



FEE Position on EC Consultation on IFRS for SMEs

General

- (1) FEE (The Federation of European Accountants) commends the EC for carrying out a consultation on IFRS for SMEs and for seeking the views of all stakeholders. FEE welcomes a debate on the role IFRS for SMEs can play within the EU, before deciding at EC level on the best course of action in the context of the forthcoming revision of the Accounting Directives. FEE is looking forward to actively contributing to this debate.
- (2) The position taken in this response to the consultation reflects the view of FEE. Individual Member Bodies of FEE in some Member States may submit positions which differ in certain respects from the common position expressed by FEE in this submission. There is concern in some Member States that the additional requirements in IFRS for SMEs do not add value commensurate to the costs and consequences that would result in relation to changing the existing financial reporting framework in those Member States.
- (3) However, these concerns are counterbalanced by the position taken by other Member States, who are already contemplating a reduction of their national standard setting activity and to permit or require the use of IFRS for SMEs. This could lead to real and tangible cost reductions at national level in those Member States.
- (4) As said in previous submissions, FEE believes that there is a need to have European Accounting Directives and supports a complete revision of the existing Directives. We would also welcome a fundamental debate on the objective of further accounting harmonisation in the EU. Until now, accounting harmonisation in Europe has been impacted by various factors including the strong links that exist in some Member States between financial accounting, the determination of taxable income and capital maintenance and dividend distribution requirements. These will need to be addressed before any significant improvements can be made with regard to accounting harmonisation in Europe.
- (5) FEE believes that IFRS for SMEs can contribute to enhancing harmonisation in Europe and therefore, in our view, the revision of the Directives provides a proper opportunity to address any real or perceived discrepancies between the Accounting Directives and IFRS for SMEs.
- (6) FEE supports high quality, global principles-based financial reporting standards, since these promote consistency and transparency and help companies and their advisors to respond appropriately to new developments in business practice. In this context, FEE also welcomed the IFRS for SMEs. FEE expects that in several Member States, companies, including SMEs with cross-border activities, branches and subsidiaries, will be able to simplify their financial reporting through the use of IFRS for SMEs.

- (7) Transparency in relation to accounting and financial statements is an essential facilitator for cross border trade. There is a need for more internationally comparable and harmonised financial statements, especially for medium-sized and large non-listed companies. Companies of all sizes are increasingly affected by today's more open and global economy because they increasingly engage in cross border operations, have subsidiaries and branches in multiple Member States and are subject to increasing foreign direct investments. The globalisation of the banking system is also a factor in driving the need for recognisable and comparable financial statements across borders.
- (8) In the longer term, a widespread adoption of IFRS for SMEs would also facilitate education and familiarity with two sets of global accounting standards across the world, one for listed companies and one for unlisted companies. An internationally recognised standard for SMEs will help the accountancy profession at large, as accountants – in business and in audit firms of all sizes – can all be trained in the same accounting language, making movement of accountants across borders and between firms easier in the longer term. Also users of financial statements from different jurisdictions will benefit from the same principles in different countries and sizes of companies.

Responses to the Questions

Question 1:

Do you think the IFRS for SMEs is suitable for widespread use within Europe?

X YES NO Don't know

Please comment, indicating whether there are any type(s) or size(s) of company that would benefit from adopting the Standard:

- (9) Yes, we believe that IFRS for SMEs is suitable for widespread use within Europe, although in some Member States there may be barriers currently to the use of IFRS for SMEs (see paragraph 12). Since IFRS for SMEs is based on the same fundamental principles of full IFRS (even though they are a stand-alone set of standards), IFRS for SMEs could be attractive for small subsidiaries of multinationals that apply full IFRS. Moreover, IFRS for SMEs can be used as a stepping stone by larger companies that ultimately want to move to a listing, and hence full IFRS.
- (10) IFRS for SMEs may equally be suitable for smaller companies, although for some implementation may be perceived as too complex or too costly compared to the benefits that can be derived from it. Gaining practical experience with the standards may be a good way to assess whether they are fit for application by smaller enterprises. In our view, IFRS for SMEs is a complete and robust set of standards on a stand-alone basis, with the fundamental principles of accounting based on full IFRS. Practical experience including feedback from users, may result in suggestions for changes to the IASB in future versions of IFRS for SMEs.
- (11) In several Member States, large and medium-sized private companies are currently permitted to use full IFRS for their consolidated accounts as this is a Member State option in the IAS Regulation. In some Member States, full IFRS is also permitted to be used in the annual (separate) accounts as an alternative to national GAAP. Under those circumstances, it is difficult to see why IFRS for SMEs should not equally be permitted, as IFRS for SMEs is often better suited for those purposes than full IFRS.

