

AASB response to the IASB's Discussion Paper *Preliminary Views on Accounting Standards for Small and Mediumsized Entities*

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

Question 1a. Do you agree that full IFRSs should be considered suitable for all entities? If not, why not?

Question 1b. Do you agree that the Board should develop a separate set of financial reporting standards suitable for SMEs? If not, why not?

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?

Preliminary IASB view 1.1 – Full IFRSs are suitable for all entities. The objective of financial statements as set out in the IASB *Framework* 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. ('Full IFRSs' are Standards and Interpretations adopted by the IASB. They comprise International Financial Reporting Standards, International Accounting Standards and Interpretations originated by the International Financial Reporting Interpretations Committee or the former Standing Interpretations Committee.)

Preliminary IASB 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'). Those 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 IASB 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.

AASB COMMENTS

The AASB generally requires application of Australian Accounting Standards to "reporting entities".

We note that IFRS 3 defines a reporting entity as "An entity for which there are users who rely on the entity's general purpose financial statements for information that will be useful to them for making decisions about the allocation of resources. A reporting entity can be a single entity or a group comprising a parent and all of its subsidiaries."

This is highly similar to the definition used by the AASB for application purposes.

The AASB does not favour providing relief from recognition and measurement requirements in IFRSs for any type of reporting entity. The AASB view is that there can only be one profit/result and one balance sheet determined in accordance with the standards. The whole process of standard setting and preparation of financial reports is undermined by the notion that there can be one profit/result determined using all the recognition and measurement standards and another profit/result that complies with a subset of those standards, with both being claimed to be IFRS compliant. The AASB considers it would be confusing and potentially misleading for users if there could be two different profits/results and balance sheets, with both being in accordance with a core set of standards. In jurisdictions where preparers and auditors are required to certify that financial reports reflect a "true and fair

view”, there would potentially be two different financial reports that would need to be certified – and it would be anomalous for them both to be certified as reflecting a true and fair view.

The AASB considers that there may be merit in relieving SMEs from some disclosure requirements.

Whilst there may be a correlation between size and whether an entity is a reporting entity, reporting entities may be large, medium or small and, accordingly, size should not be a factor in determining whether the IFRSs apply.

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

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?

Preliminary IASB 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.

AASB COMMENTS

Subject to our comments on Issue 1, the Preliminary view 2 appears reasonable.

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

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?

Preliminary IASB 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.

AASB COMMENTS

Yes, the AASB agrees with the IASB’s preliminary view 3.1. The AASB considers size tests to be arbitrary and contrary to the IASB’s principles-based approach to standard setting.

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?

AASB COMMENTS

If the IASB proceeds with distinguishing entities that apply all IFRSs from SMEs on the basis of public accountability, the AASB agrees that the SME standards should be applicable to all such entities.

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?

Preliminary IASB 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 nonmanagement 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 operations.

Preliminary IASB view 3.3 – Presumptive indicators of public accountability. A business entity would be regarded as having public accountability, and therefore should follow full IFRSs, if it meets any of the following criteria:

- (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.

AASB COMMENTS

If the IASB proceeds with distinguishing entities that apply all IFRSs from SMEs on the basis of public accountability, the AASB agrees that principles in the IASB’s preliminary views 3.2 and 3.3 are workable.

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?

Preliminary IASB 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 IASB 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.

AASB COMMENTS

If the IASB proceeds with distinguishing entities that apply all IFRSs from SMEs on the basis of public accountability, the AASB agrees 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. The AASB considers that there is no need to refer to the interests of other stakeholders (such creditors, regulators and employees or employee representatives), provided the IASB retains its “public accountability test”, whereby entities that are publicly accountable, as outlined in the IASB’s preliminary view 3.3, are not SMEs.

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?

Preliminary IASB 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.

