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(EFRAG)
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Ref: ESMA response to EFRAG's Draft Comment Letter on the IFRS Foundation Exposure Draft – *Proposed amendments to the IFRS Foundation Due Process Handbook*

Dear Mr Gauzès,



The European Securities and Markets Authority (ESMA) thanks you for the opportunity to provide input to EFRAG's draft comment letter relating to the consultation on the Exposure Draft (ED) *Proposed amendments to the IFRS Foundation Due Process Handbook*. We are pleased to provide you with the following comments with the aim of contributing to improving the IFRS Foundation's due process thereby promoting the development of high-quality IFRS Standards.

As part of its mandate, ESMA contributes to the consistent application of financial markets legislation in the European Union, including financial reporting requirements that are applicable to European issuers. Ensuring the consistent application of IFRS is a pre-requisite to their enforceability across Europe and ESMA is committed to continue cooperating with the IFRS Foundation to pursue this objective, as also indicated in our *Statement of protocols for cooperation on International Financial Reporting Standards*¹.

Like EFRAG, ESMA generally supports the IFRS Foundation's proposal to provide more clarity around the IASB's work on analysing and reporting on the expected effects of amended or new IFRS requirements. In ESMA's view, assessing and reporting on the expected costs and benefits of any proposed changes to IFRS during the entire standard setting process would help identifying and addressing on a timely basis any short-comings that may result in implementation and enforceability issues once the standards have become applicable.

¹ https://www.esma.europa.eu/file/20056/download?token=mgKW_E8x

ESMA has considered the proposals addressing the timing of application of agenda decisions issued by the IFRS Interpretations Committee (IFRS IC) and the possibility also for the IASB to issue agenda decisions. Like EFRAG, we are not convinced that these proposals would effectively achieve the IASB's objective of supporting consistent application of IFRS.

Particularly, while we agree with the clarification that IFRS IC agenda decisions do not have the status of IFRS and, therefore, cannot change or add requirements to the IFRS, ESMA is not convinced that the ED proposals with regards to the timing of application of these decisions will ultimately achieve their intended objective. This is because setting an expectation that issuers would be entitled to 'sufficient time' to apply agenda decisions would be inconsistent with the status of this type of pronouncements. Agenda decisions have no authoritative value in themselves as they derive their practical relevance from the underlying IFRS requirements whose application they merely illustrate. As these requirements are, in most cases, already applicable, there cannot be any expectation that issuers would be entitled to an arbitrary delay in their application on the basis of the specific illustration provided by an agenda decision.

Furthermore, the reference to 'sufficient time' may result in diversity in the timing of application of any change in an accounting policy or correction of an error stemming from the publication of an agenda decision. In our view, the IFRS Foundation should rather set the expectation that issuers will reflect in their financial statements the consequences of the publication of agenda decisions – be it, for example, a change in accounting policy or a correction of an accounting error – as soon as possible, unless it is impracticable. In this respect, we would encourage the IASB to further consider how the notion of impracticability can be applied in practice.

We also believe that IFRS IC agenda decisions should not be intended as providing explanatory material that results in new information which cannot be retrieved already from the reading of IFRS requirements. Otherwise this may challenge the assumption underlying the conclusion of the IFRS IC that the principles and requirements in IFRS already provide an adequate basis to determine the appropriate accounting treatment and that, therefore, standard-setting is not necessary.

Regarding the proposal to add to the IASB's toolbox the possibility to issue agenda decisions, like EFRAG, ESMA is concerned that the benefits of introducing this new tool for the Board would be outweighed by the risks of confusion between the role of the IFRS IC and the standard-setting role of the IASB. We believe that if the IASB has ruled out that standard-setting is necessary for a certain fact pattern, but that a clarification would still be useful in the form of an agenda decision, the IASB can defer the matter to the IFRS IC.

In addition, while ESMA notes that the work of the Transitional Resource Groups (TRGs) provides useful educational material to promote the consistency in application of new standards, we regret that the Due process handbook is still silent on the existence and the role of these groups.

Finally, ESMA supports the clarifications on the level of review of the educational material supporting the consistent application of IFRS. However, we would recommend retaining the clear statement in the Due process handbook clarifying that the IASB and the technical staff have a responsibility to ensure that any educational material is not confused with an IFRS or perceived as being mandatory.



Our detailed comments on the ED are set out in the Appendix to this letter. In case you have any questions or comments please do not hesitate to contact me or Evert van Walsum, Head of the Investors and Issuers Department (Evert.vanWalsum@esma.europa.eu).

