

DRAFT COMMENT LETTER
Comments should be submitted by 12 November 2012 to
Commentletters@efrag.org

[Date]

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear Sir/Madam,

Re: Request for Information: Comprehensive Review of the IFRS for SMEs

On behalf of the European Financial Reporting Advisory Group (EFRAG), I am writing to comment on the Request for Information *Comprehensive Review of the IFRS for SMEs* (the RFI).

When answering the questions included in the RFI, EFRAG has been uncertain as to the extent that the discussion on the objective of the standard has now been re-opened. According to EFRAG the RFI seems to deal with both fundamental questions about the direction of the standard, such as the scope of the standard, and detailed requirements of the IFRS for SMEs.

During its discussions, EFRAG has learned that the fundamental questions and the questions related to the detailed requirements are highly interrelated. The answers to the questions on the detailed requirements depend on what needs the standard is meant to fulfil. EFRAG therefore thinks that a two-step approach could have been useful in relation to the review. In this context the first step should be a high level review covering the reconsideration of the objectives of the IFRS for SMEs, what types of entities one should have in mind when considering the requirements of the standard, and how the standard should be linked to full IFRS. EFRAG thinks that when these general issues had been agreed, the second step, including more detailed questions on, for example, what changes to full IFRS that should also be reflected in the IFRS for SMEs, would have been much simpler to answer.

In lack of such a two-step approach, EFRAG has experienced that its responses to many of the questions relating to detailed requirements, in particular the questions on whether changes in full IFRS should be reflected in the IFRS for SMEs, are driven by the priority attached to various factors including (but not limited to):

- the need for stability in a standard for SMEs,
- the need to reflect changes in users' needs,
- the need to align the IFRS for SMEs with full IFRS.

Question to EFRAG's constituents

EFRAG TEG members agree that the IFRS for SMEs should be based on the same conceptual framework as full IFRS taking into account the different user needs. They also agree that factors such as stability, changes in users' needs, and alignment with full IFRS should be considered when reviewing the standard. However, they do not agree on the weight to be attached to each of these factors.

View 1

Some EFRAG TEG members consider that the IFRS for SMEs should only be amended when a problem has been identified through post-implementation reviews or there is other evidence that the standard does not work appropriately. These members think that the first phase of a review of the IFRS for SMEs should be a post-implementation review involving field tests of how the standard is applied. The post-implementation review would provide evidence of any deficiencies in the existing requirements as well as evidence on whether the requirements in the IFRS for SMEs meet the users' needs. The focus of the post-implementation review should be on whether the existing requirements in the IFRS for SMEs result in effective financial reporting for SMEs taking their current economic context and business reality into account.

These members think that this would have been a more systematic approach that would ensure that most relevant information would be considered for the review. Without performing a post-implementation review, the members are concerned that some information would not be addressed adequately, for example, how the information resulting from the IFRS for SMEs is used and whether the requirements of the standard are applied in a consistent manner around the world.

These members consider that the review of the IFRS for SMEs should follow the same procedure as suggested by EFRAG in its letter on the agenda consultation of 5 December 2011. Accordingly, when there is evidence that a new standard, or amendment to an existing standard, is needed, a thorough and specified project proposal should be developed. The proposal should address the results of the post-implementation review and set out the objectives and the scope of the project.

These members therefore also think that it would have been useful to have the results of a post-implementation review before commenting on the specific questions raised in the RFI.

EFRAG TEG members holding the view that the IFRS for SMEs should only be amended when a problem has been identified through post-implementation reviews or there is other evidence that the standard does not work appropriately, do not think the standard should be amended as a result of changes to full IFRS. Changes to full IFRS should only be considered when there is evidence that current requirements of the IFRS for SMEs do not result in effective financial reporting and it is assessed that changes similar to those of full IFRS could solve the issues identified. Members of this view assess that if amendments made to full IFRS would automatically be considered for the IFRS for SMEs, the IFRS for SMEs would change more frequently than what would be beneficial given the particular characteristics of the SME environment. They think that stability is very important and consider it unlikely that any attempt to try to limit the number of amendments to the IFRS for SMEs could be successful if changes to full IFRS should be considered each time the IFRS for SMEs should be reviewed.

View 2

Other EFRAG TEG members believe that all available and relevant information should

be considered when amending the IFRS for SMEs. The relevant information includes, but is not limited to, identified problems and changes to full IFRS.

These members believe that considering a broad range of information will potentially enable the IASB to identify and resolve an issue in the IFRS for SMEs before such issue will result in a problem for those applying the standard.

These members note, however, that changes to full IFRS should not automatically trigger changes to the IFRS for SMEs. The amendments, including the costs and benefits related to these, should be assessed from the perspective of SMEs and the users of financial statements of SMEs. This could, for example, mean that an amendment made to full IFRS may first have to prove useful for entities applying full IFRS before being considered for the IFRS for SMEs. In addition, the amendments may have to be modified to make them appropriate for SMEs.

View 3

Finally, some EFRAG TEG members consider that applying the IFRS for SMEs should result in financial statement figures that are close to the figures that would be reported under full IFRS. These members therefore believe that most changes to full IFRS regarding measurement and recognition should also be reflected in the IFRS for SMEs as a result of the periodic reviews.

These members believe that a standard named 'IFRS for SMEs' will have to be close to full IFRS regarding recognition and measurement requirements. These members therefore favour a stronger alignment between full IFRS and the IFRS for SMEs compared to the two previous groups of members. The members consider that a closer alignment will improve comparability between listed and unlisted entities and that it would generally make financial statements more understandable if the figures reported under different standards would be similar.

What factors do you think should be considered when reviewing the IFRS for SMEs, what should be the weight of each of these factors, and to what extent should amendments to full IFRS be considered when reviewing the IFRS for SMEs?

Another, but related, issue that seems to affect many of the answers to the questions relating to the detailed requirements of the IFRS for SMEs included in the RFI is whether the IFRS for SMEs should include options that would result in a more similar outcome to full IFRS on measurement and recognition. As it appears from paragraphs BC89 to BC94 of the Basis for Conclusions accompanying the IFRS for SMEs, this was also a controversial issue when issuing the standard.

Note to EFRAG's constituents

Currently, EFRAG is split on this issue.

View A

Some EFRAG TEG members share the view that is explained in paragraphs BC91 to BC92 of the Basis for Conclusions accompanying the IFRS for SMEs. They think that options generally would increase the costs related to the standard. The standard is intended for small entities that are just interested in knowing what to do. It will therefore be more costly for preparers to introduce options as the preparers then will have to make decisions about what options to choose. In addition, it will be more costly for users as financial statements will be less comparable and users will have to examine the

accounting practice chosen by an entity and assess the effects of the chosen accounting practice.

View B

Other members believe that the IFRS for SMEs should include the same options for entities that are non-publicly accountable as for those that are, although they may be formulated in a simplified manner. They believe that this is important because if the entities applying the IFRS for SMEs were not allowed to use the same accounting treatment as publicly accountable entities, it could be more onerous for the non-publicly accountable entities to prepare financial statements than for those publicly accountable. This could be the case when an entity would want to measure or recognise certain transactions in a manner that would be allowed under full IFRS but not under the IFRS for SMEs. Such a situation would be illogical. EFRAG TEG members holding this view acknowledge that it could be argued that options reduce comparability. However, they note that many European jurisdictions include options in their national accounting regulation and that this has not been considered to be a problem.

These EFRAG TEG members also note that subsidiaries of listed parent entities are an important group of users of the IFRS for SMEs. These entities want to be able to prepare financial statements in accordance with the recognition and measurement requirements used for the consolidation under full IFRS. If the same options are not provided for in the IFRS for SMEs as in full IFRS, this would make the use of the IFRS for SMEs less attractive.

The different views have resulted in questions to constituents in relation to some of the responses included in Appendix 1 of this draft comment letter.

EFRAG notes that its comments reflect that the various issues have been considered from a European perspective. In order to be able to consider the issues from a global perspective, information about the implementation issues that have arisen across the world and knowledge about these issues would be necessary.

Our detailed responses to the questions in the ED are set out in Appendix 1. If you would like to discuss our comments further, please do not hesitate to contact Rasmus Sommer, Apostolena Theodosiou or me.

Yours sincerely,

Françoise Flores

EFRAG Chairman

APPENDIX 1

EFRAG's responses to the questions raised in the *Comprehensive Review of the IFRS for SMEs*

Question S1 - Use by publicly traded entities (Section 1).

The IFRS for SMEs currently prohibits an entity whose debt or equity instruments are traded in a public market from using the IFRS for SMEs (paragraph 1.3(a)). The IASB concluded that all entities that choose to enter a public securities market become publicly accountable and, therefore, should use full IFRSs.

Some constituents believe that governments and regulatory authorities in each individual jurisdiction should decide whether some publicly traded entities should be eligible to use the IFRS for SMEs based on their assessment of the public interest, the needs of investors in their jurisdiction, and the capabilities of those publicly traded companies to implement full IFRSs.

