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Accounting Standards Committee of Germany

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Mr Hans Hoogervorst
Chairman of the
International Accounting Standards Board
Columbus Building
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London E14 4HD

Berlin, 22 November 2019

Dear Hans,

IASB Exposure Daft ED/2019/6 *Disclosure of Accounting Policies - Proposed amendments to IAS 1 and IFRS Practice Statement 2*

On behalf of the Accounting Standards Committee of Germany (ASCG) I am writing to comment on the Exposure Daft ED/2019/6 *Disclosure of Accounting Policies - Proposed amendments to IAS 1 and IFRS Practice Statement 2* issued by the IASB on 1 August 2019 (herein referred to as 'ED'). We appreciate the opportunity to comment on the ED.

We appreciate the IASB's intention to help entities providing accounting policy disclosures that are more useful to primary users of financial statements and to eliminate immaterial accounting policy disclosures from their financial statements. We agree with the IASB's objective, since, in practice, accounting policy disclosures often only duplicate the requirements of IFRS Standards and, hence, only contain to a limited extent entity-specific information.

However, we do not believe that the objective will be achieved by replacing the requirement to disclose 'significant' accounting policies with a requirement to disclose 'material' accounting policies. In our opinion, the guidance provided should point out more clearly the distinction between a) those accounting policy disclosures that are relevant and, thus, shall be provided, and b) those disclosures that shall be omitted.

We welcome that the ED proposes guidance and examples to IFRS Practice Statement 2. However, these examples focus on the identification of accounting policy disclosures that contain only information that duplicates the requirements of IFRS Standards. We suggest the IASB equally provide positive examples illustrating the purpose of the proposed requirements (i.e. entity-specific accounting policy disclosures that provide relevant information to the users of the financial statements).

For the reasons above, we do not believe that the proposed amendments to IAS 1 and IFRS Practice Statement 2 will lead to changes in the practice of accounting policies disclosures.

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Our response to the ED questions is laid out in the appendix to this letter. If you would like to discuss our comments further, please do not hesitate to contact Ilka Canitz (canitz@drsc.de) or me.

Yours sincerely,

Andreas Barckow

President

Appendix – Answers to the questions in the ED

Question 1
The Board proposes to amend paragraph 117 of IAS 1 to require entities to disclose their 'material' accounting policies instead of their 'significant' accounting policies. Do you agree with this proposed amendment? If not, what changes do you suggest and why?

Whilst we are sympathetic to embedding the requirements of accounting policy disclosures into the concept of materiality, we doubt that merely changing terminology from 'significant' to 'material' is sufficient to change entities' behaviour.

Firstly, in many languages the words 'significant' and 'material' are often translated the same or very similarly, the understanding in both cases being that entities should (only) disclose 'important' policies that are necessary for primary users to understand the financials. In German, both 'significant' and 'material' would achieve that objective, so the suggested change in wording would likely not yield any tangible results. Secondly, we doubt that entities have misunderstood the meaning of 'significant'; rather, many may simply have sought to bypass the necessary use of judgment involved and may therefore have presented more accounting policy disclosures than necessary or warranted.

We therefore doubt that the proposed new paragraph 117 of IAS 1 stating that '*information about an accounting policy is material if, when considered together with other information included in an entity's financial statements, it can reasonably be expected to influence decisions that primary users of general purpose financial statements make on the basis of those financial statements*' would achieve the desired objective. Whilst we concur with the substance of that statement, we believe that it is too generic and missing a clear link as to how this principle would apply to accounting policy disclosures. We therefore doubt that the proposed amendments to IAS 1 and IFRS Practice Statement 2 will lead to changes in the practice of accounting policy disclosures.

In order to achieve the objective, we suggest the IASB investigate and clarify further:

- what the purpose of accounting policy disclosure requirements was, by providing a clear disclosure objective;
- which kind of accounting policy disclosures be considered as immaterial or 'boilerplate' in order to demonstrate which disclosure the IASB would not think to provide relevant information to primary users of financial statements;
- which accounting policy disclosures be provided, by including positive examples of entity-specific accounting policy disclosures (please refer to our answer to question 4); and
- to what extent primary users of financial statements should be assumed to have the knowledge about specific requirements in IFRS Standards. In other words: Providing some introductory notes in order to provide context may increase the understandability of entity-specific information provided in the notes.

