

RESPONSE TO IASB DISCUSSION PAPER 'Preliminary Views on Accounting Standards for Small and Medium-Sized Entities'

CL 24

The Federation represents nearly 1400 independent, not for profit housing providers. Our members include Registered Social Landlords, Housing Associations, Co-ops, Trusts and transfer organisations. They manage more than 1.8 million homes provided for affordable rent, Supported Housing and Low Cost Home Ownership as well as delivering a wide range of community and regeneration services.

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The Federation is pleased to have the opportunity to comment on the discussion paper *Preliminary Views on Accounting Standards for Small and Medium-Sized Entities*. This response sets out the preliminary views of the Federation and the questions asked in the discussion paper.

Issue 1 – Should the International Accounting Standards Board (IASB) develop special financial reporting standards for SMEs?

Preliminary Views Expressed by the IASB

Preliminary view 1.1 – Full IFRSs are suitable for all entities. The objective of financial statements as set out in the IASB *Framework for the Preparation and Presentation of Financial Statements* is appropriate for SMEs as well as for entities required to follow full IFRSs. Therefore, full IFRSs should be regarded as suitable for all entities.

Preliminary view 1.2 – The Board will develop standards for SMEs. The Board will develop a set of financial reporting standards that is suitable only for those entities that do not have public accountability 'IASB Standards for SMEs'. Such standards would not be intended for use by publicly accountable entities, including those whose securities have been listed for trading in a public securities market, even if national law or regulation were to permit this. Public accountability is discussed in issue 3 and preliminary views 3.13.6.

Preliminary view 1.3 – Disclose the basis of presentation. If an entity follows IASB Standards for SMEs, the basis of presentation note and the auditor's report should make that clear.



Question 1a.

Do you agree that full IFRSs should be considered suitable for all entities? If not, why not?

We believe that the same concepts of financial reporting should be applicable to entities of all sizes. Currently the SORP for Registered Social Landlords does not permit the use of the UK FRSE. However, also see the response to 1 (b) below.

Question 1b.

Do you agree that the Board should develop a separate set of financial reporting standards suitable for SMEs? If not, why not?

We agree that the Board should develop a separate set of financial reporting standards. It may be that the recognition and measurement principles can be expressed more simply and that many of the disclosure requirements would be removed. We also support the IASB objective set out in paragraph 8 of the discussion paper “to develop, in the public interest, a single set of high quality, understandable and enforceable global accounting standards that require high quality, transparent and comparable information in financial statements and other financial reporting to help participants in the various capital markets of the world and other users of the information to make economic decisions”.

Question 1c.

Do you agree that IASB Standards for SMEs should not be used by publicly listed entities (or any other entities not specifically intended by the Board), even if national law or regulation were to permit this? Do you also agree that if the IASB Standards for SMEs are used by such entities, their financial statements cannot be described as being in compliance with IFRSs for SMEs? If not, why not?

We agree that IASB Standards for SME’s should not be used for publicly listed entities. We agree that if the IASB Standards for SMEs are used their financial statements cannot be described as being compliant with IFRS for SMEs.

Issue 2 – What should be the objectives of a set of financial reporting standards for SMEs?

Preliminary Views Expressed by the IASB

Preliminary view 2 – Objectives of IASB Standards for SMEs. Financial reporting standards for SMEs should:

(a) provide high quality, understandable and enforceable accounting



- standards suitable for SMEs globally;
- (b) focus on meeting the needs of users of SME financial statements;
- (c) be built on the same conceptual framework as IFRSs;
- (d) reduce the financial reporting burden on SMEs that want to use global standards; and
- (e) allow easy transition to full IFRSs for those SMEs that become publicly accountable or choose to switch to full IFRSs.

Question 2.

Are the objectives of IASB Standards for SMEs as set out in preliminary view 2 appropriate and, if not, how should they be modified?

We consider that the objectives of IASB Standards for SME's are appropriate.

Issue 3 – For which entities would IASB Standards for SMEs be intended?

