

Draft Comment Letter

Comments should be submitted by 11 February 2014 to
commentletters@efrag.org

31 October 2013

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

Dear Sir/Madam,

Re: Proposed amendments to the International Financial Reporting Standard for Small and Medium-sized Entities (IFRS for SMEs).

On behalf of the European Financial Reporting Advisory Group (EFRAG), I am writing to comment on the proposed amendments to the International Financial Reporting Standard for Small and Medium-sized Entities (IFRS for SMEs), issued by the IASB on 3 October 2013 (the 'ED').

EFRAG welcomes the proposed amendments to the IFRS for SMEs and appreciates the IASB's efforts to consider the issues identified during the Request for Information (RfI) process.

EFRAG's starting point when answering the specific questions included in the Exposure Draft was that IFRS for SMEs should only be changed when the suggested change addresses an identified problem for SMEs and the change is likely to solve that problem and thus result in improved financial reporting for its intended users.

EFRAG broadly agrees with the IASB's developed framework for how to deal with new and revised IFRS during future reviews of the IFRS for SMEs, except that we think the IFRS for SMEs should not be changed based on changes in full IFRS that have not yet been implemented. We also consider that post-implementation reviews of new and revised IFRS represent the best opportunity to assess the suitability of the changes for SMEs and users of their financial statements. We do not support this suitability to be assessed at the same time as the changes to full IFRS are open to consultation, because it would de facto call for too heavy a consultation burden on those who have an interest in the IFRS for SMEs

EFRAG supports the IASB's proposal to align the main principles of Section 29 *Income Tax* with IAS 12 *Income Taxes* for the recognition and measurement of deferred tax. In our view, extensive experience already exists in relation to calculating deferred tax in accordance with IAS 12 *Income Taxes* and it will, therefore, be easier to transfer this knowledge to SMEs when both requirements are aligned.

EFRAG is generally against allowing accounting policy options in the IFRS for SMEs as the induced lack of comparability amongst entities using IFRS for SMEs is contrary to the need of users to have financial reporting as standardized as possible. It also increases the complexity of the standard and increases the costs related to the application of the standard for both preparers and users. It is on this basis that we recommend to eliminate the option of how to recognise all actuarial gains and losses and mandate that they are recognised in other comprehensive income and hence align the IFRS for SMEs on full IFRS.

We also acknowledge the fact that the IASB discussed the use of options and concluded that there were no convincing arguments in favour of introducing further accounting policy options in IFRS for SMEs. However, we consider important that the IFRS for SMEs is developed as a global standard that can be applied by many entities. Therefore, its applicability to entities operating in diverse economic environments should also be factored in when considering whether certain options should be allowed. We also believe that there are situations where an option to apply a sophisticated requirement (e.g. revaluation model) could result in more relevant and more reliable information for users of SMEs. Furthermore, we believe that the negative effects of adding specific accounting policy options can be outweighed by the increase of the number of SMEs adopting IFRS for SMEs, which would enhance the overall comparability of financial statements of SMEs, and increased usefulness of the information provided to users.

On this basis, EFRAG believes that, as earlier indicated in the EFRAG's response to the IASB's Request for Information (RfI) dated 20 December 2012, it would be beneficial to:

- permit the revaluation model for Property, Plant and Equipment to be used on a similar basis to IAS 16 *Property, Plant and Equipment*;
- permit an option for the borrowing costs directly attributable to the acquisition, construction or production of a 'qualifying asset' to be capitalised on a similar basis to IAS 23 *Borrowing Costs*; and
- permit an option for development costs to be capitalised on similar basis to IAS 38 *Intangible Assets*.

Our detailed comments and responses to the questions in the ED are set out in the Appendix.

If you would like to discuss our comments further, please do not hesitate to contact Filipe Camilo Alves, Apostolena Theodosiou or me.

Yours faithfully,

Françoise Flores
EFRAG Chairman

APPENDIX

Question 1 – Definition of ‘fiduciary capacity’

The IASB has received feedback that the meaning of ‘fiduciary capacity’ in the definition of ‘public accountability’ (see paragraph 1.3(b) of the IFRS for SMEs) is unclear as it is a term with different implications across jurisdictions. However, respondents generally did not suggest alternative ways of describing public accountability or indicate what guidance would help to clarify the meaning of ‘fiduciary capacity’. Based on the outreach activities to date, the IASB has determined that the use of this term does not appear to create significant uncertainty or diversity in practice.

- (a) Are you aware of circumstances where the use of the term ‘fiduciary capacity’ has created uncertainty or diversity in practice? If so, please provide details.
- (b) Does the term ‘fiduciary capacity’ need to be clarified or replaced? Why or why not? If you think it needs to be clarified or replaced, what changes do you propose and why?

Notes to constituents

- 1 *According to paragraph 1.3 of the IFRS for SMEs an entity has public accountability if (the IASB proposed amendments are underlined and strikethrough):*
 - (a) *its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market; or*
 - (b) *it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. Most ~~This is typically the case for banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks~~ will meet this second criterion.*
- 2 *In addition paragraph 1.4 of the IFRS for SMEs states that some entities may also hold assets in a fiduciary capacity for a broad group of outsiders because they hold and manage financial resources entrusted to them by clients, customers or members not involved in the management of the entity. However, if they do so for reasons incidental to a primary business (as, for example, may be the case for travel or real estate agents, schools, charitable organisations, co-operative enterprises requiring a nominal membership deposit, and sellers that receive payment in advance of delivery of the goods or services such as utility companies), that does not make them publicly accountable.*
- 3 *As noted in BC22 of the ED the term fiduciary capacity is unclear for some respondents to the RfI as it is a term with different implications across jurisdictions. However, the IASB has conducted outreach activities and has determined that the use of this term does not appear to create significant uncertainty or diversity in practice.*

EFRAG's response

EFRAG welcomes the proposed amendments to paragraph 1.3(b) and the IASB's efforts to clarify the term 'fiduciary capacity' in the standard to help local authorities/ standard setters and entities to apply the current definition of public accountability.

