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Our ref RD/288

7 March 2023

Dear Dr Barckow

ED 2022/1 *Third edition of the IFRS for SMEs Accounting Standard*

We appreciate the opportunity to comment on the International Accounting Standards Board's (IASB) Exposure Draft (ED) *Third edition of the IFRS for SMEs Accounting Standard*. We have consulted with, and this letter represents the views of, the KPMG network.

We are generally supportive of the proposals in the ED. We do however have some concerns relating to specific sections within it. Our principal comments are as follows:

(i) Description of non-publicly accountable entities

— We believe the IASB needs to set out more clearly its intended meaning of the term 'fiduciary capacity' in paragraph 1.3(b). The additional guidance added in 1.3A does not address the concerns we raised over the usage of this term in our response to the Exposure Draft ED/2021/7 *Subsidiaries without Public Accountability: Disclosures*. We are concerned that the term 'fiduciary capacity' may have a legal meaning in certain jurisdictions that is substantially narrower than the meaning intended by the IASB. We believe that the IASB should set out the meaning it intends by the phrase.

— We are also concerned that the new wording in 1.3A introduces additional areas of judgement around the meaning of the phrases 'high degree of outside interest' and 'broad group of users'.

(ii) Leases

— We recommend that the IASB conducts an interim review of the *IFRS for SMEs*® Accounting Standard (the Standard) rather than waiting for the next comprehensive review of it, in order to progress the alignment of the Standard with IFRS 16 *Leases*.

— We suggest that the IASB should start work on such an interim review once the results of its post implementation review of IFRS 16 have been considered.

(iii) Financial instruments

— We support the ED's proposed exception from the expected credit loss (ECL) model for trade receivables and contract assets, provided they do not have a significant financing component. However, we would also propose extending this exception to cover intra-group loans.

— We disagree with the proposed accounting for financial guarantee contracts. We view the proposal to initially measure such guarantees at the transaction price as problematic, as it is common for such guarantees to arise between entities within a group, and for them to be at a zero transaction price. Were the proposals in the ED to be implemented in their current form, this would result in a 'day 2' loss as the ECL exposure is unlikely to be nil. We suggest that the IASB can overcome this issue by requiring fair value to be used in situations where the transaction price is nil.

(iv) Format of the proposed Third edition of the *IFRS for SMEs* Accounting Standard

— We are generally supportive of the approach taken by the IASB in integrating the proposed amendments with the requirements in the *IFRS for SMEs* Accounting Standard. We do however believe that Section 19 *Business Combinations and Goodwill* should be rewritten without a placeholder for deleted paragraphs and that the headings and subheadings in it be reviewed, in order to make that section more accessible to the reader.

(v) Additional disclosures about areas involving estimates or significant judgements

— In our response to the July 2021 Exposure Draft ED/2021/7 *Subsidiaries without Public Accountability: Disclosures* (ED/2021/7), we made a number of comments on particular areas of the proposals in that draft Standard, mainly relating to additional disclosure requirements that we believe should be included in it. As the concept of whether or not an entity has public accountability is central to both ED/2021/7 and the current ED, we believe that the comments we made are also relevant to the ED. We have therefore included our response to Question 8 of ED/2021/7 as Appendix III to our letter.

We set out our responses to the detailed questions in the ED in Appendix I to this letter. We also include an Appendix II with some comments that are editorial in nature.

Please contact Reinhard Dotzlaw at reinhard.dotzlaw@kpmgifrg.com or Úna Curtis at una.curtis@kpmg.ie if you wish to discuss any of the issues raised in this letter.

Yours sincerely

KPMG IFRG Limited

KPMG IFRG Limited

APPENDIX I:

QUESTIONS FOR RESPONDENTS—SCOPE OF THE STANDARD

Question 1—Definition of public accountability

Respondents to the Exposure Draft *Subsidiaries without Public Accountability: Disclosures*, published in July 2021, expressed some concerns about applying the definition of public accountability. The description of 'public accountability' in the Exposure Draft *Subsidiaries without Public Accountability: Disclosures* comprises the definition and supporting guidance in paragraphs 1.3–1.4 of the *IFRS for SMEs* Accounting Standard (Standard).

In response to this feedback, the IASB is proposing to amend paragraph 1.3(b) to list banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks as examples of entities that often meet the second criterion of public accountability in paragraph 1.3(b). To assist an understanding of the basis for the definition of public accountability, the IASB is also proposing to clarify that an entity with these characteristics would usually have public accountability:

(a) there is both a high degree of outside interest in the entity and a broad group of users of the entity's financial statements (existing and potential investors, lenders and other creditors) who have a direct financial interest in or substantial claim against the entity.

(b) the users in (a) depend primarily on external financial reporting as their means of obtaining financial information about the entity. These users need financial information about the entity but lack the power to demand the information for themselves.

Paragraphs BC11–BC19 of the Basis for Conclusions on this Exposure Draft explain the IASB's rationale for clarifying the definition of public accountability in Section 1. The IASB expects that the amendments to paragraphs 1.3 and 1.3A of Section 1 will add clarity, without changing the intended scope of the Standard.

1(i) Do you agree that the amendments will add clarity without changing the intended scope of the Standard? If you do not agree, which types of entities do you believe would be newly scoped in or scoped out?

1(ii) Do you agree with the proposal to clarify the definition of public accountability? If you do not agree with the proposal, please explain what you suggest instead and why.

We do not agree that the proposed amendments have adequately addressed our concerns. In our response to the Exposure Draft ED/2021/7 *Subsidiaries without Public Accountability: Disclosures*, we recommended that the IASB consider expanding on their intended meaning of the phrase holding assets "in a fiduciary capacity for a broad group of outsiders as one of its primary businesses”, because the legal meaning of 'fiduciary capacity' in some jurisdictions may be narrower than what is envisaged by this phrase, particularly in relation to banking and insurance entities.

We acknowledge (as set out in the Basis for Conclusions to the ED) that the IASB discussed providing guidance on, or defining, the term ‘fiduciary capacity’ during the first comprehensive review and concluded that it would be difficult to develop guidance that would be applicable, translatable and capable of being consistently applied across all jurisdictions applying the Standard.

We also acknowledge the IASB’s view that specifying how often the entities in paragraph 1.3(b) of the Standard hold assets in a fiduciary capacity is unhelpful within the definition of public accountability and it would be better to clarify why those entities often have public accountability instead.

