EFRAG
European Financial Reporting Advisory Group

# Draft Comment Letter

**Comments should be submitted by 12 May 2014 to commentletters@efrag.org**

[xx May 2014]

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

28.Sitzung IFRS-FA am 23.06.2014
28_04d_IFRS-FA_EFRAG_DCL_27_05c

Dear Sir/Madam,

**Re: *Disclosure Initiative (Amendments to IAS 1)***

On behalf of the European Financial Reporting Advisory Group (EFRAG), I am writing to comment on the exposure draft, ED/2014/1 *Disclosure Initiative (Amendments to IAS 1),* issued by the IASB on 25 March 2014 (the 'ED').

This letter is intended to contribute to the IASB's due process and does not necessarily indicate the conclusions that would be reached by EFRAG in its capacity as advisor to the European Commission on endorsement of definitive IFRS in the European Union and European Economic Area.

EFRAG welcomes 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 supports this first short-term project to change some of the terminology in IAS 1 *Presentation of Financial Statements* 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 relevance of disclosures in the notes to the financial statements.

Our detailed comments and responses to the questions in the ED are set out in the Appendix. To summarise, EFRAG agrees with the proposals in the ED, but we suggest a number of improvements in the wording as explained below.

If you would like to discuss our comments further, please do not hesitate to contact Giorgio Acunzo or me.

Yours faithfully,

Françoise Flores
**EFRAG Chairman**

## APPENDIX

### EFRAG's responses to the questions raised in the ED

**Question 1 – Disclosure Initiative amendments:**

The amendments to IAS 1 arising from the Disclosure Initiative aim to make narrow-focus amendments that will clarify some of its presentation and disclosure requirements to ensure entities are able to use judgement when applying that Standard. The amendments respond to concerns that the wording of some of the requirements in IAS 1 may have prevented the use of such judgement.

The proposed amendments relate to:

(a) materiality and aggregation (see paragraphs 29-31 and BC1-8 of this Exposure Draft);

(b) statement of financial position and statement of profit or loss and other comprehensive income (see paragraphs 54, 55A, 82, 85A and 85B and BC9-BC15 of this Exposure Draft);

(c) notes structure (see paragraphs 113-117 and BC16-BC19 of this Exposure Draft); and

(d) disclosure of accounting policies (see paragraphs 120 and BC20-BC22 of this Exposure Draft).

Do you agree with each of the amendments? Do you have any concerns about, or alternative suggestions for, any of the proposed amendments?

### EFRAG's general comments

**EFRAG believes that short-term improvements to disclosures requirements are warranted and therefore appreciates the IASB's short-term project within the Disclosure Initiative.**

1 EFRAG welcomes the IASB's initiative to clarify the existing guidance in IAS 1 *Presentation of Financial Statements* that was perceived to be overly prescriptive if read and applied too literally. In their Discussion Paper *Towards a Disclosure Framework for the Notes*, published in July 2012, EFRAG, the ANC and the FRC noted that immediate action was needed to ensure that only relevant information is provided in the notes.

2 Furthermore, as noted in our comment letter on the discussion paper *A Review of the Conceptual Framework for Financial Reporting* issued in February 2014, EFRAG believes that good communication is essential to achieve relevance and faithful representation and to avoid obscuring relevant information.

3 EFRAG's responses to the questions raised in the exposure draft ED/2014/1 *Disclosure Initiative (Amendments to IAS 1)* (the 'ED'), are provided below.

### Materiality

*Notes to constituents*

*4 The IASB acknowledged that the concept of materiality of information is not being applied in practice as well as it could be and that this is one of the problems with disclosures: on the one hand there is too much irrelevant information that is being* *disclosed while on the other hand there is not enough relevant information being disclosed in the financial statements.*

5 *The IASB understood that these misconceptions may have arisen because of the wording of the presentation or disclosure requirements in IAS 1.*

6 *Therefore, the IASB proposes to amend the materiality requirements in IAS 1 to emphasise that:*

(a) *entities shall not aggregate or disaggregate information in a manner that obscures useful information;*

