



The Proposed IFRS for Private Entities

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Why Standards Are Needed for PE

- Full IFRSs required in over 80 countries
- National GAAPs converging to IFRSs
- Emerging economies – entities need capital
- Full IFRSs and non listed: User needs? Burden? Enforcement problems –> IFRS 'Lite'?



Global Context: Statutory Reporting

- GAAP reporting required by law for all or most private companies?
 - USA: Generally NO.
 - 5,000,000 private corporations: No
 - 15,000,000 other business: No
 - Only 15,000 SEC → FASB GAAP by law
 - Rest of world: generally YES.
 - Europe: 5,000,000 companies must prepare GAAP f/s and have audit by law
 - HK and Singapore: Every company by law



Why PE Standards Are Needed

- **Benefits of global accounting standards for listed companies:**
 - Improved quality of reporting
 - Investors invest globally
 - Companies seek capital globally
 - Analysts follow industries globally
 - Cross-border mergers
 - *Accounting differences reduce understandability and obscure comparisons*



Why PE Standards Are Needed

- **Global standards are also needed for unlisted SMEs:**
 - Bank lending decisions
 - Banks monitor credit risks after loan is made
 - Vendors evaluate finances of buyers
 - Credit rating agencies and banks that provide rating services
 - Overseas customers
 - Foreign venture capital
 - Non-management investors
 - Development institutions (WB etc)



Why PE Standards Are Needed

- **Benefits of global PE standards go beyond comparability:**
 - Improved quality of reporting as compared to existing GAAP
 - Ease burden on PEs where full IFRSs or full national GAAP are now required for all entities.
 - Education and training
 - Auditing efficiencies



Use of Full IFRSs Around the World

For domestic listed
companies:

Number of
Jurisdictions

IFRSs required for all

84

**IFRSs required for
some**

4

IFRSs permitted

24

Today, IFRSs are used by listed
companies in over 100 jurisdictions.



Use of Full IFRSs Around the World

For domestic unlisted
companies:

Number of
Jurisdictions

IFRSs required for all

28

**IFRSs required for
some**

19

IFRSs permitted

36

Today, IFRSs are used by unlisted
companies in over 80 jurisdictions.



IASB Exposure Draft

- **IASB's proposed IFRS for PE's:**
 - Simplified principles tailored for PE's
 - Self-contained (nearly)
 - Based on full IFRSs, which are developed for public capital markets
 - Modifications based on:
 - **User needs**
 - **Cost-benefit**



Differential User Needs

- **Focus more on short-term cash flows, liquidity, and solvency**
 - Cash flow statement essential
 - No “off balance sheet” debt – unfunded pensions, leases, derivatives, contracts, and (at least) deferred taxes that will reverse in the short term
 - Short-term items at current measurements
- **Less interest in long-term earnings forecasts or long-term cash flows**