Nevertheless, we consider that the concepts of ‘fiduciary capacity’ and ‘a broad group of outsiders’ in 1.3(b) will remain highly judgmental if the proposals in the ED are accepted. Indeed, we believe that introducing new characteristics such as “a high degree of outside interest in an entity” in the proposed 1.3A(a) will also be subject to interpretation, adding to the level of judgment that needs to be applied rather than reducing it.

We therefore continue to believe that the IASB should set out more clearly their intended meaning of the term ‘fiduciary capacity’. This would make it clear that it is not to be interpreted in a narrow legal sense. It might be helpful to use language which refers to a broad group of outsiders placing trust and confidence in an entity to manage their resources, provide them with an income after retirement or provide protection in the event of an unexpected event.

Putting aside this overarching point and concentrating on the specific text in the ED, we believe that:

- The link between 1.3(b) and the new 1.3A (which is currently discussed only in the Basis for Conclusions) should be strengthened by expanding the list of ‘users’ to encompass depositors and policy holders as examples of other creditors.
- Additional guidance should be provided on the meaning of a ‘broad group of outsiders’ given the increased use of this phrase under the proposals (we are already aware of regulators using differing numerical thresholds to interpret this phrase under the existing version of the Standard).
- 1.3A(b) should clarify that it is referring to financial information about the entity as a whole that users do not currently get, as many will of course receive information on their own investments.
- 1.3A(b) would be better supplemented by the use of examples.

Question 2—Revised Section 2 Concepts and Pervasive Principles

The IASB in its Request for Information asked for views on aligning Section 2 *Concepts and Pervasive Principles* with the *Conceptual Framework for Financial Reporting*, issued in 2018. In the Request for Information, the IASB noted that the 1989 *Framework for the Preparation and Presentation of Financial Statements* (1989 Framework) had provided the foundations of the Standard.

Based on feedback on the Request for Information, the IASB is proposing to revise Section 2 to align it with the 2018 *Conceptual Framework for Financial Reporting*.

The IASB is proposing that Section 18 *Intangible Assets other than Goodwill* and Section 21 *Provisions and Contingencies* continue to use the definitions of an asset and of a liability from the previous version of Section 2, which was based on the 1989 *Framework*, to avoid unintended consequences arising from revising the definitions of an asset and of a liability.

Paragraphs BC38–BC51 of the Basis for Conclusions on this Exposure Draft explain the IASB's rationale for the revisions proposed for Section 2.

2(i) Do you have comments or suggestions on the revised Section 2? Please explain the reasons for your suggestions.

2(ii) Do you agree that Section 18 and Section 21 should continue to use the definition of an asset and of a liability from the previous version of Section 2 (based on the 1989 *Framework*)?

Overall support

We support the proposed revision of Section 2 at an overall level, but have the following detailed comments:

Recognition criteria

Paragraph 2.70 makes reference to 'those criteria' but no criteria are actually mentioned either in this paragraph or the paragraph above it. We suggest that the paragraph should specifically refer to relevance and faithful representation to avoid any confusion here.

Relevance

There is a separate section (paragraph 2.72) on existence uncertainty but not one addressing the low probability of outflow. We recommend a section is added to address this issue.

Presentation and disclosure as communication tools

We suggest the IASB considers including in paragraph 2.120 subparagraphs (a) – (c) from paragraph 7.2 of the *Conceptual Framework for Financial Reporting*.

Other

In the same way as it has for sections 18 and 21, we believe the IASB should add a footnote to Section 20 indicating that that section also relies on the old 1989 *Framework,* as leases under IFRS 16 *Leases* meet the new definition of a liability in the revised *Conceptual Framework for Financial Reporting*.

Question 3—Proposed amendments to the definition of control in Section 9 *Consolidated and Separate Financial Statements*
The IASB in its Request for Information asked for views on aligning the definition of control in Section 9 *Consolidated and Separate Financial Statements* with the definition in IFRS 10 *Consolidated Financial Statements* and using that definition as the single basis for consolidation (control model) to facilitate greater consistency between financial statements prepared applying the Standard. Respondents to the Request for Information were in favour of the alignment, and the IASB is proposing amendments to align Section 9 with IFRS 10, introducing control as the single basis for consolidation that applies to all entities. The IASB is proposing to retain the rebuttable presumption that control exists when an investor owns more than a majority of the voting rights of an investee. The rebuttable presumption is a simplification of the control model. Paragraphs BC52–BC62 of the Basis for Conclusions on this Exposure Draft explain the IASB's rationale for aligning the definition of 'control' in Section 9 with IFRS 10 and introducing a control model as the single basis for consolidation. Do you agree with the IASB's proposal to retain the rebuttable presumption as a simplification of the definition of control? If not, please explain why you do not agree with this simplification.

Consistent with our response to the 2020 Request for Information: *Second Comprehensive Review of the IFRS for SMEs Standard* (the 2020 RFI), we support aligning the definition of control in Section 9 of the Standard with IFRS 10.

We also agree with the proposal to retain the rebuttable presumption as a simplification of the definition of control.

Question 4—Proposed amendments to impairment of financial assets in Section 11 *Basic Financial Instruments* (renamed *Financial Instruments*)
The IASB in its Request for Information asked for views on replacing the incurred loss model for the impairment of financial assets in Section 11 *Basic Financial Instruments* with an expected credit loss model aligned with the simplified approach in IFRS 9 *Financial Instruments*. Feedback suggested that the simplified approach in IFRS 9 would be complex for SMEs to apply and would not result in substantial changes in the amount of impairment for the types of financial assets held by typical SMEs, namely short-term trade receivables. The IASB anticipates that an expected credit loss model would provide relevant information for users of financial statements when SMEs hold longer-term financial assets. Consequently, the IASB is proposing to: (a) retain the incurred loss model for trade receivables and contract assets in the scope of the revised Section 23 *Revenue from Contracts with Customers*; (b) require an expected credit loss model for all other financial assets measured at amortised cost, aligned with the simplified approach in IFRS 9; and (c) retain the requirements in Section 11 for impairment of equity instruments measured at cost. Paragraphs BC72–BC80 of the Basis for Conclusions on this Exposure Draft explain the IASB's rationale for introducing an expected credit loss model for only some financial assets. 4(i) Do you agree with the proposal to introduce an expected credit loss model for only some financial assets? Why or why not? If you disagree with the proposal, please explain what you suggest instead and why. 4(ii) Do you agree that the proposal strikes the right balance in deciding which financial assets should be in the scope of the expected credit loss model, considering the costs for SMEs and benefits for users of SMEs' financial statements?

