

Second Comprehensive Review of the *IFRS for SMEs* Standard

Agenda Paper 5
User survey and user interview feedback summary

SME Implementation Group meeting
February 2021

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Project	Second Comprehensive Review of the <i>IFRS for SMEs</i> Standard		
Paper topic	User survey and user interview feedback summary		
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- The International Accounting Standards Board (Board) published a Request for Information on the second comprehensive review of the *IFRS for SMEs* Standard in January 2020
- The Request for Information (RFI) was open for comments for 270 days
- To obtain feedback from users of SMEs financial statements the Board published an online survey (user survey) and interviewed users
- The purpose of this paper is to summarise the feedback from the user survey and user interviews on the comprehensive review of the *IFRS for SMEs* Standard to help the SME Implementation Group (SMEIG) to develop recommendations that will enable the Board to decide the project's direction.

Criteria used to summarise feedback

- This paper describes the proportion of respondents sharing feedback using these terms:

Term	Extent of response among respondents
Most	A large majority
Many	A majority
Some	A minority
A small number	A small minority

	Pages
User survey: overview	6–8
User survey: user feedback	9–23
User survey: feedback from non-users	24–36
User interviews	37–47

A grayscale world map is the background for the slide. Overlaid on the map are several thick, light gray curved lines that sweep across the continents. Additionally, there are dotted lines forming a grid-like pattern across the map, suggesting a global network or survey reach.

User survey: overview

Overview of user survey

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11 August 2020

User survey available on request

27 October 2020

Survey closed



Objective

- provide insight into the **information needs of users** of small and medium-sized entities (SMEs) financial statements

10 questions on...

- A** Alignment approach—whether the *IFRS for SMEs* Standard should be aligned with full IFRS Standards
- B** Users' information needs—factors the Board considers in setting disclosures in the *IFRS for SMEs* Standard (Paragraph BC157 of the *IFRS for SMEs* Standard).
- C** Any additional matters relating to the disclosure requirements

User survey

- 54 user surveys were completed, of which 14 from users and 40 from non-users.
- The user survey was distributed via the national standard-setter network and the *IFRS for SMEs Update*.
- Although the user survey made clear the aim of the survey was to elicit users' views, the survey was also completed by some 'non-users'. Responses to the survey have been considered by type of respondent.
- Respondents are from the Americas (57%), Asia-Oceania (22%), Europe (11%) and Africa (10%).



User respondent type	Completed surveys	
	Number	Percentage
Financial institution lending to SMEs	10	72%
Investor in SMEs	2	14%
Supplier selling to SMEs on credit	1	7%
Analyst	1	7%
Total	14	100%



Non-user respondent type	Completed surveys	
	Number	Percentage
Auditor / Accountant / Consultant	32	80%
National Standard-Setter / Regulator	4	10%
Other	2	5%
Preparer	2	5%
Total	40	100%



User survey: user feedback

Alignment is continuing to develop the *IFRS for SMEs* Standard based on the principles and requirements of IFRS Standards



Question A1

Should the *IFRS for SMEs* Standard be aligned with full IFRS Standards?

Alignment approach – mixed views

- Those users that supported alignment focused on the future of the entity, for example one user said:



‘....when an SME migrates to a large company in line with its growth objective, it is important that it is already in harmony with the Standards and practices based on IFRS Standards....’

- Those users that did not agree with alignment focused on the resources available to SMEs, for example one user said:



‘A lot of SMEs are small companies and do not have the resources to fully comply with complex requirements based on IFRS Standards.’

Cost



Benefit

Relevance

Simplification

Faithful representation



Question A2

Do these principles provide a framework to assist the Board in determining whether and how the *IFRS for SMEs* Standard should be aligned with full IFRS Standards?

Arguments supporting the principles

- Most users supported the alignment principles and agreed the principles provide a framework to assist the Board in determining whether and how the *IFRS for SMEs* Standard should be aligned with full IFRS Standards



One user said: *'The alignment principles are pretty logical.'*

Disclosure simplifications and principles

Paragraph BC157 of the *IFRS for SMEs* Standard

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Users of the financial statements of SMEs are particularly interested in:

- 1** BC157(a) information about short-term cash flows and about obligations, commitments or contingencies, whether or not recognised as liabilities
- 2** BC157(b) information about liquidity and solvency
- 3** BC157(c) information on measurement uncertainties
- 4** BC157(d) information about an entity's accounting policy choices
- 5** BC157(e) disaggregation of amounts presented in SMEs' financial statements



Question B1

In order to provide users of SMEs financial statements with adequate information to make economic decisions, what factors should the Board consider when setting disclosure requirements for the *IFRS for SMEs* Standard?