Are the scope requirements of the IFRS for SMEs currently too restrictive for publicly traded entities?

- (a) No - do not change the current requirements. Continue to prohibit an entity whose debt or equity instruments trade in a public market from using the IFRS for SMEs.
- (b) Yes - revise the scope of the IFRS for SMEs to permit each jurisdiction to decide whether entities whose debt or equity instruments are traded in a public market should be permitted or required to use the IFRS for SMEs.
- (c) Other – please explain.

Please provide reasoning to support your choice (a), (b) or (c).

EFRAG's response

EFRAG is split on the issue and asks its constituents for input.

2 EFRAG is split on this issue and asks its constituents for input.

The scope should not be extended (Alternative (a))

3 Some EFRAG TEG members do not support changing the scope of the IFRS for SMEs. The standard was initially developed for entities that do not have public accountability. The accounting requirements have therefore been based on this and should also be so in the future.

4 These members thus believe that the users in a non-publicly accountable entity environment have different information needs from those of the financial statements of publicly traded entities. Accordingly, if the scope of the IFRS for SMEs would be extended to financial statements of small publicly traded entities, it would likely be necessary to introduce significant amendments to the standard to ensure that users of financial statements of these entities would receive sufficiently useful information addressing their needs. These

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amendments could likely affect the relationship between cost and benefits of the requirements for the non-publicly accountable entities and the users of financial statements of these entities.

- 5 EFRAG TEG members holding the view that the scope of the standard should not be extended note that it could be beneficial for some jurisdictions to allow or require use of the IFRS for SMEs for smaller publicly traded entities. These members, however, think that the IASB has a responsibility to safeguard the high quality of financial information resulting from the application of its standards. The IASB should therefore have the possibility to prohibit entities outside the scope of the standard to claim compliance with the IFRS for SMEs. If jurisdictions want to apply the standard for other types of entities than the entities for which the standard is intended, these entities can state that they comply with the GAAP of that jurisdiction, but not with the IFRS for SMEs.
- 6 Moreover these members believe that it is inappropriate to consider the size of publicly traded entities and allow the IFRS for SMEs to be applied for small publicly traded entities. They are of the opinion that being publicly traded, or seeking listing, brings certain additional requirements compared to non-publicly traded entities regardless of the size of the entity.

The scope should be extended (Alternative (b))

- 7 Other EFRAG TEG members support changing the scope of the IFRS for SMEs to permit each jurisdiction to decide whether publicly traded entities should be allowed to prepare financial statements in accordance with the IFRS for SMEs. These members note that it should appear clearly from the standard what types of entities the requirements are intended for and that the standard should only be developed having these entities (and not, for example, publicly traded entities) in mind. However, they also think that small publicly traded entities or entities traded on smaller equity markets could have much more in common with small unlisted entities than with large entities traded on an ordinary stock exchange.
- 8 These members therefore think that jurisdictions should be allowed to choose what entities they think the standard is suitable for, based on the particular circumstances in that jurisdiction. The role of the IASB should be to produce high quality standards, and if an entity prepares financial statements in accordance with these requirements it should also be able to claim this compliance.

Question to EFRAG's constituents

- 9 Do you support one of the views expressed by EFRAG TEG members in relation to the use by publicly traded entities of the IFRS for SMEs?
- 10 If so, which view do you support?
- 11 If not, what is your answer to Question S1 of the Request for Information?

Question S2 - Use by financial institutions (Section 1)

The IFRS for SMEs currently prohibits financial institutions and other entities that hold assets for a broad group of outsiders as one of their primary businesses from using the IFRS for SMEs (paragraph 1.3(b)). The IASB concluded that standing ready to take and hold funds from a broad group of outsiders makes those entities publicly accountable and, therefore, they should use full IFRSs.

In every jurisdiction financial institutions are subject to regulation. In some jurisdictions, financial institutions such as credit unions and micro banks are very small. Some believe that governments and regulatory authorities in each individual jurisdiction should decide whether some financial institutions should be eligible to use the *IFRS for SMEs* on the basis of their assessment of the public interest, the needs of investors in their jurisdiction and the capabilities of those financial institutions to implement full IFRSs.

Are the scope requirements of the IFRS for SMEs currently too restrictive for financial institutions and similar entities?

- (a) No—do not change the current requirements. Continue to prohibit financial institutions and other entities that hold assets for a broad group of outsiders as one of their primary businesses from using the IFRS for SMEs.
- (b) Yes—revise the scope of the IFRS for SMEs to permit each jurisdiction to decide whether financial institutions and other entities that hold assets for a broad group of outsiders as one of their primary businesses should be permitted or required to use the IFRS for SMEs.
- (c) Other—please explain.

(Please provide reasoning to support your choice of (a), (b) or (c))

EFRAG's response

EFRAG is split on the issue and asks its constituents for input.

12 EFRAG is split on the issues and seeks input from constituents.

The scope should not be extended (Alternative (a))

13 For the reasons explained above in paragraphs 3 - 6, some EFRAG TEG members do not support changing the scope of the IFRS for SMEs.

The scope should be extended (Alternative (b))

14 Other EFRAG TEG members support changing the scope of the IFRS for SMEs for the reasons explained above in paragraphs 7 and 8.

Question to EFRAG's constituents

15 Do you support one of the views expressed by EFRAG TEG members in relation to the use by financial institutions of the IFRS for SMEs?

16 If so, which view do you support?

17 If not, what is your answer to Question S2 of the Request for Information?

Question S3 - Clarification of use by not-for-profit entities (Section 1)

The *IFRS for SMEs* is silent on whether not-for-profit (NFP) entities (eg charities) are eligible to use the *IFRS for SMEs*. Some interested parties have asked whether soliciting and accepting contributions would automatically make an NFP entity publicly accountable. The *IFRS for SMEs* specifically identifies only two types of entities that have public accountability and, therefore, are not eligible to use the *IFRS for SMEs*:

- those that have issued debt or equity securities in public capital markets; and
- those that hold assets for a broad group of outsiders as one of their primary businesses.

Should the *IFRS for SMEs* be revised to clarify whether an NFP entity is eligible to use it?

- (a) Yes—clarify that soliciting and accepting contributions does not automatically make an NFP entity publicly accountable. An NFP entity can use the IFRS for SMEs if it otherwise qualifies under Section 1.
- (b) Yes—clarify that soliciting and accepting contributions will automatically make an NFP entity publicly accountable. As a consequence, an NFP entity cannot use the IFRS for SMEs.
- (c) No—do not revise the IFRS for SMEs for this issue.
- (d) Other—please explain.

(Please provide reasoning to support your choice of (a), (b), (c) or (d))

EFRAG's response

EFRAG agrees with Alternative (c).

- 18 EFRAG thinks that in many cases a not-for-profit entity would not be publicly accountable as it would neither have its debt or equity instruments traded in a public market, nor hold assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. EFRAG does not see why the fact that an entity is not-for-profit is relevant for being publicly accountable. The statutes of the not-for-profit entity determine whether such an entity is publicly accountable or not. EFRAG considers the standard to be sufficiently clear on this issue and does not see a need to revise the IFRS for SMEs.
- 19 Moreover, the IFRS Constitution is limited to financial reporting by private sector companies. In the Constitution review of 2008 the question of developing-financial reporting standards for not-for-profit entities was addressed but not accommodated. This would, in our view, be another compelling reason not to revise the IFRS for SMEs in this respect.

Question S4 - Consideration of recent changes to the consolidation guidance in full IFRSs (Section 9)

The *IFRS for SMEs* establishes control as the basis for determining which entities are consolidated in the consolidated financial statements. This is consistent with the current approach in full IFRSs.

Recently, full IFRSs on this topic have been updated by IFRS 10 *Consolidated Financial Statements*, which replaced IAS 27 *Consolidated and Separate Financial Statements* (2008). IFRS 10 includes additional, stricter guidance on applying the control principle in a number of situations, with the intention of avoiding divergence in practice. The guidance will generally affect borderline cases where it is difficult to establish if an entity has control (ie, most straightforward parent-subsidary relationships will not be affected). Additional guidance is provided under IFRS 10 for:

- agency relationships, where one entity legally appoints another to act on its behalf. This guidance is particularly relevant to investment managers that make decisions on behalf of investors. Fund managers and entities that hold assets for a broad group of outsiders as a primary business are generally outside the scope of the IFRS for SMEs.
- control with less than a majority of the voting rights, sometimes called 'de facto control' (this principle is already addressed in paragraph 9.5 of the IFRS for SMEs but in less detail than in IFRS 10).
- assessing control where potential voting rights exist, such as options, rights or conversion features that, if exercised, give the holder additional voting rights (this principle is already addressed in paragraph 9.6 of the IFRS for SMEs but in less detail than in IFRS 10).

The changes above will generally mean that more judgement needs to be applied in borderline cases and where more complex relationships exist.

Should the changes outlined above be considered, but modified as appropriate to reflect the needs of users of SME financial statements and cost-benefit considerations?