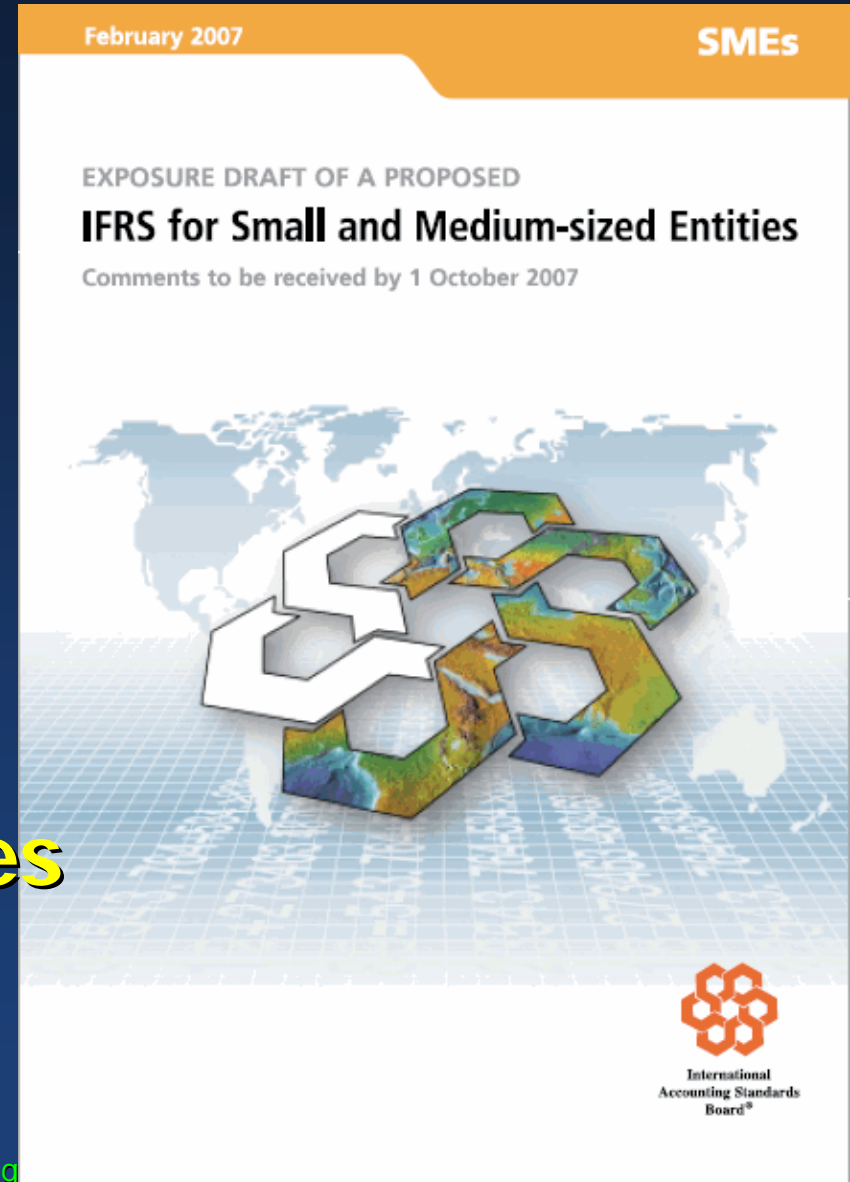
Deliberations Leading to the ED

- **Late 2004 and all of 2005: Board deliberated specific issues for PE's**
- **January 2006: Complete draft presented to the Board**
 - **Deliberations throughout 2006**
 - **Latest drafts posted on public website August 2006 and November 2006**
- **Feb 2004 – Jan 2007: 26 board meetings**
- **February 2007: ED published**



Exposure Draft – IFRS for SMEs

- Organised by topic
- ED 254 pages
 - Plus illustrative financial statements, disclosure checklist, basis for conclusions
- Board vote: 13 to 1
- Published:
 - 15 February 2007
- Translations: 5 languages
- Comment deadline:
 - 30 November 2007





IASB Definition of Private Entity

- **IASB view:**
 - **IFRS for PEs is appropriate for an entity with no public accountability:**
 - **not publicly traded; and**
 - **not a financial institution**
 - **Name changed in May 2008 from SME to PE to conform to the above (unchanged) definition.**



Objective of IFRS for PEs

- General purpose financial statements for external users, including:
 - **Non-manager owners**
 - **Existing and potential lenders, vendors, creditors, customers.**
 - **Credit rating agencies**
- Understand and compare PE's financial performance, financial position, and cash flows
- Auditor could give opinion on fair presentation (true/fair view)



Finding an Answer

- **Self-contained standard:**
 - **Though still some cross-references.**
 - **PE must try to find answers in the IFRS for PEs:**
 - by analogy, and
 - by using pervasive principles in first section of IFRS for PEs
 - **May look to full IFRSs if answer cannot be found in IFRS for PEs**
 - **But, not required**



Simplifications

- Five kinds of simplifications based on user needs and cost-benefit tradeoffs:
 1. Some topics in IFRSs omitted if irrelevant to SME
 2. Where IFRS has options, include only simpler option
 3. Recognition and measurement simplifications
 4. Reduced disclosures
 5. Simplified drafting



Topics in Full IFRSs Omitted

- Material not relevant to typical SME omitted, with cross-references to full IFRSs if needed:
 - **Hyperinflation**
 - **Equity-settled share-based payment**
 - **Determining FV of agricultural assets**
 - **Extractive industries**
 - **Interim reporting**
 - **Lessor finance leases**
 - **Segment reporting**
 - **Earnings per share**



Accounting Policy Options

- Only simpler of options in full IFRS are included. Others cross-referenced. So, only:
 - Cost for investment property
 - Cost for PP&E and intangibles
 - Expense all borrowing costs
 - Indirect operating cash flows
 - One method for all grants
- Jurisdictions could eliminate options.



