

European Financial Reporting Advisory Group

**EFRAG/EFFAS/NFF/NASB Joint outreach
event on Principles of Disclosure**

Oslo, Norway– 15 June 2017

Background



Brief history of the 'disclosure problem'



2005

- Europe moves to IFRS Standards
- Significant increase in disclosures and length of F/S for most European entities

2005+

- Newer standards bring increased disclosures, e.g. IFRS 7, IFRS 13
- Other trends also add to length of overall annual report

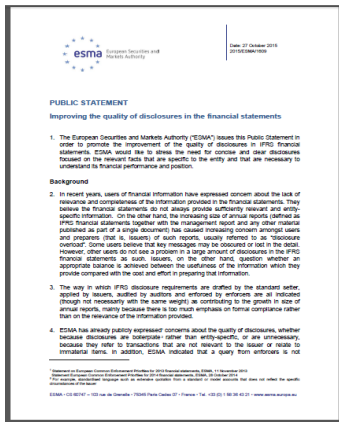
2011+

- Several studies/initiatives target the 'disclosure problem'
- EFRAG/ANC/FRC DP 'Towards a Disclosure Framework for the Notes' 2012

2013

- IASB's Discussion Forum 'Disclosures in Financial Reporting'
- IASB adds 'Disclosure Initiative' to its agenda

Some of the European initiatives



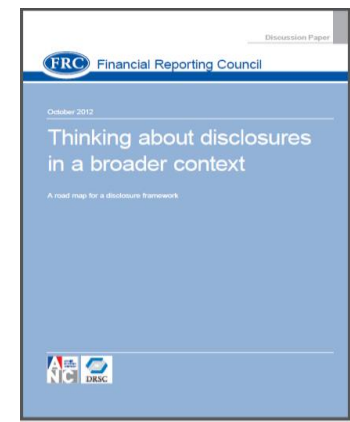
ESMA - 2011



ICAS & NZICA - 2011



EFRAG - 2012



FRC - 2012



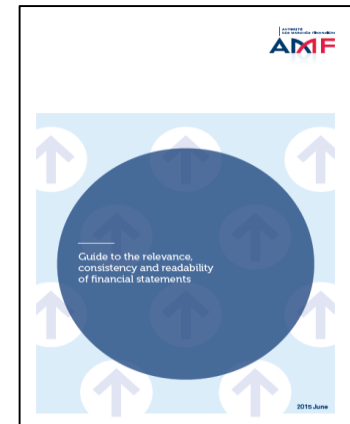
ICAEW - 2013



'Christmas letter' from the DBA - 2013



AFM - 2014



AMF - 2015



Key recommendations from *Towards a Disclosure Framework for the Notes*



■ EFRAG/ANC/FRC 2012 recommendations

- Define the **purpose of the notes** and their boundary
- Disclosures should be **principle-based**, set consistently across standards, proportionate and achieve reasonable cost-benefit trade-off
- Consider **how disclosure requirements** are drafted as this may influence behaviour
- Strengthen the application of **materiality**
- Articulate key features of **effective communication** (communication not just compliance exercise)
- Preparers, auditors and regulators, each in their specific role, have a **shared interest** in fostering the improvement of disclosures

What has the IASB done to date?



Completed standard-setting projects		Materiality guidance	Research projects
Amendments to IAS 1 (2014) To remove barriers to the exercise of judgement	Amendments to IAS 7 (2016) To improve disclosure of liabilities from financing activities	Practice Statement on application of materiality (expected June 2017)	Principles of Disclosure Discussion Paper (March 2017)

Definition of Material

- Now separate from the Principles of Disclosure project
- ED expected late June 2017

Outline of the Discussion Paper



Principles of effective communication in preparing financial statements



Principles on where to disclose information

Roles of the primary financial statements and the notes

Location of information



Principles to address specific disclosure concerns of users of financial statements

