May 2015

Project Summary and Feedback Statement

Initial comprehensive review of the *IFRS for SMEs*

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for SMEs

At a glance

In May 2015 the IASB completed its comprehensive review of the *IFRS for SMEs*. After consulting widely with constituents, the IASB concluded that the *IFRS for SMEs* is working well in practice. However, some areas were identified where targeted improvements could be made. Consequently, after considering the feedback it received, and taking into account the fact that the *IFRS for SMEs* is still a relatively new Standard, the IASB has made limited amendments to the *IFRS for SMEs*.

The most significant amendments that relate to transactions commonly encountered by SMEs are:

- permitting SMEs to use a revaluation model for property, plant and equipment; and
- aligning the main recognition and measurement requirements for deferred income tax with International Financial Reporting Standards (IFRS, sometimes referred to as 'full IFRS' when compared to the *IFRS for SMEs*).

Most of the other amendments clarify existing requirements or add supporting guidance, rather than change the underlying requirements in the *IFRS for SMEs*. Consequently, for most SMEs and users of their financial statements, the amendments are expected to improve understanding of the existing requirements, without having a significant effect on an SME's financial reporting practices and financial statements.

The amendments are effective for annual periods beginning on or after 1 January 2017. Earlier application is permitted.

Why did the IASB undertake an initial comprehensive review of the *IFRS for SMEs*?

The IASB issued the *IFRS for SMEs* in July 2009 in response to international demand for the IASB to develop global standards for small and medium-sized entities (SMEs). The *IFRS for SMEs* was developed using IFRS as a starting-point and then considering what modifications are appropriate in the light of the needs of users of SME financial statements and cost-benefit considerations. The *IFRS for SMEs* was developed over a five year period and included opportunities for public input at several stages throughout the process.

When the *IFRS for SMEs* was issued, the IASB stated that it planned to undertake an initial comprehensive review of the *IFRS for SMEs* after two years of use by SMEs to consider whether there was a need for any amendments.

Specifically, the IASB said it would consider whether to amend the *IFRS for SMEs* to address any implementation issues identified and also whether to consider any changes made to IFRS since the *IFRS for SMEs* was published.

Soon after the *IFRS for SMEs* was issued, the IFRS Foundation set up the SME Implementation Group (SMEIG), an international advisory group to the IASB, consisting of those that have experience preparing, using or advising on SME financial statements. The aim of the SMEIG is to support international adoption of the *IFRS for SMEs*, monitor its implementation and advise on any amendments to the Standard.

The IASB decided to commence its initial comprehensive review in 2012, with support from the SMEIG, based on its view that sufficient jurisdictions had adopted the *IFRS for SMEs* by 2010 to provide broad insight into the implementation experience.

Today, out of the 140 jurisdiction profiles posted on our website so far, 72 jurisdictions permit or require the *IFRS for SMEs* and an additional 14 are currently considering plans to adopt it.

Amendments to the *IFRS for SMEs*

The IASB made a limited number of changes to the *IFRS for SMEs*. These changes are discussed below:

Amendments that introduce accounting policy options (available in IFRS)

- Option to use the revaluation model for property, plant and equipment.
- Option to use the equity method for investments in subsidiaries, associates and jointly controlled entities in separate financial statements, if presented.

Amendments that change requirements

Changes most likely to affect SMEs:

- Alignment of the main recognition and measurement principles for income tax with IFRS.
- Modification of the criteria to be a basic debt instrument to ensure that most simple loans qualify for amortised cost measurement.
- Requirement that if the useful life of goodwill or another intangible asset cannot be established reliably, management's best estimate is used, but must not exceed 10 years. Previously a default 10-year life was presumed in such cases.

Changes to the requirements for the following less commonly encountered transactions by SMEs (not expected to affect most SMEs):

- Liabilities extinguished by issuing the entity's own equity instruments, such as shares.
- Leases with an interest rate variation clause linked to market interest rates.
- Compound financial instruments with complex characteristics.
- Exploration and evaluation assets.

Amendments that add undue cost or effort exemptions and requirements

Amendments that exempt an entity from the following requirements when application would cause undue cost or effort:

- Measurement of investments in equity instruments at fair value.
- Recognising intangible assets separately in a business combination.
- Offsetting income tax assets and liabilities.
- Measuring the liability to pay a non-cash dividend at the fair value of the assets to be distributed.

The IASB has also added guidance to emphasise that an undue cost or effort exemption is not intended to be a low hurdle. In particular, an entity is required to carefully weigh the expected effects of applying the exemption on the users of its financial statements against the cost or effort of complying with the related requirement.

Amendments that add other exemptions (based on similar exemptions in IFRS)

- Two common control exemptions:
  - An exemption from the fair value measurement requirements for equity issued in a business combination of entities under common control.
  - An exemption from the fair value measurement requirements for distributions of non-cash assets controlled by the same parties before and after the distribution.

