This paper has been prepared by the EFRAG Secretariat for discussion at a public meeting of EFRAG TEG. The paper forms part of an early stage of the development of a potential EFRAG position. Consequently, the paper does not represent the official views of EFRAG or any individual member of the EFRAG Board or EFRAG TEG. The paper is made available to enable the public to follow the discussions in the meeting. Tentative decisions are made in public and reported in the EFRAG Update. EFRAG positions, as approved by the EFRAG Board, are published as comment letters, discussion or position papers, or in any other form considered appropriate in the circumstances.

Subsidiaries that are SMEs
Cover Note

Objective

1 The objective of the session is to:

(a) discuss a number of sweep issues identified by the IASB Staff when balloting the exposure draft of a future reduced-disclosure IFRS Standard;

(b) discuss key messages for EFRAG Draft Comment Letter.

Agenda Papers

2 In addition to this cover note, agenda papers for this session are:

(a) Agenda paper 05-02 – Issues paper on sweep issues;

(b) Agenda paper 05-03 – Key messages for EFRAG Draft Comment Letter; and

(c) Agenda paper 05-04 – IASB's tentative decisions – for background only.

(d) Agenda paper 05-05 – Use of IFRS in Europe

(e) Background paper 05-06 – Presentation of the IASB to EFRAG Board on 9 July 2021

Background on the IASB's Project

3 In the 2015 Agenda Consultation, a number of respondents called for the IASB to permit subsidiaries to apply IFRS Standards but with reduced disclosure requirements. These respondents noted that the use of the IFRS for SMEs Standard is not attractive for subsidiaries that report to their parent for consolidation purposes and apply the recognition and measurement requirements of IFRS Standards.

4 In addition, it was argued that these subsidiaries preferred to use the recognition and measurement requirements of IFRS Standards but with less onerous disclosure requirements. Such an approach would reduce costs, without removing information needed by the users of the subsidiaries' financial statements.

5 In March 2016, the IASB added a research project to its pipeline and early in 2020 the IASB moved the project from the research programme to the standard-setting programme.

6 The objective is to develop a reduced-disclosure IFRS Standard that would apply on a voluntary basis to subsidiaries that are SMEs—that is, subsidiaries that do not have public accountability.

7 During the meeting, the IASB Staff will provide an overview of the IASB's project *Disclosure Initiative—Subsidiaries that are SMEs*.

Background on the EFRAG TEG discussions

8 The EFRAG Secretariat has been providing regular updates to EFRAG TEG and other EFRAG Working Groups. The key topics discussed by EFRAG TEG can be found below.

Research phase (EFRAG TEG-CFSS March 2019 and EFRAG TEG May 2020)	• Would a reduced-disclosure IFRS Standard be adopted by jurisdictions and applied by subsidiaries that are SMEs? • Can the IASB use the disclosure requirements in *IFRS for SMEs* with only minimal tailoring? • How can the project benefit subsidiaries? • Moving the project to the standard-setting programme.
Scope of the project (EFRAG TEG March 2021)	• Should the scope remain subsidiaries that are SMEs, be extended to all SMEs, somewhere between the two or be narrower?
Presentation (EFRAG TEG May 2020)	• Should the IASB require subsidiaries to apply the presentation requirements of IFRS Standards or the presentation requirements of the *IFRS for SMEs*?
Disclosures – main principles (EFRAG TEG March 2021)	• How to adapt the disclosure requirements of the *IFRS for SMEs?* • Should there be exceptions? • When should the IASB consider disclosure requirements for new and amended IFRS Standards?
Consultation document (EFRAG TEG March 2021)	• Should the consultation document be an exposure draft or a discussion paper?
Disclosures – specific issues (EFRAG TEG May 2021)	• Should the compliance statement required by IAS 1 *Presentation of Financial Statements* indicate the entities that have applied the reduced-disclosure IFRS Standard? • Should the disclosure requirements of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* be applied by subsidiaries that are SMEs? • Should the disclosure requirements for transition provisions of new and amended IFRS Standards be applied by subsidiaries that are SMEs? • Should the disclosure requirements on combined financial statements in the IFRS for SMEs Standard be included in the reduced-disclosure IFRS Standard? • Should the reduced-disclosure IFRS Standard cover omitted topics in *IFRS for SMEs* such as disclosures on insurance contracts, regulatory deferral account

	balances, interim financial reports or earnings per share. • Which disclosure requirements should be proposed in the reduced-disclosure IFRS Standard for cash-generating units containing goodwill and intangible assets with indefinite useful lives?
Transition to the reduced-disclosure IFRS Standard. (EFRAG TEG May 2021)	• Is there a need to amend to IFRS 1 *First-time Adoption of International Financial Reporting Standards* or include transition provisions in the reduced-disclosure IFRS Standard? • Could the reduced-disclosure IFRS Standard be applied for the 'first time' more than once? • Is first-time application of the reduced-disclosure IFRS Standard an accounting policy choice?