Yours sincerely,



Steven Maijor

Appendix – ESMA's detailed answers to the questions in the ED

Question 1 – Effect Analysis

The DPOC proposes to amend the section 'Effect analysis' to:

- *embed explicitly the process of analysing the effects throughout the standard-setting process;*
- *explain the scope of the analysis;*
- *explain how the Board reports the effects throughout the process; and*
- *differentiate the effect analysis process from the final effect analysis report.*

Do you agree with these proposed amendments?

1. ESMA generally supports the proposed clarifications on the IFRS Foundation's and the IASB's commitments towards performing and reporting on effect analyses throughout the whole standard-setting process and not only at the end.
2. Particularly, ESMA welcomes the introduction of a new paragraph 3.80 of Appendix A to the ED addressing the importance of including financial stability implications as part of the effect analysis. In our 2015 comment letter² in response to the IFRS Foundation's consultation on the then *Trustees' Review of Structure and Effectiveness: Issues for Review*, ESMA indicated already that: "*While effect analyses should be an integral part of the standard-setting process [...], we believe that the extent of changes in the existing practice/standards should not be used in itself as an argument against the change of an existing standard*". In this respect, broader considerations on the expected improvements and challenges for financial stability of any proposals of new or amended requirements may contribute to providing a broader, public interest, perspective into the effect analysis.
3. ESMA notes that the Due process handbook highlights that the effect analysis should address both potential advantages and disadvantages arising from the proposals. In this regard, it would be helpful that the IFRS Foundation clarifies why, in paragraph 3.77 of Appendix A to the ED, when referring to the example of the effect analysis conducted during the research phase, the proposed amendment includes only a reference to the assessment of the likely benefits of any new proposals and omits any references to the potential costs.
4. Finally, ESMA also recommends that in paragraph 3.79 of Appendix A to the ED, the IFRS Foundation includes an explicit reference to the fact that the assessment of the likely effects shall also consider what implications the proposals for new or amended IFRS requirements may have for the consistent application of IFRS. In our view, this clarification would be in line with the specific focus that the Due process handbook attributes to the importance of consistent application and to the related enforceability of IFRS. ESMA stands ready to contribute to this assessment based on the enforcement experience.

² Available here: https://www.esma.europa.eu/sites/default/files/library/2015-1738_esma_letter_to_ifrs_-_trustees_review_of_the_structure_and_effectiveness_of_the_ifrsf.pdf

Question 2 – Agenda decisions

The DPOC has proposed the following amendments relating to agenda decisions:

- to provide the Board with the ability to publish agenda decisions;
- to better explain the objective and nature of explanatory material in an agenda decision; and
- to reflect in the Handbook that an entity should be entitled to sufficient time both to determine whether to make an accounting policy change as a result of an agenda decision, and to implement any such change.

Do you agree with these proposed amendments?

5. ESMA generally supports the IFRS Foundation's objective of promoting consistent application of IFRSs, as this is one of the areas where ESMA and the Foundation cooperate most closely, as also stated in our *Statement of protocols for cooperation on International Financial Reporting Standards*³. However, when considering the proposed amendments to the Due process handbook in relation to agenda decisions, ESMA is not convinced that they would fulfil this objective for the reasons set out below.

IFRS IC agenda decisions

6. ESMA has since 2011⁴ held a position with respect to agenda decisions (or 'rejection notices' as they are currently referred to in the Due process handbook) according to which: "*Rejection notes published by the IFRS Interpretations Committee often provide clarification of the standards. There is an expectation on the part of the stakeholders in IFRS that rejection notes [...] will be carefully considered by preparers in determining their accounting policies. In the case of a change in a previous accounting treatment following the issue of a rejection note, an issuer should apply IAS 8 and provide proper and sufficient disclosure on the reasons for the change, having regard to the particular facts and circumstances of the individual case, including reference to the rejection note*".
7. We welcome the fact that the IFRS Foundation has taken the opportunity to address the role and status of IFRS IC agenda decisions as part of its work to revise the Due process handbook, however we are concerned by the proposed amendments in relation to: (i) the role of explanatory material accompanying the agenda decisions; and (ii) the timing of application of agenda decisions.
8. While ESMA agrees with clarifying that agenda decisions do not have the status of IFRS and therefore they cannot change or add requirements to IFRS, we believe that including in agenda decisions explanatory material that, as stated in paragraph 8.5 of the Appendix A to the ED '*provides new information that was not otherwise available and could not otherwise reasonably have been expected to be obtained*' may confuse issuers on the role and status of agenda decisions. This is because explanatory material should illustrate the application of the existing requirements included in the authoritative IFRS material

