International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

XX January 2018

Dear Mr Hoogervorst,

Re: ED/2017/6 Definition of Material - Proposed amendments to IAS 1 and IAS 8

On behalf of the European Financial Reporting Advisory Group (EFRAG), I am writing to comment on Exposure Draft ED/2017/6 *Definition of Material - Proposed Amendments to IAS 1 and IAS 8*, issued by the IASB on 14 September 2017 (the 'ED').

This letter is intended to contribute to the IASB's due process and does not necessarily indicate the conclusions that would be reached by EFRAG in its capacity as advisor to the European Commission on endorsement of definitive IFRS Standards in the European Union and European Economic Area.

Our detailed comments and responses to the questions in the ED are set out in the Appendix.

To summarise, EFRAG agrees with the IASB's objective to remove the existing inconsistencies in the definition of "material" in the *Conceptual Framework for Financial Reporting* and in IFRS Standards. EFRAG also supports replacing the threshold 'could influence' with 'could reasonably be expected to influence' which, in EFRAG's view, helpfully emphasises that materiality decisions require judgement and clarifies the nature of the judgement to be made in assessing when information is material

However, EFRAG suggests removing the references to 'omitting', 'misstating' and 'obscuring' from the definition of 'material' and defining material information more simply and directly as information that can reasonably be expected to, individually or collectively, influence the economic decisions that the primary users of financial statements make.

EFRAG agrees that it is important that material information is not omitted, misstated or obscured but considers that these matters relate to principles of fair presentation or communication and should be addressed in the supporting guidance to the definition. EFRAG also highlights the importance of clarifying outside the definition, the concept of 'obscuring' and considering the potential impacts of discussions relating to other streams of the IASB's Better Communication initiative and, in particular, the discussion on the principles of effective communication contained in the Discussion Paper *Disclosure Initiative - Principles of Disclosure.*

EFRAG also observes that the definition of material in the forthcoming revised *Conceptual Framework for Financial Reporting* will still differ from the one in the amended IFRS Standards insofar as the former refers to information contained the general purpose 'financial report', rather than the financial statements. EFRAG considers that the IASB has not sufficiently debated the implications of some of proposed changes (in particular the change in the threshold and the introduction of the term 'obscuring') in the broader context of the information contained in financial reports.

Finally, EFRAG observes that the definition of material is currently repeated in several places (IAS 1 *Presentation of financial statement*, IAS 8 *Accounting policies, Changes in Accounting Estimates and Errors*, and the *Conceptual Framework for Financial Reporting*). The IASB could reconsider whether having the definition of material repeated in so many places is the most effective way of achieving consistent application.

If you would like to discuss our comments, please do not hesitate to contact Hocine Kebli, Raffaele Petruzzella or me.

Yours sincerely,

Jean-Paul Gauzès
President of the EFRAG Board

Appendix

Question 1 - Amendments to the definition of "Material"

Do you agree that the definition of material and the accompanying explanation should be clarified as proposed in this Exposure Draft? If you do not agree, what changes do you suggest and why?

Would any wording or terminology introduced in the proposed amendments be difficult to understand or to translate?

EFRAG's response

EFRAG agrees with the IASB's objective to remove existing inconsistencies in the definition of "material" between the *Conceptual Framework for Financial Reporting* and IFRS Standards.

EFRAG also supports replacing the threshold 'could influence' with 'could reasonably be expected to, influence as this helpfully emphasises that materiality decisions require judgement and clarifies the nature of the judgement to be made in assessing when information is material.

However, EFRAG suggests removing the references to 'omitting', 'misstating' and 'obscuring' from the definition of 'material' and defining material information more simply and directly as information that can reasonably be expected to, individually or collectively, influence the economic decisions that the primary users of financial statements make. EFRAG agrees that it is important that material information is not omitted, misstated or obscured but considers that these matters relate to principles of fair presentation or communication and should be addressed separately from the definition

Aligning the definition of materiality

1 EFRAG welcomes the IASB's initiative to remove inconsistencies in the definition of materiality in IAS 1/IAS 8 and in the *Conceptual Framework for Financial Reporting* as the existing differences in language are not meant to reflect different definitions of materiality and the existence of more than one definition of material can be confusing. EFRAG also supports using, as a starting point, the wording in the revised *Conceptual Framework for Financial* Reporting as it provides a direct definition of what 'material information' is whereas the current definition in IAS 1/ IAS 8 defines when an omission or misstatement is material.

Could reasonably be expected to influence

2 EFRAG supports replacing 'could influence' with 'could reasonably be expected to be influenced' to describe the threshold for deciding whether information is material as this helpfully emphasises that materiality decisions require judgement and clarifies the nature of the judgement to be made in assessing when information is material. EFRAG also observes that the reference to 'could reasonably be expected to influence' is already used in the guidance accompanying the definition of material in paragraph 7 of IAS 1.

