

Plenary Session – IFRS for SMEs

Friday 8th September 2006

16:00 to 17:15

Facilitator:

***Hans van Damme, FEE Vice-President, Financial
Reporting***

FEE Annual European SME/SMP Congress, Palais des Congrès, Versailles, France, 7th & 8th September 2006

Plenary Session – IFRS for SMEs

Friday 8th September 2006

Speakers:

Gilbert Gélard, IASB Member

***Isobel Sharp, Deputy President, ICAS, IASB Member, SME
Advisory Group, UK***

***Françoise Florès, EFRAG TEG Member and Co-Chairman of the
Joint EFRAG/FEE Group on IFRS for SMEs***

***Dominique Ledouble, Honorary President of the Conseil Supérieur
of the OEC, France***

FEE Annual European SME/SMP Congress, Palais des Congrès, Versailles, France, 7th & 8th September 2006



The IASB Project on Accounting Standards for SMEs

Gilbert GELARD, Board Member

FEE SME/SMP Congress
Versailles, September 2006.

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Why SME Standards Are Needed

- Benefits of global accounting standards for listed companies are obvious in globalised financial markets.
- Even for unlisted SMEs, financial statements that are understandable across borders are needed:
 - Banks make loans across borders and operate multi-nationally.
 - Vendors from other countries.
 - Credit rating agencies.
 - Overseas customers.
 - Foreign venture capital.

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Why SME Standards Are Needed

- **Two edged-sword for SMEs:**
 - Good accounting and more disclosure add to SME burdens, rather than reduce them.
 - Also, SMEs are often concerned about the competitive harmfulness of greater transparency.
 - At the same time, good accounting and disclosure give investors confidence to provide capital.
- **Solution: Tailor requirements for SMEs. This is what the IASB SME project is all about.**

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IASB Definition of SME

- **IASB tentative view:**
 - IFRS for SMEs is appropriate for an entity with no public accountability:
 - **not publicly traded; and**
 - **not a financial institution.**
 - An entity whose securities are publicly traded has public accountability.
 - **Need full IFRSs for investor protection – even for small listed.**

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IASB Approach

1. Focus on non-publicly accountable entities that publish general purpose financial statements for external users. No quantified "size test".
2. Each jurisdiction should develop detailed guidelines on which entities are eligible to use.

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IASB Approach

3. Focus on SME with about 50 employees.
4. Try to develop a stand-alone document as much as possible.
5. Framework concepts and pervasive principles added, to minimise need for fallback to full IFRSs.

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IASB Approach

6. Material not relevant to typical SME omitted, with cross-references if needed
- Hyperinflation
 - Equity-settled share-based payment
 - Agriculture
 - Extractive industries
 - Interim reporting
 - Lessor finance leases
 - Recoverable amount of goodwill

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IASB Approach

7. Only simpler of options in full IFRS are included. Other(s) cross-referenced. So, only:
- Cost for investment property.
 - Cost for PP&E and intangibles.
 - Expense all borrowing cost.
 - Expense all development cost.
 - Cost for associates and JVs.
 - Indirect operating cash flow.
 - One method for all grants.
- Jurisdictions could eliminate options.

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IASB Approach

8. Recognition and measurement simplifications, including:

- Financial instruments
- Goodwill impairment
- Expense all R&D
- Cost method for associates and joint ventures
- Timing difference approach to income taxes
- Less fair value for agriculture
- Defined benefit plans
- Share-based payment – intrinsic value
- First-time adoption

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IASB Approach

9. SME must try to find answers in SME standard by analogy and by using pervasive principles.

10. But – SME must look to full IFRSs as a “safety net” – if answer cannot be found otherwise.

- Expected to be rare.

