European Financial Reporting Advisory Group

EFRAG, ANC & FRC Discussion Paper: *Towards a Disclosure Framework for the Notes*

Frankfurt, 13 November 2012

Background to the Project

Why we have issued this Discussion Paper

- The objective of the Disclosure Framework is to ensure that <u>all</u> and <u>only</u> relevant information is disclosed in an appropriate manner, so that detailed information does not obscure relevant information in the notes to the financial statements.

- The Discussion Paper aims at:

Identifying relevant disclosures in the notes to the financial statements;

discussing what materiality means from a disclosure perspective; and

developing a set of principles for good communication of disclosures.

- The comment period on the DP closes on 31 December.

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Towards a Disclosure Framework for the Notes

DISCUSSION PAPER

JULY

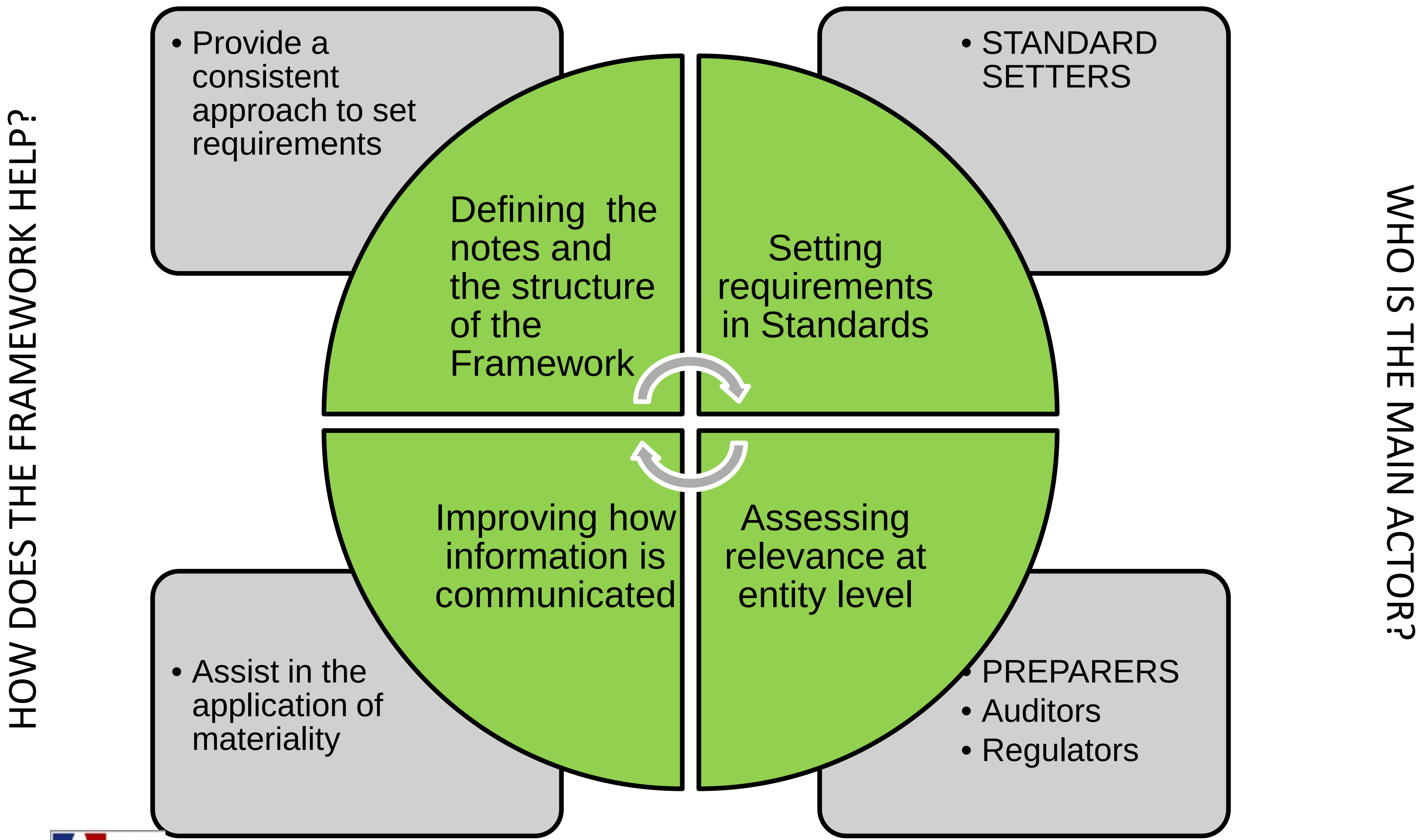
2012

Key Principles in the Discussion Paper

- A number of Key Principles have been identified in the Discussion Paper on:
  - Purpose and content of the notes
  - Setting the disclosure requirements
  - Applying the disclosure requirements
  - Communicating information.

Key Principles are detailed in slides at the back.

Overview of the Framework



Definition

Considers new definition:

The purpose of the notes is to provide relevant description of the items presented in the primary financial statements and of unrecognised arrangements, claims against and rights of the entity that exist at the reporting date.