3 Combined with the proposed clarification that the users to whom the definition refers are the 'primary users', the proposed changes have the potential to address concerns that the use of the expression 'could influence the decisions of users' is too broad and

requires too much information, because, in principle, almost anything 'could' influence the decisions of some users even if the possibility is remote.

Obscuring misstating and omitting information

4 EFRAG suggests removing the references to 'omitting', 'misstating' and 'obscuring' from the definition of 'material' and defining material information more simply and directly as information that can reasonably be expected to, individually or collectively, influence the economic decisions that the primary users of financial statements make.

5 EFRAG agrees that it is important that material information is not omitted, misstated or obscured but considers that these matters could be addressed separately from the definition as they relate more to principles of fair presentation or communication. Evidence of that is provided by the fact that the IASB is proposing to clarify the concept of 'obscuring' by stating that it refers to whether information is clearly communicated. EFRAG recommends that the concepts of omitting, misstated or obscuring information would be retained outside the definition, in the accompanying guidance, by stating that material information should not be omitted, misstated or obscured and by providing additional guidance.

6 EFRAG also notes that the concept of 'obscuring' should be further clarified by the IASB as it is unclear, and possible interpretations include:

(a) swamping, intentionally or not, material information with immaterial information;

(b) aggregating material information with different natures or functions;

(c) disaggregating material information that have same nature or function;

(d) using unclear language, terminology, or concepts; and

(e) placement of the information in areas of the financial statements where users are unlikely to look for it.

7 EFRAG notes, in that respect, that the IFRS Practice Statement 2 *Making Materiality Judgements*, issued at the same time as the ED does not provide further guidance on the notion of obscuring.

8 EFRAG observes that principles of effective communication (including the reference to 'clear communication') are already discussed as part of the IASB's Discussion Paper DP/2017/1 Disclosure Initiative - *Principles of Disclosure* issued in March 2017. EFRAG encourages the IASB to further consider the concept of obscuring in that context. The IASB could work with preparers, auditors and regulators, as the concept of obscuring needs to be understood and applied by all parties in the financial reporting process and the legal and regulatory aspects need to be carefully considered.

Other minor change

9 EFRAG observes that the ED no longer uses the phrase 'individually or collectively' without explanation. EFRAG recommends that the IASB explains the effect, if any, of these proposed changes.

Question 2- Consequential amendments to other pronouncements

Do you have any comments on the proposed amendments to the Materiality Practice Statement or to the forthcoming revised *Conceptual Framework*?

EFRAG response

EFRAG agrees with the proposed consequential amendments to the Materiality Practice Statement and to the forthcoming revised *Conceptual Framework for Financial Reporting*.

However, EFRAG recommends that that the IASB reviews the use of the terms 'immaterial' and 'not material' in both IAS 1 and the Materiality Practice Statement and clarifies their meaning.

Finally, EFRAG observes that the definition of material in the forthcoming revised *Conceptual Framework for Financial Reporting* will still differ from the one in the amended IFRS Standards insofar as it refers to information contained in the general purpose financial report, rather than the financial statements.

10 EFRAG agrees the proposed consequential amendments to the Materiality Practice Statement and to the forthcoming revised *Conceptual Framework for Financial Reporting*.

11 However, EFRAG notes that both IAS 1 and the Materiality Practice Statement currently uses the terms 'immaterial' (e.g. paragraphs 29 and 30A of IAS 1 and paragraphs 8 and 48 of the Materiality Practice Statement) and 'not material' (e.g. paragraphs 31 and 121 of IAS 1 and paragraphs 74 and 83 of the Materiality Practice Statement). In our opinion, the use of different terms may be interpreted as different levels of materiality. EFRAG recommends that the IASB uses one term consistently or clarifies that these terms are intended to have the same meaning or explains the difference in meaning.

12 Finally, EFRAG observes that the definition of material in IFRS Standards and in the *Conceptual Framework for Financial Reporting* will still differ in one respect as the latter refers to financial reports rather than to financial statements. As a consequence, the definition of material in the forthcoming revised *Conceptual Framework for Financial Reporting* applies to the whole financial report. EFRAG understands that the IASB has not specifically debated the implications of the proposed consequential amendments when deliberating on the Conceptual Framework.

Question 3

Do you have any other comments about the proposals in this Exposure Draft?

EFRAG's response

EFRAG considers that, once the Disclosure Initiative is finalised, the IASB should include the definition of "material" only in a single general standard such as IAS 1. This would prevent any risk of possible inconsistencies arising in the future as IFRS Standards are revised.

13 EFRAG observes that the definition of materiality is currently repeated in several places (IAS 1, IAS 8, and the *Conceptual Framework for Financial Reporting*). The IASB could reconsider whether having the definition of materiality repeated in so many places is the most effective way of achieving consistent application.

14 EFRAG considers that the IASB should concentrate the guidance in a single general standard, such as IAS 1 (in addition to the *Conceptual Framework for Financial Reporting*). This would reduce the risk of possible inconsistencies arising as IFRS Standards are revised.