Choosing between IFRS and IFRS for SMEs

By Wiehahn Olivier

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Over the last few years we have seen various changes being made with regards to the IFRS (International Financial Reporting Standards) accounting framework. These include new standards such as IFRS 15 (revenue), IFRS 9 (financial instruments) and IFRS 16 (leases), replacing the old IAS 18, IAS 32 and IAS 17,respectively. These changes may seem like a mere modification in abbreviations, that you can leave your accountant and auditor to worry about, but in actual fact, they have had a significant impact on all companies that elected to adopt IFRS as their accounting framework.

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The new revenue and financial instruments accounting standards under the IFRS accounting framework has become effective for all entities with a financial year starting on or after 1 January 2018, while the new leases standard is applicable to all entities with a financial year starting on or after 1 January 2019. Without going into too much detail regarding the disclosure and accounting requirements, the effect of the new standards have been found to be onerous and overly complex by most people who have dealt with these new accounting and disclosure requirements. Most companies in South Africa, aside from listed groups, struggle to see the benefit of these new standards and why they need to be adhered to.

The question is therefore raised as to why one would apply the IFRS accounting framework and what the alternatives would be. The South African Companies Act requires a company to compile its financial statements in accordance with an acceptable accounting framework, the options for which include either IFRS, IFRS for SMEs (International Financial Reporting Standards for Small and Medium-sized Entities) or a financial framework determined by the company (entity specific accounting policies). The most common of these are IFRS or IFRS for SMEs as very few companies apply entity specific accounting policies for various reasons.

Company's Act requirements

There is a general misunderstanding as to when a company needs to apply IFRS, and when it is able to apply IFRS for SMEs. The PIS (public interest score) of a company is calculated by taking a number of factors into consideration, such as the number of individuals with beneficial interests (i.e. shareholders), turnover for the financial year, third party liability at the end of the financial year and the average number of employees.

The general misunderstanding is that the application of the accounting framework is dependent on the company's PIS, which is not the case. In terms of the Company's Act a company only needs to apply IFRS if the company is a state-owned company as defined by the Act or if the company is a public company listed on an exchange such as the JSE or AltX for example, all other companies are able to apply IFRS for SMEs.

Before a change is made to the accounting framework of a company, other considerations should also be applied such as whether the MOI (memorandum of incorporation) requires a specific accounting framework and also whether there are any requirements from the shareholders in terms of the accounting framework that should be applied. The company might form part of a group of companies that apply IFRS and therefore it is required that all of the companies within the group apply the same accounting framework to make the consolidation or aggregation process more efficient and accurate.

There are various entities that are able to apply the simpler and less onerous financial reporting framework of IFRS for SMEs. Besides the fact that IFRS for SMEs is less complex and onerous, proper consideration should always be given prior to making a decision about changing the accounting framework. There are significant differences between the above mentioned frameworks, and each has pros and cons that need to be carefully assessed.

It is unlikely that smaller groups and owner managed business will see any value in the complexity and additional disclosure requirements that the new IFRS standards bring along. As such, the increase in audit, consultation, tax and compilation fees can be avoided by making the change to IFRS for SMEs. However, it is very important that an assessment is made by the shareholders and directors of the company, in consultation with its auditors, so that an informed decision can be made.

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