Deutsches Rechnungslegungs Standards Committee e.V.
Accounting Standards Committee of Germany ®

REPORT ON THE FIELD TESTS IN GERMANY

regarding the

ED-IFRS for SMEs

April 2008

In cooperation with:

BDI

PRICEWATERHOUSECOOPERS

Report on German field tests

An IFRS for SMEs is of potential relevance to millions of companies around the world. The IASB published the Exposure Draft of the IFRS for Small and Medium-sized Entities (ED-IFRS for SMEs) in February 2007 and early on announced its plan to conduct field tests because of the importance of this standard. In June 2007 the IASB launched its field tests of the ED-IFRS for SMEs. To support these IASB field tests the Accounting Standards Committee of Germany (ASCG) in cooperation with the Federation of German Industries (BDI) and PricewaterhouseCoopers AG (PwC Germany) in May 2007 initiated field tests among German SMEs.

1. Remarks on the field test design

International accounting requirements long ago found its way into the German legal system: as early as 1998 a law was introduced allowing capital market oriented companies preparing consolidated financial statements to apply IFRS or US-GAAP instead of German GAAP. With the IAS-Regulation those companies are now required to prepare consolidated financial statements in accordance with IFRS. There are about 1,000 listed companies applying IFRS now. Non-listed companies may apply IFRS for their consolidated financial statements; separate financial statements are required to be prepared in accordance with national GAAP in any case (additional separate financial statements in accordance with IFRS may be prepared for information purposes only). However, the vast majority of the approximately 2.2 million German non-listed companies does not apply IFRS. Therefore it is important to note that the participating SMEs had to adapt to the ED-IFRS for SMEs coming from a very specific existing company and tax law environment, very different from IFRS.

Contrary to IFRS, German GAAP financial statements are not only prepared to provide information for investors, but can be considered multi purpose financial statements. For one, they also function as the basis for determining distributable profits. Financial statements thereby serve the aim to protect the company’s creditors, which is the predominant objective. As a result, German GAAP focus on capital maintenance, because creditors are mainly interested in the capital remaining in the company to build up and strengthen the capacity to repay debt when due. However, only the individual financial statements (not consolidated financial statements) serve as the basis for determining distributable profits. Furthermore, individual financial statements serve as a basis for tax accounting, which explains why many SME financial statements in Germany are very much tax driven with companies often using specific tax values rather than economically relevant values. Overall, the underlying concepts of financial statements significantly differ between IFRS and German GAAP. Therefore, the preparation of trial financial statements was very time, resource and overall cost intensive. Also, despite the great effort it cannot be assumed that all conceptual issues and requirements of the ED-IFRS for SMEs were thoroughly understood and correctly applied by the participants. The analysis of the trial financial statements will give an idea of which problems the participants encountered.

As most German SMEs have not yet looked into IFRS in more detail, the field test was especially challenging for German SMEs. Before this background the ASCG and its cooperation partners asked companies participating in the field test to apply a so-called 'module approach'. Depending on the resources of the company they could contribute to the project, the contribution ranging from preparing a full set of financial statements to providing narrative information on the evaluation of the ED-IFRS for SMEs in total and its requirements with regard to the different parts of financial statements. This information was provided by filling in a questionnaire, which all of the participating companies did. In addition to this report summarizing the results, all financial statements and questionnaires are passed on to the IASB's SME Director (anonymous, where required).

In addition to this module approach the ASCG introduced another important feature: the involvement of Small and Medium-sized Practitioners (SMPs). Since the ED-IFRS for SMEs conveys an entirely new concept which German SMEs often lack the knowledge of, it was virtually impossible to find SMEs participating in the field test without additional support. Companies noted that they would hardly have been able to apply the ED-IFRS for SMEs without the support of SMPs. Since many SMEs have outsourced their accounting to tax experts and auditors, it nevertheless seemed a sensible solution to include SMPs in the project. In fact it was mainly the SMPs finding participants for the field study.

Figure 1 provides an overview of the parts of the financial statements that the participating SMEs prepared as part of the field test.

Part of financial statements	**Number of companies**
Balance sheet	8
Income statement	7
Notes	5
Cash flow statement	6
Reconciliation	4

Figure 1 Range of documents prepared as trial financial statements.

To a certain degree it reflects how companies viewed the cost/benefit-balance of the ED-IFRS for SMEs. For example, notes were too burdensome to prepare. For one solely due to the vast number of required notes, but also because additional information would have had to be generated and prepared. In addition it needs to be pointed out that – again due to cost/benefit-considerations – companies often did not apply the requirements in all detail. For example, SMEs tend to outsource the evaluation of pension liabilities; they would not, however, require an additional expert's opinion based on the ED-IFRS for SMEs. Therefore, all companies noted that it is very likely that various additional issues would arise when preparing "real financial statements" and when actually having to deal with problematic details of the requirements. For example, "cost of inventories" seemed like a sensitive approach for most participants; however, those trying to determine the cost of inventories realized just how difficult it was to apply. Therefore, the results presented in this report can only be indicative of the range of problems SMEs might face when applying an IFRS for SMEs.

In addition to the documents provided, SMEs, SMPs and members of the project team got together in several round table discussions to debate the findings of the participants, the last of which the IASB's SME-Director was able to attend.