³ Available here:

https://www.esma.europa.eu/sites/default/files/library/2016_ifrs_foundation_and_esma_statement_of_protocols_for_cooperation_on_international_financial_reporting_standards.pdf

⁴ Available here: https://www.esma.europa.eu/sites/default/files/library/2015/11/2011_211.pdf

rather than providing new information. Consequently, if the new information provided in an agenda decision '*was not otherwise available and could not otherwise reasonably have been expected to be obtained*' based on the applicable IFRS requirements, this may implicitly lead to the conclusion that standard-setting was necessary and thus an agenda decision was not an appropriate tool to be used.

9. In addition, the statement in the ED that an agenda decision '*provides new information that was not otherwise available and could not otherwise reasonably have been expected to be obtained*', may be intended by some as ruling out that changes arising from agenda decisions may constitute in some cases the correction of an error. In our view, it is important to highlight that the conclusion on the nature of the changes (e.g. changes in policy, correction of an error) that may follow from the application of an agenda decision depend of the specific facts and circumstances of the issuer and of the agenda decision.
10. In ESMA's view, identifying whether an agenda decision provides new information is a matter of entity-specific assessment which should only be based on the rationale which has led the IFRS IC to conclude, in the specific case at hand, that the principles and requirements in IFRS provide an adequate basis to determine the appropriate accounting treatment for a certain fact pattern. Therefore, in our view, arguing in the Due process handbook that explanatory material may give rise to new information that '*was not otherwise available and could not otherwise reasonably have been expected to be obtained*' may *de facto* contradict the rationale underlying the publication of an agenda decision, i.e. the fact that IFRS already provide an adequate basis for the accounting treatment. In fact, as explained earlier, some could conclude that the addition of explanatory material, especially when it builds on non-authoritative guidance, provides evidence that standard-setting may be necessary.
11. ESMA believes that, to the extent explanatory material is merely intended as playing an educational role, it should preferably be conveyed as part of educational material instead of being part of agenda decisions. However, ESMA believes that adding explanatory material to agenda decisions may be useful, under the condition that this material should be limited to explaining how the authoritative IFRS material provides an adequate basis to account for a certain fact pattern that has been brought to the attention of the IFRS IC.
12. With respect to the timing of application of agenda decisions, as already explained in our 2018 comment letter⁵ on the IASB's Exposure Draft *Accounting Policy Changes – Proposed amendments to IAS 8*, ESMA does not believe that specific requirements or expectations should be set regarding potential delays in the timing of application of any accounting policy changes arising from IFRS IC agenda decisions. Consequently, we disagree with the proposal to amend the Due process handbook in paragraph 8.5 of Appendix A to the ED which refers to the fact that: "*It is expected that an entity would be entitled to sufficient time to make that determination [that it needs to change an accounting policy as a result of an agenda decision] and implement any change*".

⁵ Available here: https://www.esma.europa.eu/sites/default/files/library/esma32-61-271_cl_to_iasb_on_ed_amendments_to_ias_8_impracticability.pdf

13. Furthermore, as stated in the above-mentioned comment letter, *"it is our understanding that agenda decisions do not have their own 'effective date' and therefore any implications of agenda decisions should be read in the context of the application date requirements of the IFRS which they refer to"*. As the IFRS requirements, which agenda decisions refer to are normally already effective and fully applicable, any clarifications provided by agenda decisions should be also regarded as immediately applicable, unless impracticable.
14. This implies that if an agenda decision clarifies the requirements of a standard and an issuer decides to change its accounting policy or to correct an accounting error, neither the Due process handbook nor the IFRS IC should set an expectation that there can be delays in taking such actions, but rather that any such adjustments should be made immediately, unless it is impracticable. In this respect, we would rather encourage the IASB to further address how the notion of impracticability can be applied in practice.
15. Moreover, in our view, if the IFRS IC realises that the new information provided by agenda decisions and any accompanying explanatory material may effectively result in a widespread change in the application of certain IFRS requirements and in burdensome transitional consequences for preparers and users, this fact may provide an indication that standard-setting may be necessary to address the issue at hand. In such extreme cases, standard-setting would enable the IASB or the IFRS IC to set dedicated transition requirements which would make it unnecessary to include any references on the timing of application of IFRS IC agenda decisions.
16. In addition, ESMA also believes that the expectation that issuers are entitled to 'sufficient time' would in fact result in the inconsistent timing of application of the consequences resulting from clarifications included in agenda decisions which would be contrary to the objective of ensuring consistent application of IFRS.
17. Finally, we suggest developing a procedure through which when agenda decisions incorporate explanatory material that links the existing requirements in IFRS to the related basis for conclusions, the Board considers incorporating this material directly into the basis for conclusions of the revised standard. For instance, the annotated version of IFRS 9 includes references to IFRIC updates dating back to 2002, 2005 and 2007 related to paragraphs of IAS 39 that have been carried forward to IFRS 9. Incorporating the relevant clarifications directly in the basis for conclusions of the revised standards in these cases may simplify the application of IFRS.

