STAFF PAPER

June 2022

IASB® meeting

Project	Second Comprehensive Review of the *IFRS for SMEs*® Accounting Standard
Paper topic	Towards an exposure draft—Transition to the third edition of the *IFRS for SMEs* Accounting Standard
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Introduction

1. The International Accounting Standards Board (IASB) has tentatively decided to propose amendments to the *IFRS for SMEs* Accounting Standard, and in May 2022 reached a number of tentative decisions on how entities applying the *IFRS for SMEs* Accounting Standard (Standard) would apply the amendments to be proposed for the first time (transition requirements).
2. This paper continues the discussion on transition requirements, addressing:
   (a) transition requirements relating to IFRIC Interpretations and amendments to IFRS Accounting Standards; and
   (b) guidance for first-time adopters of the *IFRS for SMEs* Accounting Standard.
3. In this paper, the term SMEs refers to entities that are eligible to apply the *IFRS for SMEs* Accounting Standard.

Purpose of the paper

4. The purpose of this paper is to ask the IASB to agree on transition requirements for amendments for IFRIC Interpretations, amendments to IFRS Accounting Standards and other amendments it has tentatively decided to propose as part of this comprehensive review.

Structure of this paper

5. This paper is structured as follows:
   (a) summary of tentative decisions and issues raised so far;
   (b) approach taken to proposing transition requirements;
   (c) amendments to Section 35 *Transition to the* IFRS for SMEs, for first-time adopters; and
   (d) staff recommendation and question for the IASB.
6. Appendix A to this paper includes a summary of recommended transition requirements.

Tentative decisions and issues raised so far

7. At its May 2022 meeting, the IASB tentatively decided to propose transition requirements relating to IFRS Accounting Standards in the scope of this comprehensive review. The transition requirements to be proposed relate to the following six sections of the *IFRS for SMEs* Accounting Standard:
   (a) Section 9 *Consolidated and Separate Financial Statements*;
   (b) Section 11 *Basic Financial Instruments*;
   (c) a new section on *Fair Value Measurement*;
   (d) Section 15 *Investments in Joint Ventures*;
   (e) Section 19 *Business Combinations and Goodwill*; and

(f) Section 23 *Revenue*.

Impracticability and undue cost or effort

8. The staff were asked to consider further whether it is appropriate to use the concept of impracticability for entities to determine whether an accounting policy change arising from amendments to the Standard is to be applied retrospectively (ie when an entity is required to apply the change retrospectively, unless impracticable—sometimes referred to as the 'impracticability exemption').

9. The Standard contains an undue cost or effort exemption, set out in paragraphs 2.14A–2.14D of the Standard and to be replicated in the revised Section 2 *Concepts and Pervasive Principles* in the forthcoming exposure draft. Paragraph 2.14A of the Standard states that 'this exemption shall not be used for other requirements in the Standard'. In other words, it is not a general purpose exemption that entities can use as an option. It is made available for some requirements of the Standard, each time explicitly specified, with associated disclosure requirements. Paragraph 2.14B of the Standard states:

> Applying the requirement would involve undue cost or effort by an SME if the incremental cost (…) or additional effort (…) substantially exceed the benefits that those that are expected to use the SME's financial statements would receive from having the information.

10. The 'impracticability exemption' is in paragraph 10.12 of the Standard, which states that if a change in accounting policy is applied retrospectively (whether because of a change in the Standard or a management decision), the policy is applied to comparative information for prior periods to 'the earliest date for which it is practicable, as if the new accounting policy had always been applied'. When it is impracticable to determine the effects for one or more prior periods, the policy is applied to the carrying amounts of asset and liabilities as at the beginning of the earliest period for which retrospective application is practicable. The Glossary to the Standard explains that 'applying a requirement is impracticable when the entity cannot apply it after making every reasonable effort to do so'.

11. In the staff's view impracticability is a higher hurdle than undue cost or effort since, unlike the undue cost or effort exemption, it does not allow for an entity to weigh up the benefits of making a change to assess whether they justify the cost.

12. Based on the existing definitions and their use within the Standard, the staff do not recommend departing from the reference to impracticability in paragraph 10.12 of the Standard. Its use in transition when applying the Standard for the first time was explained in paragraph BC260 of the Basis for Conclusions on the Standard:

> The IASB observed that Section 35 does not require first-time adopters to retrospectively apply requirements in the *IFRS for SMEs* [Accounting Standard] if it would be impracticable (see paragraph 35.11 of the *IFRS for SMEs* [Accounting Standard]) and including a general 'impracticable' exemption in the transition requirements would be consistent with this. Consequently, the IASB decided that, although it does not think that applying the amendments to Sections 2–28 and 30–35 retrospectively would be significantly burdensome for SMEs, it would include an impracticable exemption that would apply to each amendment in isolation in case there are circumstances that it has not considered in which retrospective application would be impracticable.