- (a) No—do not change the current requirements. Continue to use the current definition of control and the guidance on its application in Section 9. They are appropriate for SMEs, and SMEs have been able to implement the definition and guidance without problems.
- (b) Yes—revise the IFRS for SMEs to reflect the main changes from IFRS 10 outlined above (modified as appropriate for SMEs).
- (c) Other—please explain.

(Please provide reasoning to support your choice of (a), (b) or (c)).

EFRAG's response

EFRAG is not able to provide a view on the issue (Alternative (c)).

- 20 EFRAG is not able to provide a view on the issue.
- 21 EFRAG understands that the changes to the consolidation requirements, resulting in IFRS 10, were triggered by issues that arose in larger and complex organisations. EFRAG is therefore uncertain about the effects and benefits of introducing the requirements for SMEs.
- 22 In addition, EFRAG notes that the changes were considered controversial when introduced in IFRS 10 and currently it has not been possible to test whether the changed requirements work in practice for entities applying full IFRS.
- 23 EFRAG believes that a situation where SMEs will have to spend resources on implementing changes that may result in only few or no benefits and even potentially result in unintended consequences should be avoided.
- 24 EFRAG therefore assesses that in this case it needs more evidence before it can form a view on whether the changes outlined in Question S4, modified as appropriately for SMEs, should be reflected in the IFRS for SMEs.

Question S5 - Use of recognition and measurement provisions in full IFRSs for financial instruments (Section 11)

The *IFRS for SMEs* currently permits entities to choose to apply either (paragraph 11.2):

- the provisions of both Sections 11 and 12 in full, or
- the recognition and measurement provisions of IAS 39 Financial Instruments: Recognition and Measurement and the disclosure requirements of Sections 11 and 12.

In paragraph BC106 of the Basis for Conclusions issued with the *IFRS for SMEs*, the IASB lists its reasons for providing SMEs with the option to use IAS 39. This is the only time that the *IFRS for SMEs* specifically permits the use of full IFRSs. One of the main reasons for this option is that the IASB concluded that SMEs should be permitted to have the same accounting policy options as in IAS 39, pending completion of its comprehensive financial instruments project to replace IAS 39. That decision is explained in more detail in paragraph BC106.

IAS 39 will be replaced by IFRS 9 *Financial Instruments*. Any amendments to the *IFRS for SMEs* from this comprehensive review would most probably be effective at a similar time to the effective date of IFRS 9. The *IFRS for SMEs* refers specifically to IAS 39. SMEs are not permitted to apply IFRS 9.

How should the current option to use IAS 39 in the *IFRS for SMEs* be updated once IFRS 9 has become effective?

- (a) There should be no option to use the recognition and measurement provisions in either IAS 39 or IFRS 9. All SMEs must follow the financial instrument requirements in Sections 11 and 12 in full.
- (b) Allow entities the option of following the recognition and measurement provisions of IFRS 9 (with the disclosure requirements of Sections 11 and 12).
- (c) Other—please explain.

(Please provide reasoning to support your choice of (a), (b) or (c)).

Note: the purpose of this question is to assess your overall view on whether the fallback to full IFRSs in Sections 11 and 12 should be removed completely, should continue to refer to an IFRS that has been superseded, or should be updated to refer to a current IFRS. It does not ask respondents to consider whether any of the recognition and measurement principles of IFRS 9 should result in amendments of the *IFRS for SMEs* at this stage, because the IASB has several current agenda projects that are expected to result in changes to IFRS 9 (see paragraph 13 of the Introduction to this Request for Information).

EFRAG's response

EFRAG agrees with Alternative (b). It thinks that entities should be given the option of following the recognition and measurement provisions of IFRS 9. However, post-implementation reviews should consider whether the option could be removed.

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- 25 EFRAG thinks that the IFRS for SMEs should be updated to give entities the option of following the recognition and measurement provisions of IFRS 9 (with the disclosure requirements of Sections 11 and 12).
- 26 EFRAG believes that it would not make much sense to keep the reference to IAS 39, as this standard is replaced by IFRS 9.
- 27 EFRAG has considered whether the option to depart from the recognition and measurement requirements of Sections 11 and 12 of the IFRS for SMEs should be removed. In this regard it has been noted that IFRS 9 is, to some extent, based on the IFRS for SMEs. Removing the option may therefore have limited effects. However, before considering removing the option, a post-implementation review should be performed. This review should provide evidence on the extent to which the option is used in practice.

Question S6 - Guidance on fair value measurement for financial and non-financial items (Section 11 and other sections)

Paragraphs 11.27–11.32 of the IFRS for SMEs contain guidance on fair value measurement. Those paragraphs are written in the context of financial instruments. However, several other sections of the *IFRS for SMEs* make reference to them, for example, fair value model for associates and jointly controlled entities (Sections 14 and 15), investment property (Section 16) and fair value of pension plan assets (Section 28). In addition, several other sections refer to fair value although they do not specifically refer to the guidance in Section 11. There is some other guidance about fair value elsewhere in the *IFRS for SMEs*, for example, guidance on fair value less costs to sell in paragraph 27.14.

Recently the guidance on fair value in full IFRSs has been consolidated and comprehensively updated by IFRS 13 *Fair Value Measurement*. Some of the main changes are:

- an emphasis that fair value is a market-based measurement (not an entity-specific measurement);
- an amendment to the definition of fair value to focus on an exit price (fair value is defined in IFRS 13 as “the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date”); and
- more specific guidance on determining fair value, including assessing the highest and best use of non-financial assets and identifying the principal market.

The guidance on fair value in Section 11 is based on the guidance on fair value in IAS 39. The IAS 39 guidance on fair value has been replaced by IFRS 13.

In straightforward cases, applying the IFRS 13 guidance on fair value would have no impact on the way fair value measurements are made under the *IFRS for SMEs*. However, if the new guidance was to be incorporated into the *IFRS for SMEs*, SMEs would need to re-evaluate their methods for determining fair value amounts to confirm that this is the case (particularly for non-financial assets) and use greater judgement in assessing what data market participants would use when pricing an asset or liability.

Should the fair value guidance in Section 11 be expanded to reflect the principles in IFRS 13, modified as appropriate to reflect the needs of users of SME financial statements and the specific circumstance of SMEs (for example, it would take into account their often more limited access to markets, valuation expertise, and other cost-benefit considerations)?

- (a) No—do not change the current requirements. The guidance for fair value measurement in paragraphs 11.27–11.32 is sufficient for financial and non-financial items.
- (b) Yes—the guidance for fair value measurement in Section 11 is not sufficient. Revise the IFRS for SMEs to incorporate those aspects of the fair value guidance in IFRS 13 that are important for SMEs, modified as appropriate for SMEs (including the appropriate disclosures).
- (c) Other—please explain.

(Please provide reasoning to support your choice of (a), (b) or (c))

Note: an alternative is to create a separate section in the *IFRS for SMEs* to deal with guidance on fair value that would be applicable to the entire *IFRS for SMEs*, rather than leaving such guidance in Section 11. This is covered in the following question (question S7).

EFRAG's response

EFRAG is not aware of problems arising from the fair value guidance included in the IFRS for SMEs and is seeking input from constituents.

- 28 As explained in paragraph 23 above EFRAG thinks that much should be done in order to avoid a situation where SMEs will have to spend resources on implementing changes that may result in only few or no benefits.
- 29 When providing its endorsement advice on IFRS 13, EFRAG experienced that the standard was difficult to understand and it could therefore be complicated and costly to apply without further educational efforts initiated by the IASB. At the same time, EFRAG notes that it is stated in Question S6 that “in straightforward cases, applying the IFRS 13 guidance on fair value would have no impact on the way fair value measurements are made under the IFRS for SMEs.” Unless a need is demonstrated for introducing the IFRS 13 guidance, EFRAG would therefore doubt that it would be cost/benefit efficient to introduce such guidance.

Question to EFRAG's constituents

- 30 Are you aware of any problems resulting from the guidance on fair value measurement currently included in the IFRS for SMEs that could be solved by expanding the guidance to reflect the principles in IFRS 13, modified as appropriate to reflect the needs of users of SME financial statements and the specific circumstances of SMEs?

Question S7 - Positioning of fair value guidance in the Standard (Section 11)

As noted in question S6, several sections of the *IFRS for SMEs* (covering both financial and non-financial items) make reference to the fair value guidance in Section 11.

Should the guidance be moved into a separate section? The benefit would be to make clear that the guidance is applicable to all references to fair value in the *IFRS for SMEs*, not just financial instruments.

- (a) No—do not move the guidance. It is sufficient to have the fair value measurement guidance in Section 11.
- (b) Yes—move the guidance from Section 11 into a separate section on fair value measurement.
- (c) Other—please explain.

(Please provide reasoning to support your choice of (a), (b) or (c))

Please answer this question regardless of your answer to question S6.

EFRAG's response

EFRAG agrees with Alternative (b).

