IFRS Foundation Trustees' Due Process Oversight Committee (DPOC) meeting

Date	**May 2023**
Project	**Amendments to the *IFRS for SMEs* Accounting Standard—International Tax Reform—Pillar Two Model Rules**
Topic	**Comment period for proposed amendments to the *IFRS for SMEs* Accounting Standard**
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Purpose

1. In accordance with paragraph 6.7 of the *Due Process Handbook*, the International Accounting Standards Board (IASB) normally allows a minimum period of 120 days for comment on an exposure draft. If the matter is narrow in scope and urgent the IASB may set a comment period of less than 120 days (but no less than 30 days) after consulting and obtaining approval from the DPOC.

2. **The purpose of this paper is to seek the approval of the Due Process Oversight Committee (DPOC) for a shortened comment period for an exposure draft of proposed narrow-scope amendments to the *IFRS for SMEs* Accounting Standard.**

3. The posting date of this agenda paper is before the IASB's supplementary meeting scheduled on 3 May 2023, at which the IASB will discuss the staff recommendation to set a shortened comment period of 45 days (subject to DPOC approval). Therefore, we will provide an oral update on the IASB's discussion and decisions at the DPOC meeting.

Proposed narrow scope-amendments to the *IFRS for SMEs* Accounting Standard

Background

4. At its November 2022 meeting, the IASB discussed the potential effects of the OECD's Pillar Two model rules on the accounting for income taxes by an entity applying IAS 12 *Income Taxes*. The IASB published the Exposure Draft *International Tax Reform—Pillar Two Model Rules* in January 2023. The Exposure Draft was open for comment until 10 March 2023 (a period of 60 days, approved by the DPOC at its meeting on 1 December 2022). At its supplementary meeting in April 2023, the IASB discussed the feedback on the Exposure Draft and decided to finalise amendments to IAS 12. The amendments will introduce:

(a) a temporary exception to the accounting for deferred taxes arising from the jurisdictional implementation of the global tax rules; and

(b) targeted disclosure requirements for affected companies to help users of the financial statements better understand a company's exposure to Pillar Two income taxes arising from that legislation, particularly before the effective date of that legislation.

5. The final amendments to IAS 12 are expected to be issued by the end of May 2023.

Relevance to small and medium-sized enterprises (SMEs)[1]

6. The staff monitors the progress of the projects on the IASB's work plan and where necessary seeks advice from the members of the SME Implementation Group (SMEIG) about whether, and if so how, the *IFRS for SMEs* Accounting Standard should be updated for a new or amended IFRS Accounting Standard[2].

7. Our preliminary outreach with the members of the SMEIG in January 2023 on forthcoming amendments to the IFRS Accounting Standards did not provide evidence that the proposed amendments to IAS 12 for Pillar Two model rules would be relevant to SMEs and would require an urgent amendment to the *IFRS for SMEs* Accounting Standard. Furthermore, neither respondents to the Exposure Draft *International Tax Reform—Pillar Two Model Rules* nor the Exposure Draft *Third edition of the* IFRS for SMEs *Accounting Standard*, both of which comment periods ended in March 2023, identified the Pillar Two model rules as an issue for SMEs.

8. However, more recently, some jurisdictions have more clarity about how their domestic tax policy may change for the Pillar Two model rules becoming effective and our ongoing monitoring indicated that the rules might have a material effect on some SMEs' financial statements.

9. To obtain evidence about the relevance of the Pillar Two model rules (and the proposed amendments to IAS 12) to SMEs, in March 2023 we undertook further outreach with SMEIG members. We also reached out to large accounting firms. This outreach provided evidence that Pillar Two model rules could have material effects on financial statements of some entities applying the *IFRS for SMEs* Accounting Standard. Comments from respondents included:

(a) subsidiaries (of the multinational enterprises) applying the *IFRS for SMEs* Accounting Standard might be in the scope of the Pillar Two model rules—for example, a subsidiary (in South Africa applying the *IFRS for SMEs* Accounting Standard) whose parent prepares consolidated financial statements applying US GAAP. If this is the case, such entities might face significant

[1] Throughout this paper, the term 'SMEs' refers to small and medium-sized entities that are eligible to apply the *IFRS for SMEs* Accounting Standard (entities that do not have public accountability and publish general-purpose financial statements for external users).
[2] For example, the IASB consulted the SMEIG and based on the advice of SMEIG members decided no action should be taken for the amendments to full IFRS Accounting Standards relating to the IBOR reform.

complexities in recognising the deferred tax assets and deferred tax liabilities arising from the rules.

(b) there might be entities applying the *IFRS for SMEs* Accounting Standard that are parent entities that will be in the scope of the Pillar Two model rules.

(c) there is potential for entities that both apply the *IFRS for SMEs* Accounting Standard and reside in jurisdictions with tax rates below 15% to be affected.

(d) some entities applying national GAAP that is based on the *IFRS for SMEs* Accounting Standard can be affected by the Pillar Two model rules.

(e) it is unclear how domestic tax policies in various jurisdictions may change as a consequence of the Pillar Two model rules becoming effective, so it is difficult to assess potential implications of Pillar Two model rules on the accounting for deferred tax applying the *IFRS for SMEs* Accounting Standard. By the time the Third Edition of the *IFRS for SMEs* Accounting Standard is published, the domestic tax policies will be known, but it may still be unclear how to account for deferred tax arising from the rules. So, there may still be a need for some form of exemption.

Urgency

10. Determining when to align the *IFRS for SMEs* Accounting Standard with a new or amended IFRS Accounting Standard is an essential step in the periodic reviews of the *IFRS for SMEs* Accounting Standard.