- (12) In countries where the annual accounts include both financial reporting information and information related to the entity's tax return, it may not be possible at this stage to use IFRS for SMEs in the annual accounts. Tax rules may give more weight to other interpretations of principles such as prudence, whereas IFRS for SMEs is aimed at providing information for economic decision making rather than the determination of the taxable result¹. Similarly, there may be concerns about capital maintenance requirements and dividend distributions based on IFRS for SMEs. Due to these barriers, the attractiveness of IFRS for SMEs in these countries may still be limited, and companies wishing to use IFRS for SMEs would have to prepare an additional set of financial statements, over and above the statutory accounts if they wished to use the standard, which would only be justified if there were other compelling benefits for the company concerned, e.g. attracting international finance or international investors.
- (13) As indicated in our general observations, further harmonisation of accounting in Europe, including the use of IFRS for SMEs across the EU, would require addressing the barriers that stem from all areas related to accounting, in particular the linkage with taxation and profit distribution. FEE believes that Member States should be allowed to consider such concerns as the linkage with taxation for themselves and decide at a Member State level whether to permit or mandate IFRS for SMEs.

Question 2:

If you are a preparer of company accounts can you indicate any costs (both one-off and recurring) or benefits, and any other effects of adopting the IFRS for SMEs?

Please comment.....

In particular, do you think increased international comparability of accounts prepared under the IFRS for SMEs will benefit your business?

YES NO Don't know

Please comment.....

- (14) The use of IFRS for SMEs may result in greater comparability between listed and unlisted companies within EU boundaries. As indicated in paragraph 9 above, it can also be considered as a stepping stone for companies that plan to be listed at some stage and then have to use full IFRS. In paragraph 5 above, we have illustrated the role of IFRS for SMEs in helping to resolve the need for more internationally comparable and harmonised financial statements.
- (15) We recognise however that the comparability of financial statements between private companies to a certain extent will be impaired within a country depending on the way IFRS for SME is introduced. The method of adoption of IFRS for SMEs, as well as the extent to which national GAAP differs from IFRS for SMEs, will impact on comparability in the short term, as will the publication requirements for smaller entities (such as abbreviated financial statements).

¹ Prudence is the inclusion of a degree of caution in the exercise of the judgements needed in making the estimates required under conditions of uncertainty, such that assets or income are not overstated and liabilities or expenses are not understated. However, the exercise of prudence does not allow the deliberate understatement of assets or income, or the deliberate overstatement of liabilities or expenses. In short, prudence does not permit bias (para 2.9 IFRS for SMEs).

- (16) It should also be noted, though, that limited comparability of financial statements, both within individual countries and between Member States, is reflective of the current situation, where full IFRS can be used in addition to national GAAP in various Member States, and where national GAAP differs significantly between EU Member States depending on the different ways in which the Accounting Directives have been implemented at national level.

Question 3:

If you are a user of accounts (for example a bank) do you think the IFRS for SMEs will provide more useful information than national GAAP accounts?

YES NO Don't know

Please comment.....

- (17) Not applicable. Please refer to our general observations in paragraphs 1 to 8.

Question 4:

Does increased international comparability of accounts prepared under the IFRS for SMEs benefit users?

YES NO Don't know

Please comment.....

- (18) Yes, see our response to Question 2.

Question 5:

Do you think adoption of the IFRS for SMEs should be provided for within the EU accounting legal framework?

YES NO Don't know

Please comment.....