Use of performance measures

Disclosure of accounting policies

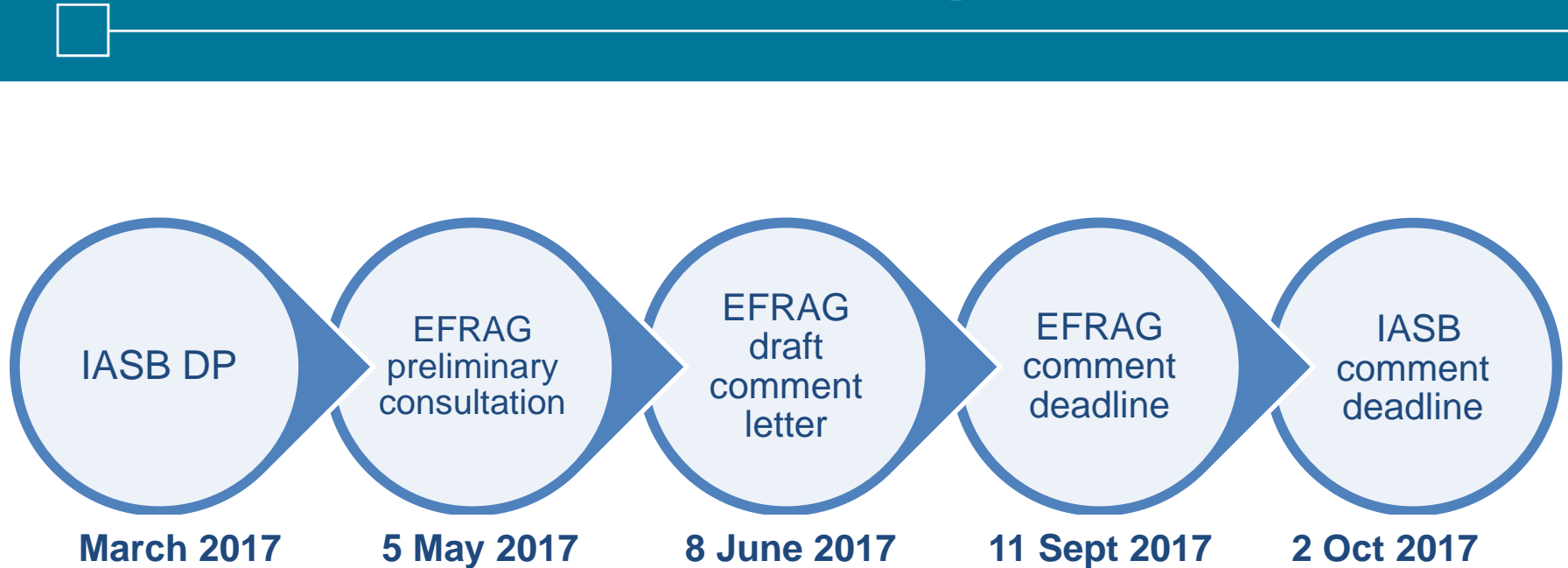


Principles for improving disclosure objectives and requirements

Centralised disclosure objectives

Drafting disclosure requirements

EFRAG's comment letter process



EFRAG's objective at the comment letter stage is the best possible outcome from a European perspective

Key questions for today's outreach



What is the problem now?	What are the main root causes?	What should the IASB focus on?	Impact of technology
<ul style="list-style-type: none">• disclosure overload, or• disclosure effectiveness?	<ul style="list-style-type: none">• requirements in IFRS Standards, and/or• application (behaviour)?	<ul style="list-style-type: none">• promoting better communication/ 'behaviour', and/or• standards-level disclosure requirements	<ul style="list-style-type: none">• enabler, or• game changer?