- 31 EFRAG notes that fair value guidance may also be relevant in other cases than for financial instruments. This is for example the case when accounting for investments in subsidiaries, associates, jointly controlled entities, business combinations, leases, share-based payment, investment properties, biological assets, and when performing an impairment test.
- 32 EFRAG therefore thinks the standard could be more user friendly if the guidance on fair value measurement is placed in a separate section.

Question S8 - Consideration of recent changes to accounting for joint ventures in full IFRSs (Section 15)

Recently, the requirements for joint ventures in full IFRSs have been updated by the issue of IFRS 11 *Joint Arrangements*, which replaced IAS 31 *Interests in Joint Ventures*. A key change resulting from IFRS 11 is to classify and account for a joint arrangement on the basis of the parties' rights and obligations under the arrangement. Previously under IAS 31, the structure of the arrangement was the main determinant of the accounting (ie establishment of a corporation, partnership or other entity was required to account for the arrangement as a jointly-controlled entity). In line with this, IFRS 11 changes the definitions and terminology and classifies arrangements as either joint operations or joint ventures.

Section 15 is based on IAS 31 except that Section 15 (like IFRS 11) does not permit proportionate consolidation for joint ventures, which had been permitted by IAS 31. Like IAS 31, Section 15 classifies arrangements as jointly controlled operations, jointly controlled assets or jointly controlled entities. If the changes under IFRS 11 described above were adopted in Section 15, in most cases, jointly controlled assets and jointly controlled operations would become joint operations and jointly controlled entities would become joint ventures. Consequently, there would be no change to the way they are accounted for under Section 15.

However, it is possible that, as a result of the changes, an investment that previously met the definition of a jointly controlled entity would become a joint operation. This is because the existence of a separate legal vehicle is no longer the main factor in classification.

Should the above changes to full IFRSs be reflected in the *IFRS for SMEs*, modified as appropriate to reflect the needs of users of SME financial statements and cost-benefit considerations?

- (a) No—do not change the current requirements. Continue to classify arrangements as jointly controlled assets, jointly controlled operations and jointly controlled entities (terminology and classification based on IAS 31 *Interests in Joint Ventures*). The existing Section 15 is appropriate for SMEs, and SMEs have been able to implement it without problems.
- (b) Yes—revise the IFRS for SMEs so that arrangements are classified as joint ventures or joint operations on the basis of the parties' rights and obligations under the arrangement (terminology and classification based on IFRS 11 *Joint Arrangements*, modified as appropriate for SMEs).
- (c) Other—please explain.

(Please provide reasoning to support your choice of (a), (b) or (c))

Note: this would not change the accounting options available for jointly-controlled entities meeting the criteria to be joint ventures (ie cost model, equity method and fair value model).

EFRAG's response

Currently EFRAG is not able to provide a view on the issue (Alternative (c)).

- 33 Currently, EFRAG is not able to provide a view on this issue. Similar to our response to Question S4 included in paragraphs 20 to 24 above, EFRAG assesses that more evidence is needed in order to form a view on this issue.

Question S9 - Revaluation of property, plant and equipment (Section 17)

The IFRS for SMEs currently prohibits the revaluation of property, plant and equipment (PPE). Instead, all items of PPE must be measured at cost less any accumulated depreciation and any accumulated impairment losses (cost-depreciation-impairment model—paragraph 17.15). Revaluation of PPE was one of the complex accounting policy options in full IFRSs that the IASB eliminated in the interest of comparability and simplification of the *IFRS for SMEs*.

In full IFRSs, IAS 16 *Property, Plant and Equipment* allows entities to choose a revaluation model, rather than the cost-depreciation-impairment model, for entire classes of PPE. In accordance with the revaluation model in IAS 16, after recognition as an asset, an item of PPE whose fair value can be measured reliably is carried at a revalued amount—its fair value at the date of the revaluation less any subsequent accumulated depreciation and subsequent accumulated impairment losses. Revaluation increases are recognised in other comprehensive income and accumulated in equity under the heading of revaluation surplus (unless an increase reverses a previous revaluation decrease recognised in profit or loss for the same asset). Revaluation decreases that are in excess of prior increases are recognised in profit or loss. Revaluations must be made with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using fair value at the end of the reporting period.

Should an option to use the revaluation model for PPE be added to the *IFRS for SMEs*?

- (a) No—do not change the current requirements. Continue to require the cost-depreciation-impairment model with no option to revalue items of PPE.
- (b) Yes—revise the IFRS for SMEs to permit an entity to choose, for each major class of PPE, whether to apply the cost-depreciation-impairment model or the revaluation model (the approach in IAS 16).
- (c) Other—please explain.

(Please provide reasoning to support your choice of (a), (b) or (c))

EFRAG's response

EFRAG is split on this issue and asks its constituents for input.

EFRAG is split on this issue and seeks input from its constituents.

No free choice (Alternative (a))

- 34 Some EFRAG TEG members do not think the current requirements should be changed. They think that it would be cost-benefit inefficient for SMEs to have the choice to measure PPE at a re-valued amount and do not think the IFRS for SMEs should include options.
- 35 As mentioned in the cover letter (View A), these members think that options will make the standard more costly for both preparers and users. The standard is intended for small entities that are just interested in knowing what to do. It will therefore be more costly for preparers to introduce options as the preparers then will have to make decisions about what options to choose. In addition, it will be

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more costly for users as financial statements will be less comparable and users will have to examine the accounting policies chosen by an entity and assess the effects of the chosen accounting policies.

- 36 These members think that if a need for revaluation can be demonstrated, it should be assessed under what circumstances the revaluation results in the most useful information and is cost-benefit efficient. Revaluation should then be required (and not only be optional) under these circumstances.

Free choice to revalue items of PPE (Alternative (b))

- 37 Other EFRAG TEG members think that the IFRS for SMEs should permit an entity to choose, for each major class of PPE, whether to apply the cost-depreciation-impairment model or the revaluation model (the approach in IAS 16). As mentioned in the cover letter (View B), these members believe that the IFRS for SMEs should include the same options for entities that are not publicly accountable as for those that are, although they may be formulated in a simplified manner. This is important for two reasons:

- (a) If the entities applying the IFRS for SMEs were not allowed to use the same accounting treatment as publicly accountable entities, it could be more onerous for the non-publicly accountable entities to prepare financial statements than for the publicly accountable entities. Such a situation would be illogical. If an accounting treatment is considered to result in useful information for publicly accountable entities, it could, as a starting point, also be assumed that it would result in useful information for non-publicly accountable entities. EFRAG TEG members holding this view acknowledge that it could be argued that options reduce comparability. However, they note that many European jurisdictions include options in their national accounting regulation on this issue and this has not been considered to be a problem.
- (b) An important group of users of the IFRS for SMEs is subsidiaries of listed parent companies. These entities want to be able to prepare financial statements in accordance with the recognition and measurement requirements used for the consolidation (full IFRS). If the same options are not provided for in the IFRS for SMEs as in full IFRS, the use of the IFRS for SMEs would be less attractive.

- 38 These EFRAG TEG members also believe that SMEs should not be deprived from the possibility to revalue their property since they, in some countries, may need to present the revalued amount of their property in the balance sheet in order to obtain loan financing.

Question to EFRAG's constituents

39 Do you support one of the views expressed by EFRAG TEG members in relation to revaluation of PPE?

40 If so, which view do you support?

41 If not, what is your answer to Question S9 of the Request for Information?

Question S10 - Capitalisation of development costs (Section 18)

The IFRS for SMEs currently requires that all research and development costs be charged to expense when incurred unless they form part of the cost of another asset that meets the recognition criteria in the *IFRS for SMEs* (paragraph 18.14). The IASB reached that decision because many preparers and auditors of SME financial statements said that SMEs do not have the resources to assess whether a project is commercially viable on an ongoing basis. Bank lending officers told the IASB that information about capitalised development costs is of little benefit to them, and that they disregard those costs in making lending decisions.

In full IFRSs, IAS 38 *Intangible Assets* requires that all research and some development costs be charged to expense, but development costs incurred after the entity is able to demonstrate that the development has produced an asset with future economic benefits should be capitalised. IAS 38.57 lists certain criteria that must be met for this to be the case*.

Should the IFRS for SMEs be changed to require capitalisation of development costs meeting criteria for capitalisation (based on the criteria in IAS 38)?

- (a) No—do not change the current requirements. Continue to charge all development costs to expense.
- (b) Yes—revise the IFRS for SMEs to require capitalisation of development costs meeting the criteria for capitalisation (the approach in IAS 38).
- (c) Other—please explain.

(Please provide reasoning to support your choice of (a), (b) or (c))

*IAS 38.57 states: “An intangible asset arising from development (or from the development phase of an internal project) shall be recognised if, and only if, an entity can demonstrate all of the following:

- (a) the technical feasibility of completing the intangible asset so that it will be available for use or sale.
- (b) its intention to complete the intangible asset and use or sell it.
- (c) its ability to use or sell the intangible asset.
- (d) how the intangible asset will generate probable future economic benefits. Among other things, the entity can demonstrate the existence of a market for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset.
- (e) the availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset.
- (f) its ability to measure reliably the expenditure attributable to the intangible asset during its development.”