Recognition and Measurement

- **Simplifications, page 1 of 3:**
 - **Financial instruments:**
 - Two classifications, not four
 - Drop “continuing involvement approach” for derecognition
 - Much simplified hedge accounting
 - Option to use IAS 39 in full
 - **Goodwill impairment – indicator approach**



Recognition and Measurement

- **Simplifications, page 2 of 3:**
 - **Expense all R&D**
 - Capitalise “D” – allowed by cross ref to IAS 38
 - **Cost method for associates and JVs**
 - Equity method – cross-ref to IAS 28
 - Proportionate consol – cross-ref to IAS 31
 - **Income taxes – exceptions eliminated, simplified explanations**



Recognition and Measurement

- **Simplifications, page 3 of 3**
 - **Less fair value for agriculture – only if “readily determinable without undue cost or effort”**
 - **Defined benefit plans – principle approach, no corridor tests**
 - **Share-based payment – intrinsic value**
 - **First-time adoption – less prior data**
 - **Leases – simplified calculations**



Disclosure Simplifications

■ Reduced disclosures:

- Full IFRSs: More than 3,000 disclosures
- IFRS for PEs: Fewer than 400
- Simplifications based on users' needs and cost-benefit:
 - Kept: short-term cash flow, liquidity, solvency, measurement uncertainties, accounting policy choices
 - Dropped: disaggregations, public capital market disclosures



Simplifications Not Adopted

- Drop the cash flow statement
 - All leases operating *
 - All pension plans defined contribution *
 - Fewer provisions *
 - Non-recognition of deferred taxes *
 - No consolidation *
 - Derivatives at cost *
 - Cost model for all agriculture
 - Non-recognition of share-based payment
 - Completed contract only
- *Something in common: Off bal sheet debt**



Micro-sized SMEs (tiny)

- Is the IFRS for PEs suitable from companies with less than 10 employees?
 - Yes
 - Key issue: Is the micro required to prepare general purpose financial statements that present fairly position, operating results, and cash flows?
 - Aimed at external capital providers?
 - This is not IASB's decision – rests with government



Other Issues

- Suitability for tax returns?
- Measurement of allowable dividends?
- Useful for managing the business?
 - **Not specific objectives of the IASB**
 - **With simple reconciliation, could also serve tax reporting**
 - **We believe the information will likely be useful for managing. But our goal is external financial reporting**
- If an SME does not prepare financial statements for lenders, creditors, outside investors: May not need IFRS for SMEs



Since ED Was Issued

- **Extraordinary outreach effort**
 - Presentations at 95 conferences and roundtables in 39 countries
 - Including 52 since ED was issued
 - Plus 8 published articles
- **Compliance checklist**
- **Field tests completed:**
 - 116 SMEs globally. Questionnaire in English, French, Spanish
- **162 comment letters**



20 Key Issues in Comment Letters

1. Eliminate all cross references to full IFRSs – both omitted topics and options
2. Do not anticipate changes to full IFRSs
3. Rewrite pervasive principles in Section 2 as clear guidance
4. Historical cost model should be default
5. Simplify income taxes
6. Eliminate or restrict consolidation
7. Amortise goodwill & other intangibles



20 Key Issues in Comment Letters

8. Restrict use of FV to:

- Market price is quoted or readily determinable without undue cost or effort, plus
- All derivatives

9. Don't say 'fair value' – describe exactly what is to be measured

10. Clarify use of IFRS for SMEs by subsidiary of a full IFRS entity

11. Simplify defined benefit pension plans

12. Simplify share-based payment

13. Leases – do not require:

- Straight-line for operating, or
- Finance lease measured only at FV



20 Key Issues in Comment Letters

14. Impairment: Allow value in use
15. Debt - equity classification
16. Fewer restatements for accounting changes and errors
17. Further disclosure simplifications
18. New name – SME suggests size test (done)
19. No need for interpretations, but yes need for guidance
20. Comprehensive post-issuance assessment after 2 years



Field Test Results

- **116 PEs from > 20 countries**
 - Restated their most recent annual financial statements using IFRS for SMEs
 - Completed a questionnaire
- **Very few companies had problems applying the ED**
- **Main issues (few companies) were:**
 - Determining fair values
 - Computing deferred taxes
 - First time: Equity and cash flow stmts.



