# INSTITUTE OF CHARTERED ACCOUNTANTS OF BARBADOS

# GUIDANCE NOTE 01/2024

# COMPLIANCE WITH THE IFRS FOR SMEs FOR INSURANCE CONTRACTS AFTER THE EFFECTIVE DATE OF IFRS 17

**Approved by the Council on March 12, 2024**

## Introduction

The International Financial Reporting Standard for Small and Medium Sized Entities (IFRS for SMEs) is based on full IFRS with modifications to reflect the needs of users of SMEs' financial statements and cost-benefit considerations. SMEs often produce financial statements only for the use of owner-managers or only for the use of tax authorities or other governmental authorities. Financial statements produced solely for those purposes are not necessarily general-purpose financial statements. This is due to the very limited distribution and usage of those financial statements.

Also to be considered, is the guidance that until the *IFRS for SMEs* is amended, any changes that the IASB may make or propose with respect to full IFRS do not apply to the *IFRS for SMEs*. The *IFRS for SMEs* is a stand-alone document. SMEs shall not anticipate or apply changes made in full IFRS before those changes are incorporated into the *IFRS for SMEs* unless, in the absence of specific guidance in the *IFRS for SMEs*, an SME chooses to apply guidance in full IFRS and those principles do not conflict with requirements in the hierarchy in paragraphs 10.4–10.5.

The IFRS for SMEs does not provide specific guidance for the recognition, measurement and disclosures for insurance contracts and contracts that qualify as insurance contracts ("insurance contracts"). In current practice, entities reporting under the IFRS for SMES generally apply the guidance of IFRS 4 Insurance Contracts. IFRS 4 however was replaced by IFRS 17 for reporting periods beginning on or after January 1, 2023. The general model requirements of IFRS 17 however, are too onerous for SMEs qualifying for reporting under the IFRS for SMES, and not aligned to the needs of their users. It is anticipated that SMEs would incur substantial costs that would outweigh the benefits of reporting under those requirements.

This paper provides the Institute of Chartered Accountants of Barbados' ("ICAB" or the "Institute") guidance on compliance with the IFRS for SMEs, after the effective date of IFRS 17, for qualifying SMEs (see appendix A) that have insurance contracts and adopt accounting policies based on the requirements of IFRS 4.

## Authoritative Guidance

The requirements where the Standard does not provide specific guidance are details in paragraphs 10.4 – 10.5 of the IFRS for SMEs as follows:

10.4: "If this Standard does not specifically address a transaction, other event or condition, an entity's management shall use its judgement in developing and applying an accounting policy that results in information that is:

(a) **relevant** to the economic decision-making needs of users; and

(b) **reliable**, in that the financial statements:
(i) represent faithfully the **financial position**, financial **performance** and **cash flows** of the entity;
(ii) reflect the economic substance of transactions, other events and conditions, and not merely the legal form;
(iii) are neutral, i.e. free from bias;
(iv) are prudent; and
(v) are complete in all material respects.

10.5: In making the judgement described in paragraph 10.4, management shall refer to, and consider the applicability of, the following sources in descending order:
(a) the requirements and guidance in this Standard dealing with similar and related issues; and
(b) the definitions, **recognition** criteria and **measurement** concepts for **assets**, **liabilities**, **income** and **expenses** and the pervasive principles in Section 2 *Concepts and Pervasive Principles*.

In addressing the concept of "Undue cost", Section 2 states the following:

> Considering whether obtaining or determining the information necessary to comply with a requirement would involve undue cost or effort depends on the entity's specific circumstances and on management's judgement of the costs and benefits from applying that requirement. This judgement requires consideration of how the economic decisions of those that are expected to use the financial statements could be affected by not having that information.
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> Applying a requirement would involve undue cost or effort by an SME if the incremental cost (for example, valuers' fees) or additional effort (for example, endeavours by employees) substantially exceed the benefits that those that are expected to use the SME's financial statements would receive from having the information. An assessment of undue cost or effort by an SME in accordance with this Standard would usually constitute a lower hurdle than an assessment of undue cost or effort by a publicly accountable entity because SMEs are not accountable to public stakeholders.

**ICAB Evaluation**

Without detailing the specific requirements of IFRS 17, complying with the recognition, measurement and disclosure requirements of IFRS 17 for contracts that are required to apply the general model require information system and employee resource support that are considered to be largely beyond the capability of SMEs and are beyond the needs of the users of their financial statements. Therefore, the Institute does not consider that SMEs that currently have accounting policies that reflect the requirements of IFRS 4 will adopt accounting policies that reflect the requirements of IFRS 17.

SMEs therefore will have to apply the guidance of Section 10.4 – 10.5 to determine what will be their accounting policies post the effective date of IFRS 17. The requirement of the IFRS for SMEs as set out in Section 10 is that SMEs shall first refer to, and consider the applicability of the requirements and guidance in the Standard dealing with similar and related issues.