- 4 EFRAG welcomes the proposed changes to paragraph 1.3 (b) of the IFRS for SMEs which, in our view, clarify the scope of application of the term 'fiduciary capacity.'
- 5 Although we acknowledge that the training material on IFRS for SMEs is prepared by IFRS Foundation education staff and this is not approved by the IASB, we suggest the IASB to include a reference (e.g. in its preface) that the accompanying training material for each section is available to demonstrate how IFRS for SMEs is intended to be implemented in practice. We consider that the proposed amendments together with training material, which should be reviewed and revised at the same time the IFRS for SMEs is reviewed, should solve the issues identified in practice.

Question 2 - Accounting for income tax

The proposal to align the main principles of Section 29 *Income Tax* with IAS 12 *Income Taxes* for the recognition and measurement of deferred tax (see amendment number 44 in the list of proposed amendments at the beginning of this Exposure Draft) is the most significant change being proposed to the IFRS for SMEs.

When the IFRS for SMEs was issued in 2009, Section 29 was based on the IASB's Exposure Draft *Income Tax* (the '2009 ED'), which was issued in March 2009. However, the 2009 ED was never finalised by the IASB. Consequently, the IASB has concluded that it is better to base Section 29 on IAS 12. The IASB proposes to align the recognition and measurement principles in Section 29 with IAS 12 (see paragraphs BC55–BC60) whilst retaining some of the presentation and disclosure simplifications from the original version of Section 29.

The IASB continues to support its reasoning for not permitting the 'taxes payable' approach as set out in paragraph BC145 of the IFRS for SMEs that was issued in 2009. However, while the IASB believes that the principle of recognising deferred tax assets and liabilities is appropriate for SMEs, it would like feedback on whether Section 29 (revised) can currently be applied (operationalised) by SMEs, or whether further simplifications or guidance should be considered.

A 'clean' version of Section 29 (revised) with the proposed changes to Section 29 already incorporated is set out in the appendix at the end of this Exposure Draft.

Are the proposed changes to Section 29 appropriate for SMEs and users of their financial statements? If not, what modifications, for example further simplifications or additional guidance, do you propose and why?

Notes to constituents

- 6 *As noted in paragraph BC55 of the ED, Section 29 was based on the IASB's March 2009 Exposure Draft Income Tax which was not finalised. It is further noted in paragraph BC56 that during the IASB's due process most of the respondents supported the continuation of the requirement for SMEs to recognise deferred tax using the temporary difference method and alignment of the recognition and measurement requirements of Section 29 with IAS 12.*
- 7 *Therefore, the IASB proposes alignment of the recognition and measurement requirements in Section 29 Income Tax with IAS 12 Income Taxes, taking into account appropriate modification in the light of user's needs and cost-benefit considerations for SMEs.*
- 8 *As referred to in paragraph BC58 of the ED, when aligning the main recognition and measurement requirements for deferred tax in Section 29 with IAS 12, the IASB has decided to keep the simplified presentation requirements in Section 29 with one further simplification: to add an undue cost or effort exemption to clarify that offsetting income tax assets and liabilities would not be required if significant detailed scheduling is required. It also decided that while aligning the recognition and measurement requirements, the existing Section 29 simplified disclosure requirements would continue to apply.*
- 9 *As a result of the IASB's decision to align Section 29 with IAS 12, the IASB also proposes to add a rebuttable presumption that the carrying amount of investment property measured at fair value will be recovered through sale. As noted in paragraph BC60 constituents applying full IFRS found that such rebuttable presumption resulted in a simplification and reduced subjectivity, therefore it was sensible to include all amendments at the same time.*

EFRAG's response

EFRAG supports the IASB's proposal to align the main principles of Section 29 *Income Tax* with IAS 12 *Income Taxes* for the recognition and measurement of deferred tax, and to add a rebuttable presumption that the carrying amount of investment property measured at fair value will be recovered through sale.

However, EFRAG believes that the wording of the proposed amendments could be improved and that some specific guidance from IAS 12 should be reflected in Section 29. Furthermore, EFRAG would encourage the IASB to consider undertaking an outreach to understand whether SMEs would find it useful to have an 'undue cost or effort exemption' for some specific requirements, in addition to the exception already suggested and commented below, or for all the requirements in Section 29.

Approach for accounting for income taxes

- 10 EFRAG supports the alignment of the main principles of Section 29 *Income Tax* with IAS 12 *Income Taxes* for the recognition and measurement of deferred tax with appropriate simplifications to accommodate SMEs needs.
- 11 EFRAG acknowledges the concerns of those who consider that the accounting for income taxes according to the main principles of IAS 12 can be complex and difficult to apply in practice. However, we note that the IFRS for SMEs is used by a wide range of entities and jurisdictions that have already experience with applying the temporary difference approach and consider that such approach provides

useful and relevant information to users. We also note that when responding to the IASB, the majority of constituents expressed the view that Section 29 should be aligned with IAS 12 and that the temporary difference approach should continue to be used for the calculation of deferred tax assets and deferred tax liabilities. Finally, as already highlighted in our comment letter in response to IASB's RfI, the EFRAG/FRC discussion paper *Improving the Financial Reporting of Income Tax* demonstrated that developing a different accounting model for income tax is not straightforward.