European Single Electronic Format (ESEF)

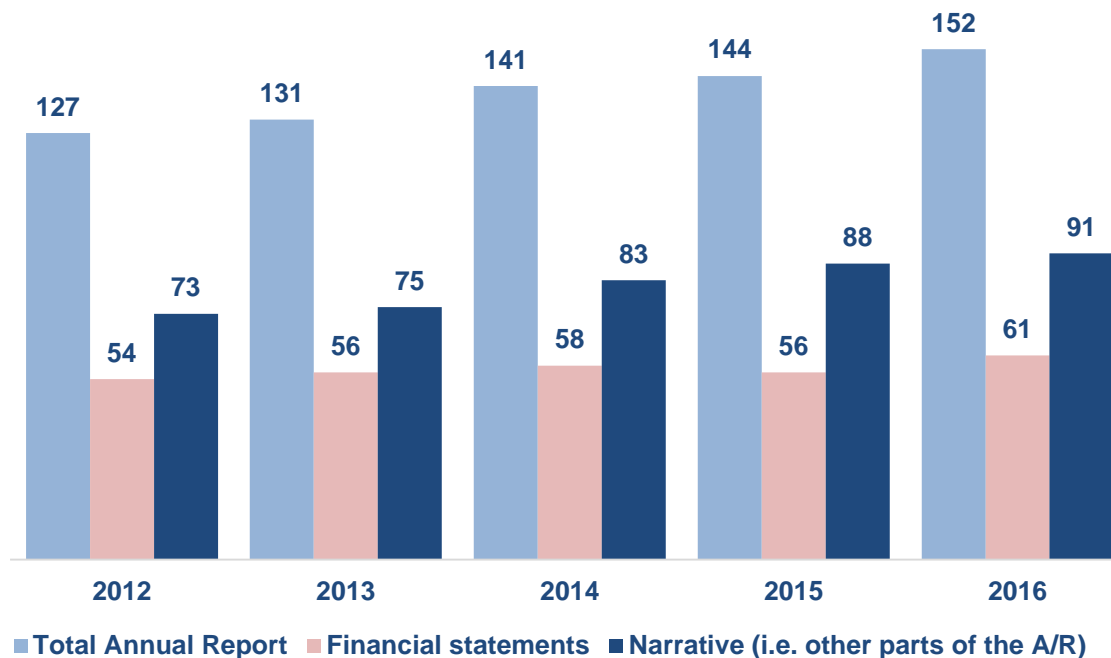
Is the Disclosure Initiative 'on track'?

Trends in length of annual report (1)

... increasing on average



Changes in length of Annual Report and Financial Statements 2012 - 2016



On average length of financial statements have increased by **13%** (+7 pages) over the last 4 years

Source: Deloitte UK Annual Reporting Insights – Surveys 2014 to 2016
Based on the Annual Reports of 100 listed UK companies surveyed for current practices

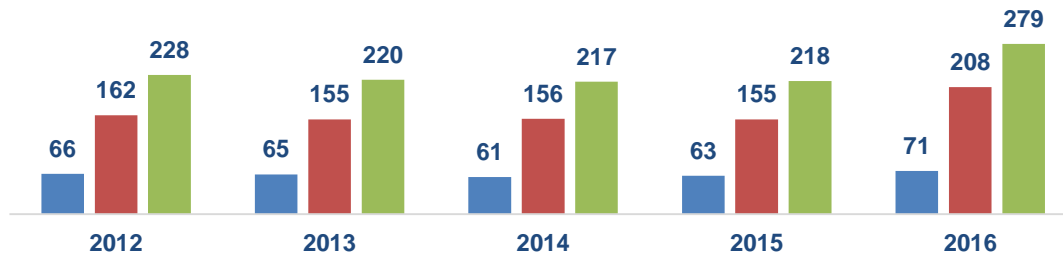
Trends in length of annual report (2)