In this regard, there is one issue that can be considered similar to this situation, being the guidance on the recognition, measurement, and disclosures requirements for financial instruments – as detailed in Section 11. The Standard specifically indicates that SMEs can choose to adopt the recognition and measurement requirements of IAS 39 (of full IFRS) and the disclosure requirements of the IFRS for SMEs. When IAS 39 was replaced by IFRS 9, the IASB's guidance – in accordance with what is noted in the second paragraph of the introduction – stipulated that the requirements of IAS 39 (even though superseded in full IFRS) was to continue to be followed by SMEs who had chosen to adopt the recognition and measurement requirements of IAS 39.

ICAB's view is that this is a precedent for continued use of the requirements of a (simpler) superseded standard of full IFRS by SMEs reporting under the IFRS for SMEs. It is therefore not a novel concept in the context of the IFRS for SMEs even when considering that a distinguishing fact is that the IFRS for SMEs is silent on accounting and reporting for contracts that qualify as insurance contracts, while for financial instruments, the Standard provides specific guidance. ICAB's assessment is that the primary guidance of the Standard when it is silent on an issue, is in relation to the accounting policies adopted by the SME, as detailed further in the next paragraph. However, ICAB considers that support for this view that this is a precedent, in both cases the accounting policies adopted by the SME are based on the requirements of a standard of full IFRS that was/will be no longer in effect. The accounting policies regarding financial instruments were considered appropriate even though the standard in full IFRS, upon which they were developed, had been superseded. Similarly, therefore, accounting policies developed based on the requirements of IFRS 4, would continue to be appropriate with IFRS 17 replacing IFRS 4.

We believe this view aligns to the guidance of Section 10.4, as detailed above, which focuses on the characteristics of the accounting policies adopted by the SMEs in the situation where the IFRS for SMEs provides no guidance. The SME can choose to continue with its accounting policies regarding insurance contracts as they would continue to be **relevant** to the economic decision-making needs of users; and **reliable**. These characteristics would not change because the Standard in full IFRS upon which they were developed, is no longer in force.

ICAB also considers that an option for SMEs seeking to initially adopt reliable accounting policies relevant to the economic decision-making needs of users that are based on the requirements of a suitable, currently effective, standard, is the United Kingdom and Republic of Ireland's FRS 103: Insurance Contracts (January 2022).

**Conclusions**

ICAB's conclusion is that, unless, or until such time as, the IASB provides specific guidance on insurance contracts, SMEs preparing financial statements using accounting policies based on the requirements of IFRS 4, despite being superseded by IFRS 17, will be compliant with the IFRS for SMEs. SMEs can therefore make an explicit and unreserved statement of such compliance in the disclosure notes of their financial statements, as required by Section 3.3 of the IFRS for SMEs.

It is expected that there will be no change to the existing accounting policies of SMEs that continue to report under IFRS for SMEs. For SMEs initially adopting the IFRS for SMEs or the financial statements of newly incorporated SMEs reporting under the IFRS for SMEs, the recommended option is to adopt reliable accounting policies based on the requirements of FRS 103. However, SMEs are free to adopt accounting policies based on the requirements of (superseded) IFRS 4 of full IFRS.

ICAB also concludes that, as the SME's accounting policies do not, and should not, refer to any other standard (for example, IFRS 4 or FRS 103), specific disclosure that the accounting policies do not meet the requirements of IFRS 17 of full IFRS, is not required. Consequently, the opinion of external auditors of the SME's financial statements, are not expected to be modified, or contain an Emphasis of Matter paragraph, arising from the SME's non-inclusion of a statement that the accounting policies do not meet the requirements of IFRS 17 of full IFRS.

**Qualifying entities**

Section 1 of the IFRS for SMES defines SMEs as entities that:
(a) do not have **public accountability**; and
(b) publish **general purpose financial statements** for external users.

The Section stipulates that 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, 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

The Insurance Act Cap 310 identifies three classes of insurance entity licensees as follows:

Class 1: licensee which shall be an insurance company which underwrites related party business.

Class 2 licensee which shall include an insurance company which underwrites risks of third parties.

Class 3 licensee which shall include an insurance intermediary, an insurance management company and an insurance holding company.

Care should be taken if attempting to determine, solely based on the license class, whether a licensee would qualify to use the IFRS for SMEs.

Class 1 licensees
They would appear to qualify to use the Standard. However, this may not necessarily be as straight-forward. The Institute has provided guidance on the considerations to determine whether such an insurer can use the IFRS for SMEs. This would have to be determined on a case-by-case basis.

Class 2 licensees
They would appear to not qualify to use the Standard. However, this may also not necessarily be as straight-forward. The Institute is aware that several insurers that currently underwrite only related party business, have applied for, and obtained, Class 2 licenses, simply to afford them the opportunity to write third party business in the future if they so decide. These licensees, however, may currently qualify to use the Standard. This would have to be determined on a case-by-case basis.

Class 3 licensees
They would appear, and are currently viewed, as generally qualifying to use the Standard.

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