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During 2005

- **Board focussed on ways to simplify recognition and measurement:**
 - **April 2005:** Brief IASB R&M questionnaire
 - 101 responses received
 - **June 2005:** Discussion with Standards Advisory Council.
 - **August 2005:** IASB SME Working Group recommendations to Board

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During 2005

- **Sept. 2005:** Discussion with World Standard Setters from nearly 50 countries
- **Oct. 2005:** Public round-table discussions of possible recognition and measurement simplifications (Board + 43 groups)

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2006 - Draft Exposure Draft

- **January 2006:**
 - IASB staff presented a draft ED to the Board. Preliminary discussion.
- **January 2006:**
 - Working Group discussed draft ED two days. 84 recommendations to Board.
- **February and March 2006:**
 - ED discussed by Board in detail.
- **May, June, July, September 2006:**
 - Revised EDs discussed by Board.

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2006 - Draft Exposure Draft

- **The draft ED now:**
 - About 216 pages
 - **Full IFRSs now 2,400 pages.**
 - Organised by topic
 - 40 sections
 - Developed by considering needs of a company with about 50 employees
 - Model financial statements
 - Disclosure checklist

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SME Concerns: "Maintenance"

- **SMEs are worried about frequent updating of IFRS for SMEs:**
 - Board decision: Update the IFRS for SMEs every 2 years.

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Next Steps

Please understand that these dates are tentative:

- **Exposure Draft – goal is September/October 2006.**
- **Field tests. Visits to SMEs.**
- **Final Standard – 2007.**
- **Effective – 2008.**

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Thank you. Questions? Comments?

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



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Thinking SME first

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Thinking SME first

Views of a 10 year old veteran

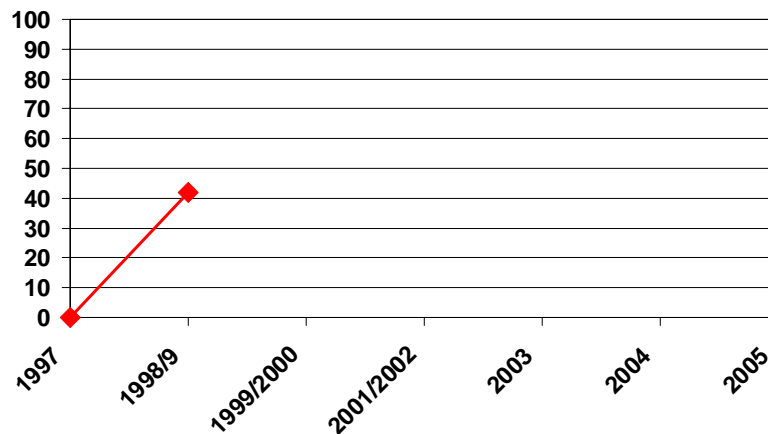


FEE Annual European SME/SMP Congress, Palais des Congrès, Versailles, France, 7th & 8th September 2006

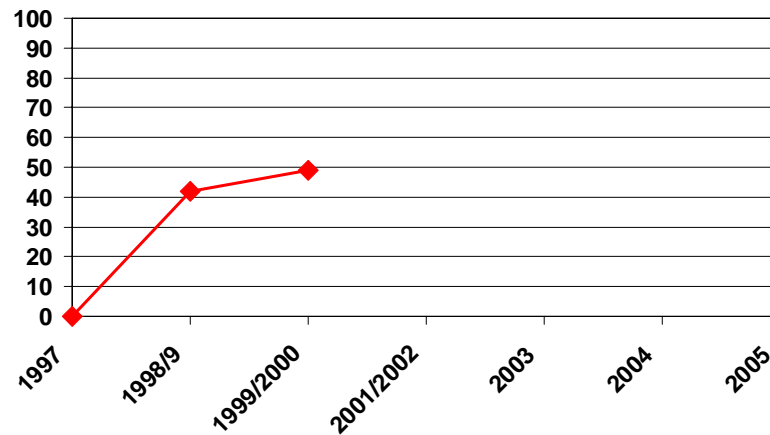
Accounting Standards for SMEs

- UK and Ireland
- 1997 – Financial Reporting for Smaller Entities (FRSSE)
- Concern that standards were burdensome / complicated / inappropriate for smaller entities