2. General remarks on participating companies

In line with the approach taken by the IASB with regard to the scope, the German field tests generally included companies that do not have public accountability. A total of 15 companies participated in the field test and prepared trial financial statements applying the ED-IFRS for SMEs. Those 15 companies are by no means representative of the overall structure of SMEs in Germany. With regard to representative data we would like to refer to our survey conducted amongst 4,000 German SMEs from which we received 410 analyzable questionnaires.[1]

Generally speaking, the average SME participating in this field test tends to be larger, more internationally involved and more likely to be part of a group structure than the average SME in Germany. Before this background the participating companies found it more relevant for their company to assess the ED-IFRS for SMEs. Following the characteristics of the 15 participating companies are described in more detail.

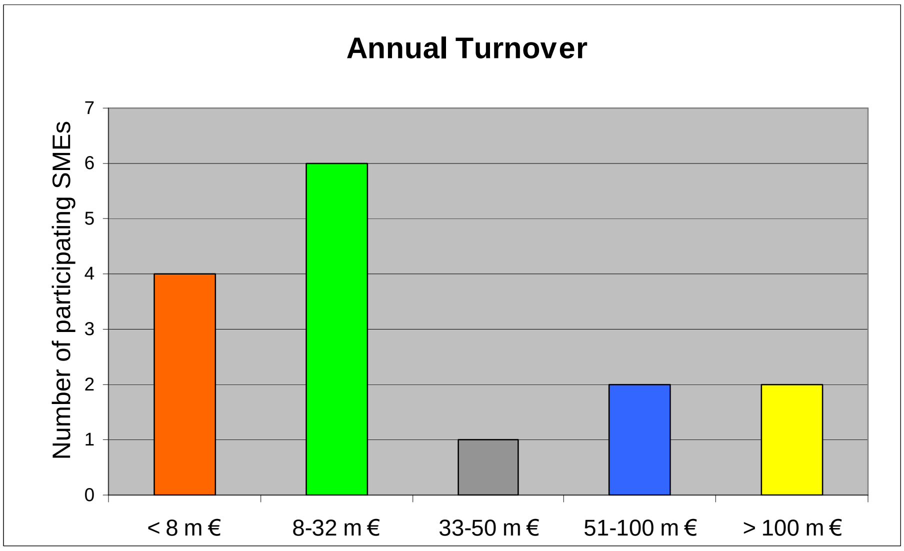

Figure 2 Annual turnover of the participating SMEs

[1] The results are attached to the GASB's comment letter on the ED-IFRS for SMEs. They can also be downloaded at www.drsc.de.