Impairment

We support the approach adopted in the Standard of having an incurred loss model for some financial assets and the introduction of an ECL model based on the simplified approach in IFRS 9 *Financial Instruments* for other financial assets.

However, we would recommend the IASB considers two amendments to the approach set out in the ED:

- We believe the incurred loss model should only apply to trade receivables and contract assets that do not have a significant financing component.

- We believe that the IASB should extend this exception to cover intra-group loans given that applying an ECL model to such assets under IFRS 9 often results in a lot of work for little change. Furthermore, it is easier to access information about other entities within a group, making an incurred loss model more acceptable for such loans, as information will be readily available to identify objective evidence of impairment at an early stage.

Financial guarantee contracts

We disagree with the proposed accounting for financial guarantee contracts.

We view the proposal to initially measure such guarantees at the transaction price as problematic, as it is common for such guarantees to arise between entities within a group and for them to be at a zero transaction price.

To expand on this, IFRS 9 requires financial guarantee contracts to be initially measured at fair value and thereafter at the higher of the amount of the loss allowance determined in accordance with IFRS 9 and the amount initially recognised less, when appropriate, the cumulative amount of income recognised in accordance with the principles of IFRS 15 *Revenue from Contracts with Customers*. When a parent guarantees the borrowings of a subsidiary and there is no transaction price, the fair value is presented as an increase in the investment in the subsidiary.

In trying to simplify IFRS 9's requirements for SMEs, the ED proposes initially measuring the guarantee at the transaction price while the subsequent measurement would be the same as IFRS 9. We consider this to be a reasonable approach for third party arrangements, as these are likely to be priced on an arm's length basis.

However, as the most common occurrences of such guarantees are intra-group guarantees and they are normally entered into at zero transaction price, problems would arise if the proposals were implemented as currently worded. This is because the accounting for such a guarantee would result in no entries on 'day 1' but then on 'day 2' the reporting entity would have an immediate remeasurement due to the recognition of an ECL amount, which would need to be recognised in profit or loss (i.e. a 'day 2 loss').

To avoid this outcome, we suggest amending the proposal so that financial guarantee contracts are initially measured at the transaction price if one is charged, but that if no transaction price is charged then they should be recognised at fair value.

Question 5—Proposal for a new Section 12 *Fair Value Measurement*
The IASB in its Request for Information asked for views on aligning the Standard with IFRS 13 *Fair Value Measurement* and introducing illustrative examples into the Standard. This alignment would not amend the requirements for when to use fair value measurement. Respondents to the Request for Information favoured aligning the Standard with the definition of fair value in IFRS 13 to provide clarity and enhance comparability between financial statements prepared applying the Standard. The IASB is proposing that the requirements on measuring fair value and related disclosure requirements be consolidated in a new Section 12 Fair *Value Measurement*. Paragraphs BC108–BC118 of the Basis for Conclusions on this Exposure Draft explain the IASB's rationale for this proposal. Do you have comments or suggestions on the new Section 12? Please explain the reasons for your suggestions.

We agree with the proposals for this section, subject to the comments on disclosure in Appendix III (reproduced from our response to ED/2021/7). In relation to the proposed disclosures in the ED, we also believe that any finalised Standard should include a full reconciliation of movements in fair value measurements classified in Level 3 of the fair value hierarchy.

Question 6—Proposed amendments to Section 15 *Investments in Joint Ventures* (renamed *Joint Arrangements*)
The IASB in its Request for Information asked for views on aligning the definition of joint control with IFRS 11 *Joint Arrangements*, while retaining the three classifications of joint arrangements in Section 15 *Investments in Joint Ventures* (jointly controlled operations, jointly controlled assets and jointly controlled entities). Respondents to the Request for Information favoured aligning the definition of joint control. However, respondents expressed mixed views on whether to align the classification and measurement requirements with IFRS 11 or to retain the Section 15 classification and measurement requirements. The IASB is proposing to align the definition of joint control and retain the Section 15 classification and measurement requirements as set out in the Request for Information. Paragraphs BC119–BC127 of the Basis for Conclusions on this Exposure Draft explain the IASB's rationale for these proposals. 6(i) Do you agree with the IASB's proposal to align the definition of joint control and retain the classification of a joint arrangement as jointly controlled assets, a jointly controlled operation, or a jointly controlled entity, and the measurement

requirements for these classifications? Why or why not? If you disagree with the proposal, please explain what you suggest instead and why.

The IASB is also proposing amendments to align Section 15 with the requirements of paragraph 23 of IFRS 11, so that a party to a jointly controlled operation or a jointly controlled asset that does not have joint control of those arrangements would account for its interest according to the classification of that jointly controlled operation or the jointly controlled asset.

Paragraphs BC128–BC129 of the Basis for Conclusions on this Exposure Draft explain the IASB's rationale for this proposal.

6(ii) Do you agree with this proposal? Why or why not? If you disagree with the proposal, please explain what you suggest instead and why.

We agree with the IASB's proposals for this section.

In our response to the 2020 RFI we had advocated adopting a simplified version of the tests in IFRS 11 *Joint Arrangements* to differentiate between joint ventures and joint operations, and had consequently recommended replacing the categories of jointly controlled assets, jointly controlled operations and jointly controlled entities in Section 15 of the *IFRS for SMEs* Accounting Standard with the IFRS 11 categories – i.e. joint ventures and joint operations.

Given however the IASB's decision to make the existence of a legal entity the differentiating point between 'jointly controlled entities' and 'jointly controlled operations', we support the ED's proposed retention in Section 15 of the existing categories of jointly controlled assets, jointly controlled operations and jointly controlled entities. To adopt the alternative of using IFRS 11's 'joint venture' and 'joint operation' categories would in our view be potentially misleading to the user, as the decision to retain the existence of a separate entity as the differentiating factor between 'jointly controlled entities' and 'jointly controlled operations' means that those categories would not be truly comparable to those in IFRS 11.