IASB agenda decisions

18. The ED proposes introducing the possibility for the IASB to issue agenda decisions when, although it decides not to add a project to its standard-setting agenda, it still concludes that consistency of application of the standards would be improved by providing material that explains how the applicable principles and requirements in IFRS apply to a particular transaction or fact pattern.

19. We appreciate the IFRS Foundation's attempt to give the IASB a more proactive role in addressing issues arising from the application of IFRS, especially when this can take the pressure off the use of educational materials, such as webcasts, to provide clarifications on the application of IFRS. However, by adding an additional tool of 'quasi standard-setting' we believe that there is a risk that, as indicated during the IFRS Advisory Council in September 2018, the introduction of IASB agenda decisions would blur the line between the work of the Board and the role of IFRS IC.
20. Furthermore, in paragraph 22 of the ED, it is indicated that the need for an agenda decision tool for the IASB arises, for example, in the context of application questions arising from discussions at the level of the Transition Resource Group (TRG), and particularly when the Board decides that it is not necessary to undertake any standard-setting activity in relation to a new IFRS, but still clarifications may help the consistent application.
21. In this respect, ESMA takes this opportunity to express appreciation for the work of the TRGs as they represent an effective tool to promote the consistency in application of new standards. Therefore, we believe that TRG should be addressed in the Due process handbook, which is currently silent on the existence and the role of these transitional groups. ESMA regrets that the proposed amendments do not address TRGs and urges the IFRS Foundation to amend the Due process handbook to provide clarity on the role, objectives, structure and outputs of TRGs. In this context, ESMA believes that it would be useful to consider how the IASB can give more prominence to the conclusions of TRG discussions which provide educational material for the application of the new standards without resulting in standard-setting activity.
22. In other cases, where the IASB receives application questions in relation to applicable IFRS for which no standard-setting is deemed necessary, ESMA believes that the IASB should refer those matters to the IFRS IC, which may then consider issuing an IFRS IC agenda decision.

Question 3 – other matters

The DPOC has proposed to amend the Handbook on other matters including:

- *the type of review required for different types of educational material;*
- *consultation in connection with adding projects to the Board's work plan;*
- *clarifications of the IFRS Taxonomy due process and Taxonomy updates and the role of the DPOC in overseeing Taxonomy due process.*

Do you agree with these proposed amendments?

Educational material

23. ESMA agrees with the proposed amendments in relation to the type of review required for educational material and particularly with the clarification in paragraph 8.9 of Appendix A to the ED that educational material does not add or change requirements in IFRS. We note that the use of educational material is an area where there is a risk of conducting

quasi standard-setting by providing clarifications that address practical application questions by referring to authoritative as well as non-authoritative material.

24. In ESMA's view, it is important that, while remaining responsive to the needs arising from the stakeholders involved in the preparation and use of IFRS financial statements, the IASB does not issue educational material, including webcasts, that address areas where there is lack of clarity in existing IFRS requirements and which may give rise to confusion on the enforceability of the IFRS requirements. ESMA believes that the IASB should continue to address any need for clarity in the application of IFRS either through specific standard-setting activities or, when this is not necessary, via IFRS IC agenda decisions.
25. In this respect, we believe that the Due process handbook should retain the reference in paragraph 6.43 of Appendix A to the ED to the fact that: *"the IASB and the technical staff have a responsibility to ensure that any educational material is not confused with an IFRS or perceived as being mandatory"* which the ED currently proposes to delete.