... Examples of Norwegian companies



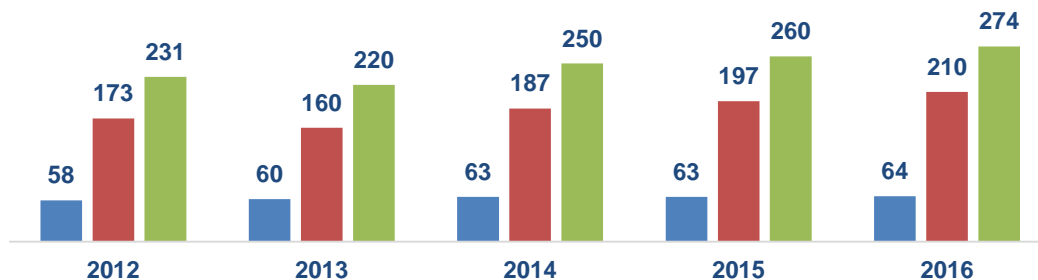
Statoil - Changes in length of A/R and Financial Statements

■ Financial Statements ■ Narrative ■ Total Annual Report



Norsk Hydro - Changes in length of A/R and Financial Statements

■ Financial Statements ■ Narrative ■ Total Annual Report



On average length the length of the financial statements of Statoil and Norsk Hydro has increased by 10% since 2012

Source: Annual Reports 2012-2016

EFRAG's tentative views on the DP

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Main messages in EFRAG's DCL



EFRAG's main messages:

- The IASB's primary focus for the next phases of this project should be to tackle **disclosure overload**
- This requires a holistic **standards-level review** to:
 - develop a coherent and comprehensive but concise package of disclosure requirements
 - remove any disproportionate/redundant requirements
- Only limited benefit in developing more **non-mandatory guidance** on effective communication and formatting
- Clarify **interactions** between IASB DP and other IASB projects (e.g. Primary Financial Statements)
- Consider in more depth the **impact of technology** on the disclosure problem
- Explore further how disclosure requirements could be focused on the entity's activities and business model. The '**tiered disclosure**' approach proposed by the NZASB staff is worth further developing.

IASB's description of the disclosure problem



The IASB DP identifies three main concerns about disclosures :

Not enough
relevant
information



Can lead to
inappropriate
investing or lending
decisions

Too much
irrelevant
information



Can obscure relevant
information and reduce
understandability of
financial statements

Ineffective
communication



Can reduce
understandability of
financial statements

Many causes

- Behavioural
- Difficulty in applying materiality judgement
- The way disclosure requirements are drafted

EFRAG's tentative views

Description of the disclosure problem



- Acknowledge that the problem is **multifaceted**
 - requirements in IFRS Standards are not the only cause
 - but stakeholders have already undertaken extensive efforts and initiatives to address behavioural issues (application of materiality and communication)
- IASB DP's description **lacks sufficient emphasis or focus** to provide a clear direction forward:
 - primary focus should be on **disclosure overload**
 - requires prioritisation of a **comprehensive review** of standards-level requirements aimed at:
 - developing a clear, effective, coherent and comprehensive but concise package of disclosure requirements
 - removing any requirements that are disproportionate/redundant

EFRAG's tentative views

Principles of effective communication



Information in financial statements should be



■ EFRAG's tentative Views

- EFRAG takes no issue with the particular principles proposed in the IASB DP
- But EFRAG is not convinced that additional non-mandatory guidance of this type brings substantial new insights
- Further work needed to determine whether some of these principles could be developed into requirements to be included in a general disclosure standard
- Similar concerns on the effectiveness development of non-mandatory guidance on formatting

Questions



Questions

Can principles make communication more effective?

What do investors think are useful examples of disclosures in the financial statements?

Does it make a difference presenting information separately in the primary financial statements rather than presenting it aggregated with other information in the primary financial statements and disclosing it solely in the notes?

