

JOINT USER OUTREACH EVENT

IASB DISCUSSION PAPER DISCLOSURE INITIATIVE – PRINCIPLES OF DISCLOSURE

SUMMARY REPORT

BRUSSELS

3 JULY 2017



Introduction

EFRAG, together with the European Federation of Financial Analysts Societies (EFFAS), the Belgian Association of Financial Analysts (ABAF/BVFA) and the IASB, organised a User Outreach event in Brussels, Belgium on 3 July 2017 covering the IASB's Discussion Paper DP/2017/1 *Disclosure Initiative - Principles of Disclosure* (the 'IASB DP'). This report has been prepared for the convenience of European constituents.

The joint outreach event was one of a series organised across Europe following the publication of the IASB DP and was focused on user views. The purpose of the outreach event was to:

- stimulate the debate in Europe;
- understand users' needs, in particular from those that did not intend to submit a comment letter to EFRAG or the IASB, and their main concerns;
- receive input from users of financial statements for EFRAG, EFFAS and ABAF/BVFA comment letters to the IASB; and
- learn to what extent the preliminary comments as set out in EFRAG's draft comment letter are shared by users and other constituents that attended the meeting.

Jean-Paul Gauzès (EFRAG Board President) opened the outreach event and welcomed the speakers and participants. Fred Nieto (IASB Head of Investor Engagement) and Mariela Isern (IASB Senior Technical Manager), presented the IASB DP. Thereafter Andrew Watchman (EFRAG TEG Chairman) summarised EFRAG's tentative views on the IASB DP.

This was followed by a round-table user panel discussion featuring users and interactive discussion with audience, moderated by Patricia McBride, EFRAG Technical Director. The user panel included:

- Kazim Razvi, Director Accounting Research & Policy at Fitch Ratings, Member of EFRAG Pension Plans Advisory Panel
- Lothar Weniger, Financial adviser at ALIAG, Member of CRUF Germany, Member of IFRS Advisory Council
- Javier de Frutos, Chairman EFFAS Financial Accounting Commission

The presentation slides and key elements mentioned in the presentation can be found on EFRAG's Website ([here](#)).

Summary of observations

Participants at the event expressed the following views:

- Principles can be useful to improve communication. The focus should be on increasing transparency, consistency and comparability of information and such principles should be made mandatory.
- Sound communication principles are needed to cater for the wider set of circumstances and financial innovation, but there is also a need to strike an appropriate balance between general principles and more detailed and prescriptive guidance (such as a minimum set of disclosures) to ensure consistency and comparability across entities and industries.
- The implications of developments in technology on the presentation of financial statements and disclosures need also to be considered. However, this does not reduce the need to improve the structure, format and presentation of information in the notes to ensure that companies communicate more effectively.
- Cross-references are useful to avoid unnecessary duplication of information or to present some unchanging information. However, safeguards on the stability of the information and the links over time are needed. Beyond year-end reporting, there is also a need to consider how other periodic information provided by management to users (e.g. quarterly reports) could be better linked to ensure consistency in the context of continuing reporting to users.
- The use of non-IFRS information should not be restricted as long as the information is explained and reconciled. Guidance to discipline the use is needed so that users are able to understand how the information is generated and how it reconciles with IFRS measures.
- There could be merits in the IASB to providing principles to determine some commonly-used measures such as EBIT and EBITDA. However, it is doubtful whether a single definition can be arrived at.
- Separate presentation of unusual and infrequently occurring items is a common practice and provides useful information; provided that events or transactions referred to are genuinely unusual or infrequent. Guidance should aim at preventing abuses and providing complete and transparent information about the transactions and events and the assessments made by management.
- The application of materiality is essential in determining what information to disclose and how to present it. It is in particular essential that no relevant information is omitted. Maintaining a dialogue with auditors and regulators is also important in that respect.

Opening comments and presentations

Opening and welcome

Jean-Paul Gauzès opened the outreach event and welcomed the participants, he invited user panellists and the IASB staff. He highlighted some of the key disclosure concerns, EFRAG's contribution to addressing the concerns and the importance of the IASB work on *Better Communication* and how EFRAG would use the feedback received in the event.

Presentation of the IASB Discussion Paper *Disclosure Initiative – Principles of Disclosure*

Fred Nieto highlighted the importance of the feedback received in the outreach activities, introduced the different projects under the theme of *Better Communication* and how these projects were interrelated. Subsequently, Mariela Isern provided an overview of the IASB DP.

The presentation slides and key elements mentioned in the presentation can be found on [EFRAG's Website](#).

Presentation of EFRAG's tentative views on the IASB DP

Andrew Watchman started by providing a brief history of the disclosure problem and referred to some European past initiatives. He subsequently summarised EFRAG's tentative views on the IASB DP and the importance of the outreach activities for EFRAG's final comment letter.

