KPMG

IFRS for SMEs Update

Andrew F. Brathwaite
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Outline

- Alignment with full IFRS
- Overview of amendments to IFRS for SMEs
- Scope of IFRS for SMEs
- Revaluation of property, plant and equipment
- Investment in subsidiaries and associates
- Financial instruments
- Income taxes

Standards not yet incorporated into the IFRS for SMEs

- IFRS 13 *Fair Value Measurement*
- IAS 19 (2011) *Employee Benefits*
- IFRS 15 *Revenue from Contracts with Customers* (Jan 1, 2017)
- IFRS 9 *Financial Instruments* (Jan 1, 2018)
- IFRS 16 *Leases* (Jan 1, 2019)

Alignment with full IFRS

- Until the IFRS for SMEs is amended, any changes made in full IFRS do not apply to IFRS for SMEs
- However SME may choose to apply changes in IFRS if they do not conflict with requirements in the hierarchy in paragraphs 10.4 to 10.5

Amendments to IFRS for SMEs

- Limited amendments published May 2015, effective for annual periods beginning on or after January 1, 2017
- Earlier application is permitted, provided that all amendments are applied at the same time
- Table of amendments included in Standard
- Increase in # of pages from 231 to 244

Future reviews of the IFRS for SMEs

- IASB expects to publish omnibus exposure draft periodically, but not more frequently than once every three years
- Expects to consider new and amended IFRSs as well as specific issues raised
- On occasion, may identify an urgent matter for which amendment of the IFRS for SMEs may be considered outside the periodic review process

Practice Aids

- Illustrative financial statements (updated)
- Disclosure checklist (updated)
- Basis for conclusions
- Comprehensive training material
- IFRS for SMEs Update newsletter
- Guide for micros using the IFRS for SMEs
- Text of standard and all other materials free at ifrs.org

Major Amendments

- Revaluation of property, plant and equipment
- Equity method in separate financials
- Undue cost or effort exemption
- Alignment of *Section 29 Income Tax* with *IAS 12 Income Taxes*

Transition

- Guidance on implementation of amendments in Appendix A
- Guidance on first-time adoption in Section 35
- Apply retrospectively unless <u>impracticable</u> to do so (and disclose which amounts were not restated)
- May elect to apply revised Section 29 Income Tax prospectively
- Must apply revaluation of PP&E prospectively

Impracticable

“applying a requirement is impracticable when the entity cannot apply it after making every reasonable effort to do so”.

Disclosure of impact of amendments to IFRS for SMEs

Disclose

(a) the nature of the change in accounting policy;

(b) for the current period and each prior period presented, to the extent practicable, the amount of the adjustment for each financial statement line item affected;

(c) the amount of the adjustment relating to periods before those presented, to the extent practicable; and

(d) an explanation if it is impracticable to determine the amounts to be disclosed in (b) or (c).

Scope of Standard

- Standard intended for use by SMEs
- SMEs are entities that:

(a) do not have public accountability, and

(b) publish general purpose financial statements for external users

Scope of Standard

An entity has public accountability if:

- Its debt or equity instruments are traded in a public market..., or
- It holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses.

Most banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks would meet this second criterion.

Question

Which of these entities is permitted to use the IFRS for SMEs?

- The country’s major hospital which is owned by government
- A public school
- A credit union with 50 members who must be employees of a specific company
- A pension plan with 20 members

Question

An entity, whose only business is operating a travel agency, prepares its financial statements in compliance with the IFRS for SMEs. The entity requires its clients to pay a deposit equal to 60 per cent of the price of package holidays when booking. The balance (40 per cent) is paid 30 days before departure. The deposit is refunded in full provided that the client cancels the booking more than 60 days before the departure date. No refunds are provided for cancellations after 60 days before departure.

PP&E – revaluation model

- Entity may choose either cost model <u>or revaluation</u> model as its accounting policy, and must apply policy to entire class
- Must apply cost model to investment property whose fair value can not measured reliably without undue cost or effort
- Change from cost model to revaluation model for a class of PP&E is accounted for <u>prospectively</u>

PP&E – revaluation model

	After revaluation:
Cost 500,000 A/D (100,000) NBV 400,000	Cost 450,000 A/D 0 NBV 450,000
Revalued at 450,000	OR??
Revaluation surplus 50,000	Cost 500,000 A/D (50,000) NBV 450,000

PP&E – revaluation model

- Fair value at date of revaluation less subsequent depreciation and impairment
- Revaluations must be made with sufficient regularity to ensure that carrying amount does not differ materially from fair value
- Must revalue entire class of property, plant and equipment
- Any increase in value recognized in OCI
- Net decrease in value through P&L

PP&E – revaluation model

DISCLOSURES

(a) the effective date of the revaluation;

(b) whether an independent valuer was involved;

(c) the methods and significant assumptions applied in estimating the items' fair values;

(d) for each revalued class of property, plant and equipment, the carrying amount that would have been recognised had the assets been carried under the cost model; and

(e) the revaluation surplus, indicating the change for the period and any

restrictions on the distribution of the balance to shareholders.

