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IFRS 19 Subsidiaries without Public Accountability: Disclosures

DEA Appendix 1 - Background paper

Objective

1 The objective of this paper is to provide EFRAG FR TEG with the revised draft version of Appendix 1 of the DEA, for background purposes.

Appendix 1: Understanding the changes brought about by IFRS 19 *Subsidiaries without Public Accountability: Disclosures*

Background of IFRS 19

2 IFRS 19 was developed by the IASB in response to stakeholder feedback on the 2015 Agenda Consultation where stakeholders - mainly preparers - requested a cost saving simplification. They requested to permit subsidiaries with a parent that applies IFRS Standards in its consolidated financial statements to apply IFRS Standards with reduced disclosure requirements.

3 In particular, stakeholders reported the following reasoning:

(a) subsidiaries applying local GAAP or the *IFRS for SMEs* Accounting Standard have recognition and measurement differences between their own financial statements and the amounts reported to their parent for group consolidation purposes; and

(b) subsidiaries applying IFRS Accounting Standards found the disclosure requirements disproportionate to the information needs of the users of their financial statements.

4 All the above creates a disproportionate reporting burden on subsidiaries resulting in excess costs and without necessarily providing useful information for the users of their financial statements.

The issue and how it has been addressed

5 IFRS 19 addresses the stakeholders’ request by allowing eligible subsidiaries apply IFRS Accounting Standards with reduced disclosure requirements. All other requirements in IFRS Accounting Standards, such as recognition, measurement and presentation, remain unchanged. IFRS 19 does not include guidance on applying disclosure requirements. The guidance in other IFRS Accounting Standards remains applicable.

6 This approach aims to reduce the reporting burden on companies by simplifying reporting systems and processes, reducing the costs of preparing eligible subsidiaries' financial statements, while maintaining the usefulness of those financial statements for their users.

7 In particular, IFRS 19 will:

(c) enable subsidiaries to keep only one set of accounting records and group unified accounting policies, meeting the needs of both their parent company and the users of their financial statements; and

(d) reduce the disclosure requirements burden by permitting reduced disclosures better suited to the needs of the users of subsidiaries' financial statements.

Interaction with the Accounting Directive

8 The EU Accounting Directive 2013/34/EU applies to all entities operating within the EU and prescribes the minimum reporting requirements for different types of entities. The AD follows the 'think small first' approach allowing entities to prepare financial statements and notes to the financial statements that are proportionate to their size and their users' information needs.

9 Although IFRS 19 has a much narrower scope, it pursues ~~the same~~a similar objective as the proportionality principle of the Accounting Directive, which is to simplify the reporting requirements for ~~the~~ eligible entities. This objective is addressed in IFRS 19 in a principles-based way used in IFRS Accounting Standards.

~~8~~10 Therefore, IFRS 19 could be seen, to a certain extent, as 'competing' with national GAAPs and the Accounting Directive 2013/34/EU ('the AD') even if in a limited way (i.e., when considering the narrow scope proposed by the IASB and the number of EU Member States ('MS') that allow or require the use of EU-endorsed IFRS Accounting Standards for non-listed entities). ~~The AD is applicable for a large number of entities as it is applicable for all entities in Europe. IFRS 19 is applicable only for a small part of those entities.~~

~~9~~11 The AD and IFRS 19 have differences in the disclosure requirements coming from two main sources:

(a) different recognition and measurement requirements; and

~~(b)~~ disclosures required in the AD but not required in IFRS 19 or in any other IFRS Accounting Standards. The majority of these differences also exist between full IFRS Accounting Standards and the AD. ~~These include:~~

~~(i) the reporting entity and the group (its parent, subsidiaries, joint arrangements and associates), for example, where the file of the company is being kept and the number in that register, the place where copies of the consolidated financial statements of the ultimate and intermediate parent may be obtained and name and registered office of undertakings in which participating interest is held;~~

~~(i) the use of specific measurement options (e.g., fair value);~~

~~(ii) exceptional items;~~

~~(iii) amounts owed falling due after more than five years;~~

~~(iv) the average number of employees;~~

~~(v) emoluments granted in respect of the financial year to the members of administrative, managerial and supervisory bodies by reason of their responsibilities;~~

~~(vi) the entity's shares (shares subscribed for, including by class and warrants, if appropriate);~~

~~(vii) any undertaking of which it is a member with unlimited liability;~~

~~(viii) business combinations within a group;~~

~~(ix) payments made to auditors (only for large undertakings and public interest entities);~~

~~(x) required analysis of turnover by geographical markets and type of activity (only for large undertakings and public interest entities); and~~

~~(xi) any necessary disclosure if an exemption is used.~~

2 ~~The majority of the above disclosures are required by the 4th and 7th Council Directives1 when entities report financial information in accordance with IFRS in EU.~~

~~10~~12 Only a few differences were added with IFRS 19. Some disclosures about the composition of the group required by IFRS 12 *Disclosure of Interests in Other Entities* and IAS 27 *Separate Financial Statements* are in line with the AD, but are not required by IFRS 19.

