



IFRS/PFRS for SMEs: Basic Framework

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Agenda



Background and overview

Scope and definition

Effective date and maintenance

Topics by section

**Considerations prior to adopting
the IFRS for SMEs**

Background and overview



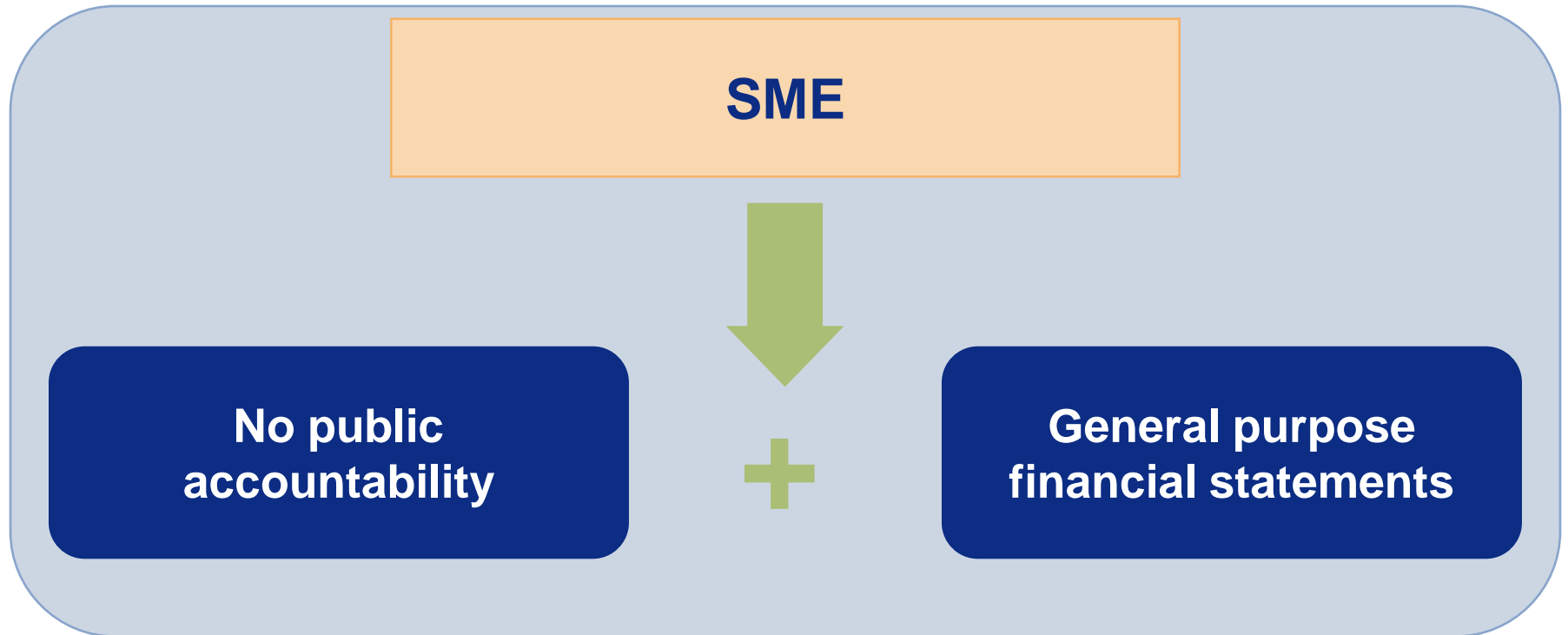
- Simplified and slimmed-down version of full IFRSs
- Separate stand-alone document
- Organized by topic – 35 sections
- The approach in developing the IFRS for SMEs included:
 - Providing significantly less guidance than full IFRSs
 - Simplifying the recognition and measurement requirements
 - Excluding topics not considered relevant for SMEs
 - Excluding some of the more complex options in full IFRSs

Simplified version of Full IFRS



- Some topics in IFRSs omitted if irrelevant to SMEs
- Where IFRS have options, only the simpler option is included
- Recognition and measurement requirements were simplified
- Reduced disclosures
- Simplified drafting

Scope and definition



Individual jurisdictions decide who is permitted or required to use the IFRS for SMEs

Scope and definition



Public accountability



Debt or equity traded in public market (or in process of issuing)

or

Holds assets in fiduciary capacity as primary business(es)

An entity with public accountability cannot claim compliance with the IFRS for SMEs (even if jurisdiction permits its use)

SEC Notice/Guidelines



Covered corporations (as SMEs):