Question 7—Proposed amendments to Section 19 *Business Combinations and Goodwill*

Based on the feedback to the Request for Information, the IASB is proposing to align Section 19 *Business Combinations and Goodwill* with the acquisition method of accounting in IFRS 3 *Business Combinations** by:

(a) adding requirements and guidance for a new entity formed in a business combination;

(b) updating the references when recognising the identifiable assets acquired and liabilities assumed in a business combination to refer to the definitions of an asset and a liability in the revised Section 2 *Concepts and Pervasive Principles*;

(c) clarifying that an acquirer cannot recognise a contingency that is not a liability;

(d) requiring recognition of acquisition-related costs as an expense;

(e) requiring measurement of contingent consideration at fair value if the fair value can be measured reliably without undue cost or effort; and

(f) adding requirements for an acquisition achieved in stages (step acquisitions).

For other aspects of the acquisition method of accounting, the IASB is proposing to retain the requirements in Section 19. The IASB is of the view that:

(a) the guidance in IFRS 3 on reacquired rights is unlikely to be relevant to entities applying the Standard;

(b) restricting the measurement of non-controlling interest in the acquiree to the non-controlling interest's proportionate share of the recognised amounts of the acquiree's identifiable net assets (and not introducing the fair value option) is an appropriate simplification; and

(c) retaining recognition criteria for intangible assets acquired in a business combination balances the costs and benefits of separate recognition of these items because goodwill recognised in a business combination is amortised.

Paragraphs BC130–BC183 of the Basis for Conclusions on this Exposure Draft further explain the IASB's rationale for these proposals.

* IFRS 3 refers to the IFRS 3 (2008) version, including subsequent amendments to IFRS 3.

Paragraph BC177 of the Basis for Conclusions on this Exposure Draft explains that there were mixed views on whether step acquisitions are relevant to SMEs. The IASB is asking for views on adding requirements for step acquisitions and on the proposed requirements themselves. Asking for views on whether to add requirements allows stakeholders to evaluate the proposals when responding to this Invitation to Comment.

7(i) Do you agree with the proposal to introduce requirements for the accounting for step acquisitions? If your answer is yes, do you agree with the proposed requirements in the Exposure Draft? If you disagree with the proposal, please explain why and give your alternative suggestion.

7(ii) Do you agree that the IASB's proposals appropriately simplify the measurement of non-controlling interests by excluding the option to measure them at fair value? If your answer is no, please explain your reasons.

7(iii) Do you have any further comments or suggestions on the proposed amendments to Section 19? Please explain the reasons for your suggestions.

We agree with the proposal to introduce requirements for the accounting for step acquisitions. We also agree with the proposed simplification of the measurement of non-controlling interests.

We have a specific comment on contingent liabilities that would be accounted for under paragraph 19.23A – i.e. contingent liabilities acquired in a business combination. We believe that having to recognise these subsequently at the higher of 19.23A(a) and (b) is quite complex for SMEs to apply. We therefore believe that a 'best estimate' approach of the amount that would be recognised under Section 21 should be sufficient in accounting for such contingent liabilities.

We also recommend that the illustrative examples included in 19B are expanded or replaced with the following examples from IFRS 3, which may be more relevant to entities applying the *IFRS for SMEs* Accounting Standard:

- Example E – acquisition of a closed manufacturing facility [IE101 – IE103]
- Example F – licence of distribution rights [IE104 – IE106]
- Example G – acquisition of brands [IE107 – IE109]

Finally, we suggest that the IASB rewrite the entire section and renumber the paragraphs to make it easier to read. The changes are extensive and a rewrite of the section would make it easier to understand.

We further suggest that in doing so, the IASB reassess the headings and subheadings used in this section, as some could be improved.

Question 8—Revised Section 23 *Revenue* (renamed *Revenue from Contracts with Customers*)

The IASB in its Request for Information asked for views on possible approaches to aligning Section 23 *Revenue* with IFRS 15 *Revenue from Contracts with Customers*.

Respondents favoured this alignment without identifying a preferred approach.

Consequently, the IASB is proposing to revise Section 23 to align it with the principles and language used in IFRS 15. The revised requirements are based on the five-step model in IFRS 15, with simplifications that retain the basic principles in IFRS 15 for recognising revenue.

Paragraphs BC184–BC193 of the Basis for Conclusions on this Exposure Draft further explain the IASB's rationale for this proposal and the proposed simplifications of the IFRS 15 requirements.

8(i) Do you agree that the revised Section 23 would be appropriate for SMEs and users of their financial statements? If not, what modifications—for example, further simplifications or additional guidance—do you suggest and why?

Determining whether a good or service promised to a customer is distinct can involve judgement. To assist entities in making this assessment, the IASB is proposing to simplify the requirements in paragraphs 27–29 of IFRS 15 by:

a) specifying that a good or service that an SME regularly sells separately is capable of being distinct (see paragraph 23.21 of the Exposure Draft);

b) expressing the criterion in paragraph 27(b) of IFRS 15 in simpler language and reflecting the objective of the criterion by focusing on whether a good or service is an input used to produce a combined item or items transferred to the customer (see paragraphs 23.20(b) and 23.23 of the Exposure Draft); and

c) including examples that illustrate the factors supporting that criterion (see paragraph 23.23(a)–(c) of the Exposure Draft).

8(ii) Do you believe the guidance is appropriate and adequate for entities to make the assessment of whether a good or service is distinct? If not, is there any guidance that could be removed or additional guidance that is needed?

We are generally supportive of the proposed introduction of a simplified version of IFRS 15's requirements, but have concern over the detailed proposals in the following areas:

Scope

We suggest amending paragraph 23.2 by adding a sentence at the start to explain in simpler terms that "An entity may earn revenue from sources other than contracts with customers, such as rental income and interest income, which should be accounted for within the scope of another section", as our experience shows that preparers struggle with this concept.

Principal vs agent considerations

We feel that the simplifications proposed in the ED could actually make the principal vs agent decision more complicated under the *IFRS for SMEs* Accounting Standard (for instance there is a potential conflict between paragraph 23.38(a) and paragraphs 23.38(b) and 23.38(c) in the ED). Also, generally speaking, more entities would be likely to be considered principal under the proposals than under IFRS 15.

We therefore feel that the IASB should go back to the IFRS 15 model that is focused solely on 'control', but with additional guidance on how to identify 'control'. Accordingly, we believe the IASB should add the guidance in IFRS 15.32-33 and IFRS 15.B35 to the text proposed in the ED. The criterion set out in 23.38(a) should be retained as an indicator of control.