- An exemption that simplifies the accounting requirements when part of an item of property, plant and equipment is replaced.

Amendments that modify presentation or disclosure requirements

- Requirement that an entity must disclose its reasoning for using any undue cost or effort exemption.
- Requirement that investment property measured at cost less accumulated depreciation and impairment is presented separately on the face of the statement of financial position.
- Requirement that entities group items presented in other comprehensive income on the basis of whether they are potentially reclassifiable to profit or loss.
- Alignment of the definition of a related party with IFRS. The revised definition is unlikely to affect most related party relationships.
- Relief from disclosing prior year reconciliations of balances for biological assets and share capital and from disclosing the accounting policy for termination benefits (for consistency with other requirements of the *IFRS for SMEs*).

Amendments for first-time adopters

The IASB has included three options and two new area of guidance for first time adopters of the *IFRS for SMEs* based on amendments to IFRS issued since the *IFRS for SMEs* was published.

Amendments that provide minor clarifications

The remaining amendments are minor and are not expected to result in changes in practice or to affect the financial statements for most SMEs. Such amendments are of the following types:

- clarifying definitions or guidance;
- clarification of the scope of a few sections; and
- redrafting of unclear requirements or removing minor inconsistencies.

Transition and effective date

Entities reporting using the *IFRS for SMEs* are required to apply the amendments for annual periods beginning on or after 1 January 2017. Earlier application is permitted provided all of the amendments are applied at the same time.

Amendments must be applied retrospectively, unless impracticable, with the following exceptions:

- If an entity chooses to apply the revaluation model to any classes of property, plant and equipment, it must apply the related requirements prospectively from the beginning of the period (ie the period in which it first applies the amendments).
- An entity is permitted to apply the revised income tax requirements prospectively from the beginning of the period.
- An entity must apply the clarified terminology ‘date of acquisition’ prospectively from the beginning of the period (only applicable if an entity has business combinations).

Changes made to the proposals in the 2013 Exposure Draft

The IASB published the Exposure Draft in October 2013 (2013 ED) with a five-month comment period. 57 comment letters were received. Most respondents supported the majority of the IASB's proposed amendments.

The result of the IASB's consideration of the issues raised by respondents is that three significant changes and a few other changes were made to the proposals in the 2013 ED.

The three significant changes are:

- adding an option to use the revaluation model for property, plant and equipment;
- aligning the main recognition and measurement requirements for exploration and evaluation assets with IFRS; and
- simplifying the transition requirements, to give relief from retrospective application in specific cases.

Some of the more notable other changes:

- requiring an entity to disclose its reasoning for using any of the undue cost or effort exemptions;
- requiring investment property measured at cost less accumulated depreciation and impairment to be presented separately on the face of the statement of financial position;
- permitting an option for an entity to account for investments in subsidiaries, associates and jointly controlled entities in its separate financial statements using the equity method; and
- adding an undue cost or effort exemption from the requirement to measure the liability to pay a non-cash dividend at the fair value of the assets to be distributed.

Due process and outreach activities

In June 2012 the IASB issued a Request for Information (RFI) to seek the views of those who have been applying the *IFRS for SMEs*, users of financial information prepared in accordance with the *IFRS for SMEs*, national standard-setters and all other interested parties, on whether there is a need to make any amendments to the *IFRS for SMEs*. In addition to encouraging respondents to raise their own issues, the RFI asked specific questions on matters frequently raised with the IASB by interested parties and also relating to changes to IFRS since the *IFRS for SMEs* was published (referred to as 'new and revised IFRSs').

After considering the feedback it received on the RFI, the IASB issued the 2013 ED. In order to supplement the views it received on the RFI and 2013 ED, the IASB staff also performed additional outreach with providers of finance to SMEs.

Respondents identified few significant new issues. However they highlighted some areas where targeted improvements to the *IFRS for SMEs* could be made. Consequently, after considering that feedback, but also considering the importance of maintaining stability during the early years of implementing the Standard, the IASB made limited amendments to the *IFRS for SMEs*.

Throughout the initial comprehensive review the IASB worked closely with, and sought the advice of, the SMEIG. The IASB and the staff also held interactive sessions at meetings of the IFRS Advisory Council and World Standards-setters on the main issues in the comprehensive review.

The four main areas where interested parties had the most significant comments during the comprehensive review were:

- the scope of the *IFRS for SMEs*;
- the IASB's approach for dealing with new and revised IFRSs;
- permitting accounting policy options, in particular for the revaluation of property, plant and equipment; and
- future reviews of the *IFRS for SMEs*.

The IASB's reasoning for how it addressed the above issues is explained in the following pages.