Overview

Most users agreed with the principles of BC157, other factors noted by users were information about:

- the entity's ability to repay debt, that is liquidity information
- accounting policy choices
- risks, including contingent liabilities

Users noted that disclosures should be simple to understand



"...liquidity ratios provide a picture of the company's financial health, which is very important for entrepreneurs and investors."

If the alignment approach is maintained



Question B2

What benefits and costs to users should the Board consider when setting disclosure requirements for the *IFRS for SMEs* Standard?

Overview

Users made the following suggestions:

- take into consideration resources of SMEs
- consider any omission of disclosure of material information in both qualitative and quantitative aspects



Question B3

Do you agree the *principle* in BC157(a) is particularly useful to users of SMEs financial statements?

Paragraph BC157(a) states that users are particularly interested in:

Information about short-term cash flows and about obligations, commitments or contingencies, whether or not recognised as liabilities

Overview

- Most users agreed that the information in BC157(a) is particularly useful
- One user said long-term cash flows are also important



“Cash-flow is always the key factor to analyse the ‘health’ of a company. We are interested to know the sources of fund i.e. from shareholder, business activities, banking facilities; in order to make sound investment decision.”



Question B4

What information about leases in the financial statements of an SME would be useful for you to evaluate the lease obligations of an entity? Please explain your answer.

Overview

Users' suggestions include:

- recognition of lease liabilities for significant lease arrangements i.e. shipping, aircraft
- the residual duration of the lease and legal obligations of leases
- maturity of lease liabilities
- cash payments for next reporting period



“In IFRS 16, present values do reflect cash payments..”



Question B5

Do you agree the *principle* in BC 157(b) is particularly useful to users of SMEs' financial statements?

Paragraph BC157(b) states:

Users are particularly interested in information about liquidity and solvency

Overview

Most users agreed the information in BC157(b) is particularly useful



"..information about liquidity and solvency are crucial for the survival of SMEs.."



Question B6

To provide information about liquidity and solvency do you believe the *IFRS for SMEs* Standard should require entities to disclose a reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities (debt reconciliation)?

Overview

- Most users agreed that the *IFRS for SMEs* Standard should require the debt reconciliation
- Some users were concerned about the cost of preparing the information
- One user who had reservations about the debt reconciliation said:



“... the reconciliation disclosure may be useful for some users, but the costs of preparing the disclosure may exceed the benefits of reporting that information”



Question B7

When you review the financial statements of SMEs, what information about liquidity and solvency is most often missing?

Overview

Many users said the information that is most often missing is:

- disaggregation of other payables and other receivables
- indebtedness and inventory turnover
- cash flow information for the next 12 months



Question B8

What information about measurement uncertainty do you consider to be most important?

Overview

Users said the following information is important:

- details about assumptions regarding contingent liabilities, pension liabilities, impairment of assets
- impact of covid-19
- going concern assumptions, including breach of bank loan covenant



“Companies need to assess expectations for the future and risks..”



Question B9

Within an SME's financial statements, which line item(s) do you consider require greater disaggregation of information in the notes?

Overview

Users identified the following line item(s) requiring greater disaggregation:

- revenue
- other payables and other receivables
- loans from or to related parties
- significant operating expenses



Question B10

To enable you to understand how and why an entity applying the *IFRS for SMEs* Standard has applied the concept of ‘undue cost or effort’, what additional information would you consider helpful?

Overview

Users made few suggestions, however, one user said:



“An entity should use judgement to determine what information would be useful to users of financial statements whenever an undue cost or effort exemption is used.”

1

Borrowing cost

Provide an option to capitalise borrowing costs on qualifying assets based on similar criteria to those in IFRS Standards

2

Enforcement

The Board should take the responsibility for ensuring entities make every reasonable effort to apply the appropriate financial reporting standard and disclose all the material and relevant financial information

A grayscale world map is the background, showing continents and oceans. Overlaid on the map are several curved, concentric lines that sweep across the globe from the bottom left towards the top right. These lines are composed of a solid gray outer edge and a dotted gray inner edge. The text is positioned in the upper right quadrant of the map.