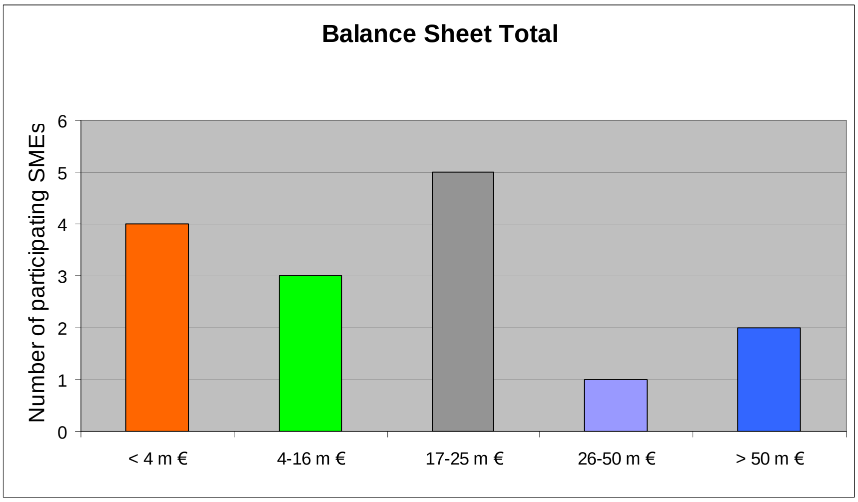

Figure 3 Balance sheet total of the participating SMEs

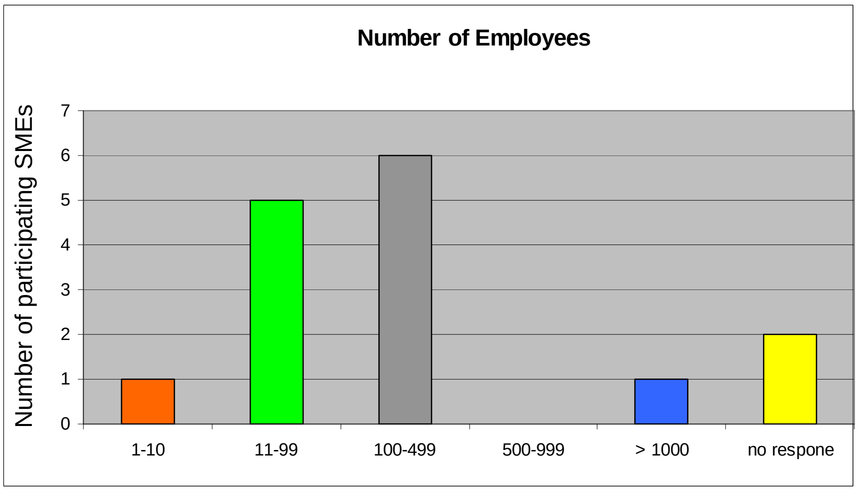

Figure 4 Number of employees in the participating SMEs

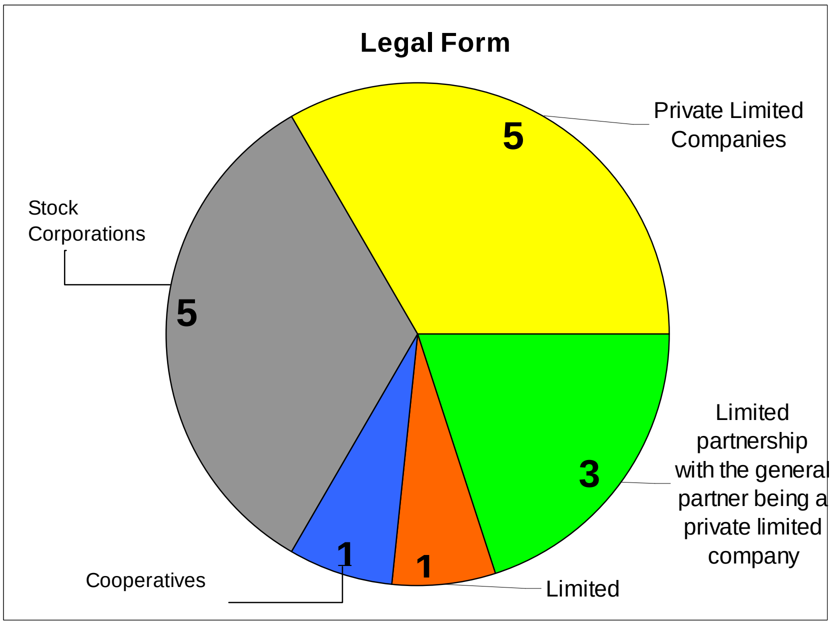

Figure 5 Legal forms of the participating SMEs

As mentioned above the German law allows non-listed companies to prepare their consolidated financial statements in accordance with IFRSs. Therefore, some non capital market oriented companies, which are considered SMEs under the IASB's definition, already apply full IFRSs. As they are already familiar with the IFRS concept, these companies could provide a different view on the ED-IFRS for SMEs and were therefore also invited to participate in this field test.

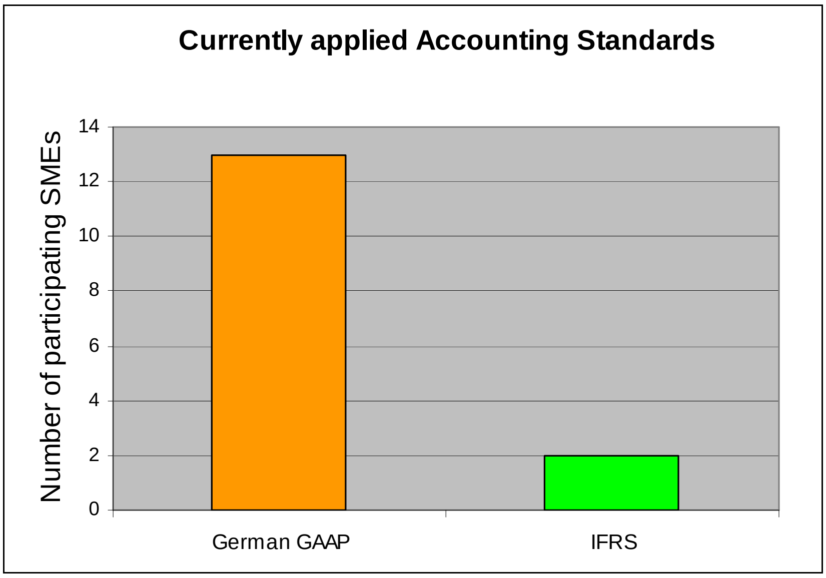

Figure 6 Accounting standards that the participating SMEs apply

As figure 6 shows two of the participating companies already prepare IFRS financial statements and evaluated the ED-IFRS for SMEs on the basis of simplifications provided compared to full IFRSs. The vast majority, however, so far has not dealt with IFRSs at all, but applied German GAAP.

The majority of the participating companies want to remain anonymous. The participating SMPs are listed below:

- **Accounting Partners**, Wirtschaftsprüfungsgesellschaft, Düsseldorf
- **Consulere** Steuerberatungsgesellschaft, Halle/Saale
- **DHPG**, Dr. Harzem & Partner, Gummersbach
- **Flick Gocke Schaumburg** GmbH, Bonn
- Steuerberatung **Holzapfel**, Hamburg
- **NorCon Revision** GmbH, Nordhorn
- **NPP** Niethammer, Posewang & Partner GmbH, Hamburg
- **Rath, Anders**, **Dr. Wanner & Partner** Wirtschaftsprüfungsgesellschaft, Berlin
- **Rödl & Partner** GmbH Wirtschaftsprüfungsgesellschaft Steuerberatungsgesellschaft, Nürnberg
- **RP Richter & Partner**, München
- **Susat & Partner** OHG, Hamburg
- WP/StB **Thomas Walther**, Minden

3. General remarks on the ED-IFRS for SMEs

3.1 *Advantages and disadvantages of applying the IFRS for SMEs*

As mentioned before, it was challenging to motivate SMEs to participate in this field test as for many of them, for various reasons, IFRS are not relevant. Generally speaking the participating SMEs were divided into two groups. On the one hand large participating SMEs were either already preparing IFRS financial statements or currently discussing possible benefits of changing from German GAAP to IFRS. On the other hand, about half of the companies did not see any reason to consider IFRS or the IFRS for SMEs as an alternative accounting approach. Mainly because of existing legal requirements to prepare German GAAP financial statements but also because they generally did not find the SME-standard superior to existing national requirements or did not have any need to prepare internationally comparable financial statements (e.g. showed a low level of international activities). Before this background companies had very different motives to participate in the field test and saw different advantages and disadvantages in an IFRS for SMEs.

