Subsidiaries that are SMEs
Key messages for EFRAG DCL

Objective

1 The objective of this agenda paper is to discuss key messages for EFRAG DCL based on the IASB's tentative decisions up to date.

Background

2 The key messages below have been prepared based on the feedback received from EFRAG TEG (please see cover note) and based on the EFRAG Secretariat analysis of the IASB's tentative decisions (please see agenda paper 05-04) and the IASB's agenda papers on this topic.

3 More detailed comments will be included once the ED is published with the IASB's proposals for disclosures.

Topic	Key messages
Introduction	• Welcome the IASB's proposals as the outcome of this project is likely to reduce the costs for many subsidiaries in preparing general purpose financial statements under IFRS, while maintaining information needed by the users of those financial statements. • Highlight that most of the European countries currently permit or require the use of IFRS in the annual accounts. Therefore, the population of European entities that may benefit from this project is significant (include an Appendix 2 – table with use of options in EU – please see agenda paper 05-05) • Highlight that there are already some jurisdictions that currently use the *IFRS for SMEs* Standard as a point of reference for local accounting requirements, including disclosures.
Objective of the project	• Agree with the objective of the project of specifying disclosure requirements for the financial statements of subsidiaries that do not have public accountability ('subsidiaries that are SMEs'). • The IASB's project has the benefit of allowing subsidiaries that are SMEs to use the recognition and measurement requirements in IFRS Standards, but with reduced disclosure requirements. • Highlight that the structure of the future reduced-disclosure IFRS Standard is fundamental to properly support the objective of the

	project. That is, the importance of having a stand-alone, well-structured and simplified set of disclosure requirements that are easy to apply by subsidiaries that are SMEs. • Question to constituents on the incremental benefits of the IASB proposals for the European stakeholders
Scope of the project	• Agree with the scope of the project focusing on subsidiaries that do not have public accountability and whose parent publishes consolidated financial statements that comply with IFRS Standard. • The proposed scope is consistent with the feedback from stakeholders about the need for reduced disclosure requirements for Subsidiaries that SMEs. • At this stage, the IASB should first test its new approach with subsidiaries that do not have public accountability and subsequently, after the implementation and application of the proposed disclosure requirements, consider whether the scope can be widened. • Illustrate how the notion of 'Public Accountability' interacts with other European concepts such as 'Public Interest Entities'. Also include a question to constituents on the definition of public accountability versus similar European Concepts. • Not clear whether a subsidiary that is an SMEs (Entity A) that prepares consolidated financial statements (i.e., it is also a parent) can elect to use the reduced-disclosure IFRS Standard if one or more (but not all) of its subsidiaries (Entities B, C, D) have public accountability. The same question applies when considering the separate financial statements of Entity A. This would be a restriction on the use of the IASB's proposals for vertical organisation structures (please see Appendix 1 – Diagram A). • Not clear whether a subsidiary that is an SME (Entity A) can elect to use the reduced-disclosure IFRS Standard if its parent does not present consolidated financial statements because it meets the conditions in paragraph 4(a) of IFRS 10. If not included in the scope, this would represent a significant restriction on the use of the reduced-disclosure IFRS Standard for vertical organisation structures (please see Appendix 1 – Diagram B).
Electing to apply the proposed disclosure requirements	• Welcome that the proposed disclosure requirements would be optional and that subsidiaries that are SMEs can apply or revoke them at any time. • Welcome that the proposed to require a subsidiary to disclose that it has applied the reduced-disclosure IFRS Standard and require this disclosure to be located with the statement required by paragraph 16 of IAS 1.
Principles for adapting the disclosure requirements of	• Acknowledge that using *IFRS for SMEs* as the starting point for the reduced-disclosure IFRS Standard has the benefit of ensuring that the disclosure requirements are sufficient to meet the needs of users of subsidiaries that do not have public

