EFRAG

European Financial Reporting Advisory Group

Disclosure Initiative (Proposed Amendments to IAS 1)

Feedback to constituents – EFRAG Final Comment Letter

August 2014

Introduction

Objective of this feedback statement

EFRAG published its final comment letter on the Exposure Draft ED/2014/1 *Disclosure Initiative (Proposed Amendments to IAS 1)* ('the ED') on 21 July 2014. This feedback statement summarises the main comments received by EFRAG on its draft comment letter and explains how those comments were considered by the EFRAG Technical Expert Group (EFRAG TEG) during its technical discussions leading to the publication of EFRAG's final comment letter.

Background to the Exposure Draft

The Agenda Consultation 2011 recommended that the IASB should review existing disclosure requirements in IFRS and develop a disclosure framework. In response to this and to the messages from the Disclosure Forum, the IASB started a Disclosure Initiative.

The initiative includes different work streams. The IASB staff presented at the March 2014 ASAF meeting two Research projects, one on materiality and one on a Disclosure Standard replacing IAS 1 *Presentation of Financial Statements*, IAS 7 *Statement of Cash Flows* and IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

Another work stream is a short-term project for narrow scope amendments to IAS 1 with the aim of avoiding a too strict interpretation of IAS 1.

On 25 March 2014, the IASB published for public comment an exposure draft containing a number of amendments to IAS 1, namely:

- Materiality: clarify that the concept of materiality applies to the specific disclosure requirements set out in Standards and that materiality applies to both the primary financial statements and the notes to the financial statements;
- Materiality: highlight that disclosing immaterial information can obscure the material information provided;
- Line items: clarify that the line items listed for inclusion in the primary financial statements can be disaggregated and should be disaggregated if that provides relevant information;
- Line items: include additional guidance to consider when an entity provides additional totals and subtotals in the statement of financial position and statement of comprehensive income;
- Notes: allow greater flexibility in the order of presentation of the notes;
- Significant accounting policies: remove the income taxes and foreign currency examples, which many constituents consider compulsory; and
- Presentation: clarify presentation of items of other comprehensive income arising from equity-accounted investments.

Further details are available on the EFRAG website.

EFRAG's draft comment letter

EFRAG published a draft comment letter on the proposals on 11 April 2014. In the draft comment letter EFRAG welcomed the Disclosure Initiative project set up by the IASB in 2013 that aims to review the disclosure requirements in existing Standards and to develop principles for disclosures in the notes.

Therefore, EFRAG supported this short-term project to change some of the terminology in IAS 1 that may have been interpreted too strictly. In EFRAG's view, this should enable entities to exercise more judgement in presenting and disclosing information and hence result in improving the quality and the relevance of disclosures in the notes to the financial statements.

However, EFRAG suggested a number of improvements in the wording of the proposed amendments in the ED.

Finally, EFRAG asked whether constituents believed that (a) the IASB should require that entities 'shall not' (rather than 'need not') disclose immaterial information, if the IASB wants to promote a change in behaviour; and (b) an entity should disclose only those accounting policies for which the entity was allowed a degree of discretion in choosing and applying the policy.

Comments received from constituents

Twelve comment letters were received from constituents and considered by EFRAG TEG in its discussions. These comment letters are available on the EFRAG website.

The comment letters received came from national standard-setters (eight), business organisations (three) and one regulator.

Almost all respondents welcomed the IASB's proposals in the ED and the overall message of the EFRAG draft comment letter. However, the majority of respondents that answered our questions did not agree with EFRAG's suggestion to prohibit disclosure of immaterial information.

Constituents also raised a number of minor concerns on the other topics covered by the amendments.

EFRAG's final comment letter

EFRAG issued its final comment letter on 21 July 2014. In its final comment letter, EFRAG remained broadly supportive of the IASB's proposals in the exposure draft.

However, EFRAG believed that the IASB should use language in the proposed amendments on materiality of disclosures that clarifies that an entity should carefully consider whether disclosures are material or not to users of financial statements even in circumstances where a Standard requires them.

Furthermore, regarding disclosures of accounting policies, EFRAG suggested stating that disclosure of accounting policies as a summary of a Standard is generally not useful. Useful disclosure provides insights into how the entity has exercised judgement in selecting and applying accounting policies.

Constituents did not raise significant new concerns on the other proposed amendments, and therefore those amendments are not described in detail in this feedback statement. Nonetheless, EFRAG incorporated comments and suggestions on the other proposals in the final comment letter.

The main differences between the comments made on the proposed amendments to IAS 1 on materiality of disclosures and on disclosures of accounting policies in the draft and final comment letter are explained in the section below.

Detailed analysis of the main issues, comments received and changes made to EFRAG final comment letter

Materiality of Disclosures

Summary of EFRAG's tentative position in its draft comment letter

These amendments aim to emphasise that entities shall not aggregate or disaggregate information in a manner that obscures useful information; and even when a Standard requires a specific disclosure, the resulting information shall be assessed to determine whether it is material.