At large, if participating SMEs acknowledged the need for IFRS or IFRS for SMEs, they felt that the following would be *major advantages* in favour of applying an IFRS for SMEs:

- internationally understandable and accepted financial statements, but still simplifications compared to full IFRSs possible,
- some participating SMEs are internationally involved and face the need to provide investors such as banks or private equity provider as well as customers and suppliers with internationally understandable financial statements,
- other, even though being internationally active, do not face such demand; however, they believe that this will eventually evolve with IFRS or an IFRS for SMEs being a commonly applied accounting standard amongst SMEs,
- IFRS for SMEs might be necessary for the comparison across companies of the same industry,
- degree of international competition decisive for tendency to apply IFRS for SMEs,
- SMEs organised in a group structure with international subsidiaries find the possibilities to harmonize the group accounting appealing as it provides a consistent reporting system across group entities,
- IFRS for SMEs as an important first step towards full IFRSs,
- presentation of economically more relevant information (dissolution of hidden reserves),
- tendency to increase equity by applying IFRS for SMEs, which might have a positive effect on rating results,
- better, more relevant, information for the management of the company.

While the participating SMEs mainly agreed that IFRS in general and possibly the IFRS for SMEs would very likely be of some relevance to German SMEs in the long run, they mostly believed that at the current stage, the costs of applying international accounting standards would outweigh the benefits. This is mainly, because neither the EU nor Germany currently seem to plan on adopting the IFRS for SMEs as the statutory accounting system. This would make any IFRS financial statement an additional burden, prepared for information purposes 'only'. Hence, the foundation for any discussion about the IFRS for SMEs in Europe will be that it is seen as a simplification with regard to the costs of preparing financial statements. Therefore, participants hope that European views will be incorporated in the final IFRS for SMEs.

Altogether the participating SMEs pointed out the following *disadvantage* of applying an IFRS for SMEs

- ED-IFRS for SMEs still very complex and burdensome, for example, with regard to the wide range of disclosure requirements,
- application of the ED-IFRS for SMEs cost intensive as German SMEs tend to lack the know-how of IFRS in general
- overall the ED-IFRS for SMEs is not attractive for the participating SMEs from a cost-benefit point of view
- there was little need for a specific IFRS for SMEs as SMEs would turn to full IFRSs if international accounting standards were needed, this applies even more when looking at what little changes and simplifications were provided in the ED-IFRS for SMEs
- international acceptance of an IFRS for SMEs questionable (only "second-best" standard?),
- the problems that arise for many German SMEs with regard to the equity/liability-definition are not solved,
- ED-IFRS for SMEs allows insights into the company that should not be provided to the vast public (users of SME financial statements generally have the possibility to require any information from the company without depending on financial statements)

The overall assessment was that while the IFRS and very likely an IFRS for SMEs will have an impact on German SMEs in the long run, the majority of the participating SMEs – in the current situation – do not find the ED-IFRS for SMEs a convincing option as it is too costly to apply with hardly any benefit to it. However, many participants are of the opinion that this will change over time as German SMEs will be even more involved internationally and foreign business partners or competitors require preparing internationally understandable financial statements.

3.2 *Evaluation of the concept of the ED-IFRS for SMEs*

Assumed German SMEs were to apply an IFRS for SMEs, the participating SMEs found the underlying concept of the ED-IFRS for SMEs convincing. Well structured and generally understandable most of the preparers concluded that they would be able to prepare their financial statements on the basis of the ED-IFRS for SMEs, subject to the restriction that additional problems might be encountered when preparing "real" financial statements. Even though most participants agreed that requirements were relatively easy to find, they nevertheless pointed out that the structure of the IFRS for SMEs could still be more oriented on the balance sheet to ease the handling of the standard. The glossary and illustrative financial statements were useful.

There were several major aspects of critique on the concept of the ED-IFRS for SMEs. For one the vast majority of the participants supported a stand-alone document and therefore did not approve of the numerous references to full IFRSs. They argued that the IFRS for SMEs was hard to handle if SMEs were asked to look back into full IFRSs to evaluate and – if applicable – apply, for example, accounting options. The majority was of the opinion that the IFRS for SMEs should be a strict stand-alone document.

However, participants were divided on how to make the document self-sufficient. For example, while those companies already oriented at full IFRSs for one reason or another, preferred to include all options available in full IFRSs, smaller SMEs tended to favour the deletion of all options to decrease the cost of applying the IFRS for SMEs and to increase the comparability across national and international companies. If the transition to full IFRSs was to be a main purpose of IFRS for SMEs including all options seems sensible, however, if the focus was on those numerous SMEs very unlikely to ever apply full IFRS the deletion of options seems more appropriate.

Furthermore, SMEs felt uneasy about the optional fallback to full IFRSs. Again different arguments were brought forward. If SMEs and SMPs were familiar with IFRS, the fallback to these requirements seemed the natural thing to do. However, as also experienced in this field test most SMEs and even SMPs are not likely to know IFRSs and therefore would possibly come up with different solutions. The IFRS for SMEs should clarify that solutions differing from full IFRS are acceptable.

Of great importance to the SMEs is the approach to the maintenance of an IFRS for SMEs. SMEs find it crucial to reduce changes to an IFRS for SMEs to a minimum as resources to obtain the knowledge about the changes and to adapt to them are scarce. In addition the comparability over periods diminishes. Along these lines SMEs found that cross-references add to the problem of too many changes to IFRS for SMEs as companies would have to follow changes in full IFRSs.