- 12 Most significantly, EFRAG thinks that having Section 29 based on the IASB's March 2009 Exposure Draft *Income Tax*, rather than the existing IAS 12, leads to more complexity in the area of deferred tax in IFRS for SMEs (as currently included in the Section 29) than the existing requirements in IAS 12. For example, Section 29 does not include some of the exemptions from recognising deferred taxes, thus eventually resulting in more deferred tax calculations being required. Therefore, alignment is expected to also reduce complexity in practice.
- 13 EFRAG also considers that the extensive experience that already exists in relation to determining deferred tax in accordance with IAS 12 *Income Taxes* makes it easier to transfer this knowledge to SMEs and users of SMEs financial statements when their requirements are aligned. This would contribute to the alleviation of potential diversity in practice.
- 14 Finally, EFRAG would encourage the IASB to consider undertaking some outreach with preparers and users of SME's financial statements to understand whether SMEs would find it useful to have an 'undue cost or effort exemption' for some specific requirements, in addition to the exception already suggested and commented below, or for all the requirements in Section 29. If an SME cannot apply the requirements in Section 29 without undue cost or effort it should be permitted to apply a taxes payable approach with additional disclosures.

Undue cost or effort exemption to offset income tax assets and liabilities

- 15 EFRAG supports the proposed amendment to add an undue cost or effort exemption so that offsetting income tax assets and liabilities is not required if significant, detailed scheduling is required.
- 16 The aim of the proposed amendment is to provide a similar relief to IAS 12 without including the more complex wording used in IAS 12. EFRAG believes that the specific amendment purports further simplification and is expected to reduce the costs for preparers.
- 17 However, EFRAG thinks that paragraph 74(b)(i) of IAS 12 should be incorporated in paragraph 29 of Section 29 to state that an entity shall offset deferred tax assets and deferred tax liabilities, if they are related to income taxes levied by the same taxation authority on the same taxable entity (as suggested in paragraph 24 below).

Clarifying guidance and wording

- 18 As a general comment, EFRAG notes that the education guidance and training material of Section 29 provide the necessary examples included in IAS 12, which help clarify the requirements of the standard, enhance understandability and apply the requirements as intended. These should be simultaneously revised and published when the revised IFRS for SMEs is finalised.

- 19 EFRAG recommends the following changes to clarify the guidance and wording of Section 29 *Income Tax*:

Paragraph 29.8A of the ED

- 20 We believe that paragraph 29.8A of the ED could be improved to appropriately define the concept of temporary differences. This could be done by incorporating some of the existing wording in paragraphs 16 and 25 of IAS 12, which provides guidance on taxable temporary differences deductible temporary differences, as follows:

It is inherent in the recognition of an asset or a liability that the reporting entity expects to recover or settle the carrying amount of that asset or liability. ~~If it is probable that recovery or settlement of that carrying amount will make future tax payments larger (smaller) than they would be if such recovery or settlement were to have no tax consequences, this section requires an entity to recognise a deferred tax liability (deferred tax asset) with certain limited exceptions.~~

When the carrying amount of the asset exceeds its tax base, the amount of taxable economic benefits will exceed the amount that will be allowed as a deduction for tax purposes. This difference is a taxable temporary difference and the obligation to pay the resulting income taxes in the future periods is a deferred tax liability. As the entity recovers the carrying amount of the asset, the taxable temporary difference will reverse and the entity will have taxable profit. An entity is required to recognise a deferred tax liability with certain limited exceptions.

Accordingly, a deferred tax asset arises in respect of the income taxes that will be recoverable in the future periods when that part of the liability is allowed as a deduction in determining taxable profit. Similarly, if the carrying amount of an asset is less than its tax base, the difference gives rise to a deferred tax asset in respect of the income taxes that will be recoverable in future periods. If the entity expects to recover the carrying amount of an asset or settle the carrying amount of a liability without affecting taxable profit, no deferred tax arises in respect of the asset or liability.

Paragraph 29.17D of the ED

- 21 EFRAG believes that the guidance in paragraph 30 of IAS 12 on “tax planning opportunities” would be also useful for SMEs. Therefore, we suggest the following addition to paragraph 29.17D (suggested text underlined):

29.17D *When there are insufficient taxable temporary differences relating to the same taxation authority and the same taxable entity, the deferred tax asset is recognised to the extent that:*

- (a) *it is probable that the entity will have sufficient taxable profit relating to the same taxation authority and the same taxable entity in the same period as the reversal of the deductible temporary difference (or in the periods into which a tax loss arising from the deferred tax asset can be carried back or forward). When evaluating whether it will have sufficient taxable profit in future periods, an entity ignores taxable amounts arising from deductible temporary differences that are expected to originate in future periods, because the deferred tax asset arising from those deductible temporary differences will itself require future taxable profit in order to be utilised; or*

- (b) *tax planning opportunities are available to the entity that will create taxable profit in appropriate periods.*

Tax planning opportunities are actions that the entity would take in order to create or increase taxable income in a particular period before the expiry of a tax loss or tax credit carryforward. Where tax planning opportunities advance taxable profit from a later period to an earlier period, the utilisation of a tax loss or a tax credit carryforward still depends on the existence of future taxable profit from sources other than future originating temporary differences.