Preliminary Views Expressed by the IASB

Preliminary view 3.1 – No size test. The Board should describe the characteristics of the entities for which IASB Standards for SMEs are intended. Those characteristics should not prescribe quantitative 'size tests'. National jurisdictions should determine whether all entities that meet those characteristics, or only some, should be required or permitted to use IASB Standards for SMEs.

Preliminary view 3.2 – Public accountability principle. Public accountability is the overriding characteristic that distinguishes SMEs from other entities. Full IFRSs, and not IASB Standards for SMEs, are appropriate for an entity that has public accountability. An entity has public accountability if:

- (a) there is a high degree of outside interest in the entity from non-management investors or other stakeholders, and those stakeholders depend primarily on external financial reporting as their only means of obtaining financial information about the entity; or
- (b) the entity has an essential public service responsibility because of the nature of its business. A business entity would be regarded as having public accountability, and therefore should follow full IFRSs, if it meets any of the following criteria:

Preliminary view 3.3 – Presumptive indicators of public accountability.

- (a) it has filed, or it is in the process of filing, its financial statements with a



securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market;

- (b) it holds assets in a fiduciary capacity for a broad group of outsiders, such as a bank, insurance company, securities broker/dealer, pension fund, mutual fund or investment banking entity;
- (c) it is a public utility or similar entity that provides an essential public service; or
- (d) it is economically significant in its home country on the basis of criteria such as total assets, total income, number of employees, degree of market dominance, and nature and extent of external borrowings. operations.

Preliminary view 3.4 – Required assent of all owners. An entity that does not satisfy any of the presumptive indicators of public accountability would nevertheless be regarded as having public accountability unless it has informed all of its owners, including those not otherwise entitled to vote, that it intends to prepare its financial statements on the basis of IASB Standards for SMEs rather than on the basis of IFRSs, and none of those owners objects to using IASB Standards for SMEs.

Preliminary view 3.5 – Scope: all entities that do not have public accountability. The Board intends to include all entities that do not have public accountability as potential adopters of IASB Standards for SMEs.

Preliminary view 3.6 – Subsidiaries, joint ventures and associates. If a subsidiary, joint venture or associate of an entity with public accountability prepares financial information in accordance with full IFRSs to meet the requirements of the parent, venturer or investor, it should comply with full IFRSs, not IASB Standards for SMEs, in its separate financial statements.

Question 3a.

Do you agree that the Board should describe the characteristics of the entities for which it intends the standards but that those characteristics should not prescribe quantitative 'size tests'? If not, why not, and how would an appropriate size test be developed?

We consider that there are significant practical difficulties in establishing a size test on global basis for entities for which the Board intends the standards, and therefore the characteristics type test is likely to be an appropriate route. However, we have some concerns that this may lead to the smallest Not for Profit or Public Benefit entities having to comply with full IFRS as and when UK standards converge with IFRS.



Question 3b.

Do you agree that the Board should develop standards that would be suitable for all entities that do not have public accountability and should not focus only on some entities that do not have public accountability, such as only the relatively larger ones or only the relatively smaller ones? If not, why not?

We agree that to apply the criteria effectively the Board should focus on all entities that have public accountability.

Question 3c.

Do the two principles in preliminary view 3.2, combined with the presumptive indicators of 'public accountability' in preliminary view 3.3, provide a workable definition and appropriate guidance for applying the concept of 'public accountability'? If not, how would you change them?

Generally we agree with preliminary views in 3.2 and 3.3. Whilst the SORP for registered social landlords does not currently permit the use of the FRSSE by smaller housing associations, this is a restriction that may be reversed in the future. We consider, however, that public accountability as defined by preliminary view 3.3 (c) might mean that the smallest housing associations, who still provide an essential public service, would be excluded from adopting any standards adapted for SMEs. Potentially the reporting requirements for such entities may outweigh the costs.

Question 3d.

Do you agree that an entity should be required to use full IFRSs if one or more of the owners of its shares object to the entity's preparing its financial statements on the basis of IASB Standards for SMEs. If not, why not?