Lastly, the SMEs emphasised that they would benefit from a less abstract language and more examples in the IFRS for SMEs. At the same time they acknowledged that – just like for full IFRSs or German GAAP – additional literature will evolve providing examples and possible solutions to specific issues. A separate volume of examples, e.g. as part of the illustrative financial statements, could nevertheless be helpful. Despite the fact that German SMEs need to get used to a different accounting concept, most of them found that the wording could benefit from further simplification. Most difficult to understand were the sections on financial assets and financial liabilities (section 11) and on income taxes (section 28). While all SMEs need to apply, for instance section 11, in one way or another, some participating SMEs at first did not actually realize that they are within the scope of section

11 as to them it was not apparent that for example, plain receivables or payables were also addressed in this section.

4. Results on individual sections

Section 3: Financial Statement Presentation

No major results could be reported on this section. Due to the approach to the field test which did not require comparative information to be generated, there was no need to handle questions such as Going Concern, Frequency of Reporting and Comparative Information. Few companies actually prepared a full set of financial statements.

SMEs found it too costly and time consuming to prepare a full set of financial statements as part of these trial financial statements. But the companies did not see major difficulties understanding this section. The applicability cannot be evaluated in greater detail. Especially generating comparative information was not possible for the participating SMEs, as they based the trial financial statements on a different accounting background (German GAAP). A restatement would have been too costly to prepare in this field test.

Conclusion: ***For many participants it was too costly to prepare a full set of financial statements in this field test.***

Section 4: Balance Sheet

Questions about this section were not addressed by the participants of the field test. During the interviews with the companies, no questions or comments on this section came up, but they found the illustrative financial statements – containing a presentation scheme for a balance sheet – very helpful.

Conclusion: ***There were no problems understanding and applying this section.***

Section 5: Income Statement

Overall, this section was seen as comprehensible and easy to apply. There was only one company (listed company with total revenue > 100 m €), which rose the question whether par. 5.3 (e) concerning the presentation of discontinued operations was necessary as a single line item within the income statement.

Conclusion: ***There were no problems understanding and applying this section.***

Section 6: Statement of Changes in Equity and Statement of Income and Retained Earnings

This section was seen more critical concerning the comprehensibility and applicability of the standard. A sample structure of the statement of changes in equity was requested by several companies. The illustrative financial statement is not sufficient at this point, since it does not contain a statement of changes in equity.

Conclusion: ***Including guidance on statement of changes in equity in the illustrative financial statements could be helpful.***

Section 7: Cash Flow Statement

The comments on this section were generally positive. Six of the fifteen companies prepared a cash flow statement. In the interviews this topic was not addressed as critical. Moreover, those companies, which did not prepare a cash flow statement, felt that this section of the standard was comprehensible and applicable. Two companies were critical. But most preparers agreed that the cash flow statement was one of the main analysis tools of banks, who are as the most important users of their financial statements. One company (listed, total revenue > 100 m €) believed par. 7.13 (unrealised gains and losses arising from changes in foreign currency exchange rates) to be too burdensome.

Conclusion: ***The cash flow statement is seen as a useful instrument, the section was easy to understand and to apply.***

Section 8: Notes to the Financial Statements

The note requirements addressed in section 8 are generally seen as useful. Section 8 also provides a paragraph on the purpose of notes. Therefore, at this point a general statement on all disclosure requirements (as part of the notes or on the face of the balance sheet or income statement): The overall impression of participants familiar with IFRSs was, that disclosure requirements were reduced compared to full IFRSs. However, despite this reduction, most participants found the total amount of disclosure requirements not appropriate for SMEs. Disclosures were seen as either too cost intensive to derive or too sensitive to provide in the context of the specific SME environment.

Conclusion: ***Generally, a further reduction of disclosure requirements is necessary.***

Section 9: Consolidated and Separate Financial Statements

Participants asked for more guidance on which subsidiaries have to be consolidated or not (examples) as well as guidance for consolidation methods, acquisition and disposal dates. However, this section was relevant for only four out of the participating companies. These four participants (with group structures) belong to the group of the biggest corporations participating in this field test with a turnover of more than 51 m €.

Conclusion: ***This section should be improved. Topics addressed in section 9 should be part of an implementation guidance providing examples for SMEs.***

Section 10: Accounting Policies, Estimates and Errors

Comments on this section evolve around the hierarchy described in 10.2 – 10.4. As described in 3.2 of this report, SMEs found the general reference to full IFRSs troublesome as it remains unclear whether SME specific solutions can be derived at. While specifically larger SMEs were of the opinion that full IFRS would be relevant to derive accounting solutions, the majority of the SMEs thought it is crucial to not have to consider other IFRS literature.

Conclusion: ***Clarification of the hierarchy and the degree of relevance of full IFRSs needed.***

- **Section 11: Financial Assets and Financial Liabilities**

While in fact this section is usually relevant for all companies, the participants often felt that section 11 is relevant mostly for companies with hedging instruments. When the section was explained in more detail, companies noted that a clarification of the transactions addressed in the section (e.g. by using simpler language, less abstract wording) would be necessary. Overall, companies preferred cost accounting to be the default category, with fair value to only rarely be applied. Moreover, more guidance should be provided for certain transactions such as hedge accounting or factoring.

The five preparers explicitly commenting this section saw a medium or high relevance of financial instruments for their entity. Even hedge accounting seemed to be relevant in the areas of interest rate or cross currency swaps. The rest of the preparers deemed financial instrument not to be relevant for their entity. At least three preparers were not content with the accounting principles of financial instruments in the ED. They preferred to see more measurement at cost, at least for receivables and liabilities.

The main issue for the preparers was that this section is hard to understand. Participants felt that this section did not clearly address SME-specific issues.