Paragraph 29.21 of the ED

- 22 EFRAG believes that paragraph 29.21 of the ED should be expanded to reflect the guidance in paragraph 51C of IAS 12 which clarifies that the presumption is rebutted in certain circumstances. We suggest the following wording (underlined):

29.21 *If a deferred tax liability or asset arises from investment property that is measured at fair value, there is a rebuttable presumption that the carrying amount of the investment property will be recovered through sale. Accordingly, unless that presumption is rebutted, the measurement of the deferred tax liability or the deferred tax asset shall reflect the tax consequences of recovering the carrying amount of the investment property entirely through sale. This presumption is rebutted if the investment property is depreciable and is held within a business model whose objective is to consume substantially all the economic benefits embodied in the investment property over time, rather than through sale. If the presumption is rebutted, the requirements of paragraph 29.20 shall be followed.*

Paragraph 29.27 of the IFRS for SMEs

- 23 EFRAG believes that paragraph 29.27 of the IFRS for SMEs could be improved to better reflect one of the main requirements in IAS 12, that is, an entity shall account for tax consequences of transactions and other events in the same way that it accounts for transaction and other events themselves. Thus, for transactions and other events recognised in profit and loss, any related tax effects are also recognised in profit or loss. For transactions and other events recognised outside of profit or loss any related tax effects are also recognised outside of profit or loss.

Paragraph 29.29 of the ED

- 24 We believe that paragraph 29.29 of the ED could be improved by stating that an entity shall offset deferred tax assets and liabilities if the income taxes were charged by the same taxation authority on the same taxable entity, as required in paragraph 12.74(b)(i) of IAS 12 (suggested text is underline below):

29.29 *An entity shall offset current tax assets and current tax liabilities, or offset deferred tax assets and deferred tax liabilities, only when it has a legally enforceable right to set off the amounts and it is **clear without undue cost or effort** that such assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity, or different taxable entities that it intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.*

Additional guidance

- 25 EFRAG believes that the following guidance in IAS 12, **appropriately modified and simplified**, should be incorporated in Section 29:
- (a) paragraphs 66 to 68 of IAS 12 to provide guidance on deferred tax arising from a business combination, and
 - (b) paragraphs 68A to 68C of IAS 12 to provide guidance on current and deferred tax arising from share-based payment transactions.

Question 3 - Other proposed amendments to the IFRS for SMEs

The IASB proposes to make a number of other amendments to the IFRS for SMEs. The proposed amendments are listed and numbered 1–43 and 45–57 in the list of proposed amendments. Most of those amendments are minor and/or clarify existing requirements.

- (a) Are there any amendments that you do not agree with or have comments on?
- (b) Do any of the amendments require additional guidance or disclosure requirements to be added to the IFRS for SMEs? If so, which ones and what are your suggestions?

If you disagree with an amendment please state any alternatives you propose and give your reasoning.

Notes to constituents

- 26 *At the beginning of the Exposure Draft the IASB has included a 'List of the proposed amendments' to assist respondents in their review of the changes in the different sections. EFRAG highlights some of those proposed amendments below:*

Undue cost or effort exemption

- 27 *The IASB proposes to add paragraphs 2.14A–2.14C of the ED with the objective of providing guidance on the 'undue cost or effort' exemption that is used in several sections of the IFRS for SMEs.*
- 28 *This guidance was based on Q&A 2012/01 Application of 'undue cost or effort', published by the IASB in April 2012, which explained how 'undue cost or effort' and 'impracticable' should be understood.*
- 29 *The IASB also proposes, due to cost-benefit reasons, the addition of an undue cost or effort exemption for the following requirements:*
- (a) *when measuring investments in equity instruments at fair value in Sections 11 and 12;*
 - (b) *when recognising intangible assets separately in a business combination;*
 - (c) *when measuring the entity's own equity instruments, which are issued to a creditor to extinguish a liability, at fair value (which results from incorporating the conclusions of IFRIC 19 Extinguishing Financial Liabilities with Equity Instruments; see paragraph BC37 of the ED); and*

- (d) when offsetting income tax assets and liabilities.

Different reporting dates

- 30 Paragraph 9.16 of the IFRS for SMEs states that the financial statements of the parent and its subsidiaries used in the preparation of the consolidated financial statements shall be prepared as of the same reporting date unless it is impracticable to do so.
- 31 The IASB proposes to add additional guidance in paragraph 9.16 to explain that if it is impracticable to prepare the financial statements of a subsidiary as of the same reporting date as the parent, the parent shall consolidate the financial information of the subsidiary using the most recent financial statements of the subsidiary, adjusted for the effects of significant transactions or events that occur between the date of the reporting date of the subsidiary financial statements and the date of the consolidated financial statements.

Leases with an interest rate variation clause linked to market interest rates

- 32 Currently, a lease with an interest rate variation clause linked to market interest rates (e.g. linked to changes in LIBOR) is within the scope of Section 12 Other Financial Instrument Issues.
- 33 The IASB considers that such clauses are relatively common for finance leases entered into by SMEs and that such an embedded risk (embedded derivative) would not normally require separate accounting under full IFRSs. Therefore, the IASB proposes revising paragraph 12.3(f) and 20.1(e) to exclude such leases from Section 12, meaning they will be accounted for under Section 20 Leases.

Original issue of shares or other equity instruments

- 34 The IASB proposes to add an exemption from the initial measurement requirements set in paragraph 22.8 of the IFRS for SMEs for equity instruments issued as part of a business combination, including business combinations of entities or businesses under common control. As noted in BC8 of the ED this issue was raised by the respondents to RfI, who noted that the current requirement in paragraph 22.8 of IFRS for SMEs to measure equity instruments at the fair value of the cash or other resources received would prohibit the use of the pooling of the interests method for business combinations under common control.