We agree with this view and note that for many public benefit entities that regulators or government are able to prescribe financial reporting requirements.

Question 3e.

Do you agree that if a subsidiary, joint venture or associate of an entity with public accountability prepares financial information in accordance with full IFRSs to meet the requirements of its parent, venturer or investor, the entity should comply with full IFRSs, and not IASB Standards for SMEs, in its separate financial statements? If not, why not?

We agree with this view.

Issue 4. If IASB Standards for SMEs do not address a particular accounting



recognition or measurement issue confronting an entity, how should that entity resolve the issue?

Preliminary View of the IASB

Preliminary view 4 – Mandatory fallback to IFRSs. If IASB Standards for SMEs do not address a particular accounting recognition or measurement issue that is addressed in an IFRS, the entity would be required to look to that IFRS to resolve that particular issue only. The entity would continue to use IASB Standards for SMEs for the remainder of its financial reporting. Each IASB Standard for SMEs should explicitly mention the required fallback to IFRSs.

Question 4.

Do you agree that if IASB Standards for SMEs do not address a particular accounting recognition or measurement issue, the entity should be required to look to the appropriate IFRS to resolve that particular issue? If not, why not, and what alternative would you propose?

We consider that the entity should be allowed to refer to IFRS in order to make an assessment of accepted practice (see the response to question 5).

Issue 5. May an entity using IASB Standards for SMEs elect to follow a treatment permitted in an IFRS that differs from the treatment in the related IASB Standard for SMEs?

Preliminary View of the IASB

Preliminary view 5 – Optional reversion to an IFRS. If an IASB Standard for SMEs provides an exemption or simplification from a recognition or measurement requirement in the related IFRS, an entity that uses IASB Standards for SMEs would not be prohibited from applying the related IFRS in its entirety, while otherwise continuing to use IASB Standards for SMEs. Optional reversion would not be permitted for only some, but not for all, principles in the related IFRS.



Question 5a.

Should an SME be permitted to revert to an IFRS if the treatment in the SME version of the IFRS differs from the treatment in the IFRS, or should an SME be required to choose only either the complete set of IFRSs or the complete set of SME standards with no optional reversion to individual IFRSs? Why?

We consider that an entity should be allowed to revert to IFRS as our view is that any standards developed should only be a simplification of IFRS and should be consistent with the recognition and measurement concepts of the IFRS. However, this should be as a means of establishing accepted practice and not a mandatory requirement.

Question 5b.

If an SME is permitted to revert to an IFRS, should it be:

- (a) required to revert to the IFRS in its entirety (a standard-by-standard approach);*
- (b) permitted to revert to individual principles in the IFRS without restriction while continuing to follow the remainder of the SME version of the IFRS (a principle-by-principle approach); or*
- (c) required to revert to all of the principles in the IFRS that are related to the treatment in the SME version of that IFRS while continuing to follow the remainder of (d) the SME version of the IFRS (a middle ground between a standard-by-standard and principle-by-principle approach)?*

Please explain your reasoning and, if you favour (c), what criteria do you propose for defining 'related' principles?

In accordance with our responses to questions 4 and 5 we consider that entities should be allowed to follow the principles in the IFRS without restriction on the basis of establishing accepted practice. It might be useful to include a disclosure requirement explain that the entity has chosen this course of action.

Issue 6. How should the Board approach the development of IASB Standards for SMEs? To what extent should the foundation of SME standards be the concepts and principles and related mandatory guidance in IFRSs?

Preliminary	View	of	the	IASB
Preliminary view 6 – IFRSs are the starting point for developing SME standards. Development of IASB Standards for SMEs should start by extracting the fundamental concepts from the IASB <i>Framework</i> and the principles and related mandatory guidance from IFRSs (including Interpretations).				



Question 6.

Do you agree that development of IASB Standards for SMEs should start by extracting the fundamental concepts from the Framework and the principles and related mandatory guidance from IFRSs (including Interpretations), and then making modifications deemed appropriate? If not, what approach would you follow?

We agree with this view.