For most SMEs the relevant financial instruments will be in the category to be accounted for at cost (particularly 11.7 a). This circumstance should be considered in drafting the standard. It should be aimed at deriving at more SME-specific requirements, for example the principle described in the standard is the effective interest rate method, but fixed interest rate liabilities/receivables – common in SMEs – are accounted for at notional amount which should therefore be laid out as the principle in the ED-IFRS for SMEs.

Some participants were of the opinion that the accounting principles are generally too complex and that they might have difficulties with the application. Others (in particular the ones which believed this section to be of high relevance) saw fewer difficulties; for example a widely discussed issue: “derivatives” did not seem problematic, as the issuing banks provide fair values. While generally the participants found hedge accounting requirements sufficient and beneficial, most problems seemed to appear in connection with effectiveness testing. Further guidance should be given with regard to hedging instruments typical in an SME environment. Other problems were seen with regard to factoring transactions (relevant, but not clear how to treat factoring) and the effective interest rate method.

Regarding the cost/benefit ratio again the views were mixed. The preparers giving financial instruments a higher relevance tentatively saw a higher benefit in the accounting principles of the ED than in those of local GAAP. This is in particular valid for hedge accounting.

Conclusion: ***Since to the participants this section is very hard to understand, simplifications and clarifications for SME-typical financial instruments seem to be needed. Additional guidance with regard to effectiveness testing is desirable. Amortised costs should be described at the prevalent principle.***

Section 12: Inventories

This section was overall evaluated positively concerning comprehensibility and applicability. Overall, the full cost approach as well as the cost formulas were appreciated and seen as beneficial for internal and external information. Several companies saw application problems with the full cost approach: usually a problem to determine the costs included (e.g. how to allocate transportation costs; how to determine cost not directly attributable to one product). Clarification of selling price as “estimated future selling price” could be helpful.

Conclusion: ***Guidance on the determination of costs for inventories would be helpful. The concept in general is appropriate, but the application in detail is still difficult.***

Section 13: Investments in Associates

The participants view was:
- options are highly appreciated.
- equity-method is more beneficial for external users, but also more costly to apply.
- options should be stated within IFRS for SMEs (i.e. no cross reference).

This section was relevant only for two out of the fifteen companies. These two belong to the group of the biggest corporations participating in this field test with a turnover of more than 51 m €.

Conclusion: ***Participants had no specific problems with regard to this section. If the options are available they should be explained within ED-IFRS for SMEs.***

Section 14: Investments in Joint Ventures

The participants view was:

- options are highly appreciated.
- equity-method is more beneficial for external users, but also more costly to apply (proportionate consolidation was not relevant).
- options should be stated within IFRS for SMEs (i.e. no cross reference).

This section was relevant for only two out of fifteen companies. These two belong to the group of the biggest corporations participating in this field test with a turnover of more than 51 m €.

Conclusion: ***Participants had no specific problems with regard to this section. If the options are available they should be explained within ED-IFRS for SMEs.***

Section 15: Investment Property

The participants view was:

- option between cost-method and fair-value-method rated beneficial by three companies for which investment properties are relevant; corporations still preferred cost-method, if no market prices exist.
- good cost/benefit ratio if market prices exist; if not, using DCF-method is too complex and time-consuming.

This section was relevant for only three out of the fifteen participating companies. Two belong to the group of the biggest corporations participating in this field test with a turnover of more than 51 m €. One company had a turnover of less than 8 m €.

Conclusion: ***The option to apply the fair value model is beneficial only to the point that market prices exist. Otherwise, no changes to this section needed.***

Section 16: Property, Plant and Equipment

A vast majority of the participants (twelve out of fifteen) considers this section easy to understand and to apply. It contains clear measurement rules. However, for some aspects more guidance should be provided: for example, on the determination of useful life and on the component approach.

The participants felt that the option to apply the revaluation method was not needed and separate measurement requirements for assets held for sale were seen as too burdensome for SMEs.
This section was relevant for all participants in this field test.

Conclusion: ***The IASB could provide more guidance, e.g. on the component approach.***

Section 17: Intangible Assets other than Goodwill

About half of the corporations criticized the section in total as too undifferentiated and unclear (differentiation between definite and indefinite life; differentiation between research and development). A clear guidance would be necessary, especially for the differentiation between research and development. Half of participants would use the option to capitalize the development cost. Those who would capitalize development costs found the cross-reference to IAS 38 very burdensome. The participating SMEs pointed out, however, that they to date do not have sufficient cost documentation structures to determine the cost of internally generated intangible assets.

Participants found the revaluation method unnecessary. This section has had relevance for all participants in this field test.

Conclusion: ***The participants agreed with the conceptual approach in this section. However, the IASB could provide more guidance on the differentiation between research and development.***

Section 18: Business Combinations and Goodwill

Participating companies did not have much experience with business combinations, but considered a possible application of this section rather difficult as it included very complex requirements and was unclear to them.

The disclosure of the cost of business combination is seen as very sensitive for SMEs. Overall, it appears that it would be very costly to apply these requirements while the benefits are rather limited.

This section has had relevance for only five of the participants.

Conclusion: ***The IASB should discuss this section again and try to reach material reliefs for SMEs, especially with regard to disclosure requirements.***

Section 19: Leases

The relevance of this section seemed to be quite high as eight preparers explicitly commented on leasing. Six of them more or less limited this relevance to lease accounting as lessee. Only two preparers also used lessor accounting, in particular in connection with operate leasing transactions (for one company it is the explicit business model).