EFRAG's response

EFRAG welcomes most of the proposed amendments as we believe that they will clarify existing guidance, remove unintended consequences and address some of the concerns raised by respondents to the Rfl. However, as further explained below, EFRAG thinks that:

- entities applying the 'undue cost or effort' exemptions in the standard should be required to disclose when an undue cost and effort exemption has been used and their reasons for doing so (subject to materiality);
- paragraph 9.16 of the ED should be aligned with paragraph B93 of IFRS 10 to state that when preparing consolidated financial statements and applying the impracticable criteria, the difference between the date of the subsidiary's financial statements and that of the consolidated financial statements shall not be more than three months before or after the date of the consolidated financial statements;
- the wording in paragraph 12.3 (f), excluding leases from the scope of Section 12, could be simplified.; and
- the measurement exemption in paragraph 22.8 for equity instruments issued as part of a business combination should be made optional, not mandatory.

35 EFRAG generally agrees with most of the proposed amendments, but we think that some of the proposed amendments should be expanded to address the concerns referred below.

Undue cost or effort exemption

36 EFRAG welcomes the specific guidance in paragraphs 2.14A – 2.14C on how to interpret and apply the 'undue cost and effort' exemption that is used in several sections of the IFRS for SMEs.

37 However, we believe that the use of such exception should trigger an SME to disclose when it has made use of an *undue cost and effort* exemption (subject to materiality). In our view, if an entity is not applying a certain requirement of the standard on the basis of 'undue cost or effort', it should clearly state that the 'undue cost and effort' exemption has been used and explain why applying a requirement would result in excessive cost, time and effort.

38 The use of the exemption might not be clear to the user of the financial statements, thus impairing comparability with other entities; disclosures would provide better information for users at comparatively little cost to SMEs.

39 Q&A 2012/01 provided guidance on how to interpret 'undue cost or effort', namely when used in conjunction with the term 'impracticable', and how it differs from the defined term 'impracticable'. We note that paragraphs BC1 and BC2 of the Q&A 2012/01 noted that enquiries to the IASB concerning the difference between 'impracticable' and 'undue cost or effort' suggested that IFRS for SMEs was not clear as to whether cost alone could render a requirement impracticable. In our view, the added guidance in paragraphs 2.14A – 2.14C and the Basis for Conclusions of the ED do not clearly address this concern.

40 Therefore, EFRAG suggests that the IASB better explain, either in the standard or in the Basis for Conclusions, the difference between 'undue cost or effort' and the 'impracticable;' and how the terms interact with each other.

Different reporting dates

- 41 EFRAG thinks that the proposed amendment to paragraph 9.16 of the IFRS for SMEs is an improvement compared with the current requirements as it requires a parent that applies the impracticable criteria to consolidate the financial information of the subsidiary to use the most recent financial statements of the subsidiary and provides guidance on necessary adjustments if uniform reporting dates do not exist.
- 42 Although EFRAG agrees with the proposed amendment, EFRAG is concerned about the considerable flexibility of the standard when it comes to the difference between the date of the subsidiary's financial statements and that of the consolidated financial statements. EFRAG notes in this respect the 'most recent financial statements' could be from a previous year.
- 43 Consequently, EFRAG recommends aligning paragraph 9.16 of the ED with paragraph B93 of IFRS 10 to state that when preparing consolidated financial statements and applying the impracticable criteria, the difference between the date of the subsidiary's financial statements and that of the consolidated financial statements shall not be more than three months before or after the date of the consolidated financial statements.

Leases with an interest rate variation clause linked to market interest rates

- 44 EFRAG welcomes the proposed amendments in paragraphs 20.1(e) and 12.3(f)(iii) to include leases with an interest rate variation clause linked to market interest rates (e.g. linked to changes in LIBOR) within the scope of Section 20 *Leases*, rather than Section 12 *Other Financial Instruments Issues*.
- 45 However, EFRAG believes that the wording in paragraph 12.3(f) of the ED could be simplified as suggested below (suggested text is shown by underline and strikethrough):

12.3 Section 12 applies to all financial instruments except the following:

- (f) leases (see Section 20 *Leases*). However, Section 12 applies to ~~unless the leases that~~ could result in a loss to the lessor or the lessee as a result of contractual terms that are unrelated to:
- (i) changes in the price of the leased asset;
 - (ii) changes in foreign exchange rates;
 - (iii) changes in lease payments based on variable market interest rates; or
 - (iv) a default by one of the counterparties.

Any of the losses referred to above are covered by Section 20 *Leases*.

Original issue of shares or other equity instruments

- 46 EFRAG agrees with the IASB's proposal to include an exemption from the initial measurement requirements in paragraph 22.8 of IFRS for SMEs for equity instruments issued as part of a business combination, including business combinations under common control.

- 47 Nonetheless, EFRAG thinks that the IASB should make clear that the exemption does not prohibit entities from measuring equity instruments issued as part of a business combination at fair value. That is, it should be stated that an entity is permitted to use the exemption in paragraph 22.8 but it is not required to.
- 48 Our conclusion is based on the reasoning that we do not think that it will be clear for SMEs that such equity instruments may be measured, if considered more appropriate, at fair value after considering paragraphs 10.4-10.5¹ of the IFRS for SMEs (i.e. it will not be clear for SMEs that paragraph 22.8 could be applied by analogy).

Question 4—Additional issues

In June 2012 the IASB issued a Request for Information (Rfi) seeking public comment on whether there is a need to make any amendments to the IFRS for SMEs (see paragraphs BC2–BC15). The Rfi noted a number of specific issues that had been previously identified and asked respondents whether the issues warranted changes to the IFRS for SMEs. Additionally, the Rfi asked respondents to identify any additional issues that needed to be addressed during the review process. Any issues so identified were discussed by the IASB during its deliberations.