~~11~~13 In addition to the minimum disclosure requirements set out in the AD, MS are provided with options to simplify or exempt disclosure requirements for specific types of entities.

~~12~~14 Several layers of simplifications and exemptions are provided by the AD to avoid disproportionate reporting burden for the smaller undertakings. In addition, options are available to MS to further reduce the reporting requirements, not only disclosures. Large undertakings and groups do not benefit from any simplifications and exemptions but have additional disclosure requirements defined in Article 18 of the AD.

~~[1] Comments concerning certain Articles of the Regulation (EC) No 1606/2002: INTERPRETATIVE COMMUNICATION CONCERNING CERTAIN ARTICLES OF THE~~

~~4th Council Directive https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:31978L0660~~

~~7th Council Directive: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:31983L0349~~

What has changed?

~~13~~15 IFRS 19 is a voluntary standard for eligible subsidiaries which works alongside other IFRS Accounting Standards.

~~14~~16 An eligible subsidiary that applies IFRS 19 does so by applying the requirements in other IFRS Accounting Standards except for the disclosure requirements and instead applies the reduced disclosure requirements in IFRS 19. IFRS 19 includes all disclosure requirements to be provided by eligible subsidiaries.

Scope of the standard

~~15~~17 A subsidiary is eligible if:

(a) it does not have public accountability; and

(b) it has an ultimate or intermediate parent that produces consolidated financial statements available for public use that comply with IFRS Accounting Standards.

~~16~~18 An intermediate parent that does not have public accountability and meets the other eligibility conditions may apply IFRS 19 in its separate financial statements even if it does not apply this standard in its consolidated financial statements.

~~17~~19 According to IFRS 19 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 (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets); or

(b) it holds assets in a fiduciary capacity for a broad group of outsiders as one of its primary businesses (for example, banks, credit unions, insurance companies, securities brokers/dealers, mutual funds and investment banks often meet this second criterion).

~~18~~20 Thus, the majority of financial institutions and insurance companies are excluded from the scope of IFRS 19.

~~19~~21 The "public accountability" definition used in IFRS 19 is the same as in *IFRS for SMEs* Accounting Standard. Subsidiaries without public accountability are in fact a subset of entities within the scope of the *IFRS for SME* Accounting Standard (which is not endorsed in Europe). Therefore, the definition was taken from this standard, but since the recognition and measurement requirements between *IFRS for SME* and IFRS 19 differ, it must be noted that these two standards are different.

Reduced disclosure requirements

~~20~~22 In developing the reduced disclosures in IFRS 19, the IASB was guided by the below set of principles, detailing the information needs of the users of eligible subsidiaries' financial statements:

(a) Liquidity and solvency - Information about the entity's ability to generate cash flows and continue as a going concern;

(b) Short-term cash flows, obligations, commitments and contingencies - Information about the entity's ability to meet its obligations;

(c) Measurement uncertainty - Information about how amounts in the financial statements are measured, including inputs (for example, significant judgements and estimates) used in those calculations;

(d) Disaggregation of amounts - Information about separation of amounts presented in the financial statements into component parts;

(e) Accounting policy choices - Information about the accounting policy applied by the entity especially when more than one accounting policy option is allowed.

~~21~~23 These principles were already used in developing the disclosure requirements for *IFRS for SMEs* Accounting Standard. They help identify what information is important to users of the financial statements of entities without public accountability.

~~22~~24 By applying these principles the IASB did not reduce the disclosure requirements for IAS 33 *Earnings per Share*, IFRS 8 *Operating Segments* and IFRS 17 *Insurance Contracts*. Subsidiaries eligible to apply IFRS 19 are not required to apply IAS 33 or IFRS 8, but may do so voluntarily and in this case the full disclosures are deemed to be relevant for the users of the financial statements. IFRS 17 represents a new model for accounting for insurance contracts and thus users need to be informed how entities apply this model.

~~23~~25 The disclosures in the following IFRS Accounting Standards were reduced the most: IFRS 12 *Disclosure of Interests in Other Entities* - 68%, IAS 16 *Property, Plant and Equipment* – 64%, IAS 12 *Income Taxes* – 53% and IFRS 15 *Revenue from Contracts with Customers* – 52%.