Regarding the conceptual basis the preparers seemed to be content with the distinction between operate and finance leasing. However, most of the preparers commented that the corresponding section in the ED-IFRS for SMEs might be too complex as problems in the area of categorizing lease transactions are likely to arise. Some of them suggested that examples and quantitative thresholds might help. It was also mentioned that fair value accounting for the leased assets is less practicable than minimum lease payments. In addition, the two participants applying lessor accounting requirements felt that the fallback to IAS 17 was problematic.

Most participants saw a medium or high benefit of the proposed lease accounting but also possible high costs for the preparation of the accounts.

Conclusion: ***The IASB should provide additional guidance and examples for SMEs so that it will be easier for them to categorize lease contracts.***

Section 20: Provisions and Contingencies

This section was comprehensive for all companies concerning recognition criteria, initial measurement and subsequent measurement. Participating SMEs said not to have provisions with significant effects from discounting. The discounting requirement was predominantly seen positively.

Conclusion: ***No changes to this section necessary.***

Section 21: Equity

The distinction between equity and liability presents a major issue for many SMEs in Germany, including some of the corporations participating in this field test. For German SMEs with certain legal forms this section does not reflect the economic substance and is therefore not in line with the principle of substance over form. It was criticized as too undifferentiated. Furthermore, a clear guidance on the differentiation between equity and liability seems necessary and participants suggested that changes to IAS 32 should be integrated in the SME standard.

This section is relevant for all field test participants. Five corporations have had major problems applying this section, because they were partnerships or cooperatives and therefore had no equity under IFRS for SMEs.

Conclusion: ***The amendment to IAS 32 should be integrated in the IFRS for SMEs in order to reflect economic situation in partnerships.***

Section 22: Revenue

One focus was on the percentage of completion method (PoC). Only for four companies accounting requirements for construction contracts were actually relevant. These companies had a positive view on the comprehensiveness of the PoC-method. Examples to the section were considered useful. Overall, participants associated high benefit for internal and external users with the proposed accounting treatment even though the costs to provide the information were estimated as being high as well.

Conclusion: ***No changes to this section needed.***

Section 23: Government Grants

This section was relevant for two of the participating SMEs. Generally the concept is understandable and easy to apply. But the entities found the description of the options rather unclear. The entities found it favourable to apply the IAS 41 option.

Conclusion: ***Clarification needed on the content of each option.***

Section 24: Borrowing Costs

Entities did not comment on this section.

Conclusion: ***Not applicable.***

Section 25: Share-based payments

Share-based payments were not relevant for the participating entities.

Conclusion: ***Not applicable.***

Section 26: Impairment of Non-financial Assets

The participants felt that the definition of the triggering events was difficult to understand which made it difficult to apply the section. Furthermore, participants felt uncomfortable with the relinquishment of the value in use notion. Because the fair value does not reflect user specific synergies, they are concerned about write-offs which lack economic justification. Overall, participants rejected the triggering event and suggested the amortisation of goodwill for reason of simplicity.

This section was relevant for eight of the participants.

Conclusion: ***The IASB should reconsider the amortisation of goodwill instead of using the triggering event approach. Furthermore, the value in use should be reconsidered as a measurement basis.***

Section 27: Employee Benefits

Employee benefits were only of little relevance for the participating companies. There were five preparers with defined benefit (one of them with only one contract) and defined contribution plans. The comprehensibility of the standard concerning recognition and measurement was satisfying. The companies were asked to evaluate the impact of the recognition and measurement rules to the financial statements. There would be a considerable impact on the volatility of net earnings. The use of information for internal and external users was considered high, the accounting provisions would lead to a realistic presentation of the economic reality of the company. With regard to the costs, companies emphasized the need of expert opinions.

Since employee benefits are of little relevance, there is only a little effect on profit or loss for the participating SMEs. Therefore, SMEs were indifferent to the options and considered the suggested approach as the easiest.

Conclusion: ***No changes to this section needed, as participating companies generally outsource the determination of the benefit obligation.***

Section 28: Deferred Taxes

Deferred taxes were of high relevance for the preparers and all participants explicitly commented on this topic. The opinions about the conceptual basis of this section were mixed: Half of the preparers agreed with the concept. The others disagreed with the approach or argued that it is too complex and not intuitive for SMEs. Particular problems were raised concerning:

- tax loss carry forward (SMEs doubt the reliability of tax assets on carry forwards because of very short forecast horizons, or none existing forecasts in SMEs);
- explanations of the concept should be improved (usage of the similar sounding terms ‘timing’ and ‘temporary’ differences).

Regarding the understandability of the section the views were similarly divided. Problems were raised primarily with regard to determining the recognizable amount of tax loss carry forwards and the offsetting of deferred tax assets and liabilities.

Most preparers could see a medium or high benefit of the accounting for deferred taxes but are also of the opinion that high costs for the preparation of the accounts will occur.

Conclusion: ***The approach suggested is difficult to understand. It would be easier if the IASB would stick to one concept, being either the timing or the temporary concept (i.e. wording). SMEs were divided on the need/benefit of accounting for deferred taxes.***

Sections 29: Financial Reporting in Hyperinflationary Economies

This issue was not applicable for the participating SMEs.

Conclusion: ***Not applicable.***

Sections 30: Foreign Currency Translation

This section was irrelevant for some of the participants which have no transactions abroad at all. For other participants with international businesses the section was very relevant. Most preparers seemed to be content with the approach of the functional currency.

Those seeing relevance in this section feel that the understandability is given with regard to determining the functional currency and the treatment of foreign currency transactions. Few participants commented on hedge accounting or the treatment of foreign currency net investments which to them seemed less understandable. No comments were made on reconciling functional currency into reporting currency, since it was not applicable.