Approach to proposing transition requirements

13. The underlying approach for all existing transition requirements comes from several places in the Standard:
    (a) paragraph 10.11(a) of the Standard requires that when an entity changes its accounting policy because of a change in requirements of the Standard, it looks to any transition requirements specified in that amendment.
    (b) Appendix A to the Standard addresses arrangements for entities that were already applying the *IFRS for SMEs* Accounting Standard when the 2015 amendments were issued. It requires that in general amendments are applied in accordance with Section 10 *Accounting Policies, Estimates and Errors*, with a small number of specific exceptions.

(c) as described in paragraph 10 of this paper, there is an impracticability exemption in place that can be applied to any change in accounting policy for which retrospective application is otherwise required.

14. The table in Appendix A to this paper sets out each of the amendments that the IASB has tentatively decided to propose to the Standard based on amendments to full IFRS Accounting Standards or new IFRIC Interpretations. Each amendment is summarised, and the next column explains the approach to transition taken in full IFRS Accounting Standards. The table then summarises the staff recommendation for transition in the *IFRS for SMEs* Accounting Standard with a final column for any notes.

15. The starting point for the staff recommendations was to use the transition requirements in full IFRS Accounting Standards. If full IFRS Accounting Standards offered options, it is generally recommended to remove these on the grounds of simplicity; if the requirements in full IFRS Accounting Standards were judged to be likely to have costs for SMEs that could not be justified by the benefits to users, then further simplifications have been recommended.

16. In most cases, the staff recommendation is to carry the transition requirements from full IFRS Accounting Standards into the *IFRS for SMEs* Accounting Standard. As an exception, it is recommended to remove the option for retrospective application are in Sections 16 *Investment Property* and 26 *Share-based Payment*. In both of these cases, the staff recommendation to remove the option for retrospective application is based on the principle of simplicity through reducing options; however it may be argued this particular option would not add complexity.

17. The single case for which a substantial difference from full IFRS Accounting Standards is recommended is in Section 7 *Statement of Cash Flows.* The IASB amended IAS 7 *Statement of Cash Flows* to require disclosure of changes in liabilities arising from financing activities, including changes arising from cash flows and non-cash flows. Entities applying this amendment for the first time were not required to provide give comparative disclosures because there was less than

one year between the IASB issuing the amendment and its effective date.[1] However, taking into consideration the long time between the expected issue date of the third edition of the *IFRS for SMEs* Accounting Standard and its effective date (the IASB agreed to propose a gap not less than two years) it is considered that there is ample time to collect information and prepare comparative disclosures, so this exemption is not needed in the Standard.

Amendments to Section 35 *Transition to the* IFRS for SMEs

18. Transition requirements are included in Section 35 of the Standard. These apply to first-time adopters of the Standard. Section 35 does not in general require retrospective application; instead it requires application of the new policies from the date of transition. Further exceptions and exemptions are set out in paragraphs 35.9 and 35.10 of the Standard.

19. Paragraph 35.11 of the Standard states:

> If it is impracticable for an entity to make one or more of the adjustments required by paragraph 35.7 at the date of transition, the entity shall apply paragraphs 35.7–35.10 for such adjustments in the earliest period for which it is practicable to do so, and shall identify which amounts in the financial statements have not been restated. If it is impracticable for an entity to provide any of the disclosures required by this Standard, including those for comparative periods, the omission shall be disclosed.

20. In the second edition of the Standard issued in 2015, the amendments made to the Standard were reflected as transition requirements in Appendix A to the Standard, but not in extra exceptions for first-time adopters. The staff recommend to use this approach again, except in the case of accounting for revenue from contracts with customers, for which the Exposure Draft will include a revised Section 23. For the amendments to be proposed to Section 23 only, a modification is recommended to Section 35 to allow the same choices for first-time adopters as those permitted for entities already using the Standard when they change accounting policies when the third edition becomes effective.

[1] Paragraph BC27 of the Basis for Conclusions on IAS 7.

Staff recommendation and question for the IASB

21. In the light of the staff analysis in paragraphs 16–20 of this paper, the staff recommend the IASB propose transition requirements as set out in Appendix A to this paper.

Question for the IASB
Does the IASB agree with the staff recommendation to propose transition requirements in the *IFRS for SMEs* Accounting Standard as set out in Appendix A to this paper, to be included in Appendix A to the Standard in circumstances in which these requirements differ from the default approach of fully retrospective application?