Our view is partly influenced by the fact that most industries have considered the IFRS 15 guidance and determined which entities are principals and agents, and that much of this analysis is publicly available. Were the IASB to change the criteria in the *IFRS for SMEs* Accounting Standard, then it might not be possible for entities to rely on the analyses carried out under IFRS 15, which seems burdensome for SMEs.

Over time criteria

We have the following reservations over the proposals in this area.

We do not agree with the content of subparagraph 23.78(b) being treated as a separate criterion.

The equivalent text in IFRS 15 is not considered a separate criterion, but rather an outcome of applying the criterion which has been transposed to subparagraph 23.78(a) of the *IFRS for SMEs* Accounting Standard.

We consider that it has the potential to be misinterpreted without the qualification that the entity taking over the promise would not get access to the work in progress of the entity ceasing to deliver under the promise. For example, without this clarification it could be argued that a part-built house would meet 23.78(b).

We recommend then that subparagraph 23.78(b) should be deleted, with the example given in it instead being dealt with under 23.78(a).

We also consider the example given in 23.78(c) unhelpful, as it does not provide any guidance as to how to assess that the entity is obtaining control as the asset is created or enhanced. We recommend that guidance is added to address this point.

Warranties

We do not understand why paragraph 23.26 cross-references paragraphs 23.16-24 given those paragraphs discuss how to identify a separate promise, whereas paragraph 23.26 has already concluded that a separate promise exists.

We question whether the proposed concept in subparagraph 23.27(a) of assessing whether a warranty is “significant to the contract” effectively introduces a new materiality threshold. We recommend the IASB provides guidance on how to interpret this phrase.

Non-refundable fee that gives customers an option to renew the contract on similar terms

Similar to the comment on 23.27 above, we feel that paragraph 23.31 will raise questions of interpretation over materiality. We are also unsure why paragraphs 23.16-23.24 are being referenced, and recommend that the IASB explains this.

Output method based on units delivered

We note that the method set out in subparagraph 23.92(b) would seem to allow “units to be delivered” on a broader basis than under IFRS 15. For example, there is no consideration of whether material WIP exists. We recommend the IASB reflect on whether this is appropriate.

Disclosure

Lastly, we recommend separating the requirements related to contract assets from those for contract liabilities, as this will simplify the understanding and application of the disclosure.

Question 9—Proposed amendments to Section 28 *Employee Benefits*
The IASB in its Request for Information asked for views on applying paragraph 28.19 of the Standard, that is the measurement simplifications for defined benefit obligations. The feedback identified challenges when applying paragraph 28.19, resulting in diversity of application. However, the feedback also provided evidence that only a few entities apply paragraph 28.19. Therefore, the IASB is proposing to delete paragraph 28.19. Paragraphs BC197–BC203 of the Basis for Conclusions on this Exposure Draft explain the IASB's rationale for this proposal. 9(i) Do you agree that only a few entities apply the measurement simplifications for defined benefits? Therefore, do you agree with the IASB's proposal to delete paragraph 28.19? Alternatively, if you do not agree with deleting paragraph 28.19, should the IASB clarify the paragraph by: a) stating that an entity may apply any, or all, of the simplifications permitted by paragraph 28.19 when measuring a defined benefit obligation; and b) explaining that when an entity applies paragraph 28.19(b), examples of future service of current employees (assumes closure of the plan for existing and any new employees) that can be ignored include: (i) the probability of employees' not meeting the vesting conditions when the vesting conditions relate to future service (future turnover rate); and (ii) the effects of a benefit formula that gives employees greater benefits for later years of service. 9(ii) If you disagree with the proposal in 9(i), do you agree that this alternative approach clarifies paragraph 28.19?

We agree with the proposed deletion of paragraph 28.19.

We agree that only a few entities apply the measurement simplifications in paragraph 28.19 for defined benefit plans. We say this as our experience is that most entities with defined benefit plans use reports provided by actuaries, and so do not need to use the measurements simplifications. We therefore agree with the IASB's proposal to delete paragraph 28.19.

Question 10—Transition
The IASB, in paragraphs A2–A39 of this Exposure Draft, sets out limited relief from retrospective application for those proposed amendments for which the IASB thought the costs of retrospective application would exceed the benefits. Do you agree with the proposed transition requirements for the amendments to the *IFRS for SMEs* Accounting Standard? Why or why not? If not, please explain what you suggest instead and why.

We agree with the proposed transition requirements.

In our response to the 2020 RFI, we had supported providing transition relief similar to IFRS 15 when issued, by permitting an entity to continue its current recognition policy for any contracts already in progress at the date of transition that are scheduled to be completed within a set time after the date of transition.

The ED widens this transition relief by providing an exemption for all contracts in progress at the date of initial application. We are comfortable that this wider transition relief is proportionate to the needs of preparers using the *IFRS for SMEs* Accounting Standard. We therefore agree with the proposed transition requirements.

Question 11—Other proposed amendments
Table A1, included in the Introduction, summarises the proposals for amending sections of the Standard not included in questions 2–10. Do you have any comments on these other proposed amendments in the Exposure Draft?

We disagree with the lack of an option in the ED to capitalise borrowing costs.

To expand on this, we believe that in simplifying the requirements of IFRS® Accounting Standards for use by SMEs, the IASB should not automatically exclude options but should sometimes permit alternative treatments if they are relevant to SMEs.

We believe including an option to capitalise borrowing costs that are directly attributable to the acquisition, construction or production of a 'qualifying asset' could be very relevant for SMEs in certain sectors and would be more closely aligned with the requirements of IAS 23 *Borrowing Costs*. We therefore recommend the IASB allows such an option to capitalise borrowing costs.

As discussed in more length in our response to question 13, we also support the IASB in introducing an accounting policy option that permits an entity applying the *IFRS for SMEs* Accounting Standard to recognise intangible assets arising from development costs that meet the criteria in paragraphs 57(a)–(f) of IAS 38 *Intangible Assets*.