Roles of the primary financial statements and of the notes



Component of financial statements	Role
Primary financial statements are statements of: <ul style="list-style-type: none">• financial position• financial performance• changes in equity• cash flows	To provide a structured and comparable summary of an entity's recognised assets, liabilities, equity, income and expenses
Notes	To explain and supplement the primary financial statements

■ EFRAG's tentative Views

- EFRAG would have preferred a broader discussion about the relevance of the distinction between the primary financial statements and the notes
- The proposed role of the primary financial statements focuses too much on assets, liabilities etc and too little on the objective of providing summarised financial information
- The proposed role of the notes does not clarify the boundary of financial statements

Location of information



Principles for the location of information

Information necessary to comply with IFRS Standards can be placed outside financial statements but within the annual report, providing the following are met

- annual report more understandable;
- financial statements understandable; and
- information faithfully represented, clearly identified and cross-referenced.



Information labelled as 'non-IFRS' can be placed inside the financial statements if it is

- listed, together with a statement of compliance with IFRS Standards;
- identified as not in accordance with IFRS Standards and, if applicable, as unaudited; and
- accompanied by explanation of why it is useful.

■ EFRAG's tentative views

Cross referencing

EFRAG welcomes guidance on cross-referencing, but:

- The IASB should first identify the issues associated with the use of cross-references
- Further work needed with audit authorities and regulators to assess the audit, legal and regulatory implications of the proposed guidance across a range of jurisdictions
- Guidance should remain principles-based rather than referring to specific documents:
 - source documents should be available on the same terms, at the same time and for the same duration as the financial statements
 - question the practicality of the proposed test that cross-referencing is allowed only if 'it makes the annual report as a whole more understandable'

Location of information (continued)



Principles for the location of information

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- accompanied by explanation of why it is useful.

■ EFRAG's tentative views (continued)

Non-IFRS information:

- EFRAG is concerned that the proposed guidance on identifying non-IFRS information will lead to clutter unless targeted better
- The primary focus should be on financial information that supplements IFRS information or provides an alternative depiction of some type. For this type of information EFRAG supports the approach proposed in the IASB DP
- Non-IFRS information should be prohibited if it is so inconsistent or in conflict with IFRS Standards that it misleads or detracts from understandability

Questions



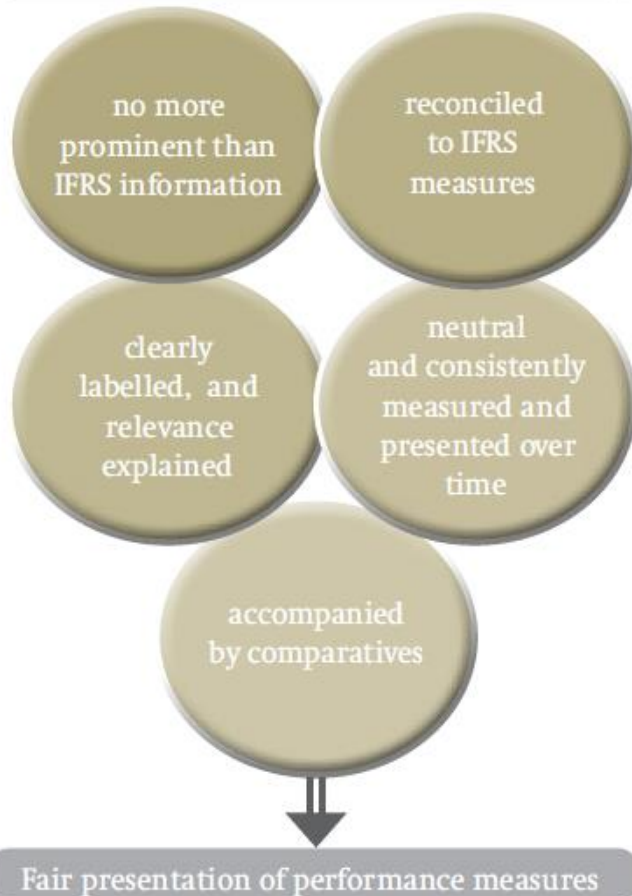
Questions

What is the impact of cross-referencing IFRS information outside the financial statements for investors?

Should 'non-IFRS information' be permitted within the financial statements?