the IFRS for SMEs Standard	accountability (when there are no measurement or recognition differences) and has the benefit of minimising the work that stakeholders and the IASB need to do (when there are measurement and recognition differences). • Consider that the key principles proposed by the IASB should encompass cost-benefit considerations, including reduction of costs for preparers, which is one of the main objectives of the project. For example, the principle of reduction of costs for preparers is implicitly used when the IASB tentatively decided that the 'disclosure objectives' included in IFRS Standards are less likely to pass the cost-benefit test than for companies(parents) traded in a public market. • Highlight the risks of not considering the existing disclosure requirements in IFRS Standards in the light of BC157 when there are no recognition and measurement differences between IFRS for SMEs and IFRS Standards <u>but</u> there are differences in timing between the two (i.e., the risk of increasing the number of exceptions and inconsistencies as only some, but not all, of those recent improvements to disclosure requirements in IFRS Standards are included in the ED). EFRAG notes that more than 15 amendments to IFRS Standards have been issued since 1 January 2016 (IFRS for SMEs was last updated in 2015). • In terms of cut-off date, the IASB should proceed with caution in regard to including in its consultation document the exposure drafts published by the IASB as at 1 January 2021 (e.g. IASB's Exposure Draft ED/2020/4 *Lease Liability in a Sale and Leaseback*). This may generate a double consultation on the same topic, not reflect the IASB's latest tentative decisions on a project and may reflect tentative decisions that might be reversed in the future
Exceptions to the principles for adapting the disclosures	• Acknowledges the challenges of this project and that specific exceptions may be needed to improve the relevance of the information provided or reduce costs for preparers. • Highlight the importance of clearly identifying to which principle the exception relates to and providing clear reasoning for the exceptions. • The list of exceptions to the process for adapting disclosure requirements for a possible reduced-disclosure IFRS Standard seems to be incomplete (please see agenda paper 05-05 - IASB Tentative Decisions). For example, the IASB's approach for IAS 8 and IFRS 17 seem to be an exception to the principle of tailoring the IFRS for SMEs when there are measurement and recognition differences and have not been included in the list as an exception. • **Disclosure objectives**: The IASB should consider the interaction between its project to have objective-based disclosure requirement (with no list of minimum requirements) and a list of simplified disclosures for Subsidiaries that are SMEs
Disclosure requirements when	• Agree with the IASB's approach that when applying IFRS Standards for the first time and simultaneously electing to apply the reduced-disclosure IFRS Standard, a subsidiary would apply

transitioning from other GAAP to IFRS Standards and electing to apply the reduced-disclosure IFRS Standard **(Interaction with IFRS 1)**	the disclosure requirements proposed in the forthcoming ED, which would be based on Section 35 of IFRS for SMEs but adapted in accordance with the IASB's adaptation principles. • Agree that there is no need to amend IFRS 1 for when a subsidiary applies IFRS Standards for the first time and elects to apply the reduced-disclosure IFRS Standard.
Disclosure requirements when electing to apply the reduced-disclosure IFRS Standard and the previous financial statements were prepared applying IFRS Standards	• Agree that transition provisions are not needed when an entity elects to apply the reduced-disclosure IFRS Standard and the previous financial statements were prepared applying full IFRS Standards. • Agree that in the first financial statements in which a subsidiary ceases to apply the reduced-disclosure IFRS Standard and applies IFRS Standards with full disclosures, a subsidiary should be required to provide comparatives for the disclosures not included in the previous years' financial statements.
Disclosure requirements for transition provisions of new and amended IFRS Standards	• Welcome the IASB tentative decision on disclosure requirements for transition provisions of new and amended IFRS Standards to be applied by subsidiaries that are SMEs that elect to apply the reduced-disclosure IFRS Standard. • As these disclosures would not be inside the reduced-disclosure IFRS Standard itself (but still required if not listed in appendix A), recommend cross references in the main body of the reduced-disclosure IFRS Standard to the transition provisions in other IFRS Standards, particularly when a new IFRS Standard is issued.
Disclosure requirements (organised by IFRS Standard)	*[**Important message**: the topics below have been raised based on the IASB's tentative decisions and EFRAG TEG discussions. More detailed comments will be included once the ED is published with the IASB's proposals for disclosures]* • **IAS 36:** the following information could be required when calculating unit's (group of units') recoverable amount: o the period over which management has projected cash flows; o the growth rate used to extrapolate cash flow projections; and o the discount rate(s) applied to the cash flow projections. • **IAS 36:** detailed information about impairments and reversal of impairments, even when using a reduce-disclosure IFRS Standard. For example, provide information at segment level when IFRS 8 is applied, the events and circumstances that led to the recognition or reversal of the impairment loss, etc.); • **IFRS 10**: by not including the disclosure requirements on combined financial statements from IFRS for SMEs, this project