EFRAG’s response

EFRAG is split on the issue and asks its constituents for input.

42 EFRAG is split on the issue and asks its constituents for input.

The IFRS for SMEs should not be amended (Alternative (a))

43 Some EFRAG TEG members do not think that a requirement to capitalise development costs should be introduced in the IFRS for SMEs.

44 Firstly, these members think it would be costly for entities to capitalise

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development costs as it would, for example, require distinction between research and development. A less costly alternative to a requirement to capitalise development costs would be to make it optional to capitalise these costs. However, these members would also be against this alternative, as even options will make the standard more costly for both preparers and users. It will be more costly for preparers as they will have to make decisions about what options to choose; and it will be more costly for users as financial statements will be less comparable and users will have to examine the accounting policies chosen by an entity and assess the effects of these choices.

- 45 Members holding the view that the IFRS for SMEs should not be amended note that if it is considered beneficial that some entities with certain special characteristics or under certain circumstances capitalise development costs, a requirement should be introduced for these entities or circumstances.

The IFRS for SMEs should be amended (Alternative (c))

- 46 Other EFRAG TEG members acknowledge that it may be cost-benefit inefficient to require capitalisation of development costs. These members would therefore not introduce a requirement – but an option for entities to capitalise these costs. The members consider that important users of the IFRS for SMEs standard are subsidiaries of listed parent companies. These entities want to be able to apply a single set of recognition and measurement requirements for both the consolidated financial statements (prepared under full IFRS) and the annual accounts. However, they do not want to prepare the note disclosures required by full IFRS.
- 47 Members favouring the option also note that if entities applying the IFRS for SMEs were not allowed to use the same accounting treatment as publicly accountable entities, it could be more onerous for the non-publicly accountable entities to prepare financial statements than for the publicly accountable entities. Such a situation would be illogical. If an accounting treatment is considered appropriate for publicly accountable entities, it would likely also be appropriate for non-accountable entities.
- 48 It could be argued that options reduce comparability. However, members note that many European jurisdictions include options in their national accounting regulation and this has not been considered to be a problem. In this regard members also note that having the same options under the IFRS for SMEs as under local GAAP would facilitate the transition to the IFRS for SMEs for entities.

Options could be introduced if need demonstrated (Alternative (c))

- 49 Finally, some EFRAG TEG members do not think that a requirement to capitalise development costs should be introduced in the IFRS for SMEs. These members think it would be costly for entities to capitalise development costs.
- 50 However, the members think it should be possible to include an option in the IFRS for SMEs regarding capitalisation of development costs, if a need for such an option has been demonstrated. This means that before introducing an option, it should be examined whether any problem related to not capitalising development costs could be solved by entities providing additional disclosures. If the problem could be solved without introducing options, for example by entities providing additional disclosures, the EFRAG TEG members would favour such a solution as they consider that the number of options included in the IFRS for SMEs should be limited. Members believe that, the more options

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are included, the more complex it will be to apply the IFRS for SMEs and use the resulting financial statements.

Question to EFRAG's constituents

- 51 Do you support one of the views expressed by EFRAG TEG members in relation to capitalisation of development costs?
- 52 If so, which view do you support?
- 53 If not, what are your answers to Question S10 in the Request for Information?

Question S11 - Amortisation period for goodwill and other intangible assets (Section 18)

Paragraph 18.21 requires an entity to amortise an intangible asset on a systematic basis over its useful life. This requirement applies to goodwill as well as other intangible assets (see paragraph 19.23(a)). Paragraph 18.20 states “If an entity is unable to make a reliable estimate of the useful life of an intangible asset, the life shall be presumed to be ten years.” Some interested parties have said that, in some cases, although the management of the entity is unable to estimate the useful life reliably, management’s judgement is that the useful life is considerably shorter than ten years.

Should paragraph 18.20 be modified to state: “If an entity is unable to make a reliable estimate of the useful life of an intangible asset, the life shall be presumed to be ten years unless a shorter period can be justified”?

- (a) No—do not change the current requirements. Retain the presumption of ten years if an entity is unable to make a reliable estimate of the useful life of an intangible asset (including goodwill).
- (b) Yes—modify paragraph 18.20 to establish a presumption of ten years that can be overridden if a shorter period can be justified.
- (c) Other—please explain.

(Please provide reasoning to support your choice of (a), (b) or (c))

EFRAG’s response

EFRAG agrees with Alternative (b).

- 54 EFRAG thinks that paragraph 18.20 of the IFRS for SMEs should be amended in order to introduce the suggested more flexible approach on how to determine the useful life of intangible assets (and particularly goodwill). EFRAG does not consider that the current presumption that the useful life of an intangible asset is ten years will result in the most useful information, when there are indications that it will be less. It therefore supports that the presumption of ten years can be overridden.

Question S12 - Consideration of changes to accounting for business combinations under full IFRSs (Section 19)

The IFRS for SMEs accounts for all business combinations by applying the purchase method. This is similar to the 'acquisition method' approach currently applied in full IFRSs.

Section 19 of the IFRS for SMEs is generally based on the 2004 version of IFRS 3 *Business Combinations*. IFRS 3 was revised in 2008, which was near the time of the release of the *IFRS for SMEs*. IFRS 3 (2008) addressed deficiencies in the previous version of IFRS 3 without changing the basic accounting; it also promoted international convergence of accounting standards.

The main changes introduced by IFRS 3 (2008) that could be considered for incorporation in the IFRS for SMEs are:

- A focus on what is given as consideration to the seller, rather than what is spent in order to acquire the entity. As a consequence, acquisition-related costs are recognised as an expense rather than treated as part of the business combination (for example, advisory, valuation and other professional and administrative fees).
- Contingent consideration is recognised at fair value (without regard to probability) and then subsequently accounted for as a financial instrument instead of as an adjustment to the cost of the business combination.
- Determining goodwill requires remeasurement to fair value of any existing interest in the acquired company and measurement of any non-controlling interest in the acquired company.

Should Section 19 be amended to incorporate the above changes, modified as appropriate to reflect the needs of users of SME financial statements and cost-benefit considerations?

- (a) No—do not change the current requirements. The current approach in Section 19 (based on IFRS 3 (2004)) is suitable for SMEs, and SMEs have been able to implement it without problems.
- (b) Yes—revise the IFRS for SMEs to incorporate the main changes introduced by IFRS 3 (2008), as outlined above and modified as appropriate for SMEs.
- (c) Other—please explain.

(Please provide reasoning to support your choice of (a), (b) or (c))

EFRAG's response

EFRAG is not able to provide a view on the issue (Alternative (c)).

- 55 Currently, EFRAG is not able to provide a view on this issue. Similar to our response to Question S4 included in paragraphs 20 to 24 above, EFRAG assesses that it needs more evidence in order to form a view on this issue.

Question S13 - Presentation of share subscriptions receivable (Section 22)

Paragraph 22.7(a) requires that subscriptions receivable, and similar receivables that arise when equity instruments are issued before the entity receives the cash for those instruments, must be offset against equity in the statement of financial position, not presented as an asset.

Some interested parties have told the IASB that their national laws regard the equity as having been issued and require the presentation of the related receivable as an asset.

Should paragraph 22.7(a) be amended to either permit or require the presentation of the receivable as an asset?

- (a) No—do not change the current requirements. Continue to present the subscription receivable as an offset to equity.
- (b) Yes—change paragraph 22.7(a) to require that the subscription receivable is presented as an asset.
- (c) Yes—add an additional option to paragraph 22.7(a) to permit the subscription receivable to be presented as an asset, ie the entity would have a choice whether to present it as an asset or as an offset to equity.
- (d) Other—please explain.

(Please provide reasoning to support your choice of (a), (b), (c) or (d))

EFRAG's response

EFRAG thinks that the subscription receivable should be presented as an asset when certain criteria are met (Alternative (d)).

- 56 It is EFRAG's view that subscriptions receivable and similar receivables that arise when equity instruments are issued before the entity receives the cash for those instruments are receivables and should be presented as such in the balance sheet (no offsetting) when:
- (a) the equity instruments provide the holder with the same rights as equity instruments that have been fully paid, and
 - (b) the entity has an enforceable right to the consideration to be received in exchange of the equity instruments.
- 57 In other situations, EFRAG does not think the equity instruments and the receivable should be presented (gross).

Question S14 - Capitalisation of borrowing costs on qualifying assets (Section 25)

The *IFRS for SMEs* currently requires all borrowing costs to be recognised as an expense when incurred (paragraph 25.2). The IASB decided not to require capitalisation of any borrowing costs for cost-benefit reasons, particularly because of the complexity of identifying qualifying assets and calculating the amount of borrowing costs eligible for capitalisation.

IAS 23 *Borrowing Costs* requires that borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset (ie an asset that necessarily takes a substantial period of time to get ready for use or sale) must be capitalised as part of the cost of that asset, and all other borrowing costs must be recognised as an expense when incurred.