In its draft comment letter EFRAG noted that paragraph 30A of the proposed amendments to IAS 1 states that an entity 'shall not' aggregate or disaggregate information that may reduce the understandability of financial information; whereas paragraph 31 states that an entity 'need not' provide a specific disclosure required by an IFRS where the information resulting from that disclosure is not material.

EFRAG tentatively thought that the use of 'need not' may fail to fully achieve the objectives of these amendments, as entities might continue to disclose immaterial information to remain on the 'safe side', i.e. not be reproached with non-compliance. Therefore, EFRAG believed that the IASB should use language that permits entities to fully exercise judgement and avoid any check-list compliance attitude in deciding what to disclose. In EFRAG's view, this would result in setting the level of compliance with disclosure requirements at a higher level than at present.

EFRAG asked its constituents whether they (a) agreed that to promote a change in behaviour, the IASB should require that entities 'shall not' (rather than 'need not') disclose immaterial information; and (b) identified any difficulty in practice in applying or enforcing this requirement.

Summary of the final position arrived at

Overall, in its final comment letter EFRAG remained supportive of the IASB's intention to improve existing guidance on materiality of disclosures pending the outcomes of its comprehensive project on the Disclosure Initiative.

However, EFRAG decided to improve the drafting of its comment letter to address its constituents' concerns. Accordingly, in its final comment letter EFRAG commented that IASB should clarify in paragraph 30A that even if a Standard requires certain disclosures, an entity should carefully consider whether these disclosures are material or not. This would encourage entities to omit information considered to be immaterial, without introducing a prohibition that may be difficult to enforce in practice.

Materiality of Disclosures

Constituents' comments

The majority of respondents while acknowledging the rationale and supporting EFRAG's initial position on the requirement to avoid disclosures of immaterial items, believed that the change proposed ('shall not' instead of 'need not') is too drastic, would not be operational in practice, and may result in adding pressure on preparers in producing financial information. Furthermore, it was noted that the exposure draft requires both a discussion of the concept of materiality and the concept of immateriality, respectively (and everything in between these two extremes). This will require additional guidance and a significantly changed mind-set of preparers of financial statements, auditors and enforcement bodies. Therefore, they believed that the IASB should address this issue within the context of the comprehensive disclosure project that includes the project regarding materiality.

Disclosures of Accounting Policies

Summary of EFRAG's tentative position in its draft comment letter

These amendments propose to remove paragraph 120 of IAS 1 that includes potentially unhelpful examples that do not illustrate why such disclosure on income taxes is significant.

EFRAG supported the IASB's proposals and noted that entities should disclose only those accounting policies that are both relevant to them and for which they are allowed a degree of discretion in choosing and applying the policy in circumstances where IFRSs permit alternatives. Accordingly EFRAG suggested that the IASB should improve the drafting of this amendment.

EFRAG asked its constituents whether they agree with the suggestion.

Constituents' comments

Respondents expressed mixed views.

Those supporting the EFRAG initial position believed that it would avoid boilerplate disclosures, enhance the relevance of financial information, and avoid the mere repetition of the known accounting methods already described in the Standards.

The other respondents believed that it is essential for the complete understanding of the financial statements that all the accounting policies are included. Some suggested dividing disclosures of accounting policies in different sections of the financial statements depending on whether they were prescriptive or an entity was allowed a degree of discretion in choosing and applying the policy.

Summary of the final position arrived at

EFRAG acknowledged that the way the question to constituents had been written could have been interpreted as a request to the IASB to require disclosures of accounting policies only in circumstances where a Standard requires an explicit choice to be made. Whereas, in EFRAG's view, disclosures are useful if they provide insight on how an entity selects and applies accounting policies.

Furthermore, EFRAG noted that many of its constituents considered that financial statements should include comprehensive descriptions of the accounting policies – including the static ones – that refer to amounts that are material.

Therefore, In its final comment letter, EFRAG recommended that the IASB should amend paragraph 119 of IAS 1 to state that disclosure of particular accounting policies as a summary of a Standard is generally not useful.

In EFRAG's view, disclosure of accounting policies are useful only if they provide insights into the judgements that an entity has exercised in selecting and applying them.

List of respondents

Accounting Standards Committee of Germany (ASCG)

Dutch Accounting Standards Board (DASB)

Instituto de Contabilidad y Auditoría de Cuentas (ICAC)

Financial Reporting Council (FRC)

Norwegian Accounting Standards Board (NASB)

Organismo Italiano di Contabilita' (OIC)

European Securities and Markets Authority (ESMA)

Autorité des Normes Comptables (ANC)

Association pour la participation des entreprises françaises à l'harmonisation comptable international, Association française des enterprises privée, Mouvement des Entreprises de France (ACTEO, AFEP, and MEDEF)

Danish Accounting Standards Committee (DASC)

German Insurance Association

Insurance Europe