~~24~~26 The disclosure requirements in IFRS 19 are organised into subsections relating to each IFRS Accounting Standard and include both the IFRS 19 reduced disclosure requirements and the requirements from the relevant IFRS Accounting Standard that remain applicable. In addition, the IASB published an *IFRS 19 disclosure tracker*[2] which lists the disclosure requirements in IFRS 19 and maps them to their equivalents in other IFRS Accounting Standards.

~~25~~27 IFRS 19 follows the fair presentation principle described in paragraph 6 of the standard: to achieve fair presentation, a subsidiary applying IFRS 19 considers whether to provide additional disclosures if its compliance with the requirements in IFRS 19 would not be sufficient for users of its financial statements to understand the subsidiary's financial position, financial performance and cash flows.

When does IFRS 19 become effective?

~~26~~28 An entity may elect to apply IFRS 19 for reporting periods beginning on or after 1 January 2027. Earlier application is permitted. If an entity chooses to apply IFRS 19 earlier, it shall disclose that fact.

Disclosure requirements if an entity applies IFRS 19 before applying IFRS 18 Presentation and Disclosure in Financial Statements

~~27~~29 IFRS 19 contains the disclosure requirements for IFRS 18 issued in April 2024, which supersedes IAS 1 *Presentation of Financial Statements*. IFRS 18 applies to annual reporting

[2] https://www.ifrs.org/supporting-implementation/supporting-materials-by-ifrs-standards/ifrs-19/ifrs-19-disclosure-tracker/

periods beginning 1 January 2027 and earlier application is permitted. The disclosure requirements for IAS 1 are listed in Appendix B of IFRS 19.

~~28~~30 If an entity elects to apply IFRS 19 before the reporting period in which it first applies IFRS 18, it shall apply the disclosure requirements of IAS 1 listed in Appendix B.

Amendments to IAS 21 The Effect of Changes in Foreign Exchange Rates

~~29~~31 *Lack of Exchangeability*, issued in August 2023, amended IAS 21, adding new disclosure requirements. IFRS 19 already contains amended disclosure requirements for IAS 21. The amendments to IAS 21 apply to annual reporting periods beginning on or after 1 January 2025, and earlier application is permitted. If an entity applies IFRS 19 for an annual reporting period that begins before 1 January 2025 and has not applied the amendments to IAS 21, it need not apply paragraphs 221-224 of IFRS 19, containing new disclosure requirements.

How IFRS 19 will be maintained?

~~30~~32 As IFRS 19 includes the complete disclosure requirements for eligible subsidiaries it will be changed whenever a change in disclosure requirements takes place under IFRS. Any upcoming Exposure Draft will include a section for consequential IFRS 19 amendments.

~~31~~33 In developing IFRS 19, the IASB took into account disclosure requirements in IFRS Accounting Standards as at 28 February 2021.

~~32~~34 The disclosure requirements added to, or amended in, IFRS Accounting Standards between 28 February 2021 and May 2024 are covered in a 'catch-up' exposure draft, published by the IASB in July 2024. It develops the proposed amendments to IFRS 19 by applying the principles for reducing disclosure requirements, described above.

~~33~~35 In the 'Catch-up' ED the IASB is proposing amendments to IFRS 19 relating to:

(a) IFRS 18 Presentation and Disclosure in Financial Statements, including amendments introduced by Non-current Liabilities with Covenants;

(b) IAS 7 Statement of Cash Flows, as amended by Supplier Finance Arrangements;

(c) IAS 12 Income Taxes, as amended by International Tax Reform—Pillar Two Model Rules; and

(d) IAS 21 The Effects of Changes in Foreign Exchange Rates, as amended by Lack of Exchangeability.

~~34~~36 The disclosure requirements in IFRS 19 for regulatory assets and regulatory liabilities relate to IFRS 14 *Regulatory Deferral Accounts*. The disclosure requirements in IFRS 19 listed under subheading IFRS 14 *Regulatory Deferral Accounts* will continue to apply until IFRS 14 is superseded by the prospective *Regulatory Assets and Regulatory Liabilities* Standard.

~~35~~37 The IASB did not propose any amendments to the requirements in IFRS 19 following the issue in May 2024 of *Amendments to the Classification and Measurement of Financial Instruments*, which amended IFRS 7 *Financial Instruments: Disclosures* and IFRS 9 *Financial Instruments*.

~~36~~38 After May 2024, IFRS 19 will be amended as necessary, with the new or amended disclosure requirements in other IFRS Accounting Standards. When the IASB publishes an exposure draft of a new or amended IFRS Accounting Standard, it will also propose consequential amendments to IFRS 19.