- Have total assets of between P3 million and P350 million or total liabilities of between P3 million and P250 million;
- Are not required to file financial statements under SRC Rule 68.1;
- Are not in the process of filing their financial statements for the purpose of issuing any class of instruments in a public market;
- Are not holders of secondary licenses issued by a regulatory agency, such as banks, investment houses, finance companies, insurance companies, securities broker/dealers, mutual funds and pre-need companies; and
- Are not public utilities

SEC Notice/Guidelines



Transitioning from one reporting framework to another

- Transition from full PFRS to PFRS for SMEs
- Transition of NPAEs from PAS 101 to PFRS for SMEs
- Transition of NPAEs from PAS 101 to full PFRS

Financial Reporting Framework of Entities (micro-business entities*) not covered by either the full PFRS or PFRS for SMEs

- full PFRS
- PFRS for SMEs
- another acceptable basis of accounting

**Micro-business entities are entities whose total assets or total liabilities are below the P3 million floor threshold for the size criteria.*

SEC Notice/Guidelines



Date for applying the size criteria and for transitioning to full PFRS or to PFRS for SMEs

- The PFRS for SMEs shall be effective for annual periods beginning on or after January 1, 2010, except for the guidance in applying the requirements of Section 23 (Revenue) in recognizing revenue from agreements for the construction of real estate which shall apply to annual periods beginning on or after January 1, 2012.
- Amount of total assets and total liabilities shall be based on the entity's audited financial statements as of December 31, 2009 or immediately preceding fiscal year as appropriate.
- In case of breach of threshold by a SME, before transitioning to applicable framework, determine if event that caused the change is:
 - ✓ significant (as a general rule, 20% or more of total assets or total liabilities) and
 - ✓ continuing.

significant and continuing – based on management's judgement (quantitative & qualitative factors)

SEC Notice/Guidelines



Date for applying the size criteria if the PFRS for SMEs is adopted early

Subsidiaries of a parent company that use full PFRS

- If qualified as SMEs, may use the PFRS for SMEs (Section 1.6)

Required disclosures

- Explanation of the transition to PFRS for SMEs (Section 35.12)
- Reconciliations (Section 35.13 – 35.15)

Early adoption of PFRS for SMEs

SEC Notice/Guidelines



Resolution: Exemption from the mandatory adoption of PFRS for SMEs that meet any of the following criteria:

- ❖ It is a subsidiary of a parent company reporting under full PFRS.
- ❖ It is a subsidiary of a foreign parent company that will be moving towards IFRS pursuant to the foreign country's published convergence plan.
- ❖ It is a subsidiary of a foreign parent company that has been applying the standards for a non-publicly accountable entity for local reporting purposes, and is considering moving to full PFRS instead of the PFRS for SMEs in order to align its policies with the expected move to full IFRS by its foreign parent company pursuant to its country's published convergence plan.

SEC Notice/Guidelines



Resolution: Exemption from the mandatory adoption of PFRS for SMEs that meet any of the following criteria: (continued...)

- ❖ It has short term projections that show that it will breach the quantitative thresholds set in the criteria for an SME, and the breach is expected to be significant and continuing due to its long-term effect on the company's asset or liability size.
- ❖ It is part of a group, either as a significant joint venture or an associate, that is reporting under full PFRS.
- ❖ It is a branch or office of a foreign company reporting under full IFRS.
- ❖ It has concrete plans to conduct an initial public offering within the next two years.

SEC Notice/Guidelines



Resolution: Exemption from the mandatory adoption of PFRS for SMEs that meet any of the following criteria: (continued...)

- ❖ It has a subsidiary that is mandated to report under full PFRS.
- ❖ It has preparing financial statements using full PFRS and has decided to liquidate its assets.

Topics by section: Overview



- Not complete overview of requirements of IFRS for SMEs
- Highlights significant differences from full IFRSs
 - focuses on recognition and measurement
- Does not address areas in which there is guidance in full IFRSs but no corresponding guidance in the IFRS for SMEs
 - other differences may arise in these areas

Some key terms



- Impracticable
 - Cannot apply a requirement after making every reasonable attempt to do so
- Undue cost or effort
 - No guidance

Concepts and pervasive principles (Section 2)



- Objective of financial statements of SMEs:
 - To provide information about **financial position**, **performance** and **cash flows** useful for the economic decision-making of a broad range of users
- Qualitative characteristics of information in financial statements:
 - Understandability
 - Relevance
 - Reliability
 - Materiality
 - Substance over form
 - Prudence
 - Completeness
 - Comparability
 - Timeliness
 - Balance between benefit and cost

Financial statement presentation (Sections 3 to 8)



