2 March 2023

Andreas Barckow
Chair
IFRS Foundation
Columbus Building, 7 Westferry Circus
Canary Wharf, London E14 4HD
United Kingdom

Via website: www.ifrs.org

Dear Andreas

Exposure draft – Third edition of the IFRS for SMEs Standard (IASB ED 2022/1)

As the representatives of over 300,000 professional accountants in Australia and New Zealand, CPA Australia and Chartered Accountants Australia and New Zealand (CA ANZ) thank you for the opportunity to comment on the above Exposure Draft (ED).

We continue to support the availability of an International Financial Reporting Standard for Small and Medium-Sized Entities (IFRS for SMEs) which, by simplifying the principles and requirements in full IFRS, promotes a consistent but proportionate reporting framework for global Small and Medium-Sized Enterprises (SMEs). Therefore, we welcome the IASB's current project to review the IFRS for SMEs standard to better align it with the current suite of full IFRS while continuing to promote necessary and useful simplifications that reflect the cost/benefit considerations of those entities expected to adopt it.

Australia does not adopt IFRS for SMEs for its SME market. However, the Australian Accounting Standards Board (AASB) does reference IFRS for SMEs in developing Australian Accounting Standards (AAS) as set out below:

- The Australian financial reporting framework takes a sector-neutral multi-tier approach based on the IFRS for SMEs concept of "public accountability". Entities with public accountability report under Tier 1 using full IFRS, those without public accountability report under Tier 2. Entities reporting under Tier 2 must adopt the recognition and measurement requirements in AAS, which are harmonised with full IFRS, when preparing General Purpose Financial Statements (GPFS). This contrasts with the simplified recognition and measurement offered by IFRS for SMEs. Reporting relief for Tier 2 entities is provided by permitting a reduced level of disclosures. Recent changes to the Australian financial reporting framework have further modified these reduced disclosures (which are now referred to as simplified disclosures). These disclosures are set out in AASB 1060 *General Purpose Financial Statements - Simplified Disclosures for For-Profit and Not-for-Profit Tier 2 Entities* (AASB 1060). The AASB used the reduced disclosures in the IFRS for SMEs as the basis for developing AASB 1060.

CHARTERED ACCOUNTANTS
AUSTRALIA • NEW ZEALAND

Chartered Accountants Australia and New Zealand
33 Erskine Street, Sydney, NSW 2000
P: +61 1 9290 1344
W: charteredaccountantsanz.com
ABN: 50 084 642 571

CPA AUSTRALIA

CPA Australia
L20, 28 Freshwater Place, Southbank
Victoria 3006
P: +1300 73 73 73
W: cpaaustralia.com.au
ABN 64 008 392 452

- The AASB is monitoring the IASB's 'Subsidiaries that are SMEs' project to inform future revisions to the Tier 2 financial reporting requirements.
- The simplifications to recognition and measurement requirements contained within IFRS for SMEs have informed the AASB's current proposals to develop a proposed new Tier 3 for smaller not-for-profit entities. This project is in response to concerns that the application of full IFRS-based recognition and measurement requirements have proved onerous for smaller not-for-profit entities (NFPs), where it is generally accepted that the costs of such an approach exceed the benefits.

New Zealand also does not adopt IFRS for SMEs but, similar to Australia, uses the principle of "public accountability" to distinguish between Tier 1 and Tier 2 entities. It also requires both tiers to adopt full IFRS recognition and measurement but permits a Reduced Disclosure Regime (RDR) for Tier 2 entities developed using the underlying principles in IFRS for SMEs.

Considering the importance of the IFRS for SMEs standard to our domestic frameworks, we broadly support the approach adopted to update IFRS for SMEs. We also agree that it is important for the IASB to update it to better reflect the current requirements of IFRS in the important areas of the conceptual framework, revenue, consolidation, and equity accounting. However, the limited implementation of IFRS for SMEs in Australia and New Zealand necessarily restricts the extent of the comments we can provide. As such, we have not provided detailed responses to specific questions raised in the ED. Nevertheless, we share our views on several specific issues being raised in the ED, and on some broader policy issues which impact on the Australian and New Zealand use of the IFRS for SMEs Standard. These issues are set out below:

Broad policy issues

Public accountability (Question 1)

We agree that there is a need to clarify the guidance supporting the "public accountability" concept and support removing the word "most" from the "fiduciary capacity" leg of the definition as this has caused jurisdictional application issues in Australia and New Zealand. Rather than insert the word "often" as proposed, we believe it would be more helpful to be even less prescriptive, using the word "may" to make it clearer that individual entities need to make their own assessments of their status based on their actual activities. Paragraph 1.3(b) would read as follows with our suggested modifications:

> *"It holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses (for example, banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks may meet this second criterion)."*

We believe that the new paragraph 1.3A will assist in this decision-making process. However, it is important to make clear that the new paragraph 1.3A is not an additional requirement but simply an aid to the application of the requirements in paragraph 1.3. Wording could be added to paragraph 1.3(b) along the lines of "Paragraph 1.3A provides further guidance on applying this paragraph" to achieve this point.

We are also aware that in some jurisdictions, including Australia and New Zealand, certain entities are deemed to have public accountability for differential financial reporting purposes. Therefore, we encourage the IASB to review the implementation experience of those countries that have fully or partially adopted the IFRS for SMEs. The list of entities deemed to have public accountability in each jurisdiction may allow for the identification of other common features of public accountability which may assist in further expanding the implementation guidance for applying this concept. It may also be helpful if the IASB included commentary in paragraphs BC11-BC19 of the Basis for Conclusions that it expects jurisdictions applying the IFRS for SMEs to make their own decisions as to its specific applicability. This would clarify to all users that whilst the aim of the IFRS for SMEs is full international adoption, the level of adoption may be impacted by jurisdictional issues.