Amendments to IASB work plan

26. In relation to the amendments on how the IASB adds projects to its work plan, ESMA agrees that the IASB shall be empowered to add a project to its work plan in response to changing circumstances even between agenda consultations, provided that it consults on these proposed changes with the ASAF and the IFRS Advisory Council.
27. ESMA notes that paragraph 4.6 of Appendix A to the ED mentions the consultation procedure only in case the IASB intends to add a project to its work plan, but it does not address with equal detail the situation in which the IASB decides to change its priorities in response to changing circumstances. ESMA suggests being cautious when considering changes to the IASB's priorities between consultations, as we believe that this should happen quite rarely and, even when this is the case, this change should be subject to an *ad hoc* public consultation or at least to the approval of the Trustees of the IFRS Foundation.

IFRS Taxonomy

28. With regards to the IFRS taxonomy Due Process, ESMA supports the addition of a table to enhance the clarity of approval and review process associated with taxonomy updates and agrees with the other editorial changes suggested in the ED.

Relationships with securities and other regulators

29. Paragraph 3.56 of Appendix A to the ED addresses the relationship between the IASB and securities and other regulators. As mentioned in paragraph 4 with reference to the Statement of Protocols between the IFRS Foundation and ESMA, ESMA supports and highly appreciates the ongoing cooperation with the IASB inspired by the common goal of pursuing consistency in application of IFRS which is necessary to promote transparency and enforceability of IFRS financial statements, thereby ultimately contributing to investor protection and financial stability.
30. In this respect, we would suggest retaining in paragraph 3.56 of Appendix A to the ED the reference to the establishment of regular meetings with securities regulators. Ensuring

that the IASB maintains a regular and open dialogue with securities regulators is particularly important when considering that the Due process handbook does not foresee any formal technical consultative group in which the IASB collects and discusses the views of securities regulators.

Other amendments

31. ESMA questions the reason underlying the proposal in the ED to amend paragraph 3.3 of the Due process handbook to drop the word 'tentative' when referring to the decisions taken by the IASB during its meetings and reported in the *IASB Update*. ESMA believes that it is important for the correct understanding by stakeholders of the progress made of any standard-setting process to continue to clearly indicate whether or not the decisions of the Board are tentative or final.
32. Paragraph 3.40 of Appendix A to the ED refers to the Board Advisors and proposes some deletions to the existing text of the Due process handbook with respect to the role of the Board Advisors (formerly referred to as 'assigned Board members') and their appointment. ESMA would suggest providing more detail on the role of the Board Advisors rather than just referring to the fact that they provide strategic and technical advice on the concerned projects. Furthermore, it would be useful to clarify how and on which basis these Board members are appointed as advisors for a specific project. As a side note, we highlight that the heading of this section still refers to the old notion of 'assigned Board members' rather than to 'Board Advisors'.
33. Finally, ESMA stresses the importance of paragraph 7.7 of Appendix A to the ED which indicates that the fact that a topic is being addressed in a forthcoming IFRS Standard does not prevent the IFRS IC from acting on a particular matter if the short-term improvements can be justified. Particularly, ESMA recommends that the IFRS IC refrains from dismissing issues brought to its attention and that may lead to inconsistent application of IFRS requirements on the grounds that the IASB is planning to address them as part of a future broader project which may be far from its finalisation and whose outcome may still be uncertain. In our view, the dismissal of an issue for which the IFRS IC has identified relevant concerns for the consistent application of IFRS, should take place only when the standard-setting work to address that issue has already been initiated and it is expected to be finalized in the short-term.

Question 4—Consequential amendments to the IFRS Foundation Constitution

The Trustees of the IFRS Foundation have proposed to amend the IFRS Foundation Constitution as a result of the proposed amendments to the Handbook relating to the role of the IFRS Advisory Council.

Do you agree with these proposed consequential amendments?

34. ESMA agrees with the proposed amendments to the IFRS Foundation Constitution in relation to the role of the IFRS Advisory Council, however we note that the generic reference that is now made to the fact that the Council would be in charge of strategic

matters is not very informative on the exact scope of activities and therefore further clarifications would be useful.

35. We also note that while the role of the Advisory Council is no longer focused on technical matters, it is still consulted on the IASB's work plan which can be regarded as a strategic as well as a technical matter. While we agree to continue to consult the Advisory Council on the IASB's work plan, we question whether the composition of the Advisory Council may not be impacted by the fact that this body is expected to address strategic matters as well as, at least to the extent necessary to provide feedback on the work plan, also technical matters. This reinforces our suggestion to provide more clarity on the expectations on the strategic role of the Advisory Council and of its composition.