Should Section 25 of the *IFRS for SMEs* be changed so that SMEs are required to capitalise borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset, with all other borrowing costs recognised as an expense when incurred?

- (a) No—do not change the current requirements. Continue to require all borrowing costs to be recognised as an expense when incurred.
- (b) Yes—revise the *IFRS for SMEs* to require capitalisation of borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset (the approach in IAS 23).
- (c) Other—please explain.

(Please provide reasoning to support your choice of (a), (b) or (c))

EFRAG's response

EFRAG is split on the issues and asks its constituents for input.

58 EFRAG is split on the issues and seeks input from constituents.

The IFRS for SMEs should not be amended (Alternative (a))

59 For the reasons mentioned in paragraphs 43 to 45 above, some EFRAG TEG members do not think that a requirement to capitalise borrowing costs on qualifying assets should be introduced in the *IFRS for SMEs*.

The IFRS for SMEs should be amended (Alternative (b))

60 Other EFRAG TEG members think the *IFRS for SMEs* should be revised to require capitalisation of borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset (the approach in IAS 23).

The IFRS for SMEs should be amended (Alternative (c))

61 Other EFRAG TEG members think it should be optional for entities to capitalise borrowing costs on qualifying assets for the reasons mentioned in paragraphs 46 to 48 above.

Options could be introduced if need demonstrated (Alternative (c))

- 62 Finally, in accordance with the view expressed in paragraphs 49 to 50 above, some EFRAG TEG members think it should be possible to include an option in the IFRS for SMEs regarding capitalisation borrowing costs, but only if a need is demonstrated.

Question to EFRAG's constituents

- 63 Do you support one of the views expressed by EFRAG TEG members in relation to capitalisation of borrowing costs on qualifying assets?
- 64 If so, which view do you support?
- 65 If not, what are your answers to Question S14 in the Request for Information?

Question S15 - Presentation of actuarial gains or losses (Section 28)

In accordance with the IFRS for SMEs, an entity is required to recognise all actuarial gains and losses in the period in which they occur, either in profit or loss or in other comprehensive income as an accounting policy election (paragraph 28.24).

Recently, the requirements in full IFRSs have been updated by the issue of IAS 19 *Employee Benefits* (revised 2011). A key change as a result of the 2011 revisions to IAS 19 is that all actuarial gains and losses must be recognised in other comprehensive income in the period in which they arise. Previously, under full IFRSs, actuarial gains and losses could be recognised either in other comprehensive income or in profit or loss as an accounting policy election (and under the latter option there were a number of permitted methods for the timing of the recognition in profit or loss).

Section 28 is based on IAS 19 before the 2011 revisions, modified as appropriate to reflect the needs of users of SME financial statements and cost-benefit considerations. Removing the option for SMEs to recognise actuarial gains and losses in profit or loss would improve comparability between SMEs without adding any complexity.

Should the option to recognise actuarial gains and losses in profit or loss be removed from paragraph 28.24?

- (a) No—do not change the current requirements. Continue to allow an entity to recognise actuarial gains and losses either in profit or loss or in other comprehensive income as an accounting policy election.
- (b) Yes—revise the IFRS for SMEs so that an entity is required to recognise all actuarial gains and losses in other comprehensive income (ie removal of profit or loss option in paragraph 28.24).
- (c) Other—please explain.

(Please provide reasoning to support your choice of (a), (b) or (c))

Note: IAS 19 (revised 2011) made a number of other changes to full IFRSs. However, because Section 28 was simplified from the previous version of IAS 19 to reflect the needs of users of SME financial statements and cost-benefit considerations, the changes made to full IFRSs do not directly relate to the requirements in Section 28.

EFRAG's response

EFRAG thinks that the profit or loss option should be removed (Alternative (b)).

- 66 EFRAG thinks that options make the IFRS for SMEs relatively more costly for both preparers and users. Options increase costs for preparers as these will have to make decisions about what options to choose. Options also results in financial statements being less comparable and users will have to examine the accounting practice chosen by an entity and assess the effects of the chosen accounting policies. In this particular case it also notes that the option is not necessary in order to provide SMEs with the same options as entities applying full IFRS.
- 67 EFRAG would therefore welcome a revision of the IFRS for SMEs so that an entity is required to recognise all actuarial gains and losses in other comprehensive income (i.e. removal of profit or loss option in paragraph 28.24).

Question S16 - Approach for accounting for deferred income taxes (Section 29)

Section 29 of the *IFRS for SMEs* currently requires that deferred income taxes must be recognised using the temporary difference method. This is also the fundamental approach required by full IFRSs (IAS 12 *Income Taxes*).

Some hold the view that SMEs should recognise deferred income taxes and that the temporary difference method is appropriate. Others hold the view that while SMEs should recognise deferred income taxes, the temporary difference method (which bases deferred taxes on differences between the tax basis of an asset or liability and its carrying amount) is too complex. They propose replacing the temporary difference method with the timing difference method (which bases deferred taxes on differences between when an item of income or expense is recognised for tax purposes and when it is recognised in profit or loss). Others hold the view that SMEs should recognise deferred taxes only for timing differences that are expected to reverse in the near future (sometimes called the 'liability method'). And still others hold the view that SMEs should not recognise any deferred taxes at all (sometimes called the 'taxes payable method').

Should SMEs recognise deferred income taxes and if so, how should they be recognised?

- (a) Yes—SMEs should recognise deferred income taxes using the temporary difference method (the approach currently used in both the IFRS for SMEs and full IFRSs).
- (b) Yes—SMEs should recognise deferred income taxes using the timing difference method.
- (c) Yes—SMEs should recognise deferred income taxes using the liability method.
- (d) No—SMEs should not recognise deferred income taxes at all (ie they should use the taxes payable method), although some related disclosures should be required.
- (e) Other—please explain.

(Please provide reasoning to support your choice of (a), (b), (c), (d) or (e))

EFRAG's response

EFRAG is split on the issue and asks its constituents for input.

68 EFRAG is split on this issue and asks its constituents for their views.

No need for amendments (Alternative (a))

69 Some EFRAG TEG members believe that the IFRS for SMEs should only be amended when a need for a change has been demonstrated among those entities for which the standard is intended through a post implementation review. These members are not aware that a need has been demonstrated in relation to whether the temporary difference method should be applied when recognising deferred income taxes. In addition, these members note that EFRAG's proactive work in relation to reporting on income taxes (the discussion paper

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Improving the Financial Reporting of Income Tax and the following outreach events) has demonstrated the complexity of finding a proper treatment when accounting for income taxes. Accordingly, they do not think that the treatment should be changed until a solution has been found that has demonstrated to be better than the approach currently included in IAS 12.

Link to full IFRS (Alternative (a))

- 70 Other EFRAG TEG members believe that it is important that the requirements of full IFRS can also be applied under the IFRS for SMEs. They note that the IFRS for SMEs is based on full IFRS and that important users of the IFRS for SMEs standard are subsidiaries of listed parent companies. These entities want to be able to prepare financial statements in accordance with the recognition and measurement requirements used for the consolidation.
- 71 These members therefore think that the method applied when recognising deferred income taxes should be the same in full IFRS and in the IFRS for SMEs. Therefore, SMEs should recognise deferred income taxes using the temporary difference method.

Simplification (Alternative (d)/(e))

- 72 Finally, some EFRAG TEG members think it should be further investigated how costly it is for SMEs to recognise deferred income taxes. These members consider that the costs of recognising deferred income taxes could easily outweigh the benefits. These members would therefore be inclined to think that SMEs should not recognise deferred income taxes at all if doing so seems to be relatively costly for SMEs. These members would therefore require the taxes payable method.

Question to EFRAG's constituents

- 73 Do you support one of the views expressed by EFRAG TEG members in relation to deferred income taxes?
- 74 If so, which view do you support?
- 75 If not, what are your answers to Question S16 in the Request for Information?

Question S17 - Consideration of IAS 12 exemptions from recognising deferred taxes and other differences under IAS 12 (Section 29)

In answering this question, please assume that SMEs will continue to recognise deferred income taxes using the temporary difference method (see discussion in question S16).

Section 29 is based on the IASB's March 2009 exposure draft *Income Tax*. At the time the *IFRS for SMEs* was issued, that exposure draft was expected to amend IAS 12 *Income Taxes* by eliminating some exemptions from recognising deferred taxes and simplifying the accounting in other areas. The IASB eliminated the exemptions when developing Section 29 and made the other changes in the interest of simplifying the *IFRS for SMEs*.

Some interested parties, familiar with IAS 12, say that Section 29 does not noticeably simplify IAS 12 and that the removal of the IAS 12 exemptions results in more deferred tax calculations being required. Because the March 2009 exposure draft was not finalised, some question whether the differences between Section 29 and IAS 12 are now justified.

Should Section 29 be revised to conform it to IAS 12, modified as appropriate to reflect the needs of the users of SME financial statements?

- (a) No—do not change the overall approach in Section 29.
- (b) Yes—revise Section 29 to conform it to the current IAS 12 (modified as appropriate for SMEs).
- (c) Other—please explain.