User survey: feedback from non-users

Alignment is continuing to develop the *IFRS for SMEs* Standard based on the principles and requirements of IFRS Standards



Question A1

Should the *IFRS for SMEs* Standard be aligned with full IFRS Standards?

Alignment approach – mixed views

- Non-users that agreed with alignment focused on better comparison with entities applying full IFRS Standards



‘.... comparison with entities applying IFRS Standards is easier for potential investors to make economic decisions....’

- Non-users that did not support alignment focused on; resources available to SMEs, the need for simplicity, SMEs’ different information needs, users’ access to other information sources. For example, one respondent said:



‘..users would prefer a fresh perspective to all concepts and a re-write of the IFRS for SMEs Standard specifically tailored for their needs’

Cost



Benefit

Relevance

Simplification

Faithful representation

Question A2



Do these principles provide a framework to assist the Board in determining whether and how the *IFRS for SMEs* Standard should be aligned with full IFRS Standards?

Arguments supporting the principles

- The alignment principles provide a framework for assisting the Board in determining whether and how the *IFRS for SMEs* Standard should be aligned with full IFRS Standards



One non-user said: *‘A framework will be very helpful in understanding and explaining the reason behind every alignment decision of the IFRS for SMEs Standard with IFRS Standards.’*



Question B1

In order to provide users of SMEs financial statements with adequate information to make economic decisions, what factors should the Board consider when setting disclosure requirements for the *IFRS for SMEs* Standard?

Factors non-users identified included:

- cash flow information
- size of the entity
- management of financial assets and liabilities
- risks including contingent liabilities
- consider simplicity as SMEs do not have complex structures
- costs and reliability
- other sources of information available to users

If the alignment approach is maintained

Question B2

What benefits and costs to users should the Board consider when setting disclosure requirements for the *IFRS for SMEs* Standard?

Summary

- **Cost** – resources available to preparers—SMEs do not have sophisticated systems to provide information, costs of hiring accountants, complexity, cost of implementation
- **Benefits** – relevance to users, transparency, accountability, clarity, adequacy, comparability

Part B—Information about cash flows, obligation and leases

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B3

Information about cash flows

- Most non-users agreed that cash flows and obligations information is useful
- One respondent said: *'.. in the context of SMEs cash flow disclosures are of major importance and relevant because such entities are usually highly dependent on cash flow to ensure going concern.'*

B4

Information about leases in the financial statements of an SME that would be useful to evaluate the lease obligations

Non-users suggestions for new disclosures include:

- expiry date of lease arrangements
- fair value of leased assets
- discount rate
- any past default on lease payments



One non-user said: *'..the current Section 20 of the IFRS for SME Standard provides enough information for users of SMEs financial statements. IFRS 16 would be costly for preparers..'*



Question B5

Do you agree the *principle* in BC157(b) is particularly useful to users of SMEs' financial statements?

Paragraph BC157(b) states:

Users are particularly interested in information about liquidity and solvency

Overview

- Most non-users agree that liquidity and solvency information is particularly useful
- **Non-users suggestions for new disclosures include:** IFRS 9 risk management disclosures, comparative cash flow, capacity to invest without financing, main ratios i.e. working capital, debt to equity, projected cash flows, source of funding, guarantees and collateral, trends on liquidity and solvency



One non-user said:..... *liquidity and solvency are vital for investors and users of financial statements to make business decisions*



Question B6

To provide information about liquidity and solvency do you believe the *IFRS for SMEs* Standard should require entities to disclose a reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities (debt reconciliation)?

Overview

- Most non-users agree the *IFRS for SMEs* Standard should require the **debt reconciliation**



One non-user said:.... *Information about debt is crucial to assess business survival...*



Question B7

When you review the financial statements of SMEs, what information about liquidity and solvency is most often missing?

Overview

Non-users said the following information is most often missing:

- Main ratios, for example, working capital ratio, debt to equity ratio
- Projected cash flows
- Provisions
- Description of contingent liabilities
- Risk management disclosures in line with IFRS 9
- Sources of funding



Question B8

What information about measurement uncertainty do you consider to be most important?

