

# A Game-Changer for Small-Business Accounting

The International Accounting Standards Board recently issued its long-awaited "International Financial Reporting Standard for Small and Medium-sized Entities." The Standard is poised to be a "game-changer" for small-business accounting in the United States and around the world.

On July 9, 2009, the International Accounting Standards Board (IASB) published the first "International Financial Reporting Standard for Small and Medium-sized Entities" (IFRS for SMEs). The IASB refers to the IFRS for SMEs as *a* standard (i.e., singular), but it's really a complete set of financial reporting standards that is intentionally much shorter and simpler than full IFRS.

As its name implies, the IFRS for SMEs is designed around the financial reporting capabilities and needs of smaller companies and their stakeholders. In this month's column, I'll discuss key details of the IFRS for SMEs and explore the significant impact that it's likely to have on small-business accounting.

## Target Audience

The IFRS for SMEs has undergone several name changes since the IASB began working on it more than five years ago. Unfortunately,

the final name doesn't fully convey the intricacies of the Standard's entity scope. So who, exactly, is the intended audience?

The IFRS for SMEs is, like full IFRS, *a country-neutral* set of financial reporting standards. Therefore, the IFRS for SMEs is appropriate for smaller companies, regardless of which country or countries they operate in.

In countries that impose statutory financial reporting obligations on companies within the scope of the IFRS for SMEs, a company's use of the Standard in satisfying its statutory reporting obligations would have to be allowed or required by local legislative action. In contrast, in countries that don't impose such obligations on companies within the scope of the IFRS for SMEs (e.g., the U.S.), companies can decide for themselves whether and when they want to adopt the Standard.

In developing the IFRS for SMEs, the IASB focused on the kinds of transactions, events, and conditions typically encountered by entities having about 50 employees. But the Board ultimately decided to not base the Standard's entity scope on a size test. Rather, it specified that the IFRS for SMEs is for entities that

lack *public accountability*.

According to the IASB, "An entity has public accountability if: (a) its debt or equity instruments are traded in a public market or it is in the process of issuing such instruments for trading in a public market...or (b) it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses. This is typically the case for banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks." This definition of public accountability effectively excludes most small companies and therefore puts those companies within the scope of the IFRS for SMEs.

## What the Standard Is For

The IFRS for SMEs applies to the preparation of general purpose financial statements that are published for external users. SMEs often produce financial statements for use by owner-managers or for tax reporting or other statutory filing purposes, but financial statements produced solely for those purposes aren't necessarily general purpose financial statements. In contrast, general purpose financial statements are directed toward the common information needs of a

wide range of users. Such statements are intended to meet the needs of users who aren't in a position to demand reports tailored to meet their particular information needs. For a small business, those users may include

- ◆ Noncontrolling, nonmanagement investors;
- ◆ Bank and other lenders;
- ◆ Vendors;
- ◆ Credit-rating agencies; and
- ◆ Customers.

### How the IFRS for SMEs Differs from Full IFRS

The IFRS for SMEs differs from full IFRS in several ways. For example, it doesn't address topics that typically aren't relevant to SMEs. Topics that have been eliminated for this reason include earnings per share, interim reporting, and segment reporting.

The IFRS for SMEs also provides fewer accounting policy options than full IFRS. For example, the "fair value" models for the periodic measurement of property, plant, and equipment and intangible assets are absent from the IFRS for SMEs, as is the option to use proportionate consolidation for investments in jointly controlled entities. Interestingly, those deviations from full IFRS make the IFRS for SMEs more similar to U.S. Generally Accepted Accounting Principles (U.S. GAAP).

One of the most dramatic differences from a preparer's standpoint is that the number of potential disclosure items has been reduced from about 3,000 in full IFRS to about 400 in the IFRS for SMEs. On the basis of this and the foregoing differences, you might assume that the IFRS for SMEs is

Bruce Pounder will speak about the IFRS for SMEs and other IFRS-related topics at the NASBA National CPE Expo in San Antonio, Texas, September 21–23, 2009. For more information, visit [www.nationalcpeexpo.com](http://www.nationalcpeexpo.com).

a proper subset of full IFRS. This isn't true. The IFRS for SMEs isn't just a stripped-down version of "the real thing." In particular, several recognition and measurement provisions of the IFRS for SMEs are simpler than—and therefore different from—the corresponding provisions of full IFRS. As a result, some accounting treatments that are required in the IFRS for SMEs are prohibited in full IFRS and vice versa.

A notable example of such differing treatments involves accounting for goodwill. In the IFRS for SMEs, the IASB decided to sacrifice theoretical superiority for cost effectiveness in stipulating that goodwill and other indefinite-life intangible assets should be considered to have finite useful lives and be amortized over their estimated useful lives, with a maximum amortization period of 10 years. This treatment stands in marked contrast to the current treatment of goodwill under both full IFRS and U.S. GAAP.

Yet another key difference is that the sometimes-convoluted

language of full IFRS has been translated into "plain English," which will also facilitate the translation of the IFRS for SMEs into many languages, as the IASB plans to do.

### Impact of the IFRS for SMEs

By offering relief from the compliance costs and operational complexity associated with U.S. GAAP or full IFRS, the IFRS for SMEs could be a timely "economic stimulus" for millions of smaller companies worldwide. The IFRS for SMEs also exhibits several attractive characteristics supportive of better internal control over financial reporting, including high quality, simplicity, and country neutrality. Those characteristics would enable smaller companies to better manage their financial reporting risks. Given the prospect of lower costs, lower complexity, and lower risk, the IFRS for SMEs must be seen as a potential game-changer—on a global scale—for small-business accounting.

The IFRS for SMEs and accompanying implementation guidance documents are freely available in PDF format at <http://go.iasb.org/IFRSforSMEs> (registration is required). **SF**

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