(Please provide reasoning to support your choice of (a), (b) or (c))

EFRAG's response

EFRAG agrees with Alternative (b).

- 76 EFRAG thinks that the IFRS for SMEs by eliminating some exemptions from recognising deferred taxes and simplifying the accounting in other areas has introduced more complexity into the area of deferred tax than exists with the current IAS 12. EFRAG notes that it is mentioned in the RFI that “some interested parties, familiar with IAS 12, say that Section 29 does not noticeably simplify IAS 12 and that the removal of the IAS 12 exemptions results in more deferred tax calculations being required”. In addition, EFRAG notes that some experience exists in relation to calculating deferred tax in accordance with IAS 12, and it is more difficult to transfer this knowledge to SMEs when the requirements under the IFRS for SMEs are not similar to the requirements of IAS 12. EFRAG therefore thinks it will be helpful for both users and preparers to revise Section 29 to conform it to the current IAS 12 (modified as appropriate for SMEs).
- 77 EFRAG also wants to signal that this case illustrates that amendments to the IFRS for SMEs should not be based on exposure drafts related to full IFRS. Only when the IASB's due process have resulted in final standards or amendments to full IFRS could these changes be considered for the IFRS for SMEs.

Question S18 - Rebuttable presumption that investment property at fair value is recovered through sale (Section 29)

In answering this question, please also assume that SMEs will continue to recognise deferred income taxes using the temporary difference method (see discussion in question S16).

In December 2010, the IASB amended IAS 12 to introduce a rebuttable presumption that the carrying amount of investment property measured at fair value will be recovered entirely through sale.

The amendment to IAS 12 was issued because, without specific plans for the disposal of the investment property, it can be difficult and subjective to estimate how much of the carrying amount of the investment property will be recovered through cash flows from rental income and how much of it will be recovered through cash flows from selling the asset.

Paragraph 29.20 currently states:

“The measurement of deferred tax liabilities and deferred tax assets shall reflect the tax consequences that would follow from the manner in which the entity expects, at the reporting date, to recover or settle the carrying amount of the related assets and liabilities”.

Should Section 29 be revised to incorporate a similar exemption from paragraph 29.20 for investment property at fair value?

- (a) No—do not change the current requirements. Do not add an exemption in paragraph 29.20 for investment property measured at fair value.
- (b) Yes—revise Section 29 to incorporate the exemption for investment property at fair value (the approach in IAS 12).
- (c) Other—please explain.

(Please provide reasoning to support your choice of (a), (b) or (c))

Note: please answer this question regardless of your answer to question S17 above.

EFRAG's response

EFRAG is split on the issues and seeks input from constituents.

78 EFRAG is split on the issues and seeks input from constituents.

The IFRS for SMEs should not be amended unless a need has been demonstrated (Alternative (a))

79 As explained in the cover letter (View 1), some EFRAG TEG members consider that the IFRS for SMEs should only be amended when a problem has been identified through post-implementation reviews, or there is other evidence that the standard does not work appropriately. These members are not aware that the current requirements on the recovery of an investment property result in

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problems for SMEs and would accordingly, unless there is evidence of a problem, not amend the IFRS for SMEs on this issue.

- 80 In addition, these members believe that if a problem is identified, it should be assessed whether the amendment made to full IFRS would solve the problem appropriately. When performing this assessment, it should among other things be evaluated whether the amendment has worked as intended for companies applying full IFRS.

The IFRS for SMEs should be amended (Alternative (b))

- 81 Other EFRAG TEG members believe that the IFRS for SMEs should be amended to include a rebuttable presumption that investment property at fair value is recovered through sale. These members consider that amendments to full IFRS should also be considered when revising the IFRS for SMEs, however, the amendments should be assessed from the perspectives of SMEs and the costs and benefits of the amendments should be separately assessed for the SME environment.
- 82 In this particular case, members consider that if entities applying full IFRS have had difficulties with estimating how the carrying amount of investment properties will be recovered, SMEs will likely face the same problem. These members therefore think it will be efficient to consider this issue.
- 83 Before amending the IFRS for SMEs by including a rebuttable presumption about the recovery of investment property, these members, however, consider that it should be assessed whether the amendment made to full IFRS has solved the problem for entities applying full IFRS.

Question to EFRAG's constituents

- 84 Do you support one of the views expressed by EFRAG TEG members in relation to incorporating the exemption for investment property at fair value of IAS 12 in the IFRS for SMEs?
- 85 If so, which view do you support?
- 86 If not, what is your answer to Question S18 in the Request for Information?

Question S19 - Inclusion of additional topics in the IFRS for SMEs

The IASB intended that the 35 sections in the *IFRS for SMEs* would cover the kinds of transactions, events and conditions that are typically encountered by most SMEs. The IASB also provided guidance on how an entity's management should exercise judgement in developing an accounting policy in cases where the *IFRS for SMEs* does not specifically address a topic (see paragraphs 10.4–10.6).

Are there any topics that are not specifically addressed in the *IFRS for SMEs* that you think should be covered (ie where the general guidance in paragraphs 10.4–10.6 is not sufficient)?

(a) No.

(b) Yes (please state the topic and reasoning for your response).

Note: this question is asking about topics that are not currently addressed by the *IFRS for SMEs*. It is not asking which areas of the *IFRS for SMEs* require additional guidance. If you think more guidance should be added for a topic already covered by the *IFRS for SMEs*, please provide your comments in response to question S20.

EFRAG's response

EFRAG is not aware of any additional topics that should be addressed in the IFRS for SMEs.

- 87 EFRAG is not aware of any additional topics that should be addressed in the IFRS for SMEs. In this regard, EFRAG would, however, like to emphasise the importance of post-implementation reviews. These reviews can identify additional topics that should be addressed.

Question S20 - Opportunity to add your own specific issues

Are there any additional issues that you would like to bring to the IASB's attention on specific requirements in the sections of the IFRS for SMEs?

- (a) No.
- (b) Yes (please state your issues clearly, identify the section(s) to which they relate, provide references to paragraphs in the IFRS for SMEs where applicable and provide separate reasoning for each issue given).

EFRAG's response

EFRAG does not have any issues it wants to bring to the IASB's attention on specific requirements in the sections of the IFRS for SMEs.

Question G1 - Consideration of minor improvements to full IFRSs

The IFRS for SMEs was developed from full IFRSs but tailored for SMEs. As a result, the *IFRS for SMEs* uses identical wording to full IFRSs in many places.

The IASB makes ongoing changes to full IFRSs as part of its Annual Improvements project as well as during other projects. Such amendments may clarify guidance and wording, modify definitions or make other relatively minor amendments to full IFRSs that address unintended consequences, conflicts or oversights. For more information, the IASB web pages on its Annual Improvements project can be accessed on the following link: <http://www.ifrs.org/Current+Projects/IASB+Projects/Annual+Improvements/Annual+Improvements+Process.htm>.

Some believe that because those changes are intended to improve requirements, they should naturally be incorporated in the IFRS for SMEs where they are relevant.

Others note that each small change to the IFRS for SMEs would unnecessarily increase the reporting burden for SMEs because SMEs would have to assess whether each individual change will affect its current accounting policies. Those who hold that view concluded that, although the *IFRS for SMEs* was based on full IFRSs, it is now a separate Standard and does not need to reflect relatively minor changes in full IFRSs.

How should the IASB deal with such minor improvements, where the IFRS for SMEs is based on old wording from full IFRSs?

- (a) Where changes are intended to improve requirements in full IFRSs and there are similar wordings and requirements in the IFRS for SMEs, they should be incorporated in the (three-yearly) omnibus exposure draft of changes to the IFRS for SMEs.
- (b) Changes 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.
- (c) The IASB should develop criteria for assessing how any such improvements should be incorporated (please give your suggestions for the criteria to be used).
- (d) Other—please explain.

(Please provide reasoning to support your choice of (a), (b), (c) or (d))

EFRAG's response

EFRAG is split on the issue and seeks input from constituents.

88 EFRAG is split on how minor improvements to full IFRS should affect the IFRS for SMEs.

Only amend the IFRS for SMEs when a problem is identified (Alternative (b))

- 89 Some EFRAG TEG members consider that the IFRS for SMEs should only be amended when a problem has been identified through post-implementation reviews or there is other evidence that the standard does not work appropriately (View 1 in the cover letter). These members therefore think that the minor improvements to full IFRS should only be incorporated when there is a known problem for SMEs.
- 90 In addition, these members believe that if a problem is identified, it should be assessed whether the amendment made to full IFRS would solve the problem appropriately. When performing this assessment, it should, among other things, be evaluated whether the amendment has worked as intended for companies applying full IFRS.

Amend the IFRS for SMEs when it is assessed to solve a problem (Alternative (d))

- 91 Other EFRAG TEG members hold the view that all types of information, including amendments to full IFRS, should be considered when amending the IFRS for SMEs (View 2 in the cover letter). Minor improvements to full IFRS should, however, not be incorporated into the IFRS for SMEs automatically. The minor improvements should be assessed from the perspectives of SMEs and the costs and benefits of the amendments should be separately assessed for the SME environment. This may mean that minor improvements made to full IFRS may first have to prove useful without resulting in any unintended consequences before they are reflected in the IFRS for SMEs, and may only be incorporated into the IFRS for SMEs once every three years in relation to the review of the standard.