Question 2
The proposed new paragraph 117A of IAS 1 states that not all accounting policies relating to material transactions, other events or conditions are themselves material to an entity's financial statements. Do you agree with this proposed statement? If not, what changes do you suggest and why?

We agree with the proposed statement of paragraph 117A of IAS 1 that accounting policies that relate to immaterial transactions, other events or conditions are themselves immaterial and need not be disclosed. We also agree with the proposed statement that not all accounting policies related to material transactions, other events or conditions are themselves material. In our opinion, the number of circumstances in which accounting policies related to material transactions would themselves not be material might be limited. We would therefore start from the opposite angle and assume that policies related to material transactions or events are, in principle, material to the understanding of the financial statements as well and should therefore be disclosed.

An issue the IASB might want to consider when improving the guidance proposed relates to information that may be judged to have been material last year but not in the current year. Whilst we believe that accounting policy disclosures shall not simply be rolled forward from one year to another, we suggest the IASB clarify that the materiality assessment is made in relation to the financial statements as a whole, i.e. including the (minimum) comparative information presented in accordance with paragraph 38 of IAS 1. This means, that accounting policies would also have to be disclosed if they were relevant to understand material <u>prior year</u> transactions, other events or conditions (even if such policies would be considered immaterial with respect to the current period's financial statements).

Question 3
The proposed new paragraph 117B of IAS 1 lists examples of circumstances in which an entity is likely to consider an accounting policy to be material to its financial statements. Do the proposed examples accurately and helpfully describe such circumstances? If not, what changes do you suggest and why?

The statement in the proposed new paragraph 117B of IAS 1 according to which '*An accounting policy is material if information about that accounting policy is needed to understand other material information in the financial statements*' is too broad and will therefore likely not contribute to the IASB's intention to enable entities to distinguish between material and immaterial accounting policy disclosures.

We support the inclusion of a list of examples of circumstances in which an entity is likely to consider an accounting policy to be material to its financial statements. However, the given list of examples covers a wide range of circumstances. Especially, the examples given in (d) (significant judgements or assumptions) and (e) (entity's specific application of the requirements of an IFRS Standard) apply to nearly all accounting policy disclosures. Further, we are not sure, which circumstances are thought to be covered by (e) that are not already covered by (d).

Therefore, the list of examples does not make clear which kind of accounting policy disclosures are 'boilerplate' and need not be disclosed. Hence, we do not believe that the proposed list of examples will lead to a focus on more relevant, entity-specific disclosures.

Question 4
The Board proposes to add to IFRS Practice Statement 2 two examples that illustrate how the concept of materiality can be applied in making decisions about accounting policy disclosures. Are these examples useful and do they demonstrate effectively how the concept of materiality can be applied in making decisions about accounting policy disclosures? If not, what changes do you suggest and why?

We support the addition of examples to IFRS Practice Statement 2 to illustrate how the concept of materiality can be applied in making decisions about accounting policy disclosures. However, the examples provided should not merely focus on the identification of accounting policies that can be omitted. Instead, we suggest providing positive examples demonstrating how to make materiality judgements and how to provide entity-specific disclosures.

The examples provided should point out the distinction between a) those accounting policy disclosures that are relevant and thus shall be provided, and b) those disclosures that shall be omitted. In our opinion, the examples provided so far are not helpful in drawing the line between material accounting policy disclosures and 'boilerplate' disclosures.

With respect to Example T, we do not follow the IASB's reasoning and would have reached the opposite conclusion, based on the facts provided. On the one hand, identifying the cash-generating units to which an asset belongs requires significant judgement. Hence, an accounting policy disclosure with respect to the identification of cash-generating units might (and generally would) provide useful information to the primary users of the entity's financial statements. We therefore conclude that the policy disclosure would have to be provided.

Furthermore, it might also be helpful to provide additional educational material (outside of the IFRS Standards) in order to demonstrate the nature and extent of accounting policy disclosures intended by the IASB.