Appendix A—Summary of recommended transition requirements

Section of the *IFRS for SMEs* Accounting Standard	Amendments to align with full IFRS Accounting Standard	Transition requirements in full IFRS Accounting Standards	Additional reliefs recommended for the *IFRS for SMEs* Accounting Standard	Notes
Section 3 *Financial Statement Presentation*	Amendments to align with the following package of amendments to IAS 1 *Presentation of Financial Statements*			
	Definition of Material (Amendments to IAS 1 and IAS 8)	Prospective application	No further reliefs	
	Disclosure Initiative (Amendments to IAS 1)	Retrospective application	No further reliefs	
	Disclosure of Accounting Policies (Amendments to IAS 1)	Retrospective application	No further reliefs	
Section 7 *Statement of Cash Flows*	Amendments to Section 7 of the *IFRS for SMEs* Accounting Standard to require SMEs to disclose changes in liabilities arising from financing activities, including changes arising from cash flows and non-cash flows. These are a simplification of the disclosure requirement introduced by *Disclosure Initiative* (Amendments to IAS 7)	No comparative information required for preceding periods.	No comparable relief recommended (ie full retrospective application and the new requirements would be applied to disclosures in all comparative periods presented)	Taking into consideration the additional time SMEs will have to implement the third edition of the *IFRS for SMEs* Accounting Standard and the importance of liquidity and solvency disclosures to users of financial statements the staff do not consider there is a need to provide relief from the requirement to provide comparative information when first applying the amendment to Section 7.

Section of the *IFRS for SMEs* Accounting Standard	Amendments to align with full IFRS Accounting Standard	Transition requirements in full IFRS Accounting Standards	Additional reliefs recommended for the *IFRS for SMEs* Accounting Standard	Notes
Section 9 *Consolidated and Separate Financial Statements*	Amendment from aligning the Section with IFRS 10 *Consolidated Financial Statements* to require a parent that loses control of a subsidiary to remeasure any retained interest in the former subsidiary at fair value.	An entity shall not restate the carrying amount of an investment in a former subsidiary if control was lost before it applied the amendments in paragraphs 25 and B97–B99 of IFRS 10 for the first time. In addition, an entity shall not recalculate any gain or loss on the loss of control of a subsidiary that occured before the amendments in paragraphs 25 and B97–B99 of IFRS 10 were applied for the first time.	Recommend replicating the relief from IFRS 10: An entity shall not restate the carrying amount of an investment in a former subsidiary if control was lost before it applied the amendments in paragraphs [9.19] and [9.19A] for the first time. In addition, an entity shall not recalculate any gain or loss on the loss of control of a subsidiary that occured before the amendments in paragraphs [9.19] and [9.19A] were applied for the first time.	

Section of the ***IFRS for SMEs*** **Accounting Standard**	**Amendments to align with full IFRS Accounting Standard**	**Transition requirements in full IFRS Accounting Standards**	**Additional reliefs recommended for the *IFRS for SMEs* Accounting Standard**	**Notes**
Section 14 *Investments in Associates*	Amendments clarifying the treatment for long-term interests in an associate or jointly controlled entity that form part of the entity's net investment in an associate or jointly controlled entity.	Retrospective application with some alterations based on timing of first-time adoption of IFRS 9 *Financial Instruments*	Retrospective application	Refinements relating to financial instruments are not considered necessary as the *IFRS for SMEs* Accounting Standard is updated infrequently.
Section 16 *Investment Property*	Amendments aligning with those in IAS 40 *Investment Property*: (a) an entity shall transfer a property to or from the 'investment property' line item only when there is evidence of a change in use. (b) determining whether a specific transaction meets the definition of both a business combination and an investment property requires the separate application of both relevant sections (Section 16 *Investment property* and Section 19 *Business combinations).*	Prospective application from the date of initial application Prospective application from the date of initial application Retrospective application available for both amendments as an accounting policy choice	No changes – recommend prospective application No changes – recommend prospective application Recommend to simplify by not including this option	Omitting the option to choose retrospective application is in line with the guidance from the Basis for Conclusions on the *IFRS for SMEs* Accounting Standard to permit only the simplest option available under IFRS Accounting Standards.