(b) *the materiality requirements apply to the statement of financial position, the statement of profit or loss and other comprehensive income, the statement of changes in equity, the statement of cash flows and to the notes; and*

(c) *when a Standard requires a specific disclosure, the resulting information shall be assessed to determine whether it is material and consequently whether presentation or disclosure of that information is warranted.*

7 *The IASB noted that some recent Exposure Drafts (e.g. on Insurance Contracts and on Leases) have included wordings that highlighted these points.*

8 *Finally, in addition to the narrow-focused amendments to the materiality requirements in IAS 1, the IASB will be undertaking a short-term project in its Disclosure Initiative to assess the existing guidance on materiality. That assessment could result in additional guidance or education material being produced on materiality.*

**EFRAG's response**

**EFRAG welcomes these proposed amendments that enhance the entities' ability to apply judgement in presenting and disclosing relevant information but believes that the drafting should be improved.**

9 In their Discussion Paper *Towards a Disclosure Framework for the Notes* issued in July 2012, EFRAG, the ANC and the FRC argued that (a) disclosures should not be required if the information is immaterial; and (b) disclosures should not be required for every line item presented in the primary financial statements unless the information would be material.

10 Therefore, EFRAG welcomes the proposed amendments as they improve the application of the materiality principle to the primary financial statements and the notes.

11 In EFRAG's view, entities should be allowed to use judgement when complying with the disclosure requirements in the Standards; they should be allowed to assess whether the resulting financial information is useful to users or whether it reduces the understandability of the financial statements by overwhelming useful information with immaterial disclosures.

12 However, we believe that the drafting of these amendments should be improved in some areas:

(a) Paragraph 5 of the Basis for Conclusions clarifies that the definition of what is material already incorporates the notions of individual and collective assessment. EFRAG believes that this should also be incorporated in paragraph 31;

(b) The IASB should clarify whether, in assessing materiality, an entity should consider only the current period or all the periods presented in the financial statements; and

(c) Paragraph 30A 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 thinks 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. EFRAG believes that the IASB should use a language that both permit entities to fully exercise judgment 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 different level of what it is currently done. Accordingly, we believe that the wording of paragraph 31 should be made consistent with paragraph 30A and refer to 'shall not'.

**Question to constituents**

13 Do you share EFRAG's view that to promote a change in behaviour, the IASB should require that entities 'shall not' (rather than 'need not') disclose immaterial information? If no, please explain.

14 Do you identify any difficulty in practice in applying or enforcing this requirement? Please explain.

**Information to be presented**

*Notes to constituents*

Information to be presented in the statement of financial position and in the statement(s) of profit or loss and other comprehensive income

15 *The IASB acknowledged that the requirements in paragraph 54 of IAS 1 have been interpreted as a prescriptive list and that the line items listed cannot be disaggregated.*

16 *The IASB noted that paragraph 55 of IAS 1 requires an entity to present additional line items, headings and subtotals if their presentation is relevant to an understanding of the entity's financial position. This highlights that the line items currently listed for presentation in paragraph 54 of IAS 1 should be disaggregated and that subtotals should be presented, when relevant.*

17 *Therefore, the IASB proposes to:*

(a) *remove the wording "as a minimum" from paragraph 54 of IAS 1 to address the possible misconception that this wording prevents entities from aggregating the line items specified in paragraph 54 of IAS 1 if those specified line items are immaterial;*

(b) *include an example of a disaggregation of a line item specified in IAS 1 to highlight that the line items listed for presentation in the statement of financial position should be disaggregated when such a presentation is relevant to an* *understanding of the entity's financial position. It also proposes to clarify that the presentation requirements in paragraph 54 of IAS 1 may be fulfilled by disaggregating a specified line item; and*

(c) *make consistent amendments to requirements on presentation for the statement(s) of profit or loss and other comprehensive income, where appropriate.*

<u>Presentation of subtotals in addition to those specifically required by IAS 1</u>

*18 The IASB was also informed that there is a perception by some that IFRS prevents them from presenting subtotals in addition to those specifically required by IAS 1.*