9 In those meetings, EFRAG TEG members:

(a) **Research Phase**: noted that the interest in such a standard in the European Union would vary across jurisdictions as some allow the use of IFRS Standards for the annual accounts (including separate financial statements) and some do not, and some have already developed reduced disclosure standards in national GAAP;

(b) **Scope of the project**: generally agreed with the scope of the project and the IASB's key principles on how to adapt the disclosure requirements of IFRS for SMEs. When discussing whether the scope of the project should be expanded, some EFRAG TEG members noted that:

(i) the project was focused on reducing the costs for a subset of SMEs that have to report in IFRS to the group;

(ii) that the IASB was experimenting something new and restricting the scope would allow the IASB to better test its new approach; and

(iii) that if the scope were to be extended, then users may not receive the information needed.

(c) **Presentation:** did not disagree with the IASB proposal to apply the presentation requirements of IFRS Standards (rather than those in the IFRS for SMEs)

(d) **Consultation document:** most agreed with the IASB decision to issue an Exposure Draft as next step. This is because the IASB's proposals would be best illustrated in an exposure draft as this would enable stakeholders to assess the proposed disclosure requirements in more detail. However, a few members noted that the publication of a Discussion Paper would allow the IASB to obtain feedback from stakeholders and to refine its preliminary views.

(e) **Disclosures - main principles**: noted that considering all the disclosure requirements in IFRS Standards in the light of paragraph BC157 of IFRS for SMEs was perhaps the most appropriate approach but acknowledged that such an approach would be time consuming. As the IASB was going to publish an ED with detailed proposals and an extended consultation period, EFRAG TEG members would have the chance to see whether the IASB's approach was going to work in practice;

(f) **Disclosures specific issues**: welcomed many of the IASB tentative decisions. Nonetheless, EFRAG TEG members:

(i) noted that this project raised the issue of lack of disclosure requirements for combined financial statements in IFRS Standards;

(ii) considered that entities that are in the scope of the project could provide more relevant information about goodwill impairments and calculation of the recoverable amount without necessarily increasing the costs for preparers;

(iii) asked if the carveout regarding IFRS 14 *Regulatory Deferral Accounts* was an envisaged procedure;

(iv) Some found that the IASB arguments for not proposing the reduced disclosure requirements for insurance contracts were not compelling and disagreed with the IASB tentative decision to require full disclosures in accordance with IFRS 17. Other EFRAG TEG members agreed with the IASB arguments but highlighted the importance of consulting the stakeholders to identify the size of the population to which this standard might apply and what simplifications to disclosure requirements could be useful.

(g) **Transition to the reduced-disclosure IFRS Standard**: highlighted the importance of having a reduced-disclosure IFRS Standard which is aligned with the implementation dates of full IFRS Standards, so that subsidiary and its parent could present the same information.

Background on the EFRAG Board discussions

10 On 7 July 2021, EFRAG Board received an update on this project and provided the following key messages:

(a) raised questions about the effects of an endorsement of the future reduced-disclosure IFRS Standard in Europe as member states currently use different options in respect of permitting or requiring IFRS in the annual accounts of listed entities and for non-publicly traded entities;

(b) observed that some European jurisdictions may be interested in this project, in particular if the scope had to be broadened to include also all the entities without public accountability, irrespective of the fact that their parent company prepares an IFRS consolidated financial statements;

(c) raised questions on the definition of ‘public accountability’. For example, the interaction of the IASB’s concept ‘public accountability’ with other existing European concepts such as ‘public interest entity’ and ‘entities obliged to file annual accounts’;

(d) one EFRAG Board member questioned why insurance companies were out of the scope of this project and considered that European insurers could also benefit from this project;

(e) a few EFRAG Board members noted that since IFRS for SMEs is not allowed in Europe, there may be demands from stakeholders to widen the scope of this project to include all SMEs (including those that do not have a parent that presents financial statements under IFRS);

(f) one EFRAG Board member referred to the IASB’s project *Disclosure Requirements in IFRS Standards—A Pilot Approach*, which proposes a new approach to developing disclosure requirements in IFRS Standards. This member questioned whether the IASB’s project on *Subsidiaries that are SMEs* should wait for and benefit from the results of the IASB’s project on *Disclosure Requirements in IFRS Standards—A Pilot Approach;* and

(g) considered that there was a need to research on what the incremental benefit would be for the European stakeholders, whether the reduced-disclosure IFRS Standard would be adopted by jurisdictions and applied by subsidiaries that are SMEs (considering that today they already prepare a full IFRS reporting package for their parent company).

EFRAG Secretariat project planning

11 The IASB is planning to issue an Exposure Draft on *Disclosure Initiative — Subsidiaries that are SMEs* in the third quarter of 2021 (late July 2021). At its February 2021 meeting, the IASB decided to have a 180-day comment period (late January 2022).

12 After the publication of the ED, the EFRAG Secretariat is planning to have an additional EFRAG TEG meeting early in September (7 Sept, after the joined session with EFRAG Board) to discuss the remaining key messages for EFRAG DCL and have the voting on EFRAG DCL on 16 September 2021.

13 Finally, in September the EFRAG Secretariat is also planning to consult the EFRAG CFSS on the key messages to be included in EFRAG's DCL.