Do respondents have any further issues that are not addressed by the 57 amendments in the list of proposed amendments that they think the IASB should consider during this comprehensive review of the IFRS for SMEs? Please state these issues, if any, and give your reasoning.

Notes to constituents

New individual and revised IFRS

- 49 *As referred in paragraph BC34 of the ED the IASB considered how to address new or revised IFRS issued since 2009 that had potential to result in the most significant changes to the IFRS for SMEs, namely IFRS 3 (2008), IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Arrangements, IFRS 13 Fair Value Measurement and IAS 19 Employee Benefits (2011).*
- 50 *The IASB decided not to amend the IFRS for SMEs during this initial review to incorporate any of the new principles or changes made to the standards referred to above for the reasons outlined in paragraphs BC33 and BC34 of the ED. These include:*
- (a) *IFRS 3 (2008): incorporating the main changes from IFRS 3 would result in significant complexity for SMEs, particularly because of additional fair value measurements required.*

¹ The IFRS for SMEs states that in the absence of a requirement in the standard that applies specifically to a transaction or other event or condition, paragraph 10.4 provides guidance for making a judgement and paragraph 10.5 establishes a hierarchy for an entity to follow in deciding on the appropriate accounting policy in the circumstances.

- (b) *IFRS 10, IFRS 11 and IFRS 13 only recently became effective and they introduce complex changes that would have a limited practical impact on the majority of SMEs.*
- (c) *IAS 19 (2011): as the IASB is currently considering its treatment of OCI, which may result in changes to some or all of the requirements encompassing an OCI treatment under full IFRS, it decided to maintain the requirements until the treatment of OCI has been discussed further.*

Use of the IFRS for SMEs by publicly accountable entities

51 *In paragraphs BC19-BC21 of the ED the IASB explains that during its discussions the IASB considered whether the scope was too restrictive and whether jurisdictions should have the authority to decide whether some publicly accountable entities should be eligible to use the IFRS for SMEs. However, IASB members were concerned about risks with widening the scope because:*

- (a) *the IFRS for SMEs was specifically designed to provide a simplified set of accounting principles that are appropriate for smaller non-publicly accountable entities and so it may not appropriately cater for a wider group of entities;*
- (b) *it may lead to pressure to make changes to the IFRS for SMEs to accommodate that wider group, which would increase its complexity; and*
- (c) *of the risks of inappropriate use of IFRS for SMEs.*

52 *Therefore the IASB decided that the scope of the IFRS for SMEs should not be changed, but noted that jurisdictions could incorporate the IFRS for SMEs into their local GAAP if they wished.*

Accounting policy options

53 *The IASB states in paragraphs BC44 and BC48 of the ED that it did not feel that there is a convincing argument to reconsider the current approach in the IFRS for SME and introduce further accounting policy options. Therefore, the IASB did not support permitting an accounting policy option for:*

- (a) *the revaluation model to be used for property, plant and equipment (PPE);*
- (b) *development costs to be capitalized on a similar basis to IAS 38 Intangible Assets; and*
- (c) *borrowing costs to be capitalized on a similar basis to IAS 23 Borrowing Costs.*

54 *The IASB argues in paragraphs BC40-BC44 of the ED that adding a revaluation model for PPE would add complexity in other areas of the IFRS for SMEs, such as the requirements for impairment and deferred tax. The IASB also noted that users would benefit from less variation in the accounting requirements between SMEs and, if needed, entities could disclose additional information considered relevant to users.*

55 *In paragraphs BC45-BC48 of the ED the IASB observed that permitting accounting policy options to capitalise development and borrowing costs that meet the criteria for capitalising in IAS 38 / IAS 23 would result in more accounting policy options than full IFRS because full IFRS do not permit an expense-only option.*

Share subscription receivables

56 Paragraphs BC9, BC64-BC66 and BC86 of the ED highlight a number of issues referred by respondents to the Rfi for which the IASB has not proposed amendments. EFRAG notes in particular that the IASB has not proposed amendments to permit or require share subscription receivables to be presented as an asset.

EFRAG's response

EFRAG agrees with the IASB that the main changes from IFRS 3 *Business Combinations* (2008), IFRS 10 *Consolidated Financial Statements* (and other related standards such as IAS 27 *Separate Financial Statements*), IFRS 11 *Joint Arrangements* and IFRS 13 *Fair Value Measurement* should not be incorporated in the IFRS for SMEs until there is practical experience with their use.

However, EFRAG thinks that the IASB should explain why IFRS for SMEs is not suitable for publicly accountable entities. EFRAG also believes that, as already suggested in EFRAG's response to the Rfi, it could be beneficial for SMEs if the following changes were made to IFRS for SMEs:

- **use of revaluation model for property, plant and equipment on a similar basis to IAS 16 *Property, plant and equipment* was permitted;**
- **an option was introduced for those borrowing costs that are directly attributable to the acquisition, construction or production of a 'qualifying asset' to be capitalised on a similar basis to IAS 23 *Borrowing Costs*;**
- **paragraph 22.7(a) was modified or deleted as it does not permit share subscription receivables to be presented as an asset;**
- **an option for development costs to be capitalised on similar basis to IAS 38 *Intangible Assets* was introduced; and**
- **all actuarial gains and losses were recognised in other comprehensive income (i.e. removal of profit or loss option in paragraph 28.24 to reflect a key change from a revision to IAS 19 *Employee Benefits* in 2011).**

57 In its comment letter in response to the Request for Information, issued on 20 December 2012, EFRAG considered that that the main changes from IFRS 3 *Business Combinations* (2008), IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements* and IFRS 13 *Fair Value Measurement* should not be incorporated in the IFRS for SMEs until there is practical experience with their use. Therefore, EFRAG welcomes the IASB's decision to not amend the IFRS for SMEs during this initial review to incorporate any of the new principles or changes made to the standards referred to above.