11. The IASB normally proposes amendments to the *IFRS for SMEs* Accounting Standard by publishing an omnibus Exposure Draft periodically, but not more frequently than approximately once every three years. In developing those Exposure Drafts, the IASB considers new and amended full IFRS Accounting Standards as well as specific issues that have been brought to its attention regarding application of the *IFRS for SMEs* Accounting Standard.[3] The IASB is undertaking its Second Comprehensive Review of the *IFRS for SMEs* Accounting Standard. However, the Third Edition of the *IFRS for SMEs* Accounting Standard, resulting from the second comprehensive review, is not expected to be issued until late 2024 at the earliest.

12. Paragraph P16 of the Preface to the *IFRS for SMEs* Accounting Standard states that, in rare cases, some matters may need to be considered outside the periodic reviews of the Accounting Standard:

> On occasion, the IASB may identify an urgent matter for which amendment of the *IFRS for SMEs* may need to be considered outside

[3] Paragraph P16 of the Preface to the *IFRS for SMEs* Accounting Standard.

> the periodic review process. However, such occasions are expected to be rare.

13. Paragraph BC190 of the Basis for Conclusions on the 2015 *IFRS for SMEs* Accounting Standard states:

> The IASB decided that new and revised full IFRS Standards should not be considered until they have been issued. This is because, until a final full IFRS Standard is issued, the IASB's views are always tentative and subject to change.

The IASB's tentative decision and project timing

14. Considering the nature of the potential amendments and the relevance of the Pillar Two model rules, at its April 2023 meeting the IASB decided to undertake urgent narrow-scope standard-setting outside the Second Comprehensive Review of the *IFRS for SMEs* Accounting Standard, even though the amendments to IAS 12 have not been issued yet. This would be first urgent amendment to the *IFRS for SMEs* Accounting Standard since it was issued in 2009.

15. The IASB noted, in the absence of the relief from accounting for deferred tax assets and liabilities related to Pillar Two income taxes, some SMEs would incur additional costs compared to entities applying full IFRS Accounting Standards.[4]

Recommended comment period

16. At its meeting in April 2023, the IASB deferred a decision on the length of the shortened comment period until it has decided on what amendments to propose to the *IFRS for SMEs* Accounting Standard. The IASB's discussion indicated that the IASB was generally supportive of a shortened comment period. The discussion also indicated that the length of the shortened comment period might depend on the nature of the disclosures the IASB decides to propose in the exposure draft.

17. The posting date of this agenda paper is before the IASB's supplementary meeting scheduled on 3 May 2023, at which the IASB will discuss the staff recommendation to set a shortened comment period of 45 days (subject to DPOC approval). Therefore, we will provide an oral update on the IASB's discussion and decisions at the DPOC meeting.

[4] Paragraph P17 of the Preface to the *IFRS for SMEs* Accounting Standard states: 'SMEs shall not anticipate or apply changes made in full IFRS before those changes are incorporated into the *IFRS for SMEs* unless, in the absence of specific guidance in the *IFRS for SMEs*, an SME chooses to apply guidance in full IFRS Accounting Standards and those principles do not conflict with requirements in the hierarchy in paragraphs 10.4–10.5.'

18. The staff will be recommending a 45-day comment period to enable the IASB to finalise any amendments to the *IFRS for SMEs* Accounting Standard urgently, while providing sufficient time for stakeholders to comment on the proposals.

19. In reaching its recommendation, the staff took the following matters into consideration:

    (a) The Pillar Two model rules are relevant to only a subset of SMEs, which are either subsidiaries of large multinational enterprises (which will be already assessing their exposure and preparing to comply with Pillar Two legislation) or large SMEs generating revenues exceeding the thresholds specified in the Pillar Two model rules. Consequently, the matter will affect only that subset of SMEs, many of which are likely to be familiar with the issue and have the resources to respond quickly.

    (b) The Exposure Draft *International Tax Reform—Pillar Two Model Rules* was open for comments for 60 days and (by the comment letter deadline) the IASB received 94 comment letters from a broad range of stakeholders across all regions, suggesting that a shortened comment period did not impair stakeholders' ability to respond. The feedback will help to inform the IASB in developing the narrow-scope amendment to the *IFRS for SMEs* Accounting Standard. Similarly, affected SMEs will be able to build on this feedback and the IASB's deliberations, which will inform their views on the proposals and mean they require less time to understand the matter.

    (c) The proposed amendments would be narrower in scope than the proposed amendments to IAS 12—the staff are not recommending new disclosure requirements in periods in which Pillar Two legislation is enacted or substantively enacted but not yet in effect. This is because the *IFRS for SMEs* Accounting Standard has different disclosure requirements to full IFRS Accounting Standards and the staff is proposing the IASB uses those disclosure requirements, rather than propose new disclosure requirements.

    (d) We expect some respondents to the proposed amendments to the *IFRS for SMEs* Accounting Standard to be the same as the respondents to the Exposure Draft (for example, national standard-setters, large accounting firms).

    (e) The IASB would need to finalise any amendments expeditiously for them to be effective.

    (f) The proposed amendments respond to stakeholders' concerns about the urgent need for clarity given the imminent implementation of the Pillar Two model rules in various jurisdictions around the world.

    (g) The proposed amendments would support consistent application of the *IFRS for SMEs* Accounting Standard for the benefits of users of SMEs' financial statements.

    (h) The IASB may consider using an online survey, to help stakeholders respond within the shortened comment period.

(i) Overall, the IASB received positive feedback on the Exposure Draft of the proposed amendments to IAS 12. In particular, almost all respondents agreed with the proposed temporary exception to the accounting for deferred taxes.

Question for the DPOC

20. **Assuming the IASB agrees with the staff's recommended comment period, does the DPOC give its approval for a shortened comment period of 45 days for an exposure draft of proposed narrow-scope amendments to the *IFRS for SMEs* Accounting Standard?**