Question 12—Section 20 *Leases* and IFRS 16 *Leases*
The IASB in its Request for Information asked for views on aligning Section 20 *Leases* with IFRS 16 *Leases* by simplifying some of the recognition and measurement requirements, the disclosure requirements and the language of IFRS 16. Feedback on the Request for Information was mixed. Stakeholders suggested the IASB assess the costs and benefits of aligning the Standard with IFRS 16, even with the simplifications, and obtain more information about the experience of entities that apply IFRS 16. The IASB decided not to propose amendments to Section 20 at this time and to consider amending the Standard to align it with IFRS 16 during a future review of the Standard. Therefore, the Exposure Draft does not propose amendments to Section 20. In making this decision the IASB placed greater emphasis on cost–benefit considerations and prioritised timing—that is, to obtain more information on entities' experience of applying IFRS 16. The IASB is asking for further information on cost–benefit considerations, particularly on whether: (a) aligning Section 20 with IFRS 16 at this time imposes a workload on SMEs disproportionate to the benefit to users of their financial statements—specifically, considering: (i) the implementation costs that preparers of financial statements could incur; (ii) the costs that users of financial statements could incur when information is unavailable; and (iii) the improvement to financial reporting that would be realised from recognising the lessee's right to use an underlying asset (and the lessee's obligation to make lease payments) in the statement of financial position. (b) introducing possible simplifications—for example, for determining the discount rate and the subsequent measurement of the lease liability (reassessment)—could help to simplify the requirements and reduce the cost of implementing an amended Section 20 (aligned with IFRS 16) without reducing the usefulness of the reported information. Paragraphs BC230–BC246 of the Basis for Conclusions on this Exposure Draft further explain the IASB's rationale for not proposing amendments to Section 20 at this time and instead for considering amending the Standard to align it with IFRS 16 during a future review of the Standard. Do you agree with the IASB's decision to consider amending the Standard to align it with IFRS 16 in a future review of the Standard? In responding to this question, please comment on the cost–benefit considerations in paragraphs (a) and (b).

We accept the IASB's decision to consider amending the Standard to align Section 20 with IFRS 16 in a future review of the Standard, although we would have preferred the IASB to have aligned Section 20 with IFRS 16 (with appropriate simplifications) in the current review.

Given that the IASB does not intend to align Section 20 with IFRS 16 in the current review, we recommend that it conducts an interim review of the *IFRS for SMEs* Accounting Standard rather than waiting for the next comprehensive review of the *IFRS for SMEs* Accounting Standard. We say this as we believe that waiting for the next comprehensive review of the *IFRS for SMEs* Accounting Standard would result in the principles in this section of the Standard not being aligned with the approach taken under IFRS Accounting Standards and with the revised definition of a liability for too long a period. We believe that a suitable time to undertake such an interim review would be once the results of the IASB's post implementation review of IFRS 16 have been considered.

Question 13—Recognition and measurement requirements for development costs

The Standard requires all development costs to be recognised as expenses, whereas IAS 38 *Intangible Assets* requires the recognition of intangible assets arising from development costs that meet specified criteria. This simplification in the Standard was made for cost–benefit reasons. However, feedback on this comprehensive review questioned this cost–benefit decision. Therefore, the IASB is seeking views on whether it should amend the Standard to align it with IAS 38, including views on the costs and benefits of doing so.

Paragraphs BC253–BC257 of the Basis for Conclusions on this Exposure Draft further explain the IASB's rationale.

What are your views on the costs and benefits, and the effects on users, of introducing an accounting policy option that permits an SME to recognise intangible assets arising from development costs that meet the criteria in paragraphs 57(a)–(f) of IAS 38? The entity would be required to demonstrate all of these criteria:

(a) the technical feasibility of completing the intangible asset so that it will be ready for use or sale;

(b) its intention to complete the intangible asset and use or sell it;

(c) its ability to use or sell the intangible asset;

(d) how the intangible asset will generate probable future economic benefits;

(e) the availability of adequate technical, financial and other financial resources to complete the development and to use or sell the intangible asset; and

(f) its ability to measure reliably the expenditure attributable to the intangible asset during its development.

As discussed in our response to question 11 above, we believe that in simplifying the requirements of IFRS Accounting Standards for use by SMEs, the IASB should not automatically exclude options but should sometimes permit alternative treatments if they are relevant to SMEs.

We therefore support the introduction of an accounting policy option that permits an SME to recognise intangible assets arising from development costs that meet the criteria in paragraphs 57(a)–(f) of IAS 38.

Technological developments in recent decades have resulted in the recognition of many more intangible assets, and the SME market is no exception to this. For some SMEs, not recognising the intangible assets that arise from their development activity obscures the picture of their performance and does not allow investors and other stakeholders to accurately gauge the returns that those SMEs have made on their investment in intangible assets. We do not believe that introducing such an accounting policy option would add unnecessary complexity for SMEs as a whole.

Should the IASB decide to introduce such an option, we would suggest that it should use the same words as included in paragraphs 57(a)–(f) of IAS 38. Doing so will enable the proposed requirement to be interpreted in the same way as the requirements of IFRS Accounting Standards, thereby promoting consistency and comparability, whereas using different words to convey the same principle would introduce additional complexity and uncertainty about the intended meaning.

Question 14—Requirement to offset equity instruments
Paragraph 22.7(a) of the Standard states that if equity instruments are issued before an entity receives cash or other resources, the amount receivable is presented as an offset to equity in the statement of financial position, instead of being presented as an asset. Feedback from the first comprehensive review suggested that this requirement may conflict with local legislation. Stakeholders provided similar feedback during this second comprehensive review, suggesting that the IASB remove the requirement in paragraph 22.7(a) because it diverges from full IFRS Accounting Standards, which include no similar requirement for equity instruments. What are your views on removing paragraph 22.7(a)?

We believe paragraph 22.7(a) should be removed.

In a situation where an entity is owed an amount in respect of a contribution for new equity shares that have already been issued, our view under IFRS Accounting Standards is that the equity and a corresponding receivable should be recognised if the receivable meets the definition of a financial asset or a receivable of non-monetary consideration (i.e. the entity has a contractual right to receive the amount at the reporting date).

Paragraph 22.7(a) conflicts with the above view that we have taken under IFRS Accounting Standards, resulting in what we consider to be an unnecessary and illogical difference between IFRS Accounting Standards and the *IFRS for SMEs* Accounting Standards.

We therefore support removing paragraph 22.7(a) in order that a receivable would be recorded when the definition of a financial asset is met (or, in the case of non-monetary consideration, when the definition of an asset has been attained).

