory requirements,
     ii. tax purposes,
     iii. Financing
  b. The above purposes require financial statements to be:
     i. prepared according to authoritative standards, so they can be comparable,
     ii. Reliable (usually audited)
  c. Although measurement of income is important, the precise measurement, however, is not of concern to an SME or users of its financial statements as long as the statements are prepared according to the Standards.

Benefits of the suggested approach:

1. Reducing the cost on IASB in developing the standard by using exactly the same text and format of full IFRSs.
   a. Language of full IFRSs has never been reported as a barrier to apply these standards by SMEs.
   b. There will be no longer two financial reporting frameworks; rather, there will be full IFRSs and a reduced version (not only disclosures) of the same.
2. Reducing the cost of learning (academic study, professional training, books and manuals).
3. Reducing the cost of implementation (IT systems) on both preparers and auditors by offering the same basis for preparation and auditing of financial statements. That is because there is no different requirements; rather, there would be reduced requirements for SMEs.

(G1B) What extent of alignment of the IFRS for SMEs Standard with full IFRS Standards do you consider most useful, and why?

Our view:

- We suggest that alignment should include principles, important definitions and the precise wording of requirements, taking into consideration our suggested approach to alignment stated in previous slides.

(G2) The Board decided that in assessing whether and how to consult on aligning the IFRS for SMEs Standard with full IFRS Standards not currently included in the IFRS for SMEs Standard, the Board would apply three principles: (a) relevance to SMEs; (b) simplicity; and (c) faithful representation

Our view:

Principles (a) and (c) are beyond question and intuitively apply with no need to state them as principles for alignment. Principle (b) is the reason why we need the IFRS for SMEs in the first place. The dilemma, however, is about striking balance between simplicity and faithful representation as the latter is not determined as black and white matter. Rather, it is judgmental. The mission of the Board, therefore, is to prescribe those requirements that are simplified without compromising the level of faithful representation required to fulfill the objective of financial reporting.

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- Unfortunately, the simplicity in the current version of the IFRS for SMEs (2015) is sometimes in form of deleting texts from the standard without considering the effect on the preparers' ability to follow the requirements without referring to full IFRSs (i.e., the master reference of the Standard). In our opinion, simplicity can be fulfilled by either removing a specific requirement, or replace it with a rule-based requirement, without adversely affecting the coherence of the simplified topic.
- Following are just few examples from the current version where simplicity was in form of deletion of texts without due consideration to the effect on preparers understanding the requirements without the need to refer to full IFRSs. In other words, it was just a deletion of texts and not a simplification.

- **Section 16** - Definition of investment property and transfer from and to the investment property.
- **Section 17** - The application of revaluation model.
- **Section 28** – Application of the projected credit unit without definition or description of the method, or guidance on how to apply it without the need to refer to the full IFRSs. The simplifications offered were made without considering how such simplifications can be applied.
- **Section 35** - Exemptions were offered, some of which was copied from full IFRSs without due consideration of the requirements in the IFRS for SMEs, for example, the exemption related to the deemed cost related to investment property.

(S1) Aligning Section 2 Concepts and Pervasive Principles of the IFRS for SMEs Standard with the 2018 Conceptual Framework for Financial Reporting

(a) Aligning Section 2 with the 2018 Conceptual Framework?

Yes. No matter what set of standards for financial reporting is used (i.e., full IFRSs or the IFRS for SMEs), the conceptual framework should be the same.

(b) Making appropriate amendments to other sections of the *IFRS for SMEs*?

Yes. It is an automatic result of aligning Section 2.

(c) Retaining the concept of 'undue cost or effort'?

- No. This concept is the main source of all flaws in the application of the IFRS for SMEs and it causes lots of tension between entities, auditors and local standard setters.
- The judgement required to consider how the economic decisions of expected users of financial statements could be affected by not having a piece of information is likely to be beyond the normal ability of the preparers of financial statements, especially in the case of an SME.
- IASB should assess the cost and benefit of a requirement and decide whether to retain such requirement, remove it or make it optional.

It might be relevant to bring to the attention of the Board that the Board has decided to carry out such an assessment in various standards. Here are few examples:

1. In its basis for conclusions for IFRS 1 (BC42), the Board stated that, "… the Board concluded that balancing costs and benefits was a task for the Board when it sets accounting requirements rather than for entities when they apply those requirements."
2. The Board itself acknowledges the difficulty of such an assessment. In IFRS 9 (BCE.3), the Board stated that, "The evaluation of costs and benefits are necessarily qualitative, instead of quantitative. This is because quantifying costs and, particularly, benefits, is inherently difficult…"

3. In its basis for conclusion for IAS 1 (BC36) and for IAS 8 (BC24), the Board stated that, "… the Board decided that an exemption based on management's assessment of undue cost or effort was too subjective to be applied consistently by different entities. Moreover, balancing costs and benefits was a task for the Board when it sets accounting requirements rather than for entities when they apply them. Therefore, the Board retained the 'impracticability' criterion for exemption. … . Impracticability is the only basis on which IFRSs allow specific exemptions from applying particular requirements when the effect of applying them is material."

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Thank you!