Amend the IFRS for SMEs to align it with full IFRS (Alternative (a))

- 92 Finally, some EFRAG TEG members consider that applying the IFRS for SMEs should result in financial statement figures that are not too far away from the figures that would be reported under full IFRS (View 3 in the cover letter). These members therefore favour a stronger alignment between full IFRS and the IFRS for SMEs as the two previous groups of members. These members consider that a closer alignment will improve comparability between listed and unlisted entities and that it would generally make financial statements more understandable if the figures reported under different standards would be similar. These members therefore think that where changes are intended to improve requirements in full IFRS and there are similar wordings and requirements in the IFRS for SMEs, the changes should, as a starting point, be incorporated into the IFRS for SMEs.

Question to EFRAG's constituents

- 93 Do you support one of the views expressed by EFRAG TEG members in relation to incorporating the minor improvement to full IFRS in the IFRS for SMEs?
- 94 If so, which view do you support?
- 95 If not, what is your answer to Question G1 in the Request for Information?

Question G2 - Further need for Q&As

One of the key responsibilities of the SMEIG has been to consider implementation questions raised by users of the *IFRS for SMEs* and to develop proposed non-mandatory guidance in the form of questions and answers (Q&As). These Q&As are intended to help those who use the *IFRS for SMEs* to think about specific accounting questions.

The SMEIG Q&A programme has been limited. Only seven final Q&A have been published. Three of those seven deal with eligibility to use the *IFRS for SMEs*. No additional Q&As are currently under development by the SMEIG.

Some people are of the view that, while the Q&A programme was useful when the *IFRS for SMEs* was first issued so that implementation questions arising in the early years of application around the world could be dealt with, it is no longer needed. Any new issues that arise in the future can be addressed in other ways, for example through education material or future three-yearly updates to the *IFRS for SMEs*. Many who hold this view think that an ongoing programme of issuing Q&As is inconsistent with the principle-based approach in the *IFRS for SMEs*, is burdensome because Q&As are perceived to add another set of rules on top of the *IFRS for SMEs*, and has the potential to create unnecessary conflict with full IFRSs if issues overlap with issues in full IFRSs.

Others, however, believe that the volume of Q&As issued so far is not excessive and that the non-mandatory guidance is helpful, and not a burden, especially to smaller organisations and in smaller jurisdictions that have limited resources to assist their constituents in implementing the *IFRS for SMEs*. Furthermore, in general, the Q&As released so far provide guidance on considerations when applying judgement, rather than create rules.

Do you believe that the current, limited programme for developing Q&As should continue after this comprehensive review is completed?

- (a) Yes—the current Q&A programme should be continued.
- (b) No—the current Q&A programme has served its purpose and should not be continued.
- (c) Other—please explain.

(Please provide reasoning to support your choice of (a), (b) or (c))

EFRAG's response

EFRAG supports Alternative (c).

EFRAG considers that it could be necessary to issue additional guidance; however, the procedure should be different from that currently applied.

- 96 EFRAG acknowledges that between reviews of the *IFRS for SMEs*, issues could arise that would benefit from further guidance. EFRAG would therefore be in favour of having something similar to the *IFRS Interpretation Committee* for the

IFRS for SMEs.

- 97 EFRAG has, however, not been in favour of the procedure applied when issuing Q&As so far since EFRAG believes that the criteria set for the development of Q&As in the SMEIG's terms of reference were often not respected.
- 98 In its comment letters in response to the Q&As issued, EFRAG has expressed concerns that the focus was not limited to a number of pervasive issues, as specified as an expectation in the SMEIG's terms of reference and operating procedures. EFRAG has been concerned that although the Q&As were issued as non-mandatory guidance, they are likely not perceived as such because they have been issued by the IFRS Foundation. This means that entities will have to study the Q&As in addition to the standard itself before applying the IFRS for SMEs. Accordingly, if the focus was not on a limited number of pervasive issues, this could result in many more pages of literature that SMEs would have to familiarise themselves with – and this would mean that the benefits of issuing a simple standard for SMEs would disappear. To solve the problem EFRAG recommended that the IFRS Foundation's SME Implementation Group developed criteria for when a Q&A should be issued that would limit the number.

Question G3 - Treatment of existing Q&As

As noted in question G2, there are seven final Q&As for the IFRS for SMEs. This comprehensive review provides an opportunity for the guidance in those Q&As to be incorporated into the IFRS for SMEs and for the Q&As to be deleted.

Non-mandatory guidance from the Q&As will become mandatory if it is included as requirements in the IFRS for SMEs. In addition, any guidance may need to be incorporated in the IFRS for SMEs in a reduced format or may even be omitted altogether (if the IASB deems that the guidance is no longer applicable after the Standard is updated or that the guidance is better suited for inclusion in training material). The IASB would also have to decide whether any parts of the guidance that are not incorporated into the IFRS for SMEs should be retained in some fashion, for example, as an addition to the Basis for Conclusions accompanying the IFRS for SMEs or as part of the training material on the IFRS for SMEs.

An alternative approach would be to continue to retain the Q&As separately where they remain relevant to the updated IFRS for SMEs. Under this approach there would be no need to reduce the guidance in the Q&As, but the guidance may need to be updated because of changes to the IFRS for SMEs resulting from the comprehensive review.

Should the Q&As be incorporated into the IFRS for SMEs?

- (a) Yes—the seven final Q&As should be incorporated as explained above, and deleted.
- (b) No—the seven final Q&As should be retained as separate guidance from the IFRS for SMEs.
- (c) Other—please explain.

(Please provide reasoning to support your choice of (a), (b) or (c))

EFRAG's response

EFRAG considers that the seven final Q&As should be incorporated into the IFRS for SMEs or the training material depending on the detail of the guidance (Alternative (c)).

99 EFRAG has concerns about incorporating non-mandatory guidance that is sometimes very detailed into the IFRS for SMEs, but at the same time it does not consider it useful to keep the seven final Q&As as separate guidance.

100 EFRAG therefore suggests that the Q&As are only incorporated into the standard itself to the extent that clarification on a principle level is achieved. More detailed guidance could, on the other hand, be included in the training material only. An analysis needs to be made for each of the seven Q&As, so that the principles based character of IFRS for SMEs is not undermined by including too many details that would not fit the overall level and balance of the standard. Where the Q&A is too detailed or too narrow in its focus, inclusion in the training material could be appropriate.

Question G4 - Training material

The IFRS Foundation has developed comprehensive free-to-download self-study training material to support the implementation of the *IFRS for SMEs*. These are available on our website: <http://www.ifrs.org/IFRS+for+SMEs/Training+material.htm>. In addition to your views on the questions we have raised about the *IFRS for SMEs*, we welcome any comments you may have about the training material, including any suggestions you may have on how we can improve it.

Do you have any comments on the IFRS Foundation's *IFRS for SMEs* training material available on the link above?

- (a) No.
- (b) Yes (please provide your comments).

EFRAG's response

EFRAG has been informed that the training material is of high quality.

101 The people that EFRAG has consulted on the training material have all noted that they think it is of high quality.

Question G5 - Opportunity to add any further general issues

Are there any additional issues you would like to bring to the IASB's attention relating to the IFRS for SMEs?

- (a) No.
- (b) Yes (please state your issues clearly and provide separate reasoning for each issue given).

EFRAG's response

EFRAG has no other issues relating to the IFRS for SMEs that it would like to bring to the IASB's attention.

Question G6 – Use of IFRS for SMEs in your jurisdiction

This question contains four sub-questions. The purpose of the questions is to give us some information about the use of the IFRS for SMEs in the jurisdictions of those responding to this Request for Information.

- 1 What is your country/jurisdiction?
- 2 Is the IFRS for SMEs currently used in your country/jurisdiction?
 - (a) Yes, widely used by a majority of our SMEs.
 - (b) Yes, used by some but not a majority of our SMEs.
 - (c) No, not widely used by our SMEs.
 - (d) Other (please explain).
- 3 If the IFRS for SMEs is used in your country/jurisdiction, in your judgement what have been the principal benefits of the IFRS for SMEs?

(Please give details of any benefits.)
- 4 If the IFRS for SMEs is used in your country/jurisdiction, in your judgement what have been the principal practical problems in implementing the IFRS for SMEs?

(Please give details of any problems.)

EFRAG's response

Based on the input EFRAG has received, the IFRS for SMEs is only applied to a very limited extent within the EU.

- 102 Within the EU, the IFRS for SMEs cannot be applied by entities as an alternative to national requirements. In addition, Member States cannot allow the use of the IFRS for SMEs when it is not in accordance with the European Accounting Directives.
- 103 Based on the input EFRAG has received, the IFRS for SMEs is only applied to a very limited extent within the EU.