Question 15—Updating the paragraph numbers of the *IFRS for SMEs* Accounting Standard
The proposed amendments to the requirements in the *IFRS for SMEs* Accounting Standard include the addition of new paragraphs and the deletion of existing paragraphs. A new paragraph is numbered in continuation from a previous paragraph. A deleted paragraph retains the paragraph number. Sometimes, the addition or deletion of paragraphs within a section may complicate the readability of the Standard (for example, Section 19 *Business Combinations and Goodwill*). As an alternative, a section may be revised, with paragraphs renumbered to show only requirements that would still be applicable, without a placeholder for deleted paragraphs (for example, Section 2 *Concepts and Pervasive Principles*). What are your views on the approach taken to retain or amend paragraph numbers in each section of this Exposure Draft?

As discussed in our response to Question 7, we believe that Section 19 *Business Combinations and Goodwill* should be rewritten without a placeholder for deleted paragraphs, in order to be more accessible to the reader. We also recommend that the headings and subheadings should be reviewed.

Other than that, we have no objection to the approach that has been taken in the ED on the addition or deletion of paragraphs.

APPENDIX II:

EDITORIAL COMMENTS ON INDIVIDUAL SECTIONS

Section 3 Financial Statement Presentation

Para ref.	Amendment	Rationale
3.2(b)	Delete "in accordance with this Standard".	Unnecessary.
3.17(e)	The ED proposes the following amendments "…comprising material ~~a summary of significant~~ accounting policy information ~~policies~~ and other explanatory information". We suggest changing this text to read "…comprising material accounting policies and other explanatory information".	Information is repeated in close succession. We suggest retaining 'accounting policies' to avert this.

Section 4 Statement of Financial Position

Para ref.	Amendment	Rationale
4.2	Suggest deleting the section titles referred to in subparagraphs (e), (h) and (i).	It is not clear why the section title is referred to in subparagraphs (e), (h) and (i) but not in the other subparagraphs?

Section 5 Statement of Comprehensive Income and Income Statement

Para ref.	Amendment	Rationale
5.4(b)	Suggest amending to read "the effects of corrections of errors and changes in accounting policies are presented as retrospective adjustments of prior periods instead of as part of profit or loss in the period in which they ~~arise~~ are found" (see Section 10); and	Use of the word 'arise' may be confusing to the reader.

Section 7 Statement of Cash Flows

Para ref.	Amendment	Rationale
7.19A	Suggest expanding the list to include interest accrued.	

Section 9 Consolidated and Separate Financial Statements

Para ref.	Amendment	Rationale
9.13(c)	"measure and present non-controlling interest in the profit or loss and total comprehensive income of consolidated subsidiaries for the reporting period separately from the interest of owners of the parent."	Suggest that this be extended to also require separate disclosure of the NCI share of "total comprehensive income". It is more consistent with 5.6 which requires both.

Section 10 Accounting Policies, Estimates and Errors

Para ref.	Amendment	Rationale
10.15	"A change in the measurement basis applied is a change in accounting policy (except as set out in 10.9(c)), and is not a change in accounting estimate."	Paragraph 10.9(c) specifically says that a change from fair value to cost is not a change in accounting policy where the reason for the change is the unreliability of the fair value measurement.

Section 11 Financial Instruments

Para ref.	Amendment	Rationale
11.9	A debt instrument that satisfies all of the conditions in (a)–(d) shall be accounted for in accordance with ~~with~~ Part I of Section 11:	Delete duplicated word.
11.9(a)(iii)	Define SONIA	The acronym, which has not been used before, should be defined when first used.
11.13	Example 3 contains the phrase "future premium payments receivable". Suggest	The juxtaposition of 'payments' and 'receivables' may be

	changing this to "future premiums receivable".	confusing to readers, particularly those for whom English is not their native language.
11.20	The "Example of determining amortised cost for a five-year loan using the effective interest method" contains a footnote stating "**The carrying amount is shown before the allowance for expected credit losses". Consider substituting 'presented' for 'shown'.	
11.26G	"…would be consistent with the estimation~~s~~ of cash shortfalls for the asset subject to the guarantee	Should be "estimation" (singular)
11.56	"…At the end of each reporting period, an entity shall measure all financial instruments within the scope of ~~of~~ Part II	Delete duplicated word.
11.57	Change "Dividends are recognised in profit or loss only when…" to "Dividend income is recognised in profit or loss only when…"	

Section 13 Inventories

Para ref.	Amendment	Rationale
13.1(c)	We recommend that the cost of providing services is excluded from the scope of this section.	This is to maintain a similar scope to IFRSs, as the cost of providing services is not within the scope of IAS 2 *Inventories*, but is treated as costs of fulfilling a contract in IFRS 15 *Revenue from Contracts with Customers*. In addition, paragraphs 106-113 of Section 23 *Revenue from Contracts with Customers* in this Standard provide guidance on recognition and measurement of costs of fulfilling a contract, which can provide sufficient

		guidance for cost of providing services.

Section 15 Joint Arrangements

Para ref.	Amendment	Rationale
15.1	"This section applies to an entity that is a party to a joint arrangement in <u>its</u> consolidated financial statements <u>and</u>, if the entity is not a parent, ~~and~~ in ~~the~~ <u>its</u> individual financial statements."	To improve clarity.
15.8	"A jointly controlled entity is a joint arrangement that involves the establishment of a corporation, partnership, other entity <u>or a financial structure that is separate from the parties themselves</u> in which each party has an interest. The entity operates in the same way as other entities, except that an arrangement between ~~the~~ <u>certain</u> parties establishes joint control."	In the first sentence to align the wording with the wording in 15.4. In the second sentence to acknowledge that not all the parties may exercise joint control.

Section 17 Property, Plant and Equipment

Para ref.	Amendment	Rationale
17.10-12	We recommend providing guidance on proceeds before intended use of an item of property, plant and equipment, similar to IAS 16.20A.	Under IAS 16.20A, an entity recognises the proceeds from selling any such items, and the cost of those items, in profit or loss in accordance with applicable Standards. The entity measures the cost of those items applying the measurement requirements of IAS 2. We believe this would also provide useful guidance for SMEs.
17.28	We recommend providing guidance on the proceeds from selling items of property, plant and equipment in the	We believe this would also provide useful guidance for SMEs.

	course of an entity's ordinary activities, similar to IAS 16.68A.	