- (19) FEE believes that Member States should be allowed to decide at a Member State level whether to permit or require IFRS for SMEs. We understand that some EU Member States are already actively contemplating either to permit or require IFRS for SMEs directly or to adopt the standards as their national GAAP.
- (20) To the extent that there may presently be conflicts between the Accounting Directives and IFRS for SMEs, the revision of these Directives provides a proper opportunity to address any existing impediments. The draft study prepared by EFRAG comparing IFRS for SMEs and the Accounting Directives provides an overview of such potential conflicts and provides a good basis for the Commission's work on the overhaul of the Accounting Directives.
- (21) There are different ways to permit the use of IFRS for SMEs in Europe. Each way has its own merits and disadvantages. One way would be for the Directives to explicitly mention IFRS for SMEs using a company option or Member State option. Alternatively, the Accounting Directives could remain silent on IFRS for SMEs and, so long as they contain no impediments that would create barriers for the use of IFRS for SMEs, Member States would be free to permit the use of IFRS for SMEs and still be in compliance with the

Accounting Directives, whilst any impediments arising at national level can be dealt with by adapting national legislation.

- (22) In our response to Question 8, we have commented on the other alternative of introducing a company option in the Accounting Directives.
- (23) The Directives could include a Member State option to permit or require the use of the IFRS for SMEs by all unlisted companies covered by the Accounting Directives. This would give Member States the possibility to grant a free choice to individual companies to apply IFRS for SME or apply national legislation based on the Accounting Directives. It will then be up to the Member State to decide, if and for which companies IFRS for SMEs should be permitted or required. A possibility could be that a Member State could require the use of IFRS for SMEs for large and medium-sized private companies, whereas smaller companies could be given a free choice between IFRS for SMEs and national GAAP. Alternatively, some Member States may decide not to permit the use of IFRS for SMEs at all.
- (24) Inclusion in the Accounting Directives of a Member State option, permitting or requiring IFRS for SMEs, would give Member States the possibility to allow the use of IFRS for SMEs directly without having to adapt their national legislation. Member States would also be free to make a distinction between the individual and consolidated accounts, as discussed in our response to Question 1. Finally, an explicit Member State option may also provide directional guidance to (smaller) Member States and may result in a wider adoption of IFRS for SMEs.
- (25) For those Member States not wishing to permit IFRS for SMEs, there may be some concern that an explicit Member State option in the Accounting Directives gives too much acknowledgement to IFRS for SMEs. There may also be a concern in those Member States that the provision of such an option in the Directives (explicitly or implicitly), could undermine the comparability of financial statements of private companies, given that some companies in the EU would use IFRS for SMEs or national GAAP based thereon, and others would have to apply national GAAP that has no relation with IFRS for SMEs. However, the possible lack of comparability is no different from the current situation, where there are 27 different versions of national GAAP being used, based on the existing Accounting Directives.
- (26) A reference to IFRS for SMEs in the Accounting Directives also raises the question of endorsement of IFRS for SMEs. Some new form of endorsement mechanism could be envisaged or, alternatively, the existing endorsement mechanism under the 2002 IAS Regulation could be extended to cover this as well. In the latter case, it would need to be considered if the same endorsement criteria should be used. IFRS for SMEs will be amended every three years and therefore it is essential that an endorsement process takes place every three years.
- (27) Member States should be allowed to decide at a Member State level whether to permit or require IFRS for SMEs. As long as the Directives do not include any barriers for adopting IFRS for SMEs, a specific reference to IFRS for SMEs may not be necessary. Any differences at national level could be solved by adapting the national law. However, if a later revision of IFRS for SMEs would result in incompatibilities with the Directives it may subsequently be more difficult to change the Directives than in a situation where the use of IFRS for SMEs is directly referred to in the Directives. Some form of explicit and formal



acknowledgement that there are no conflicts between the Accounting Directives and IFRS for SMEs would be needed at EU level. This would need to be supported by a similar acknowledgement, directed towards national law or GAAP, issued by those Member States that wish to allow the use of IFRS for SMEs. This would give companies the comfort needed to apply IFRS for SMEs.