IFRS for PEs in Europe

- **Decision rests with Member States:**
 - Whether to require or permit
 - Which companies
 - When
- IAS Regulation neither requires nor prohibits MS to use IFRS for PEs
- Consistent with 4th and 7th Directives
- Nearly all EU MS now either require or permit all PEs to use full IFRSs at least in consolidated F/S (next slide):



IFRS for non listed in Europe

- Under IAS Regulation, MS may require or permit full IFRSs for unlisted companies. Status for 25 member states (ex two new MS):

	Consoli- dated F/S	Legal entity
Not permitted	0	9
Required for all	3	2
Required for some	8	5
Permitted for all	14	6
Permitted for some	0	3



IFRS for PEs in Europe

- **2003: European Commission (EC) wrote to IASB, saying:**
 - IASB mission includes standards for SMEs
 - A separate IASB SME standard is needed.
 - IASB should develop SME-GAAP built on the same concepts as IFRS but with simplifications.
- **2004: European Commission wrote to IASB Trustees:**
 - Development of an SME standard should be prioritised.



IFRS for PEs in Europe

- **Autumn 2008: Mazars survey of 1,500 SMEs in France, Germany, UK, Italy, Spain, and Netherlands about:**
 - **The IFRS for SMEs accounting standard: perceptions and expectations across Europe.**
 - **“A vast majority of European SMEs support the adoption of a common set of accounting standards, whether on an optional or mandatory basis. This is particularly the case among Italian, Spanish, Dutch and French SMEs.”**



Early Movement toward Adoption

- **South Africa:**

- Adopted the IFRS for PEs ED word for word as required SA GAAP for all unlisted companies that do not use full IFRSs

- **Australia:**

- Proposed for largest 25,000 unlisted

- **Tanzania:**

- “We have agreed in principle to require the IFRS for PEs for all NPAEs”



“Early Adoption” – South Africa

- **In a published article, the CEO of South African Institute of Chartered Accountants said:**

“The majority of companies in South Africa will use it. It is very welcome. The standard in its current form already offers SMEs real relief, and when the final standard comes it will be even better.”



Potential Adoption in EU

- **Denmark (EU):**
 - Planning legislation to permit
- **UK (EU):**
 - Likely to permit for all unlisted but also keep FRSSE for micros
- **Bulgaria (EU):**
 - Most accounting professionals “strongly support adoption”
 - “Definitely our national standards will be replaced by the IFRS for PEs”
 - “The only question is when, not if”



Interest in the United States

- **Could private companies in the US use the IFRS for PEs?**
- **No reason why not:**
 - No statutory audit requirement in US
 - Basis of presentation note would refer to conformity with IFRS for PEs
 - If audited, auditor would report on conformity with IFRS for SMEs
- **AICPA: Designate IASB under Rule 203**
- **Strong support from FEI and IMA**



IASCF Training Materials for PEs

- **Developed by IASC Foundation**
 - One module per Section (ED has 38 sections). Example:
 - **Sec. 16 PP&E is 7 A5 pages long**
 - **Training module is 32 A4 pages, many examples, good stuff!**
 - Finish by mid/late 2009
 - Multiple languages
 - Free of charge!
 - Train the trainers
- **Software? Yes commercial, not IASB**



Next Steps

- **Staff analyses of comments and field tests, recommendations for changes to the ED: To the Board March 2008**
- **Working Group met: April 2008**
- **Board redeliberations: 2Q-4Q 2008**
- **Final Standard: End of 2008**
- **Effective: Whenever adopted locally**
- **Training materials: Mid-late 2009**



Thank you.

**Questions and
comments?**

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**EXPRESSIONS OF INDIVIDUAL VIEWS BY
MEMBERS OF THE IASB AND ITS STAFF ARE
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THIS PRESENTATION ARE THOSE OF GILBERT
GELARD. OFFICIAL POSITIONS OF THE IASB
ON ACCOUNTING MATTERS ARE DETERMINED
ONLY AFTER EXTENSIVE DUE PROCESS AND
DELIBERATION.**