Section of the *IFRS for SMEs* Accounting Standard	**Amendments to align with full IFRS Accounting Standard**	**Transition requirements in full IFRS Accounting Standards**	**Additional reliefs recommended for the *IFRS for SMEs* Accounting Standard**	**Notes**
Section 17 *Property, Plant and Equipment*	Amendments to align the Section with IAS 16 *Property, Plant and Equipment* to clarify that while the depreciation method should reflect the expected pattern of consumption of future economic benefits of an asset, the use of a depreciation method based on revenue is not appropriate.	Prospective application	No changes – recommend prospective application	
Section 18 *Intangible Assets other than Goodwill*	Amendments to align the Section with IAS 36 *Impairment of Assets* to clarify why the use of revenue-based methods is generally presumed to be an inappropriate basis for measuring the consumption of future economic benefits embodied in an intangible asset.	Prospective application	No changes – recommend prospective application	

Section of the *IFRS for SMEs* Accounting Standard	Amendments to align with full IFRS Accounting Standard	Transition requirements in full IFRS Accounting Standards	Additional reliefs recommended for the *IFRS for SMEs* Accounting Standard	Notes
Section 26 *Share-based Payment*	Minor amendments for alignment of the Section with IFRS 2 *Share-based Payment* relating to: (a) the effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payment (b) the accounting treatment of share-based payment with a net settlement feature for withholding tax obligations (c) the accounting treatment for modifications to the terms and conditions that change an arrangement's classification from cash-settled to equity-settled (d) definitions of vesting condition and market condition	Prospective application for unvested awards from the beginning of the first period (or optional retrospective application with (b) and (c)) Prospective application for unvested awards and vested but not exercised awards (or optional retrospective application with (a) and (c)) Prospective application (or optional retrospective application with (a) and (b)) Prospective application (or optional retrospective application)	Recommend prospective application for all from beginning of earliest period presented, with no option to apply retrospectively	Omitting the option to choose retrospective application is in line with the guidance from the Basis for Conclusions on the *IFRS for SMEs* Accounting Standard to permit only the simplest option available under IFRS Accounting Standards. It also removes the complexity from IFRS 2 where the option to apply each of amendments (a) to (c) retrospectively is only available if the other two are also applied retrospectively

Section of the *IFRS for SMEs* Accounting Standard	Amendments to align with full IFRS Accounting Standard	Transition requirements in full IFRS Accounting Standards	Additional reliefs recommended for the *IFRS for SMEs* Accounting Standard	Notes
Section 28 *Employee Benefits*	Multiple editorial amendments plus: (a) the deletion of the measurement simplification in paragraph 28.19 for defined benefit obligations; and (b) alignment with the recognition requirements for termination benefits in IAS 19 *Employee Benefits*.	None relevant to the *IFRS for SMEs* Accounting Standard Termination benefits – retrospective application	No reliefs recommended – require full retrospective application	
Section 29 *Income Tax*	Amendment to align with IFRIC 23 *Uncertainty over Income Tax Treatments* on uncertainty over income tax treatments Amendment for recognition of deferred tax assets for unrealised losses	Prospective application from beginning of earliest period Retrospective application but adjustments to opening equity need not allocate the adjustment between retained earnings and other components of equity	Recommend prospective application as in full IFRS Accounting Standards Recommend reproducing retrospective application with the relief from full IFRS Accounting Standards	

Section of the *IFRS for SMEs* Accounting Standard	Amendments to align with full IFRS Accounting Standard	Transition requirements in full IFRS Accounting Standards	Additional reliefs recommended for the *IFRS for SMEs* Accounting Standard	Notes
Section 30 *Foreign Currency Translation*	Amendments relating to IFRIC 22 *Foreign Currency Transactions and Advance Consideration* addressing the exchange rate to use for transactions that involve advance consideration paid or received in another currency	Prospective application for items initially recognised on or after the beginning of the reporting period in which the Interpretation is first applied or the beginning or a prior period presented as a comparative period; retrospective application permitted.	Recommend prospective application with the option to apply retrospectively.	Unlike in other sections, the removal of the option to apply the amendments retrospectively would not be appropriate as it would lead to difficulties for advance payments made or received before the transition date.
Section 34 *Specialised Activities*	Amendments to align with IAS 16 and IAS 41 *Agriculture* to require SMEs to account for a bearer plant on initial recognition separately from the produce growing on the bearer plant if SMEs can measure the bearer plant and the produce growing on the bearer plant separately without undue cost or effort	Permit use of fair value as deemed cost at the beginning of the earliest comparative period; exemption from disclosing the adjustment for each financial statement line item affected that would otherwise have been required by paragraph 8.28(f) of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*	Recommend the same transition requirements as in full IFRS Accounting Standards	Note that SMEs using the undue cost or effort exemption from separating out their bearer plants and produce will have no changes to their accounting policy and thus need no transition requirements