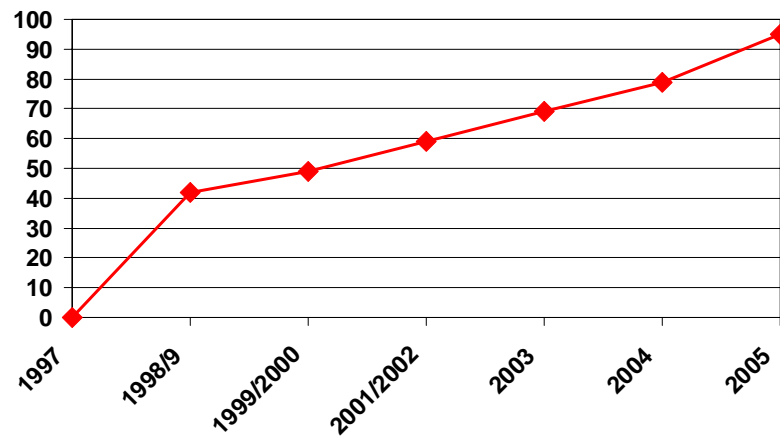
Use of the FRSSE



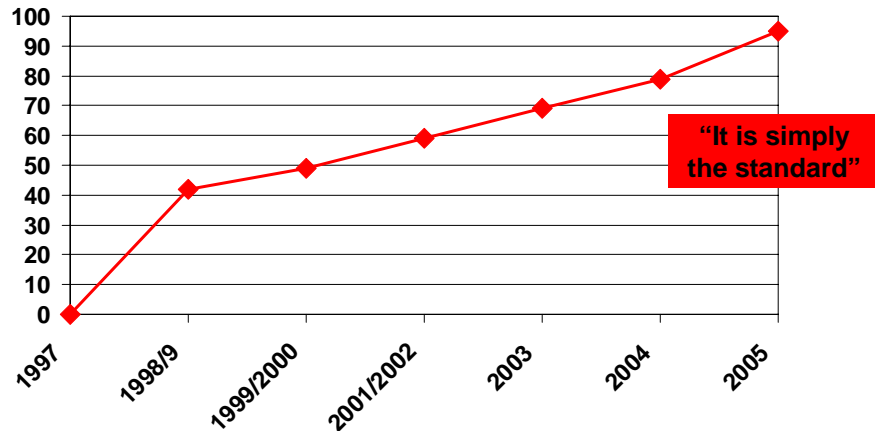
Use of the FRSSE



Use of the FRSSE



Use of the FRSSE



Why the FRSSE?

- One stop shop, i.e. all the rules in one place
- Language is simpler, easier to use and shorter
- Supporting guidance on formats of financial statements
- Software suppliers now produce the templates
- The full standards (big GAAP) are too...

What is not right?

- FRSSE updates are big GAAP diluted to taste, not designed to fit

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Financial Reporting **FRSSE**

Think FRSSE first

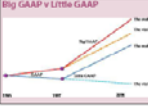


Is the current standard designed to fit or simply diluted to taste? **Robert Sharp**

FRSSE is a diluted version of GAAP. It is a watered-down version of GAAP that is designed to fit the needs of the UK market. It is not designed to fit the needs of the global market. It is a diluted version of GAAP that is designed to fit the needs of the UK market. It is not designed to fit the needs of the global market. It is a diluted version of GAAP that is designed to fit the needs of the UK market. It is not designed to fit the needs of the global market.

FRSSE Financial Reporting

Big GAAP v Little GAAP



The graph shows that Big GAAP is growing faster than Little GAAP. This is because Big GAAP is a more comprehensive standard that covers more areas of financial reporting. Little GAAP is a more limited standard that only covers the basics. As a result, Big GAAP is more useful for companies that want to provide a more complete picture of their financial performance. Little GAAP is only useful for companies that want to provide a basic picture of their financial performance.

The ASB is now consulting on a proposal to extend the application of FRSSE to medium-sized entities.



What is not right?

- FRSSE updates are big GAAP diluted to taste, not designed to fit
- Rules are added because they may be needed by 1% of companies
- Insufficient use of the true and fair principle and providing additional disclosures

Looking forward to the IASB's ED

- Focus on 50 employees – EU's small
- Much shorter
- Updating every two years
- Working on the English

Possible improvements?