Definition

b. 'description' means that notes are supposed to provide quantitative descriptions of the items (e.g. breakdowns, maturity analysis) as well as qualitative descriptions of these items (e.g. accounting policies, judgements) which amplify and explain the primary financial statements;

Setting the requirements

Notes provide information on			
Aggregation/ disaggregation of line items	What the item is	How the item fits in the entity's operations and financial structure	How the item has been accounted for

Proposed indicators to assess when each information is relevant

Disclosure tools considered

Breakdowns(disaggregation)

Roll-forwards

Maturity analysis

Description

Accounting policies

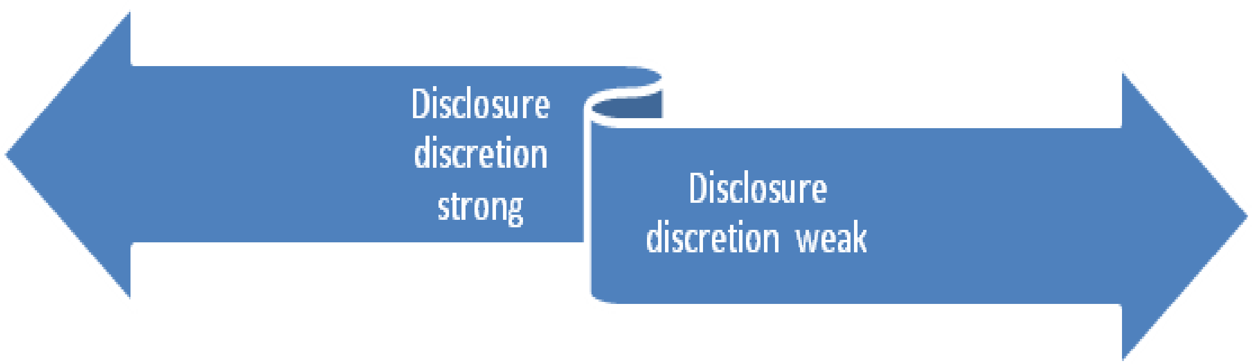
Measurements inputs and uncertainties

Unrecognised items

Alternative measures

Setting requirements – different approaches

Range of alternatives				
Preparers have complete discretion on disclosures.	Standard setters define general objectives only.	Disclosures tailored to specific industry.	A single set of requirements for all items and transactions.	Detailed requirements for all class of items and transactions.



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Differential disclosure regimes

Possible approaches to differential regimes:		
• Based on relative importance of item	• Based on type of entity	• Based on other factors

Pros	Cons
More flexibility of requirements to reflect users' needs Can achieve better cost/ benefit balance Complements materiality principle that does not work as it should be	Finding suitable differentiating criteria that fulfill users' needs in different circumstances

Applying the requirements

- The Discussion Paper suggests that if an item is material, that does not necessarily mean that all disclosure requirements relating to that item are also material.

Applying the requirements

What we have said

- Materiality plays an important role in disclosures. Disclosure of immaterial information reduces the effectiveness of disclosures.

BUT: could a Framework explicitly prohibit the disclosure of immaterial information?

- Should a Framework include specific guidance to assess materiality?

- The Framework includes indicators to guide the assessment of materiality.

Communicating information

- Quality of disclosures is not only about the “what” is disclosed, but also “how”. Information in the notes should meet these principles:

Be entity-specific	Be current
Inform and explain the substance of transactions	Be organised
Be clear, balanced, concise and written in plain language	Be linked

Communicating information

The DP discusses merits of prioritisation of information versus standardisation, with no conclusive support for one or the other.

Standardised presentation	Prioritised presentation
More consistency between entities and across time	Prominence to most important information
Less subjective	More flexibility
Easier to apply – no reassessment required	

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Key Principles in detail

Purpose and content of the notes	
Given the purpose of the notes, the disclosures in the notes should: o provide information which amplifies and explains the primary financial statements; o focus on past transactions and other events existing at the reporting date (no information about the future that is unrelated to past transactions); o be entity-specific.	As a complement to reported numbers in primary statements, notes should provide information such as (but not limited to) assumptions and judgments built into the reported numbers; risks that may affect these reported numbers; and relevant alternative measurements. It is necessary to consider the implications of recognition and measurement attributes to assess the usefulness of information as a whole. In particular, the more uncertainty affects the amounts in the primary statements, the more disclosures are usually needed.

Key Principles in detail

Setting disclosure requirements	
Disclosure needs to be an objective distinct from other objectives, specifically from recognition, measurement and presentation. Disclosure requirements should: o be developed and justified with the same level of depth and scrutiny as recognition, measurement and presentation requirements; o be set in a consistent manner across the whole set of accounting standards, including the level of granularity; o be principle-based and avoid detailed rules.	Disclosure requirements should achieve proportionality to the entity's users' needs, and meet a reasonable cost-benefit trade-off in all circumstances. Alternative disclosure regimes may have to be put in place to achieve proportionality. Disclosure requirements should not be used to compensate for inadequacies in other requirements. Disclosure requirements should be set as to avoid any possible overlap within notes and reviewed over time to eliminate requirements that are no longer relevant.

Key Principles in detail

Applying the requirements
Care should be taken in applying the materiality principle in practice, bearing in mind that disclosing immaterial information (and information on situations that do not apply in practice to the reporting entity) reduces the relevance and the understandability of disclosures.

Communicating information
Disclosure requirements should be applied with a view to communicating information to users rather than a compliance exercise.