Section 19 Business Combinations and Goodwill

Para ref.	Amendment	Rationale
19.3	We suggest the definition of a business combination is underlined and included in the Glossary of terms.	

Section 21 Provisions and Contingencies

Para ref.	Amendment	Rationale
Appendix to Section 21	A couple of the examples in the Appendix have been deleted, so the examples need to be renumbered.	

Section 23 Revenue from Contracts with Customers

Para ref.	Amendment	Rationale
23.105	Suggest that this exemption is extended to also cover costs of fulfilling a contract.	
23.121-129	Consider separating the disclosure wording between the literature that is relevant for contract assets and for contract liabilities.	This will help to simplify the application for SMEs.

Section 26 Share-based Payment

Para ref.	Amendment	Rationale
26.14A	A cash-settled share-based payment transaction might be conditional on satisfying specified vesting conditions. Vesting conditions are accounted for as follows: (a) ~~all vesting conditions related to employee service~~ a service condition or ~~to~~ a non-market performance condition shall be taken into account when estimating the number of awards that are expected to vest and subsequently adjusting the number of awards included	The suggested change is to align with the proposed changes in paragraphs 26.9 and newly added definition for service condition. More preferably, to align with full GAAP wordings (IFRS 2.33A): "Vesting conditions, other than market conditions……"

	in the measurement of the liability arising from the transaction. The entity shall initially recognise an amount for the goods or services received during the vesting period based on the number of awards that are expected to vest. Subsequently, the entity shall revise that estimate if new information indicates that the number of awards expected to vest differs from previous estimates. On the vesting date, the entity shall revise the estimate to equal the number of awards that ultimately vested. ~~Vesting conditions related to employee service~~ The service condition and a nonmarket performance condition shall not be taken into account when estimating the fair value of the cash-settled share-based payment at the measurement date.	
26.15	In circumstances (a) and (b), the entity shall account for the transaction as an equity-settled share-based payment transaction in accordance with paragraphs 26.7–26.13 and apply paragraphs 26.15A-26.15C to circumstance (c).	The accounting for the newly introduced circumstance (c) is currently unaddressed.

Section 28 Employee benefits

Para ref.	Amendment	Rationale
28.17	17 ~~An entity shall measure its defined benefit obligation on a discounted present value basis.~~ The entity shall determine the rate used to discount the benefit in order to determine the present value of the defined benefit obligation, ~~the future payments~~ by reference to market yields at the reporting date on high quality corporate bonds.	When the first sentence is deleted in the ED, it is hard to reconcile to the discounting requirement. We therefore suggest adding the missing part in the following sentence. It also reconciles to Paragraph 28.18, which does not mean that it is to discount the future payments, rather discounting is one of the

		steps to determine the defined benefit obligation.

Section 29 Income Tax

Para ref.	Amendment	Rationale
29.16A	An entity considers: (a) the extent that it is probable that <u>future</u> taxable profit will be available; and	Suggest inserting the word 'future'.
29.34C	An entity shall assume that a taxation authority will examine amounts it has a right to examine and have full knowledge of all related information when making those examinations. <u>Then an entity shall consider whether it is probable that a taxation authority will accept an uncertain tax treatment or not, and account for its conclusion as follows</u> ~~If an entity includes either~~:	Suggested change to align with the wordings in IFRIC 21.9-11.

Section 30 Foreign Currency Translation

Para ref.	Amendment	Rationale
	The phrase 'reporting entity' is used in several places. The term is defined in Appendix B – and refers to "an entity …", however the word 'entity' is not itself defined. We suggest that a definition is provided.	Lack of a definition could lead to questions of whether to apply the requirements to a component of a legal structure (for example, a company) and the impact on foreign currency translation.

Section 32 Events after the End of the Reporting Period

Para ref.	Amendment	Rationale
32.3	We question the use of the phrase 'public announcement'.	Will this phrase be readily understood in markets around the world?

Section 33 Related Party Disclosures

Para ref.	Amendment	Rationale
33.2(a)(i)	Consider defining key management personnel.	The phrase is defined under IAS 33 Related Party Disclosures. Not disclosing it may leave it open to interpretation.

APPENDIX III:

Extract from KPMG IFRG's response to Exposure Draft ED/2021/7 Subsidiaries without Public Accountability: Disclosures

Question 8 – The proposed disclosure requirements
Paragraphs 22–213 of the draft Standard set out proposed disclosure requirements for an entity that applies the Standard. In addition to your answers to Questions 4 to 7: (a) Do you agree with those proposals? Why or why not? If not, which proposals do you disagree with and why? (b) Do you recommend any further reduction in the disclosure requirements for an entity that applies the Standard? If so, which of the proposed disclosure requirements should be excluded from the Standard and why? (c) Do you recommend any additional disclosure requirements for an entity that applies the Standard? If so, which disclosure requirements from other IFRS Standards should be included in the Standard and why?

We agree with the majority of the proposed disclosure requirements, but have a number of comments on particular areas of the proposals, mainly relating to additional disclosure requirements that we believe should be included in the draft Standard.

We set out these details in Appendix II* to this letter.

A consistent theme however is the need for disclosures about areas involving estimates or significant judgements which we believe should be added to the draft Standard. Examples include the following.

— Revenue
  — Significant judgements made in applying IFRS 15. [IFRS 15.110(b), 123]
  — Separate disclosure of revenue in the scope of IFRS 15. [IFRS 15.113(a)]
  — Timing of revenue recognition and the nature of goods or services provided. [IFRS 15.119(a), (c)]
— Provisions
  — Disclosures about assumptions relating to future events. [IAS 37.85(b)]
— Income tax
  — Recognition of deferred tax assets. [IAS 12.82]
  — Uncertain tax treatments. [IFRIC 23.A4–A5]

— Impairment of assets
  — Disclosure of the growth rate. [IAS 36.134(d)(iv)]
  — Disclosure of the discount rate. [IAS 36.134(d)(v)]
— Financial instruments
  — Nature and extent of risks arising from financial instruments.
— Fair value measurement
  — Change in valuation technique. [IFRS 13.93(d)]
  — The need for additional detail, in particular quantitative disclosures on Level 3 inputs.
  — The need for additional detail on movements in Level 3 items.

* Note we are referring here to Appendix II in our response to Exposure Draft ED/2021/7 *Subsidiaries without Public Accountability: Disclosures*.