The presentation slides and key elements mentioned in the presentation can be found on [EFRAG's Website](#).

Panel discussion

Patricia McBride welcomed the panellists and opened the debate.

Main comments received

Can principles make communication more effective?

The panellists expressed support for the IASB's initiative to develop principles of effective communication. Such principles were all the more called for in the context of a fast-changing business environment.

The panel members emphasised the importance of having financial statements that provide consistent, transparent and

Communication principles can be helpful to improve transparency, consistency and comparability.

comparable information across periods and companies in the same industry. In particular:

- one panellist highlighted the importance for users to understand how numbers in the financial statements have been generated and to reconcile that information across the different statements (statement of financial position, statement of financial performance and statement of cash flows) which is not always possible today.
- one panellist observed that the content and structure of financial statements of entities within the same industry could vary significantly, including the labelling of line items on the face of the financial statements. This panel member called for more guidance on the format of the primary financial statements to improve comparability (e.g. minimum set of line items).

Panellists generally considered that, to be effective, some of the proposed principles should be made mandatory in particular those aiming at greater transparency and comparability.

One panellist however noted that there was a downside to a principle-only approach insofar as it involved the exercise of judgement. Therefore, there should be an appropriate balance between high-level principles and more prescriptive guidance (e.g. minimum set of disclosures) to ensure consistency and comparability across entities and industries.

Two panellists observed that the communication issue was not limited to the year-end financial statements and that entities generally provide information to users on a more frequent basis (e.g. earnings releases, quarterly reporting). There was a need to have the same principles of effective communication applied to the continuous stream of information.

One participant observed that all panellists had underlined the importance of comparable information. He noted that the European Accounting Directive included layouts for financial statements and highlighted the work of the Basel Committee Working Group on Disclosures, set up to ensure that disclosure initiatives for Pillar 3 are coordinated and consistent.

Disclosures about accounting policies should not be a mere reproductions or summaries or IFRS Standards.

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

One panellist provided participants with a number of examples of disclosures of listed companies and explained why, in his view, these disclosures provided useful information. The examples illustrated in particular:

- appropriate level of disaggregation of information and the presentation of directly readable intermediate subtotals; and
- the presentation of accounting policies in the same notes as the information to which they relate (rather than in single note).

Panellists generally considered that disclosures about accounting policies were more useful when they were not a mere reproduction or a summary of an IFRS Standard but provided insights into how the entity has exercised judgement in selecting and applying accounting policies. In particular, the following comments were made:

- it was important to keep information about past accounting policies (not just the effect of the year-on-year changes) but this would not need to be done within the financial statements.
- the description of accounting policies that have not changed, do not involve significant judgement or contain options could be presented outside the financial statements (e.g. entity's website).
- presenting accounting policies in the same notes as the information to which they relate is more useful.

One panellist noted that there was also a need for more consistent disclosures about transactions that are not specifically addressed in existing IFRS literature and he gave the example of reverse factoring transactions. This was the reason why disclosure principles (rather than rigid rules) were all the more needed to cater to a wider set of circumstances and financial innovation.

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?

Increased use of technology should be considered but this does not reduce the need to improve the structure, quality and presentation of information in the notes.

Panellists were generally relatively indifferent as to whether information is presented on the face of the primary financial statements or in the notes as long as it was there.

They noted the increased use of technology in financial reporting and considered that the IASB should analyse the implications. In particular:

- one panellist observed that although technology was increasingly used to access information, the situation was not yet that of fully digitalised information. There would be a long transition period and in the meanwhile it was important to have a suitable structure for the notes to facilitate access to information.
- one participant recalled that European listed companies would have to prepare their annual financial statements under a European Single Electronic Format as soon as 2020. Other regulatory developments were taking place across jurisdictions and it was important to consider their interactions. This participant expressed concerns that the XBRL technology being considered by the European Union was somewhat outdated and that new solutions could work better with mobile devices such as smartphones and tablets.

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

Cross-references are useful to avoid duplication of information but stability of linked information over time is essential.

Panellists generally supported the use of cross-references to avoid unnecessary duplication of information or to present some standing information such as accounting policies that have not changed or have become irrelevant. However, safeguards would be needed on the stability of the information and of the links over time.

One panellist stated that, in addition to the incorporation by reference of IFRS information placed outside of the financial

statements (as envisaged by the IASB), there were other aspects of cross-referencing to consider:

- the need to link information presented in the primary financial statements and in the notes; and
- the need to link periodic information (e.g. quarterly and semi-annual reports with annual report) so as to ensure a form of continuous reporting.

Should ‘non-IFRS information’, such as Alternative Performance Measures, be permitted within the financial statements? Are they misleading or useful?

The use of non-IFRS information should not be prohibited or restricted in financial statements but guidance is needed to discipline the use.

Panellists considered that non-IFRS information is useful for investors as it provides the management’s view of performance and the IASB should not prohibit their use within financial statements as long as the information is explained and reconciled.