Scope of the *IFRS for SMEs*

The *IFRS for SMEs* is intended for SMEs, defined to be those entities that publish general purpose financial statements for external users but do not have public accountability. Paragraph 1.5 of the *IFRS for SMEs* prohibits publicly accountable entities from stating compliance with the *IFRS for SMEs*. The 2013 ED proposed no change to this restriction.

Respondents' comments

Some respondents to the 2013 ED said that paragraph 1.5 is too restrictive and local authorities and standard-setters should have the authority to decide which publicly accountable entities in their jurisdiction should be able to use and state compliance with the *IFRS for SMEs*.

Our response

The *IFRS for SMEs* was specifically designed for entities without public accountability. The IASB observed that it may not be appropriate for a wider group of entities. The IASB also noted that if the scope was widened to include some publicly accountable entities, it might lead to pressure to make changes to the *IFRS for SMEs* to address issues from that wider group, which would increase the complexity of the *IFRS for SMEs*. The IASB also had concerns about the risks associated with the inappropriate use of the *IFRS for SMEs* if the restriction was removed.

The IASB noted that jurisdictions can incorporate the *IFRS for SMEs* into their local accounting regime if they wish to allow some publicly accountable entities to use it. However, those entities would state compliance with local GAAP, not with the *IFRS for SMEs*.

Consequently the IASB decided to keep the restriction in paragraph 1.5.

In the 2013 ED the IASB clarified that its primary aim when developing the *IFRS for SMEs* was to provide a stand-alone, simplified set of accounting principles for entities that do not have public accountability and that typically have less complex transactions, limited resources to apply IFRS and that operate in circumstances in which comparability with their listed peers is not an important consideration.

Respondents' comments

Some respondents expressed concern that there was a disparity between the scope (all entities that do not have public accountability) and the primary aim of the IASB, perceived to be a focus on the smaller/less complex entities in the scope.

Other respondents had concerns that the *IFRS for SMEs* is too complex for some small owner-manager entities.

Our response

The *IFRS for SMEs* is intended for all SMEs. Nevertheless, the IASB observed that when deciding on the content of the *IFRS for SMEs*, its primary aim was to focus on the kinds of transactions encountered by SMEs that typically have less complex transactions, limited resources to apply IFRS and that operate in circumstances in which comparability with their listed peers is not an important consideration. If the *IFRS for SMEs* covered all possible transactions that SMEs may enter into, it would have had to retain most of the content of IFRS.

The IASB observed that if an entity has complex transactions and activities, it would be expected to have more sophisticated systems and greater resources/expertise, and so may find IFRS more suitable to its reporting needs. Consequently the IASB continues to support its primary aim in developing the *IFRS for SMEs*.

The IASB also noted that the *IFRS for SMEs* is intended for entities that are required, or elect, to publish general purpose financial statements. These are financial statements directed to the needs of a wide range of users who are not in a position to demand reports tailored to their particular information needs. The *IFRS for SMEs* is not intended for small owner-managed entities preparing financial statements solely for tax reasons or to comply with local laws. However, those entities may still find the *IFRS for SMEs* helpful in preparing such financial statements.

New and revised IFRSs

One of the most significant issues confronting the IASB during the comprehensive review was how the *IFRS for SMEs* should be updated in the light of the new and revised IFRSs issued after the *IFRS for SMEs* was issued in 2009—in particular, how to balance the importance of maintaining alignment with IFRS with having a stable, stand-alone Standard that focuses on the needs of SMEs.

In developing the 2013 ED the IASB considered each of the new and revised IFRSs that had been published individually. On the basis of this assessment, and considering the importance of maintaining stability during the early years of implementing the *IFRS for SMEs*, the IASB proposed to incorporate some minor changes to IFRS that were relevant to SMEs and that clarified or simplified requirements or addressed a problem. However, the IASB proposed not to incorporate some more significant changes, including those in IFRS 3 (2008) *Business Combinations*, IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements*, IFRS 13 *Fair Value measurement* and IAS 19 (2011) *Employee Benefits*.

Respondents' comments

Some respondents said that complex changes should not be introduced for SMEs until sufficient implementation experience exists under IFRS and supported the IASB's decision not to incorporate changes in IFRS 3 (2008), IFRS 10, IFRS 11, IFRS 13 and IAS 19 (2011). In contrast, others thought that the *IFRS for SMEs* should be closely aligned with IFRS during this review to prevent a long time lag.

Others respondents asked the IASB to clarify the criteria it used during this initial review, and will use in future reviews, for assessing whether and when changes to IFRS should be incorporated in the *IFRS for SMEs*.

Our response

The IASB noted that there is a greater need for stability during this initial review period than there may be in future review periods. Although the *IFRS for SMEs* was issued in 2009, in many of the jurisdictions that have adopted it the *IFRS for SMEs* has been effective for a shorter period of time. In addition, in jurisdictions that permit, instead of require, the *IFRS for SMEs*, many SMEs have only started the transition to it. As a result, for the majority of SMEs it is still a new Standard. Consequently the IASB decided that its basis for making limited changes for new and revised IFRSs during this initial review was appropriate.