- Set of financial statements prepared in accordance with the IFRS for SMEs comprises:
 - Statement of financial position
 - Statement of comprehensive income (or a separate income statement and statement of comprehensive income)
 - Statement of changes in equity
 - Statement of cash flows (using direct or indirect method)
 - Notes
- Explicit and unreserved statement of compliance with the IFRS for SMEs must be made when, and only when, financial statements comply with all requirements of the IFRS for SMEs
- Allows a true and fair override when regulatory framework permits

Financial statement presentation (Sections 3 to 8)



- Combined statement of income and retained earnings:
 - Only profit or loss, dividends, error correction, change in accounting policy
- Third statement of financial position not required
- If expenses presented by function in statement of comprehensive income, then further disclosure by nature not required in notes

Consolidated financial statements (Section 9)



- A SME that is a parent prepares consolidated financial statements unless:
 - Entity is itself a subsidiary and its ultimate or intermediate parent’s financial statements comply with full IFRSs or IFRS for SMEs; or
 - Its only subsidiaries were acquired with intention of selling or disposing of them within one year
- Subsidiaries consolidated using same reporting date as parent, unless impracticable
- Uniform accounting policies

Separate financial statements (Section 9)



- Permitted but not required
- Accounting policy choice to account for each of investments in subsidiaries, associates and jointly controlled entities:
 - Cost less impairment; or
 - Fair value through profit or loss

Accounting policy hierarchy (Section 10)



- When no specific guidance is available in the IFRS for SMEs, consider in descending order:
 - Guidance in the IFRS for SMEs on similar and related issues
 - Definitions, recognition criteria and measurement concepts in Section 2 *Concepts and Pervasive Principles*
- May consider full IFRSs, but not required to do so
- No reference made to considering the pronouncements of other standard-setters



Financial instruments (Sections 11 and 12)



Accounting policy choice for all financial instruments to apply either:

- Financial instruments sections of IFRS for SMEs; or
- IAS 39 plus disclosure requirements of IFRS for SMEs

Financial instruments dealt with in two sections:

- Section 11 – basic financial instruments
- Section 12 – other financial instruments

Two classification categories:

- Amortized cost
- Fair value through profit or loss

Basic financial instruments (Section 11)



Examples normally within scope of Section 11:

- Cash
- Demand and fixed-term deposits
- Debt instruments such as accounts, notes and loans receivable and payable
- Bonds and similar debt instruments
- Investments in non-convertible preference shares
- Investments in non-puttable ordinary or preference shares
- Commitments to receive a loan that cannot be settled net in cash

Other financial instruments (Section 12)



Examples normally within the scope of Section 12:

- Options, rights, warrants, futures, forwards
- Interest rate swaps that can be settled net in cash or by exchanging another financial instrument
- Qualifying hedging instruments
- Asset-backed securities
- Commitments to make a loan
- Commitments to receive a loan that can be settled net in cash

Investments in associates and joint ventures (Sections 14 and 15)



- Accounting policy choice in consolidated financial statements for all associates and / or all jointly controlled entities:
 - Equity method
 - Cost model (but fair value if public price quotation available)
 - Fair value through profit or loss (but cost if undue cost or effort)
- Proportionate consolidation not permitted

Investment property (Section 16)



Measurement:

- Fair value through profit or loss, if fair value can be determined reliably without “undue cost or effort” on an ongoing basis
- Otherwise accounted for as PPE (see slide 22)

Mixed-use property

- Separated between investment property and PPE
- If fair value of investment property cannot be determined reliably without undue cost or effort, account for entire property as PPE

Investment property (Section 16)



Property held by a lessee under an operating lease

- May be classified as investment property if:
 - Otherwise would meet definition of investment property; and
 - Its fair value can be measured without undue cost or effort on an ongoing basis
- Classification alternative available on a property-by-property basis

Property, plant and equipment (Section 17)



Measurement after initial recognition

- Cost less accumulated depreciation and impairment losses
- Component accounting applies
- Revaluation model not permitted
- Review useful lives, residual values and depreciation methods only when indication they have changed

Intangible assets other than goodwill (Section 18)



Measurement after initial recognition

- Cost less accumulated amortization and impairment losses
- Revaluation model not permitted
- Amortized over useful life; if unable to reliably estimate, presumed to be 10 years
- Test for impairment only when indication in all cases
- Review useful lives, residual values and amortization methods only when indication they have changed

Useful lives

- All intangible assets are considered to have finite useful lives

Intangible assets other than goodwill (Section 18)



Research and development expenditure

- Expense as incurred
- Capitalization of development expenditure not permitted

Acquired as part of a business combination

- Not recognized separately from goodwill if its fair value cannot be measured reliably:
 - Not separable from goodwill
 - No history / evidence of exchange transactions, and estimates depend on immeasurable variables