- Removal of selected fall backs to make it a one-stop-shop
- Further simplifications

Final score

- A lengthy process but IASB is listening
- Need to keep the spirit
- Europe needs to consider how to make best use of the IASB's SME standards

Final score

- A lengthy process but IASB is listening
- Need to keep the spirit
- Europe needs to consider how to make best use of the IASB's SME standards
- IASB scores 8½ out of 10



IFRS and SME : A French perspective

by

Dominique LEDOUBLE

Which entities ?

- Two criteria defined by IASB :
 - No public accountability
 - Presentation of financial statements to third parties
- No quantitative measurement but an indication of a threshold of 50 employees
- In France, this would represent 23 500 entities employing between 50 and 250 persons
- The net effect is probably lower since a part of these entities are subsidiaries of groups reporting in IFRS

Which financial statements ?

- If only consolidated accounts are concerned, the real impact might be minimal.
- If this is a platform applicable to statutory accounts, then it would require :
 - Modification of those French standards which are not in accordance with IFRS basics (income tax, leases...)
 - A decision on whether the SMEs book applies to all enterprises

Which principles ?

- Cost or value : cost as often as possible
- Balance sheet or income statement : balance sheet
- Notes : The major part should directly derive from the accounts and be presented as a schedule with a minimum of text
- Format of financial statements : as formalized as possible

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How to implement the standards

- The presentation of the standards
 - “All in one” approach : a dream ?
 - Simplified standards or simplified drafting ?
- The interpretation of the standards
 - Conceptual framework
 - “normal” IFRS
- How to maintain a consistent implementation ?
 - A far more difficult task than for “normal” standards : greater number of entities, greater influence of local culture

Less difficult than anticipated ?

- A major overhaul of our domestic legislation has already been achieved
- French rules should be amended on : funds statement, ordinary activities, post-balance sheet events
- The tax authorities already made public that they did not object to differed tax accounting as it will have no tax effect
- Major remaining items : leases, transactions with impact on equity

Concluding remarks

- Extensive field testing is vital during the exposure period
- The tax authorities should explicitly indicate which rules they are not prepared to accept for the time being
- Two routes towards convergence :
 - Implicit and progressive modification of domestic rules
 - Direct use in selected cases of the IFRS benchmark

IFRS for SMEs Preliminary Assessment by EFRAG

Françoise Flores
Partner, Mazars
Member of EFRAG TEG
Co-Chair, EFRAG- FEE working group on IFRS for
SMEs

Areas of satisfaction

- Project has received level of priority it deserves
- Definition of non-public accountability broadened, decision of applicability clearly left to jurisdictions
- Objective of stand-alone document understood and pursued
- Disconnection of amendments to full IFRS and IFRS for SMEs

Areas for improvement

- No analysis and no acknowledgement of specific needs of SME financial statement users (entity-specific approach)
- Too many cross-references to full IFRS to meet objective of stand-alone document
- Constraint of close link to full IFRS to be lifted if genuine user-friendliness wanted
- No attempt at presenting fewer and clearer recognition and measurement principles

Areas of concerns

- Refusal to search for genuine simplification may generate difficulties
 - Shortening, rather than simplifying, results in most detailed guidance gone
 - Elimination of exceptions, instead of true simplification, results in more complex accounting (ie financial instruments)
 - Elimination of alternative measurements, instead of genuine simplification, may lead to lack of relevant financial information (impairment based on fair value less costs to sell)

Room for good surprise

- Pension and deferred tax accounting requirements still to be re-written and adjusted for SMEs:
 - Some simplification requests might be satisfied

Conclusion

- A sound consultation process has already helped place the IFRS for SMEs on tracks more appropriate than was intended at first by IASB
- Improvements and further simplifications are however needed ...and achievable, if the IASB can be convinced to more substantially cut the link with full IFRS
- All constituents in Europe interested in the debate need to have their voice taken into account: all comments sent to EFRAG during the exposure period will be duly considered