Refresher - Government Grants

On December 31, 2015, an entity received a government grant of $500,000 as an incentive to establish a manufacturing plant in a particular location. All conditions to earn the grant have been met and the plant has been built at a cost of $10,000,000. The entity prepares its financial statements using the IFRS for SMEs.

How should the grant be recorded in the December 2015 financial statements?

Refresher - Comparatives

True or False:

Under the IFRS for SMEs, an entity is required to show comparative information for the movement on the following:

- property, plant and equipment
- investment property
- intangible assets
- provisions
- number of shares outstanding

Investment Property

- Land/building held to earn rentals or for capital appreciation or both
- Must carry at fair value, if fair value can be measured reliably without undue cost or effort; changes in fair value recognized in profit or loss
- Otherwise carry at cost less depreciation and impairment
- On balance sheet show investment property carried at FV separately from investment property carried at cost

Investment Property

- historical cost of property $1,000,000
- property generates annual rental income of $300,000 and has annual expenses of $350,000.
- quotes received for professional appraisals of property at next balance sheet date, ranging from $3,000 to $15,000.
- financial statements expected to be used only by company's two shareholders, one of whom manages the company and the other who has no involvement.
- financial statement info used to file annual corporation tax return

How should the investment property be carried in the company's financial statements at the next balance sheet date?

Undue Cost or Effort Exemption

- Assessment of undue cost or effort depends on the entity's specific circumstances and on management's judgment of the costs and benefits from applying the requirement
- Consider whether incremental cost or additional effort substantially exceed benefits to expected users of financial statements
- Applicable only to specific requirements, not generally
- Must disclose fact that exemption has been used and reasons why applying the requirement would involve undue cost or effort
- Not intended to be a low hurdle

Undue Cost or Effort Exemption

Existing exemptions:

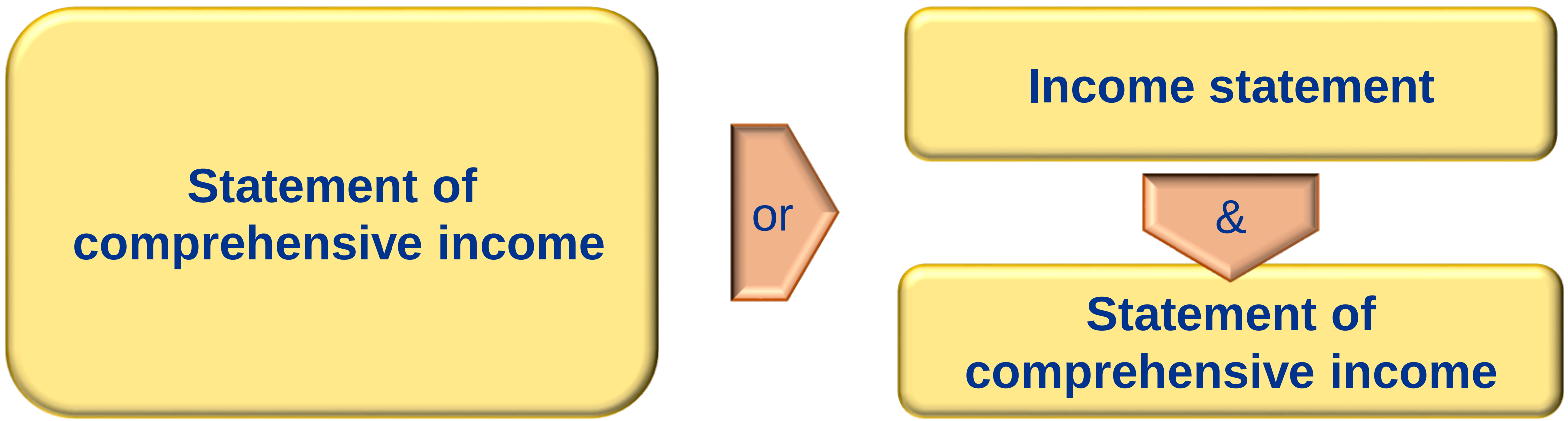
- Measurement of investment property at fair value
- Disclosing estimate of financial effect of contingent assets
- Use of projected unit credit method to measure defined benefit obligation
- Measuring biological assets under fair value model

Undue Cost or Effort Exemption

New exemptions:

- Measurement of investments in equity instruments at fair value
- Recognition of intangible assets separately in a business combination
- Requirement to measure liability to pay a non-cash distribution at the fair value of the non-cash assets to be distributed
- Requirement to offset income tax assets and liabilities

Statement of comprehensive income



Sources of other comprehensive income

Some gains and losses on translating the financial statements of a foreign operation

Some actuarial gains and losses

Some changes in fair value of hedging instruments (*)

Revaluation of property, plant and equipment

Titles of Statements

Are these titles mandatory under the IFRS for SMEs?