	raises the issue of lack of disclosure requirements for combined financial statements in IFRS Standards; • **IFRS 14**: Carveout considerations regarding IFRS 14 *Regulatory Deferral Accounts.* • **IFRS 14:** highlights that the Rate Regulated Activities (RRA) project is already at the stage of Exposure Draft (issued in January 2021) and that the disclosure requirements in the ED are much more detailed than in IFRS 14 and would most probably need to be simplified to reflect the needs of subsidiaries that are SMEs. Recommend that the developments of the RRA project are closely monitored by the IASB staff. Should the final RRA standard be issued before the reduced-disclosure IFRS Standard, the provisions of this new RRA Standard and not IFRS 14 should be analysed and included in the reduced-disclosure IFRS Standard
Omitted topics from IFRS for SMEs	*[**Important message**: the topics below have been raised based on the IASB's tentative decisions and EFRAG TEG discussions. More detailed comments will be included once the ED is published with the IASB's proposals for disclosures]* • **IFRS 17**: The arguments for not proposing the reduced disclosure requirements for insurance contracts are not compelling and highlight 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. • **IFRS 17**: Question to constituents on which entities that issue insurance contracts are expected to be included in the scope of the project. • **IFRS 6** - Exploration and evaluation assets are quite significant in value and if a company is in this field of activities, it would most probably be the only activity it is engaged in. This raises the question of whether full disclosures on IFRS 6 should be required (i.e. require paragraphs 23 to 25 of IFRS 6 rather than simply require paragraph 25 of IFRS 6 as in agenda paper xx-xx).
Disclosure Requirements in other IFRS Standards not applicable (Appendix A)	• Express concerns that when an entity elects to apply the IASB proposals on reduced-disclosure requirements, it would have to: (a) apply the proposed disclosure requirements included in the main body of the ED; and (b) apply the disclosure requirements of other IFRS Standards which are not listed in appendix A (i.e. they would remain applicable). • Such an approach means that subsidiaries that are SMEs would have to apply not only the proposed disclosure requirements in the main body of the ED but would have also to scan all the disclosure requirements of other IFRS Standards which are not listed in appendix A to ensure completeness. • The use of Appendix A for compliance purposes seems to be complex and confusing for subsidiaries that are SMEs.

	• Highlight the importance of having an independent and stand-alone reduced-disclosure IFRS Standard that focuses on the disclosure needs of subsidiaries that are SMEs. That is, a reduced-disclosure IFRS Standard that clearly identifies all the disclosure requirements that subsidiaries that are SMEs need to comply to that it is simple for them to apply. • Would prefer that the IASB refers to all the required disclosures in the main body of the ED, including cross references to the disclosures in other IFRS Standards when necessary. Such an approach would ease compliance and Appendix A could be retained for information purposes only.

Questions for EFRAG TEG

4 Does EFRAG TEG agree with key messages identified above for:

(a) **the introduction?**

(b) **the objective of the project?**

(c) **the scope of the project: Considering the comments received from the EFRAG Board, do EFRAG TEG members still support the scope of the project as proposed by the IASB?**

(d) **the scope of the project: Do EFRAG TEG members want to include a question to constituents on the scope of the project (i.e. whether the voluntary adoption of this standard should be made available to a broader range of entities, such as entities without public accountability in general also if they do not have a parent company that issues IFRS financial statements)?**

(e) **electing to apply the proposed disclosure requirements?**

(f) **the principles for adapting the disclosure requirements of the IFRS for SMEs Standard?**

(g) **the exceptions to the principles for adapting the disclosures?**

(h) **the disclosure requirements when transitioning from other GAAP to IFRS Standards and electing to apply the reduced-disclosure IFRS Standard (Interaction with IFRS 1)?**

(i) **the disclosure requirements when electing to apply the reduced-disclosure IFRS Standard and the previous financial statements were prepared applying IFRS Standards?**

(j) **the disclosure requirements for transition provisions of new and amended IFRS Standards?**

(k) **the disclosure requirements (organised by IFRS Standard)?**

(l) **the omitted topics from IFRS for SMEs?**

(m) **the disclosure Requirements in other IFRS Standards not applicable (Appendix A)?**

Appendix 1 – Scope of the project

Diagram A – Subsidiary A holds a subsidiary (Insurance B) that has public accountability.

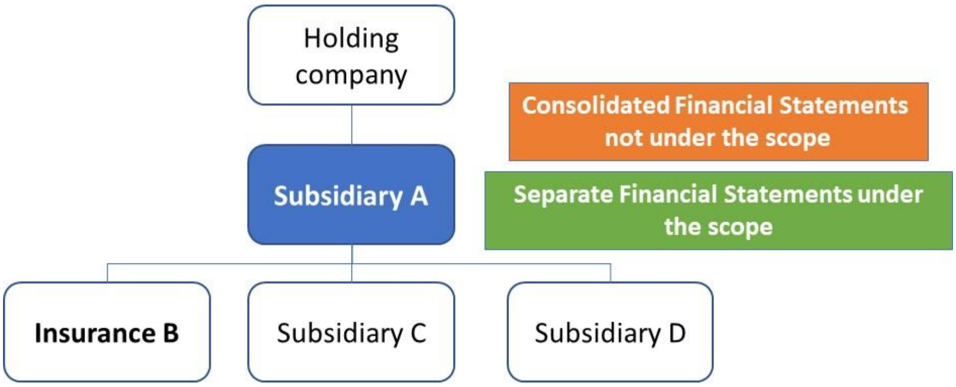

Diagram B – Subsidiary A only presents separate financial statements (exemption from consolidation in accordance with paragraph 4 of IFRS 10.