58 However, we also expressed the view in our December comment letter that:

- (a) the IASB should explain why IFRS for SMEs is not suitable for publicly accountable entities and that EFRAG could see some merits in allowing entities for which the standard is not intended to claim compliance with the requirements of the IFRS for SMEs, if all the requirements of the standard are met (*reply to Question S1 in Appendix 1 of the letter*);

- (b) an option to revalue property, plant and equipment should be included (*reply to Question S9 in Appendix 1 of the letter*);
- (c) an option to allow an entity to either capitalise or expense borrowing costs on qualifying assets should be included (*reply to Question S14 in Appendix 1 of the letter*);
- (d) share subscription receivables should be presented as an asset when certain criteria are met (*reply to question S13 in Appendix 1 of the letter*);
- (e) an option to allow an entity to either capitalise or expense development costs should be included (*reply to Question S10 in Appendix 1 of the letter*);
- (f) IFRS for SMEs should be revised so that an entity is required to recognise all actuarial gains and losses in other comprehensive income (*reply to question S15 in Appendix 1 of the letter*)

59 EFRAG considers that the above concerns have not been solved in the ED in the way we had wished they would and we refer for further details to our letter of 20 December 2012.

Question 5 - Transition provisions

The IASB does not expect retrospective application of any of the proposed amendments to be significantly burdensome for SMEs and has therefore proposed that the amendments to the IFRS for SMEs in Sections 2–34 are applied retrospectively.

Do you agree with the proposed transition provisions for the amendments to the IFRS for SMEs? Why or why not? If not, what alternative do you propose?

Notes to constituents

- 60 *The IASB proposes full retrospective application of the suggested changes, meaning that it will not include any exceptions.*
- 61 *The proposal to align the main principles of Section 29 Income Tax with IAS 12 Income Taxes for the recognition and measurement of deferred tax is expected to result in the most significant change for most SMEs.*

EFRAG's response

In general, EFRAG considers that full retrospective application is likely to provide the most useful information to users, as it facilitates the year-to-year comparison. However, EFRAG thinks that the IASB should consider ways of providing relief from full retrospective application of section 29 *Income Tax*.

- 62 In general, EFRAG considers that full retrospective application is likely to provide the most useful information to users as it facilitates the year-to-year comparison. However, EFRAG is aware that such application may be costly and in some cases impracticable.
- 63 The IASB proposes to align the main principles of Section 29 *Income Tax* with IAS 12 *Income Taxes* for the recognition and measurement of deferred tax. To align

the main principles the IASB has proposed a number of amendments that affect both the structure and the wording of several paragraphs.

- 64 EFRAG believes that the requirement to apply section 29 retrospectively can be costly and burdensome for some SMEs as SMEs will need to assess whether each individual change to the requirements for recognising, measuring and disclosing deferred tax will have an impact when applied retrospectively. For example, the information required to apply section 29 retrospectively might not be available or available only with undue cost or effort - it could be challenging for an entity as it may have to track the tax bases of many assets for which the entity has discontinued tracking in accordance with IFRS for SMEs (2009).
- 65 In light of these concerns, EFRAG thinks that the IASB should consider ways of providing relief from full retrospective application of section 29 *Income Tax* (and not only when it is impracticable). EFRAG notes that, according to paragraph 35.10 of the IFRS for SMEs, a first-time adopter is not required to recognise deferred tax assets or deferred tax liabilities, at the date of transition if recognition would involve undue cost or effort.
- 66 EFRAG would suggest that if an SME cannot apply the proposed amendments to the requirements in Section 29 *Income Tax* retrospectively without undue cost or effort, the IFRS for SMEs should permit an entity to evoke an “undue cost or effort exemption” and apply it to the annual period immediately preceding the effective date. EFRAG believes that this could preserve trend information which is critical for users’ analysis.

Question 6 - Effective date

The IASB does not think that any of the proposed amendments to the IFRS for SMEs will result in significant changes in practice for SMEs or have a significant impact on their financial statements. It has therefore proposed that the effective date of the amendments to the IFRS for SMEs should be one year after the final amendments are issued. The IASB also proposes that early adoption of the amendments should be permitted.

Do you agree with the proposed effective date and the proposal to permit early adoption? Why or why not? If not, what alternative do you propose?

Notes to constituents

- 67 *While the IASB has not yet decided on the effective date of the resulting amendments, it has been agreed that the effective date should be one year after the final amendments are issued. Early application will be permitted.*

EFRAG’s response

EFRAG thinks that the effective date should coincide with the beginning of the first annual reporting period starting one year after the publication of the final amendments. EFRAG agrees with the IASB’s proposals to allow early application.

- 68 EFRAG considers that most of the proposals clarify requirements, remove unintended consequences of existing wording or align requirements with some full

IFRS which have been applied by entities, including SMEs, in many jurisdictions for years.

- 69 Thus, EFRAG thinks that a minimum of one year should be given to entities to implement the amendments. However, we recommend that the effective date of the amendments to the IFRS for SMEs should be more explicitly defined and suggests as effective date the first reporting period that commences one year after the publication of the amendments to IFRS for SMEs.

Question 7 - Future reviews of the IFRS for SMEs

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

During the comprehensive review, the IASB has received feedback that amendments to the IFRS for SMEs once every three years (three-year cycle) may be too frequent and that a five-year cycle, with the ability for an urgent issue to be addressed earlier, may be more appropriate.