Use of performance measures in the financial statements

Performance measures should be



■ EFRAG's tentative views

- EFRAG is concerned about the significant overlap between the Disclosure Initiative and the Materiality and Primary Financial Statements projects
- EFRAG would have preferred a more holistic and comprehensive discussion:
 - on the use of metrics such as EBIT/EBITDA,
 - on unusual or infrequently occurring items in the context of the Primary Financial Statements project, which would look at all aspects of the issue, potentially including other adjustments made to performance figures

which would be better addressed in the Primary Financial Statements project

Questions



Questions

Alternative (non-IFRS) performance measures in the financial statements: misleading or useful?

Should EBITDA be permitted or required in the financial statements?

Should unusual and infrequent items be separately presented and if so how?

Disclosure of accounting policies



Three categories of accounting policies

Category 1—always necessary to understand the financial statements

The accounting policy relates to material items, transactions or events and:

- is selected from alternatives in IFRS Standards;
- reflects a change from a previous period;
- is developed by the entity in the absence of specific requirements; and/or
- requires use of significant judgements or assumptions.

Category 2—not in Category 1 but necessary to understand the financial statements

The accounting policy is not in Category 1 but relates to material items, transactions and events.

Category 3—not in Categories 1 and 2 but is used in preparing the financial statements

This category includes all other accounting policies used in preparing the financial statements.

■ EFRAG's tentative views

- EFRAG does not support prescriptive requirements as entities should have some flexibility on how best to meet users' needs
- Focus should be on disclosure of those accounting policies that relate to items, transactions or events that are material to the financial statements without always being necessary (Category 2), where judgement is most needed
- The IASB should not provide guidance on information that is not required by IFRS Standards (Category 3)

Centralised disclosure objectives and drafting disclosure requirements



	Method A	Method B
Basis for developing	Type of information focus	Entity's activity focus
Standards-level objectives	Developing disclosure objectives for individual standards	Not developing disclosure objectives in individual standards
Disclosure requirements in Standards	Developed on the basis of the <i>disclosure objectives of an individual standard</i>	Developed on the basis of <i>centralised disclosure objectives</i>

■ EFRAG's tentative views

- Support exploring how to achieve a more holistic and unified approach in developing disclosure objectives/requirements
- Support further analysis of how disclosure requirements could be focused on the entity's activities and business model (Method B in the IASB DP) as this has the potential to provide improved information for users but we are not yet to assess its practicality and outcomes
- Location of the disclosure requirements is not the primary issue

How important is the application of materiality?



- **Materiality is critical to effective communication:** acts as a filter when deciding what and how to disclose information
- **Proposed changes to the Definition of Materiality**
 - Now a separate project form the Principles of Disclosure Project (ED expected in June 2017)
 - New definition: *information is material if omitting, misstating or obscuring it could reasonably be expected to influence the decisions that the primary users of a specific reporting entity's general purpose financial statements make on the basis of those financial statements.*
- **Proposed Practice Statement on Materiality**
 - Provides non-mandatory guidance on the application of Materiality to Financial Statements (Publication expected in June 2017)

■ Questions

- Do participants consider that the IASB's initiatives are helpful?
- What else could be done?

Concerns raised about the disclosures in IFRS 13

Fair Value Measurement



- IFRS 13 provides the guidance on assessing fair value measurements within three levels of the fair value hierarchy:
 - Level 1: Unadjusted quoted prices in active markets
 - Level 2: Other observable inputs not included within Level 1
 - Level 3: Unobservable inputs for the asset or liability
- Concerns have been raised about **disclosures on Level 3** measurements:
 - generic information rather than entity-specific information failing to reflect entities' business management
 - aggregation of disclosures for dissimilar underlying assets or liabilities so that the disclosures are not sufficiently granular

■ Question

- Do you think the principles in the Discussion Paper will address concerns raised about disclosures on Fair Value Measurement?



Thank you for your attention!

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