Conclusion: ***The participants supported the functional currency approach. More guidance on the application of net investments in a foreign operation would be helpful.***

Sections 31: Segment Reporting

There was no company in the field study, which used the option to disclose information about operating segments corresponding to IFRS 8. This link to full IFRSs was not specifically discussed, but generally speaking the participants felt that cross references were too burdensome.

Conclusion: ***The standard does not require segment information. Therefore this section and the link to full-IFRS implied no problems to the preparers.***

Sections 32: Events after the End of the Reporting Period

This section was neither applied nor discussed by the companies. For the reason of partial financial statements, prepared for one period only, the preparers were not concerned by this section.

Conclusion: ***Not applicable.***

Sections 33: Related Party Disclosures

All preparers commenting on this section believed related party disclosures to be highly relevant for their entity. In particular companies frequently commented on the disclosures of key management personnel compensation. Some preparers had doubts about the concept of related party disclosures in the ED. The relevance of this information in a non-listed environment was questioned. Furthermore, some preparers claimed that disclosures of related party transaction might cause a competitive disadvantage for SMEs.

Several SMEs seemed to have problems with the understandability of this section (e.g. particularly referring to paragraphs 33.7 to 33.10). They had the opinion that these disclosure requirement for certain transactions are too complex and that they might have difficulties with the application. Regarding the cost/benefit ratio several preparers connected their response on section 33 to their general statements about disclosure requirements. Most of them said that the disclosure requirement – although reduced compared to full IFRS – are still too complex for SMEs. Some preparers admitted that the information regarding related party disclosures are beneficial to users. Others were concerned that related party disclosures might contain sensible data which might cause indirect or opportunity costs. Several SMEs (mainly “owner management entities”) saw less need for disclosures, but argued that in particular disclosures of key management personnel are private information, not to be published for external users.

Conclusion: ***There is general doubt about the concept as some SMEs fear competitive disadvantages. They are particularly worried about information about key management personnel compensation.***

Sections 34: Earnings per Share

This section was not relevant for the participating companies.

Conclusion: ***Not applicable.***

Sections 35: Specialised Industry

This section was not relevant for the participating companies.

Conclusion: ***Not applicable.***

Sections 36: Discontinued Operations and Asset Held for Sale

The majority of the participants felt that separate measurement requirements for assets held for sale were too burdensome and were not adequate from a cost/benefit point of view.

Conclusion: ***Due to the additional burden, participants did not support different measurement requirements for discontinued operations/asset held for sale.***

Sections 37: Interim Financial Reporting

This section was not discussed in detail in this field test.

Conclusion: ***Not applicable.***

Sections 38: Transition to the IFRS for SMEs

Participants felt that this section was difficult to apply. Questions arose as to how the impracticability clause was to be interpreted. For example, companies wondered whether as a result of this section, a German GAAP balance sheet could be the opening balance sheet. It also seemed possible to them that in applying this section, only some items need to be transferred to IFRS for SMEs, while others are still measured at German GAAP (as long as it is impracticable to measure at IFRS for SMEs).

Conclusion: ***Clarification is necessary.***

5. Brief summary

The field test was an interesting experience for all SMEs, which had very different motives to participate in the field testing. Overall, it must be noted that the participating companies needed the support of SMPs or additional IFRS-literature to apply the ED-IFRS for SMEs. There are various reasons why SMEs found it troublesome to apply the ED-IFRS for SMEs, among which is the different German accounting background, little or no experience with IFRS in general or the lack of time to look at every accounting issue in great detail. However, while supporting the overall approach of the ED-IFRS for SMEs, the participants also had to deal with the complexity of the draft, which made it difficult to prepare financial statements in accordance with the ED.

Due to the different current accounting environment in Germany often the prerequisites to apply the ED-IFRS for SMEs (IT-system or internal documentation structures) did not exist. Therefore, apart from the complexity of the ED-IFRS for SMEs companies also encountered many problems not inherent in this exposure draft but in the change from one accounting system to another.

With regard to the ED-IFRS for SMEs it can be noted that the majority of the companies supported the approach taken and felt that the requirements would generally be well understandable and applicable due to explanations and examples given within the standard. Nevertheless, many participants pointed out that they would expect to encounter problems when having a closer look at the details of the requirements. In parts, such as subsequent accounting for goodwill, deferred taxes or pensions, the majority of the participants did not agree with the conceptual approach in the SME standard. According to the participants, the major drawback was the sheer extent of required information that would make the application of the IFRS for SMEs very burdensome especially for smaller SMEs. Therefore, participants suggested the IASB should again discuss the disclosure requirements. Many participants pointed out that examples or further guidance would be of great value, especially for accounting issues that virtually all SMEs encounter.

Overall, the participants – very much depending on the entity-size – were split about the further relevance of an IFRS for SMEs in their company. While the smaller SMEs reject the application of the IFRS for SMEs as they do not see any additional value in doing so, larger companies believe that IFRS in general or an accounting standard for SMEs could be relevant for them in the medium-term. Few will also actively seek changes in their accounting system. To the understanding of the participants, the acceptance of an IFRS for SMEs will heavily depend upon further reductions of complexity of the IFRS for SMEs in order to reduce the burden to prepare those financial statements but also the general acceptance of an IFRS for SMEs will be crucial. Without adoption in the EU most participants are not considering applying IFRS for SMEs optionally due to cost/benefit considerations. Others fear that this SME-standard might internationally be viewed as “second-class” accounting, which would make the application of it infeasible for them.