Furthermore, bringing non-IFRS information into the financial statements could have the benefit of having more consistency and discipline on their use.

Panellists expressed concerns about the lack of transparency about the determination of some performance measures not specified in IFRS Standards and, in that respect, the proposed guidance could help provide some discipline in their use. In particular, panellists considered that:

- there should be a clear distinction between IFRS and non-IFRS information in the financial statements; and
- non-IFRS information has to be transparent, consistent and understandable and reconciled to IFRS information.

One panellist observed that a distinction should be made between performance measures and other measures of activity (e.g. same-store sales) that provide a different measure of performance that supplements, but is not in competition with, IFRS information.

Should EBITDA be permitted or required in the financial statements?

Panellists observed that some metrics, such as EBITDA or EBIT, are widely used while others are very industry specific. There could be merits for the IASB to provide guidance on commonly used measures such as EBIT/EBIDTA so as to ensure consistency and comparability.

One participant, while appreciating the work done by the IASB, in particular in the context of the *Primary Financial Statements* project, expressed doubts as to whether it would be possible for the IASB to define EBIT and EBITDA. Rather the IASB should focus on developing principles and general guidelines that would help entities determine such metrics.

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

Separate presentation of unusual and infrequently occurring items provides useful information. Guidance is needed to avoid misuses of the concept.

Panellists acknowledged that separate presentation of unusual and infrequently occurring items is a common practice. They considered this information to be useful, because it helps them to assess the recurring/sustainable performance and make assessments about the future, provided that events or transactions referred to are genuinely unusual or infrequent.

Panellists considered that information about unusual and infrequent items is sensitive and involved significant judgement.

Therefore, providing principles to discipline the presentation of such information and the related disclosures is important. Although it would be difficult to try and define what non-recurring or unusual is, panellists considered that guidance is needed to avoid misuses of the concept. They noted that often, only events or transactions with negative effects tended to be adjusted and that some of these expenses labelled as infrequent (e.g. restructuring costs) sometimes appeared recurrently.

One panellist reminded that it was important that the infrequent or unusual nature of an event or transaction be assessed at the group level and that the effects be presented separately (or disclosed in the notes) not just in the statement of financial performance but also in the other statements (in particular the statement of cash flows) which was not always the case.

How important is the application of materiality when deciding what and how to disclose information?

The application of the materiality concept is key to ensure that relevant financial information is provided in a timely manner

Panellists concurred that the application of materiality was key in determining what and how to disclose information. They considered that difficulties or unwillingness to exercise judgement in determining which information to disclose was contributing to the disclosure overload.

One panellist noted that it is often easier for management to include immaterial information in the financial statements rather than monitor on an ongoing basis whether that information is material and/or justify the removal of disclosures to auditors or regulators. This could lead to obscuring, intentionally or not, useful information.

One panellist, while agreeing with the above assessments, raised concerns about the highly judgmental nature of materiality assessments. There was a risk that, if not properly applied, it could lead to omission or late communication of relevant information. Therefore, there was a need for an appropriate balance between that general principle and, in some cases, more prescriptive guidance about the information to disclose. It was also important to maintain a dialogue with auditors, regulators and users on the matter.

As the issue is largely behavioural, one participant doubted whether the non-mandatory guidance expected to be included in the forthcoming IASB's *Materiality Practice Statement* would be effective in addressing the issue. The IASB staff replied that the decisions to issue non-mandatory guidance was taken because it was considered that adding mandatory requirements in a Standard could risk creating conflicts with local legal or regulatory frameworks and could undermine the emphasis on entities applying their judgement in the assessment of materiality.

Concerns have been raised about the disclosures in IFRS 13 *Fair Value Measurement*. Do you think the principles in the DP will address those concerns?

Aggregation of fair value disclosures for dissimilar items (e.g. realised and unrealised gains) is a concern.

Panellists generally considered that disclosures about the determination of fair value could be improved. In particular, one panellist expressed concerns about the need to distinguish realised gains from unrealised ones, for level 1 and 2

measurements, and to not aggregate gains and losses of different nature.

It was reminded that EFRAG was launching the same day a call for evidence on IFRS 13 disclosure in the form of online questionnaires including a separate questionnaire for users, and participants were invited to respond to that questionnaire.

One participant asked whether users would like to have a separate presentation of realised and unrealised gains and losses in the financial statements. One panellist replied that this was important information in particular for the determination of distributable reserves. He referred to the latest discussions of the IASB on possible amendments to IAS 7 *Statement of Cash Flows* (regarding restrictions affecting an entity's decisions to use cash for distributions) and to the UK FRC Lab Report *Disclosure of dividends – policy and practice*.

Conclusion - Closing remarks

Jean-Paul Gauzès thanked the panellists and participants in this event for the valuable feedback, which will be considered by EFRAG in the drafting of its final comment letter.