Overview

- Many non-users said information about provisions and contingencies is important because it involves management judgement
- Others topics mentioned were:
 - ✓ key assumptions and estimates
 - ✓ judgments used
 - ✓ uncertainty about the future
 - ✓ going concern
 - ✓ qualitative information
 - ✓ sensitivity analysis



Question B9

Within an SME's financial statements, which line item(s) do you consider require greater disaggregation of information in the notes?



'..... provide movements of the major accounts in the financial statements to make them more understandable.'

Overview

Many non-users said greater disaggregation is required for all material items in the financial statements

Non-users identified the following line item(s) requiring greater disaggregation:

- inventories
- account payables
- equity
- financial assets and liabilities
- impairment of trade receivables
- revenue
- amount due to and from related parties.



Question B10

To enable you to understand how and why an entity applying the *IFRS for SMEs* Standard has applied the concept of ‘undue cost or effort’, what additional information would you consider helpful?

Summary

Non-users made many suggestions including:

- alternative forgone
- list of all exemptions with brief rationale
- comparison with an entity with the same characteristics
- reason cost is disproportionate
- disclaimer of the nature of each situation considered "undue cost effort"
- information about cost or effort including date at which cost or effort becomes undue
- effect of not applying a requirement including materiality consideration
- effort required to apply a requirement

Key differences

Many SMEs do not apply the *IFRS for SME* Standard because the key differences with IFRS Standards are not clear

Include a Section in the *IFRS for SMEs* Standard on the comparison

Irrelevant disclosures

IFRS 7 and IFRS 13 disclosures are not relevant to SMEs, except for liquidity risk disclosures

IAS 33 *Earnings per Share*

EPS is useful for users and preparers of financial statements

Include some disclosure requirements of IAS 33 in the *IFRS for SMEs* Standard

A grayscale world map is the background for the slide. Overlaid on the map are several thick, light gray curved lines that sweep across the continents. Additionally, there are several dotted lines that form a grid-like pattern across the map, intersecting the curved lines.

User interviews

User interviews – overview

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13



users from 7 jurisdictions



Objective

- provide insight into the **information needs of users** of SMEs financial statements

Questions on...

- A** principles for setting disclosure requirements (paragraph BC157)
- B** useful information about leases
- C** disclosure of reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities

Interview process

- The staff identified users of SME financial statements with the help of SMEIG members and Board members
- A list of questions was sent to interviewees in advance of the interview

Broad principles for setting disclosure requirements

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Question 1

Do you agree with the principles in BC157 in setting disclosure requirements for the *IFRS for SMEs* Standard?

Summary

Most users interviewed agreed with principles in BC157 for setting disclosure requirements.

One interviewee said:



'Disclosure principles explained in paragraph BC157 are right for credit analysis and should be maintained'



Question 2

What other factors should the Board consider when setting disclosure requirements in the *IFRS for SMEs* Standard?

Summary

Most important information from the financial statements for users:

- lenders' ability to repay
- whether the business is sustainable

A small number of users said that 70%–80% of SMEs in their jurisdiction are very small and may not have the capacity to provide the disclosures required by the *IFRS for SMEs* Standard



Question 3

What information about leases in the financial statements of an SME would be useful for you to evaluate the lease obligations of an entity?

Summary

Recognising leases on the statement of financial position:

- will help assess repayment capacity
- will result in better disclosure - ie maturity of lease liabilities
- should not be challenging for SMEs

A small number of users said recognising leases does not impact credit assessments because the asset cannot be collateralised



Question 4

Do you believe the *IFRS for SMEs* Standard should require entities to disclose a reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities?

Summary

Most users said a debt reconciliation would be useful to lenders – it would avoid manual reconciliations



'... a debt reconciliation will provide a clear picture of how much a borrower owes to other banks.'