Finally, we believe there is a need for alignment between the terms "public accountability" and "public interest entity". We recommend the IASB liaises with the International Ethics Standards Board for Accountants (IESBA) and the International Auditing and Assurance Standards Board (IAASB) to achieve alignment.

Global role of IFRS for SMEs

As noted above, the Australia and New Zealand decisions to not adopt IFRS for SMEs reflects, for the most part, challenges associated with the different recognition and measurement requirements of full IFRS and IFRS for SMEs. We presume Australia and New Zealand are not unique in this regard as the number of jurisdictions that have globally adopted the IFRS for SMEs (86) remains significantly below the number that have adopted full IFRS (145). We therefore continue to recommend that the IASB focus on this issue to better understand and articulate jurisdictional concerns in order to continue to guide the development of IFRS for SMEs as a globally accepted standard that can be applied by SMEs in preparing GPFS. We believe the complexities regarding jurisdictional application of IFRS for SMEs will be further exacerbated by the planned release of the "Subsidiaries without Public Accountability: Disclosure" standard, given the IASB's current stated intention that it can only be applied by subsidiaries without public accountability (see the comments in our joint submission on ED 2021/7).

Specific accounting issues

Intangible assets (Questions 2(ii) and 13)

We have concerns with the proposals that will require SMEs to deal with two separate definitions of assets and liabilities, with Section 18 (Intangible Assets other than Goodwill) and Section 21 (Provisions and Contingencies) applying the extant definition, and all other assets and liabilities applying a revised definition that is aligned with the definition used in the 2018 Conceptual Framework for Financial Reporting. We believe this approach is both conceptually unsound and, particularly in the context of intangible assets in the SME sector, could give rise to confusion in the application of the IFRS for SMEs standard.

We also do not support the proposals to permit the inclusion of a policy option for development costs at this time. We believe that the inclusion of too many policy options in IFRS for SMEs can be counterproductive to the objectives of simplicity, consistency, and comparability.

To address the above concerns, we reiterate the recommendations made in the separate CA ANZ and CPA Australia submissions on the IASB's Third Agenda Consultation that a high priority needs to be given to the revision of IAS 38 *Intangible Assets* as the conflict described above is yet another example of how IAS 38 is no longer fit for purpose. Any changes made to IAS 38 should then be incorporated into IFRS for SMEs at the earliest available opportunity.

An emerging area of significant economic activity in the SME sector, that is currently not addressed in the IFRS for SME, is the accounting for crypto assets including crypto currencies. We recommend considering requirements/guidance that will assist SMEs to account for these transactions when applying the IFRS for SMEs standard.

Impairment of financial assets (Question 4)

We recommend retaining the incurred loss model for all financial assets. We believe the scope of the incurred loss model can be expanded to include many more of the simple transactions giving rise to financial assets that are common in the SME sector. We are also of the view that measuring impairment loss using the expected credit loss model could be overly complex and impose undue costs on SMEs.

In our 2020 submission to the IASB's Request for Information – Comprehensive Review of the IFRS for SMEs, we recommended the introduction of the simplified approach to impairment under the expected credit loss model in IFRS 9 *Financial Instruments.* This simplified approach included a provision matrix approach for trade receivables and other similar financial assets. However, we note that feedback received by the IASB indicated that this proposed approach would still be complex for SMEs to apply and would not result in substantial changes in the amount of impairment. Accordingly, for the reasons stated above, we recommend retaining the incurred loss model for all financial assets.

Fair value (Question 5)

We agree that the new Section 12 (Fair Value Measurement) clearly sets out the fundamental principles that are inherent in IFRS 13 *Fair Value* and so should provide a clear and consistent basis that will support the application of the fair value concept by SMEs. However, we believe the IFRS for SMEs standard will need to be supported by SME specific guidance on matters such as highest and best use, exit value and market participant assumptions to ensure that the standard it is consistently applied.

Leases (Question 12)

Feedback from our members in Australia and New Zealand who have implemented IFRS 16 *Leases* is that the costs of doing so in the SME sector substantially outweighs the benefits that preparers and users achieve from these requirements. Therefore, we agree that the accounting requirements of IFRS 16 should not be introduced into the IFRS for SMEs standard.

Additional Matters – amendments to IAS 1 *Presentation of Financial Statements* (IAS 1) regarding classification of current and non-current liabilities

We note that, due to the 2019 cut-off date for IFRS changes that would be considered as part of this update, the recent revisions to the classification requirements for current and non-current liabilities in IAS 1 have not been included in this latest IFRS for SMEs update. These amendments, addressing the classification of liabilities (July 2020) and the classification of long-term debt with covenants (October 2020) are significant presentation clarifications incorporated into IAS 1 that will assist not only publicly accountable entities but also SMEs that apply the IFRS for SMEs. Therefore, it is important that these changes are incorporated into the IFRS for SMEs as part of this update.

If you have any questions about our submission, please contact either Ram Subramanian (CPA Australia) at ram.subramanian@cpaaustralia.com.au or Amir Ghandar (CA ANZ) at amir.ghandar@charteredaccountantsanz.com.

Yours sincerely

Gary Pflugrath FCPA
Executive General Manager, Policy and Advocacy
CPA Australia

Simon Grant FCA
Group Executive – Advocacy and International Development
Chartered Accountants Australia and New Zealand