Question 5
Would any wording or terminology introduced in the proposed amendments be difficult to understand or to translate?

'Significant' vs. 'Material'

We are aware of languages where the two terms 'significant' and 'material' are used and translated in the same way. In German, whilst both 'significant' as well as 'material' are translated using different words ('bedeutend' vs. 'wesentlich'), they are often used interchangeably when it comes to narrative reporting. 'Important' would be another word that may be used in this context. As said before, we doubt that the mere change in terminology will lead to any noticeable effect in disclosure behaviour, at least as far as our constituency is concerned.

Further, we do not completely agree with the IASB's statement that only materiality was an established concept: The use of 'significant' in the literature (cf. IAS 28's 'significant influence', for example) is equally evident, even though not defined as stringently as material. This might in itself create confusion as it may question what the IASB's objective for the proposed amendments would have been: We have heard some saying that a change from 'significant' to 'material' would constitute an *increase* in the level of disclosures, rather than a decrease. Bearing the use of the term 'significant' in the literature in mind, we can understand why some would come to that conclusion. Even if we do not concur with that view, it seems to demonstrate that the proposals might not be as clearly articulated as the IASB thinks they are.

Question 6
Do you have any other comments about the proposals in this Exposure Draft?

Missing reference to the concept of materiality (i.e. to paragraph 31 of IAS 1)

According to paragraph 31 of IAS 1, disclosure requirements in IFRS Standards are subject to the application of materiality, i.e. a disclosure that would otherwise be required by a Standard need not be provided if the information resulting from that disclosure is not material. Hence, under current IFRS it is already clear that the concept of materiality shall be applied to the disclosure of accounting policies.

Therefore, instead of requiring entities to disclose their 'material' accounting policies, we suggest requiring entities to disclose their accounting policies and including a reference to the concept of materiality in the proposed paragraph 117 of IAS 1. In doing so, confusion with respect to the wording can be avoided. Furthermore, the new requirements will be linked to the overarching concept of materiality included in paragraph 31 of IAS 1. Therefore, we suggest the following wording in the proposed paragraph 117 of IAS 1:

> 117 An entity shall disclose its ~~material~~ accounting policies, subject to the general concept of materiality per paragraph 31 of this Standard. Information about an accounting policy is material if, when considered together with other information included in an entity's financial statements, it can reasonably be expected to influence decisions.'

Immaterial accounting policies 'need not' be disclosed

According to the proposed new paragraph 117A of IAS 1, accounting policies that relate to immaterial transactions, other events or conditions are themselves immaterial and need not be disclosed. The IASB is proposing this amendment to help entities eliminate immaterial accounting policy disclosures from their financial statements (ref. paragraph BC10(a) of the proposed ED). Thus, the intention would be to encourage but not require eliminating immaterial disclosure.

However, the definition of materiality covers information that '*if omitting, misstating or obscuring it could reasonably be expected to influence decisions that primary users of general purpose financial statements make on the basis of those information*' (ref. paragraph 7 of IAS 1). Further, paragraph 7 of IAS 1 states that material information may be obscured if '*the understandability of the financial statements is reduced as a result of material information being hidden by immaterial information to the extent that a primary user is unable to determine what information is material*.'

General explanations within accounting policy disclosures might be helpful for primary users of financial statements. Therefore, we agree with the proposed wording of paragraph 117A of IAS 1 that immaterial accounting policies 'need not' be disclosed (instead of: 'shall not' be disclosed). However, as entities tend to present accounting policy disclosures that are too broad and contain entity-specific information only to a small degree, we suggest placing more emphasis on the IASB's intention to eliminate immaterial ('boilerplate') accounting policy disclosure.

Proposed consequential amendments to other IFRS Standards

According to the IASB, amendments to other requirements in IFRS Standards are not necessary (ref. proposed paragraph BC16 of IAS 1). Nevertheless, the ED is proposing some consequential amendments to other IFRS Standards. We presume that the IASB is proposing these amendments in order to align the wording to the proposed new paragraph 117 of IAS 1 ('material' instead of 'significant'). However, we wonder whether specific disclosure requirements of other IFRS Standards would not also be in need of being updated if these are requiring entities to disclose the accounting policies adopted.