The IASB noted its intention to discuss to what extent a more developed framework for future reviews of the *IFRS for SMEs* should be established before the next review of the *IFRS for SMEs*.

Adding options to the *IFRS for SMEs*

IFRS permits a choice between the cost and revaluation model for property, plant and equipment. The *IFRS for SMEs* requires the cost model to be used.

IFRS requires the capitalisation of borrowing and development costs that meet certain criteria; otherwise they are recognised as expenses. The *IFRS for SMEs* simplifies the requirements in IFRS by requiring all borrowing and development costs to be recognised as expenses.

The 2013 ED did not propose to change these requirements.

Respondents' comments

The most common and widespread concern by respondents to the 2013 ED was the decision of the IASB not to propose to add an accounting policy option for the revaluation of property, plant and equipment. Some respondents also asked the IASB to consider permitting options to capitalise development costs or borrowing costs.

Our response

Users of SME financial statements that need to understand the accounting policies used, and that make comparisons between different SMEs, have said that they prefer SMEs to have no, or only limited, accounting policy options. The IASB also noted that adding additional options to the *IFRS for SMEs* adds complexity throughout the Standard. Consequently the IASB supports restricting options in the *IFRS for SMEs*.

Nevertheless, on the basis of the responses received, the IASB acknowledged that not allowing a revaluation model for property, plant and equipment appears to be the single biggest impediment to adoption of the *IFRS for SMEs* in some jurisdictions. The IASB also agreed with those respondents who stated that current value information is potentially more useful than historical cost information. The IASB therefore decided that the benefits of a wider use of the *IFRS for SMEs*, and hence the potential for global improvements in reporting and consistency, together with the usefulness of the information provided, outweigh the perceived costs to users and preparers of financial statements of adding this option.

The IASB also noted that there was nothing to prevent authorities and standard-setters in individual jurisdictions from requiring all SMEs in their jurisdiction to use only the cost model (or only the revaluation model) for property, plant and equipment. Such action would not prevent SMEs from stating compliance with the *IFRS for SMEs*.

However, the IASB noted that allowing options to capitalise certain development and borrowing costs would involve different considerations than allowing a revaluation option for property, plant and equipment. This is because the *IFRS for SMEs* simplifies the requirements in IFRS, instead of removing an option permitted by IFRS. Consequently, permitting options to capitalise development and borrowing costs meeting certain criteria would result in more accounting policy options than IFRS. The IASB noted that it continues to support its rationale for requiring the recognition of all development and borrowing costs as expenses, for cost-benefit reasons.

Future reviews of the *IFRS for SMEs*

When the *IFRS for SMEs* was issued the IASB stated that after the initial review, it expected to propose amendments to the *IFRS for SMEs* by publishing an omnibus Exposure Draft approximately once every three years. It also noted that, on occasion, it may identify a matter for which an amendment may need to be considered earlier than in the normal three-year cycle; for example to address an urgent issue.

The 2013 ED asked whether respondents agreed with this tentative plan for maintaining the *IFRS for SMEs*.

Respondents' comments

Respondents were evenly divided on whether the IASB should aim to update the *IFRS for SMEs* approximately once every three years, or if it should follow a longer cycle, with five years being the most common alternative suggestion.

Most respondents were supportive of the IASB addressing urgent issues outside the normal review cycle, but some had concerns that urgent issues should only be addressed in rare cases to provide a stable platform for SMEs.

Our response

The IASB tentatively agreed on the following approach for future reviews:

- a comprehensive review should start approximately two years after the effective date of the amendments from a previous comprehensive review. This would allow time for SMEs to apply the amendments, and for interested parties to identify any implementation issues that arise from those amendments. Comprehensive reviews would likely begin with the issuance of a Request for Information document.
- between comprehensive reviews, the IASB, with input from the SMEIG, would decide whether there is a need for an interim review to consider new and revised IFRSs not yet incorporated or any urgent amendments that have been identified. Urgent amendments on their own would be expected to be rare.

This approach would mean that amendments to the *IFRS for SMEs* would not be expected to be more frequent than once every three years, to provide SMEs with a stable platform.

Further information

SME webpages: http://go.ifrs.org/IFRSforSMEs

Use of the *IFRS for SMEs* around the world:
http://www.ifrs.org/Use-around-the-world/Pages/Analysis-of-SME-profiles.aspx

A complete revised 2015 version of the *IFRS for SMEs* (a version with all the amendments incorporated that has also been subject to a full editorial review) will be made available on the SME webpages of the IASB website shortly after the amendments are issued, together with a complete mark-up of the *IFRS for SMEs*, which includes all paragraphs/subparagraphs of the Standard.

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