Business combinations and goodwill (Section 19)



- Recognition and measurement requirements largely consistent with IFRS 3 (2004) rather than IFRS 3 (2008):
 - Definition of a business combination
 - Treatment of transaction costs, contingent consideration, contingent liabilities
 - Calculation of goodwill and non-controlling interest
- Scope consistent with IFRS 3 (2008):
 - Business combinations achieved by contract alone and business combinations between mutual entities not excluded from scope

Business combinations and goodwill (Section 19)



Goodwill

- Calculation of goodwill consistent with IFRS 3 (2004)
- Considered to have a finite useful life
- Subsequent measurement consistent with intangible assets, i.e., cost less accumulated amortization and impairment losses
- Amortized over useful life; if unable to reliably estimate, presumed to be 10 years
- Tested for impairment only when indication

Employee benefits (Section 28)



Defined benefit schemes

- Accounting policy choice for actuarial gains or losses:
 - Profit or loss; or
 - Other comprehensive income
- Calculation of obligation:
 - If necessary information can be obtained without undue cost or effort, use projected unit credit method consistent with IAS 19
 - If necessary information cannot be obtained without undue cost or effort, a simplified approach is applied

Employee benefits (Section 28)



- Actuarial valuations:
 - Not required annually
 - Roll-forward procedures
- Introduction, change, curtailment, settlement
 - Any gain or loss recognized in profit or loss in current period

Group plans

- Permitted to recognize charge based on reasonable allocation of group charge (if parent presents consolidated financial statements under full IFRSs or IFRS for SMEs)

Specialized industries (Section 34)



Extractive activities

- No specific guidance
- Apply relevant sections of IFRS for SMEs

Agriculture

- Measure biological assets at cost less accumulated depreciation and impairment losses if fair value is not reliably determinable without undue cost or effort

Service concessions

- Accounting treatment like that in full IFRSs
- Not clear whether same arrangements will be classified as service concession arrangements under full IFRSs and IFRS for SMEs

Transition to IFRS for SMEs (Section 35)



- Transitional provisions apply to all first-time adopters of the IFRS for SMEs (including an entity that previously used full IFRSs)
- An entity can be a first-time adopter of the IFRS for SMEs only once
- Mandatory exceptions:
 - Derecognition
 - Accounting estimates
 - *Discontinued operations*
 - Measuring NCI
- Voluntary exemptions:
 - Business combinations
 - Share-based payments
 - Fair value as deemed cost
 - Revaluation as deemed cost
 - Cumulative translation differences

Transition to IFRS for SMEs (Section 35)



- Voluntary exemptions (continued):
 - Deferred income tax
 - Service concession arrangements
 - *Extractive activities*
 - Compound financial instruments
 - Arrangements containing a lease
 - Decommissioning liabilities
 - Separate financial statements
- Apply transitional provisions to earliest period practicable

Other differences from full IFRSs



Borrowing costs (25)

- Expensed as incurred (capitalization prohibited)

Foreign currency translation (30)

- On disposal of a foreign operation cumulative exchange differences relating to that operation recognized in OCI are not reclassified to profit or loss

Operating leases (20)

- If payments are structured to increase in line with expected inflation, then timing of recognition of income and expenditure reflects this

Inventories (13)

- Permitted to use most recent purchase price if this approximates cost

Other differences from full IFRSs



Revenue: construction of real estate (23)

- If accounted for as a sale of goods, then revenue recognised only upon delivery of completed real estate to the buyer

Impairment of non-financial assets (27)

- Test for impairment only when indication

Other topics with differences from full IFRSs



- Equity (Section 22)
- Government grants (Section 24)
- Share-based payment (Section 26)
- Income Tax (Section 29)
- Related party disclosures (Section 33)

Topics in full IFRSs excluded from IFRS for SMEs



- Earnings per share
- Segment reporting
- Assets held for sale and discontinued operations
- Interim reporting
- Insurance

Topics with no significant differences from full IFRSs



- Provisions and contingencies (Section 21)
- Hyperinflation (Section 31)
- Events after the end of the reporting period (Section 32)

Considerations prior to adopting the IFRS for SMEs



- Local financial reporting requirements
- Users and comparability to other entities
- Business impacts
- Long-term goals
- Group reporting
- Cost

Implementation Support



Materials available at IASB website

<http://www.ifrs.org/IFRS+for+SMEs/IFRS+for+SMEs.htm>

- **Illustrative financial statements**
- **Presentation and disclosure checklist**
- **IFRS Foundation training material**
- **IFRS for SMEs Update newsletter**

SME Implementation Group

- **Q&As**



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