Summary of other comments

- The information most frequently requested when reviewing SMEs financial statements was additional information about other liabilities and other assets
- Information that is sometimes requested includes:
 - business model
 - post-balance sheet events
 - environmental/sustainability information
- Some lenders noted changes in technology have or will changed the information used for lending decisions – see next slides

Information used to assess credit risk

Central database

- Credit bureau operated by the central bank
- Financial clearance bureau, a voluntary system maintaining information provided by banks
- Credit rating of borrower

Cash flow

- Cash flow information and profile based on analysis of transactions reported on bank statements
- Cash flow projections

Other sources

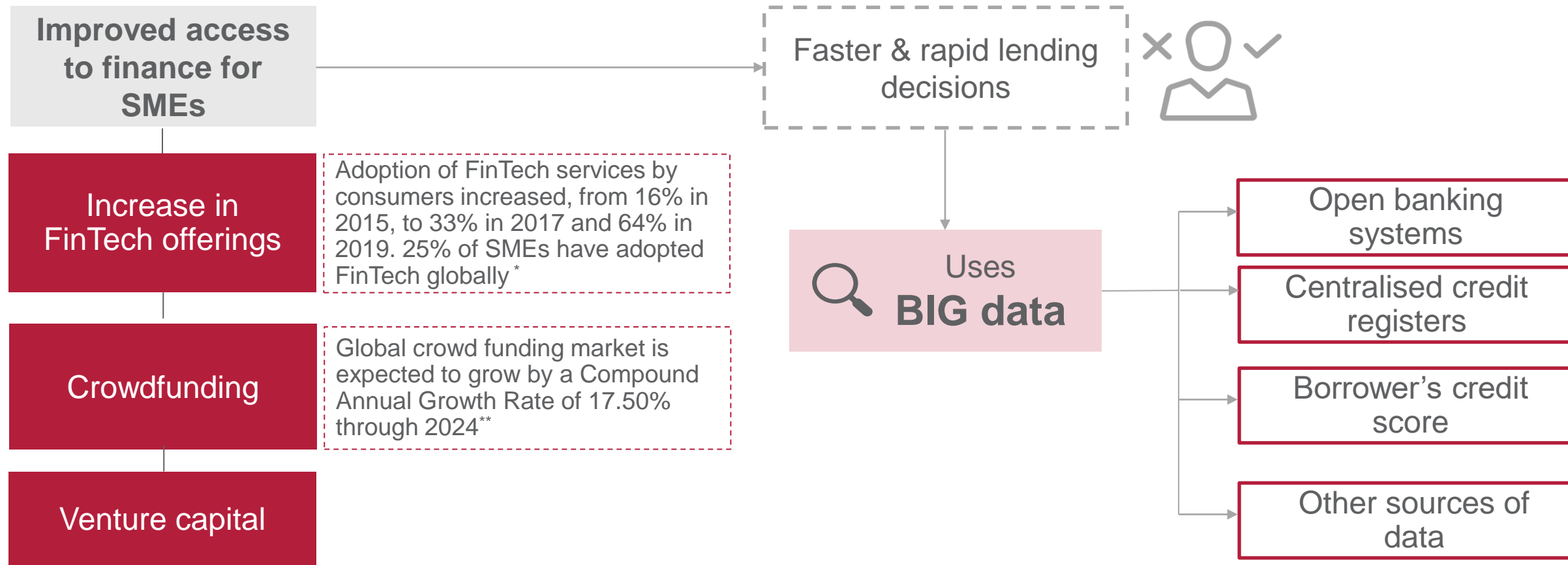
- Interviews and background check of borrowers
- Outsourcing company collecting data from banks



“Most banks do not rely solely on the financial statements to tell the story - we have a lot of qualitative ways to measure the sustainability of the business”

SMEs and sources of finance

Following users interviews staff reviewed 'new' sources of finance to SMEs



* EY Global FinTech Adoption Index 2019

** Crowdfunding Market by Type and Geography - Forecast and Analysis 2020-2024, Technavio.com

Are there implications of new sources of finance on the second comprehensive review?

Investors & lenders

Historically had access to other information:

- could request information from management
- undertake financial due diligence

Impact of technology

What impact does technology have on SMEs?

- new sources of funding are available
- managing data is important, including for raising finance

Implications

What does this mean to SMEs financial statements?

- financial statements are not the single source of data for making lending decisions
- financial statements have confirmatory role

Staff preliminary thoughts:

- The Board should continue to monitor the information needs of users of SMEs financial statements
- The relevance of financial reports should continue to be a focus
- The Board should engage with Fintech to understand information needs

Thank you

- The Board appreciates the engagement by stakeholders who responded to the user survey and users interviewed about SME financial statements
- The Board would also like to thank SMEIG members for promoting the user survey in their jurisdictions and establishing contact with users for interviews

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