- Statement of Financial Position
- Statement Comprehensive Income or separate Income Statement and Statement of Other Comprehensive Income
- Statement of Changes in Equity
- Statement of Cash Flows

ICAC Sales and Services Inc.
Statement of Income and Retained Earnings
For the year ended December 31, 2015

	2015 $	2014 $
Revenue	6,863,545	5,808,653
Cost of sales	(5,178,530)	(4,422,575)
Gross profit	1,685,015	1,386,078
Other income	88,850	25,000
Distribution costs	(175,550)	(156,800)
Administrative expenses	(810,230)	(660,389)
Other expenses	(106,763)	(100,030)
Finance costs	(26,366)	(36,712)
Profit before tax	654,956	457,147
Income tax expense	(270,250)	(189,559)
Profit for the year	384,706	267,588
Retained earnings at start of year	2,171,353	2,003,765
Dividends	(150,000)	(100,000)
Retained earnings at end of year	2,406,059	2,171,353

Exemption from presenting consolidated financial statements

Both of these conditions must be met

The parent is itself a subsidiary

Ultimate or any intermediate parent of the parent produces consolidated financial statements that comply with IFRS or IFRS for SMEs

Exclude from consolidation a subsidiary acquired with the intention of disposing within one year

Investments in associates in consolidated financials

Cost

- Measure at cost less impairment except for those where there is a published price quotation, in which case measure at fair value

Equity

- Measure initially at transaction price and adjust subsequently to reflect share of profit or loss and OCI of investee, and for impairment

Fair value

- Measure at fair value at each balance sheet date, with changes in fair value through profit and loss
- Measure at cost where fair value cannot be measured reliably without undue cost or effort

Investments in subsidiaries and associates in separate financials

Cost	• Measure at cost less impairment
Equity	• Measure using equity method
Fair value	• Measure at fair value with changes in fair value through profit and loss

Financial Instruments

Cost/ Amortized cost	• Accounts/notes receivable/payable, and loans from banks or other third parties. • accounts payable in a foreign currency • loans to/from subsidiaries /associates due on demand. • Bonds and similar debt instruments • Shares not captured under fair value
Fair value through P&L	• Shares which are publicly traded or fair value can be measured reliably without undue cost or effort • Asset-backed securities • Derivatives

NO AVAILABLE-FOR-SALE CATEGORY

Fair value of financial instruments

Fair value

- quoted price for identical (or similar) asset in an active market
- price in a binding sale agreement, or recent transaction for identical (or similar) asset in an arm’s length transaction between knowledgeable willing parties
- valuation technique

Financial Instruments

<u>Fallback to IAS 39</u>

Entity shall choose to apply either:

(a) The requirements of Sections 11 and 12 in full

(b) The recognition and measurement requirements of *IAS 39 Financial Instruments: Recognition and Measurement* and the disclosure requirements of sections 11 and 12

Intangible assets including goodwill

Modification to require that if an entity is unable to make a reliable estimate of the useful life of goodwill or an intangible asset, the useful life should not exceed 10 years (rather than presumed to be 10 years), based on management's best estimate

Accounting for income taxes

- Main principles of Section 29 Income Tax aligned with IAS 12 Income Taxes for recognition and measurement of deferred tax
- Still some disclosure simplifications
- Minimal impact expected in practice

Accounting for income taxes

Deferred tax – common examples

- Fixed assets (excluding land)
- Defined benefit pension liability
- Allowance for bad debt?
- Inventory provision?
- Depreciable intangible asset?
- Deferred tax asset re tax losses

Accounting for income taxes

Presentation

- Deferred tax not to be classified as current
- Offsetting current tax assets and liabilities, or deferred tax assets and liabilities

Accounting for income taxes

Disclosure

- Disclose an explanation of any significant differences between the tax expense (income) and accounting profit multiplied by the applicable tax rate.
- Amount and expiry date of unused tax losses for which deferred asset not recognized
- For each type of temporary difference, analysis of change in deferred tax during the period

Accounting for income taxes

Disclosure

Deferred tax liabilities	Machinery and equipment	Pension Plan Liability	Bad debt allowance	Total
Deferred tax at January 1, 2015	150,124	(46,367)	(12,189)	91,568
Charge for year	12,633	8,013	(2,666)	17,980
Deferred tax at December 31, 2015	162,757	(38,354)	(14,855)	109,548

Q&A's

Contact Us

Andrew Brathwaite
Audit Partner
T: 246 434 3903
C:246 230 8188
E: andrewbrathwaite@kpmg.bb

kpmg.com/socialmedia

kpmg.com/app