Issue 7. If IASB Standards for SMEs are built on the concepts and principles and related mandatory guidance in full IFRSs, what should be the basis for modifying those concepts and principles for SMEs?

Preliminary View of the IASB

Preliminary view 7.1 – Justification for modifications. Any modifications to the concepts or principles in IFRSs must be based on the identified needs of users of SME financial statements or cost-benefit analyses.

Preliminary view 7.2 – Likelihood of disclosure and presentation modifications. It is likely that disclosure and presentation modifications will be justified on the basis of user needs and cost-benefit analyses. The disclosure modifications could increase or decrease the level of disclosure relative to full IFRSs.

Preliminary view 7.3 – Rebuttable presumption of no recognition and measurement modifications. There would be a rebuttable presumption that no modifications would be made to the recognition and measurement principles in IFRSs. Such modifications can be justified only on the basis of user needs or cost-benefit analyses.

Question 7a.

Do you agree that any modifications for SMEs to the concepts or principles in full IFRSs must be on the basis of the identified needs of users of SME financial statements or cost-benefit analyses? If not, what alternative bases for modifications would you propose, and why? And if so, do you have suggestions about how the Board might analyse the costs and benefits of IFRSs in an SME context?

We agree with this view.



Question 7b.

Do you agree that it is likely that disclosure and presentation modifications will be justified on the basis of user needs and cost-benefit analyses and that the disclosure modifications could increase or decrease the current level of disclosure for SMEs? If not, why not?

We agree that it is likely that disclosure and presentation modifications will be justified on the basis of user needs and cost benefit analyses, although we have some concerns regarding the smallest entities as outlined above. We consider that such modifications should ensure that information is available to ensure that users are able to take effective economic decisions and the disclosures required are able to provide information to facilitate assessment of the stewardship of an entity.

Question 7c.

Do you agree that, in developing standards for SMEs, the Board should presume that no modification would be made to the recognition or measurement principles in IFRSs, though that presumption could be overcome on the basis of user needs and a cost-benefit analysis? If not, why not?

We consider that the development of standards for SMEs should be based on the concepts of financial reporting and agree with the principle that the recognition criteria for assets and liabilities are critical to this.

Issue 8. In what format should IASB Standards for SMEs be published?

Preliminary View of the IASB

Preliminary view 8.1 – Separate volume. IASB Standards for SMEs should be published in a separate printed volume. The Board may also use other means of publication, such as Web publishing.

Preliminary view 8.2 – Organised by IAS/IFRS (and Interpretation) number. IASB Standards for SMEs should:

- (a) follow the IAS/IFRS (and Interpretation) numbering system – ie SMEIAS 1, SMEIAS 2 etc and SMEIFRS 1, SMEIFRS 2 etc; and
- (b) not be reorganised by topic, such as integrated in a balance sheet-income statement line item sequence like the UK *Financial Reporting Standard for Smaller Entities* (FRSSE).

Preliminary view 8.3 – Foreword material in each Standard. Each IASB Standard for SMEs should include a statement of its objective and a summary.



Question 8a.

Do you agree that IASB Standards for SMEs should be published in a separate printed volume? If you favour including them in separate sections of each IFRS (including Interpretations) or some other approach, please explain why.

We consider that in order to simplify and provide clear guidance to SMEs a separate volume should be issued.

Question 8b.

Do you agree that IASB Standards for SMEs should be organised by IAS/IFRS number rather than in topical sequence? If you favour topical sequence or some other approach, please explain why.

On balance an approach which organises standards by IAS/IFRS number is likely to provide a logical, consistent and ordered reference for accounts preparers and is therefore preferred. There is some merit in including Standards in topical sequence as it might group related topics and issues together for example based on elements of the financial statements assets, liabilities etc and thus form a simpler guide for accounts preparers.



Question 8c.

Do you agree that each IASB Standard for SMEs should include a statement of its objective, a summary and a glossary of key terms?

We fully support this view.

Question 9.

Are there any other matters related to how the Board should approach its project to develop standards for SMEs that you would like to bring to the Board's attention?

None currently