Do you agree with the current tentative three-year cycle for maintaining the IFRS for SMEs, with the possibility for urgent issues to be addressed more frequently? Why or why not? If not, how should this process be modified?

Notes to constituents

70 *The IASB states in paragraph BC29 of the ED that the primary aim when developing the IFRS for SMEs was to provide a standalone, simplified set of accounting principles. With this primary aim in mind the IASB states in BC30 that it considered a framework for how to deal with new and revised IFRS during this comprehensive review and future reviews of the IFRS for SMEs. The IASB developed the following principles:*

- (a) *each new and revised IFRS should be considered individually on a case-by-case basis to decide if, and how, its requirements should be incorporated into the IFRS for SMEs.*
- (b) *new and revised IFRS should not be considered until they have been published. However, it would generally not be appropriate to wait until their Post-implementation Reviews have been completed.*
- (c) *minor changes/annual improvements to full IFRS should also be considered on a case-by-case basis.*
- (d) *changes to the IFRS for SMEs could be considered at the same time that new and revised IFRS are published. However, the IFRS for SMEs would only be updated for those changes at the next three-yearly review, in order to provide a stable platform for SMEs.*

- 71 *BC 33 also states that although the current review is carried out after a three-year implementation period of this standard. The standard has been effective for a much shorter period of time to the majority of SMEs, therefore, it is considered a relatively new standard.*
- 72 *According to the IASB's timetable, the standard was issued in 2009, and the commencement of its comprehensive review was in June 2012 with the issuance of the Rfl. The final revised IFRS for SMEs is expected to be issued in the first half of 2015. The IASB has also tentatively decided that the effective date should be one year after the final amendments are issued. Early application will be permitted. Therefore, this is not expected to be any earlier than 1 January 2016.*

EFRAG's response

EFRAG broadly agrees with the IASB's developed framework for how to deal with new and revised IFRS during future reviews of the IFRS for SMEs, except that we think the IFRS for SMEs should not be changed based on changes in full IFRS that have not yet been implemented. We also consider that post-implementation reviews of new and revised IFRS represent the best opportunity to assess the suitability of the changes for SMEs and users of their financial statements. We do not support this suitability to be assessed at the same time as the changes to full IFRS are open to consultation, because it would de facto call for too heavy a consultation burden on those who have an interest in the IFRS for SMEs.

EFRAG thinks that a five-year cycle policy should be introduced since SMEs have a strong demand for stability. This should be accompanied with some flexibility in the due process so that specific issues can be considered earlier if they respond to an urgent need or solve significant divergence or unforeseen circumstances in practice and remove an impediment to improved faithful information.

EFRAG suggests having something similar to the IFRS Interpretations Committee for the IFRS for SMEs and would not favour the continuation of the Q&A process given the earlier experience.

- 73 EFRAG continues to believe that it is imperative that the IFRS for SMEs remains stable. Therefore, in EFRAG's view, the standard should be changed only when the suggested change addresses an identified problem for SMEs and the change is likely to solve that problem, and thus result in improved financial reporting. Unless a change is considered particularly urgent, the change should only be incorporated into the IFRS for SMEs as part of the multi-annual review.
- 74 EFRAG agrees with the IASB as stated in paragraphs BC29 and BC30 of the ED that the stability of the standard should be maintained and that principles should be followed by the IASB when considering new and revised IFRS. EFRAG also agrees with the intention of the IASB (as stated in the developed principles for comprehensive reviews (BC29)), to consider how changes affect SME users (and SMEs) and a possible revision of the IFRS for SMEs at the same time that full IFRS are changed.
- 75 Still, EFRAG believes that a cycle of five years rather than the current three years should be put in place and that this should be accompanied with some flexibility in the due process so that urgent issues can be considered earlier if they respond to an urgent need to remove an impediment to the usefulness of financial information or solve a significant divergence or unforeseen circumstances in practice. Such urgent changes may result, for example, from specific requests from constituents

in relation to changes from full IFRS or unforeseen circumstances and implications of the existing IFRS for SMEs.

- 76 In addition, EFRAG would suggest having something similar to the IFRS Interpretations Committee for the IFRS for SMEs. However, EFRAG would not favour the continuation of the Q&A process given the earlier experience with the large number of Q&As issued without clear criteria.

Question 8 - Any other comments

Do you have any other comments on the proposals?

EFRAG's response

EFRAG thinks that the guidance on fair value measurement in section 11 should be moved into a separate section and that some definitions in *IFRS for SMEs* should be aligned with full IFRS.

Fair value guidance in section 11

- 77 Several sections of the IFRS for SMEs (covering both financial and non-financial items) make reference to the fair value guidance in Section 11. 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.
- 78 As referred in our comment letter in response to the Request for Information (*reply to Question S6 in Appendix 1 of the letter*) EFRAG thinks the standard could be more user-friendly if the guidance on fair value measurement was placed in a separate section. Such an amendment would have the benefit of making clear that the guidance was applicable to all references to fair value in the IFRS for SMEs, and not just to financial instruments.

Definitions

- 79 The IASB has proposed to align some of the definitions included in the IFRS for SMEs with full IFRS. For example, as referred to in paragraph BC76 of the ED, the IASB proposes to align the definition of related party with IAS 24 (2009).
- 80 However, EFRAG is concerned that currently different definitions exist in the IFRS for SMEs and full IFRS. For example, the definitions of 'goodwill' and 'fair value' in the IFRS for SMEs are not completely aligned with full IFRS.
- 81 To avoid any discussion about the meaning of the same concepts, EFRAG thinks that the IASB should make efforts to align, as far as possible, the definitions and concepts between the IFRS for SMEs and full IFRS.