AASB COMMENTS

If the IASB proceeds with distinguishing entities that apply all IFRSs from SMEs on the basis of public accountability, the AASB considers that a subsidiary, joint venture or associate of an entity that is publicly accountable would only need to comply with full IFRSs in their separate financial statements if they are also publicly accountable in their own right. Accordingly, the AASB does not agree with the IASB's preliminary view 3.6, which effectively deems a subsidiary, joint venture or associate of an entity that is publicly accountable to be a publicly accountable entity in its own right.

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?

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?

Preliminary IASB 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.

AASB COMMENTS

The AASB considers that this issue highlights a major practical problem with any proposal to distinguish entities that apply full IFRSs from SMEs that might apply some subset of recognition and measurement requirements. If a SME is required to look to full IFRSs to determine the treatment of an item not dealt with in the SME standards, how will the standards draw the line between this requirement and the permission to not use full IFRSs in respect of the recognition and measurement of other items? Taken to its logical conclusion, the proposal that a SME is required to look to full IFRSs to determine the treatment of an item not dealt with in the SME standards is the same as not permitting them to depart from all the recognition and measurement requirements of full IFRSs. [If the SME has a transaction to which an IFRS applies, it uses the IFRS. If the SME does not have that transaction it need not apply that IFRS.]

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?

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?*

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 standardbystandard 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 principlebyprinciple 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 the SME version of the IFRS (a middle ground between a standardbystandard and principlebyprinciple approach)?*

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

Preliminary IASB 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.

AASB COMMENTS

If the IASB proceeds with distinguishing entities that apply all IFRSs from SMEs and insists on having differential recognition and measurement requirements, the AASB favours permitting a SME to revert to an IFRS if the treatment in the SME version of the IFRS differs from the treatment in the IFRS on the basis that this is likely to be a more relevant and reliable treatment. The AASB also favours implementing this approach on the basis that the SME would be required to revert to the IFRS in its entirety. This is on the basis that the treatments required in most standards are integrated with one another, and selecting one treatment from a standard could result in inconsistent financial reporting results.

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?

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?*

Preliminary IASB 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 *Framework* and the principles and related mandatory guidance from IFRSs (including Interpretations).

AASB COMMENTS

If the IASB proceeds with distinguishing entities that apply all IFRSs from SMEs, the AASB agrees with the IASB’s preliminary view 6.

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?

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 costbenefit 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?

Preliminary IASB 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 costbenefit analyses.

AASB COMMENTS

If the IASB proceeds with distinguishing entities that apply all IFRSs from SMEs, the AASB agrees with the IASB's preliminary view 7.1.

Question 7b. Do you agree that it is likely that disclosure and presentation modifications will be justified on the basis of user needs and costbenefit analyses and that the disclosure modifications could increase or decrease the current level of disclosure for SMEs? If not, why not?

Preliminary IASB 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 costbenefit analyses. The disclosure modifications could increase or decrease the level of disclosure relative to full IFRSs.

AASB COMMENTS

As noted under Issue 1, the AASB considers that there may be merit in relieving SMEs from some disclosure requirements. The feasibility of identifying disclosures that need not be made by SMEs will depend on whether the needs of users of SMEs' financial reports can be distinguished from those of other users.

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 costbenefit analysis? If not, why not?

Preliminary IASB 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 costbenefit analyses.

AASB COMMENTS

The AASB considers that it should not be possible to overcome the presumption that no modification would be made to the recognition or measurement principles in IFRSs. The basis of this view is explained in the AASB comments on Issue 1.

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

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.

Preliminary IASB 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.

AASB COMMENTS

If the IASB proceeds with distinguishing entities that apply all IFRSs from SMEs, the AASB agrees with the IASB's preliminary view 8.1.

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.

Preliminary IASB 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)*.

AASB COMMENTS

If the IASB proceeds with distinguishing entities that apply all IFRSs from SMEs, the AASB agrees with the IASB's preliminary view 8.2.

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?

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

AASB COMMENTS

If the IASB proceeds with distinguishing entities that apply all IFRSs from SMEs, the AASB agrees with the IASB's preliminary view 8.3.

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?

AASB COMMENTS

No comment.