Question 6:

If yes, should such an option be limited to a Member State option (i.e. that each Member States would have a possibility but no obligation to accept IFRS for SME)?

YES NO Don't know

Please comment.....

(28) Please refer to our response to Question 5 for more details.

Question 7:

Do you have other views on the possible adoption of the IFRS for SMEs within the EU accounting framework?

Please comment.....

(29) See our response to Question 5.

Question 8:

Is there a case for giving companies, at EU level, an option to adopt the IFRS for SMEs?

YES NO Don't know

If yes, for which categories:

small

medium

large

other criteria (please explain)

Please comment.....

(30) A direct company option included in the Directive would offer every non-listed company in Europe the possibility of using IFRS for SMEs directly. For some, this may be seen as an ideal solution, because it would leave full freedom to preparers and other stakeholders to individually decide on the adoption of IFRS for SMEs. However, in our view, a company option is unlikely to be a feasible solution at this stage, given the differences in accounting traditions in Europe, in particular the differences in relation to the linkage of accounting with taxation and capital maintenance and dividend distribution considerations that exist in some Member States. See also our response to Question 5.

Question 9:

What should be done, in your view, where there is incompatibility between the Directives and the IFRS for SMEs?

Please comment.....

(31) As stated in our response to Question 5, any incompatibilities between the Directives and IFRS for SMEs should be addressed as part of the revisions of the Accounting Directives.

This should be done after careful consideration of any conflicts as revealed in the EFRAG comparison study between IFRS for SMEs and the Accounting Directives. Incompatibilities should, in any case, be addressed with or without any specific mention of IFRS for SMEs in the Accounting Directives.

Question 10:

In the light of the publication of the IFRS for SMEs, do you see a need for "rules-based" Accounting Directives in the future?

YES x NO Don't know

If yes, for what type(s) or size(s) of company are detailed rules required?

small

medium

large

other criteria (please explain)

Other than the 5 items listed in paragraph 4.3 above, what aspects of financial reporting should the revised Directives address, and to what level of detail.....?

Other comments.....

- (32) No. As stated in the FEE Position on the EC Consultation Paper on Review of the Accounting Directives – Cutting Accounting Burden for Small Business/Review of the Accounting Directives of 21 April 2009, FEE believes that any future Directive(s) should provide a basic framework for financial statements by addressing reporting, filing, publication and auditing principles. The reporting requirements should introduce the main accounting principles and basic accounting requirements following the principles, leaving more detailed accounting requirements to the accounting standard setters. All measures to modernise the Directives must be in line with their principles-based character. Such an approach allows for sufficient flexibility to accommodate future accounting developments without the need to change the Directive(s) for every future development in the (international) accounting standards. FEE would not be supportive of detailed European standards for SMEs set through the Accounting Directives. The Directives should be principles-based in nature.
- (33) A fundamental revision of the Accounting Directives should consider the principles that need to be included in a modern accounting directive. The terminology and wording in the Accounting Directives need to be made consistent and modernised. To the extent possible terminology should be brought in line with IFRS. Any conflicts in terminology should be avoided (i.e. by not using IFRS terms with a different meaning in the Directives).

Question 11:

Are there any elements of the IFRS for SMEs that should be incorporated within revised Directives?

Please comment.....

- (34) See our response to Question 10.

Question 12:

Do you have any other observations or comments on the IFRS for SMEs or the project to overhaul the Accounting Directives?

Please comment.....

- (35) We believe that there is a need to have European Accounting Directives also in the longer term. A holistic approach, which we strongly favour, would require a complete revision of the Accounting Directives. Any fundamental revisions of the Accounting Directives should be accompanied by a proper due process, including consultation of all stakeholders affected by the future proposals. We would welcome a complete overhaul of the Accounting Directives based on the “think small first” principle and agree that this principle would best be met by a “bottom up” approach. In addition, the objective of further harmonisation needs further debate given the other barriers outside the accounting area that would need to be addressed (see paragraph 12). Any future Accounting Directive, while principles based, should contain as few options as possible both at company and Member State level and would have to address both the individual and the consolidated accounts.

FEE, 12 March 2010