*19 The IASB noted that paragraphs 55 and 85 of IAS 1 require the presentation of subtotals when such presentation is relevant to an understanding of the entity's financial position or financial performance.*

*20 Therefore, the IASB proposes to amend the requirements for presentation in the statement of financial position and in the statement(s) of profit or loss and other comprehensive income, by clarifying that subtotals should:*

(a) *be understandable. It should be clear from the way a subtotal is presented and labelled, what line items are included in it;*

(b) *be consistent from period to period. That is, the subtotal should be consistently presented and calculated from period to period, subject to possible changes in accounting policy or estimate assessed in accordance with IAS 8* Accounting Policies, Changes in Accounting Estimates and Errors*; and*

(c) *in the statement(s) of profit or loss and other comprehensive income, not be displayed with more prominence than the subtotals and totals specified by paragraphs 81A-81B of IAS 1. In addition, to help users of financial statements understand the relationship between the subtotals presented in accordance with paragraph 85 and the totals and subtotals specified in IAS 1, the IASB proposes that entities should present line items, subject to the materiality requirements in IAS 1, that reconcile those subtotals with those that are specifically required by IFRS.*

**EFRAG's response**

| |
|---|
| **EFRAG agrees with the proposed amendments but believes that the drafting should be improved.** |

21 EFRAG supports the proposal to improve the wording in IAS 1 to ensure that it is not perceived as a prescriptive list of line items that needs to be presented separately and cannot be disaggregated. Therefore, we support the clarification that line items should be disaggregated when it is relevant to understand the entity's financial position and performance.

22 However, we are concerned that, even after removing 'as a minimum', the language in paragraph 54 ('The statement of financial position shall include line items that present the following amounts') could still be interpreted as requiring the separate presentation of the listed items. Therefore, we would suggest to add 'when material' in the paragraph 54.

23 Furthermore, we note that the current drafting of paragraph 82 ('In addition to items required by other IFRSs') is not consistent with the proposed wording in

paragraph 54. We believe that the IASB should make the wording of these paragraphs consistent.

24 We support the proposed clarifications regarding the use of subtotals in the financial statements. However, we are concerned that paragraphs 55A and 85A ('be consistent from period to period') may be read to imply that after an entity chooses the structure of its statement of financial position and of its the statement(s) of profit or loss and other comprehensive income, it is not allowed to change them in future periods. The IASB explains in paragraph BC14(b) of the ED that changes would be possible in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors.* We suggest adding a reference to IAS 8 in paragraphs 55A and 85A.

25 Furthermore, EFRAG notes that entities should be able to justify and document their choice of presenting additional sub-totals. The inclusion of sub-totals should not be detrimental to the presentation of financial information that faithfully represents all the phenomena that affected the entity's financial position, its cash flows and its performance.

26 Finally, EFRAG encourages the IASB to promptly address other issues, including the use of non-IFRS financial information in the notes.

**Structure of the notes**

*Notes to constituents*

*27 The IASB acknowledged that there is a perception by some that paragraph 114 of IAS 1 requires a specific order for the notes.*

*28 The IASB considered the use of the word 'normally' in paragraph 114 of IAS 1 and concluded that it was not intended that entities be required to disclose their notes in the order listed in paragraph 114 of IAS 1.*

*29 Therefore, the IASB proposes to amend the requirements regarding the structure of the notes by:*

(a) *emphasising that the understandability and comparability of its financial statements should be considered by an entity when deciding the systematic order for the notes; and*

(b) *clarifying that entities have flexibility as to the systematic order for the notes, which does not need to be in the order listed in paragraph 114 of IAS 1.*

**EFRAG's response**

**EFRAG agrees with the proposed amendments but believes that the drafting should be improved.**

30 EFRAG agrees that an entity should present notes in a systematic manner that ensures the understandability and the comparability of its financial statements. Accordingly, we support the IASB's proposals to clarify current guidance in IAS 1 that was read as a prescriptive order of the notes.

31 However, we believe that the IASB should improve the drafting of these amendments by requiring that in ordering the notes 'in a way that gives prominence to disclosures that it views as more relevant to an understanding of its financial position or financial performance or makes the relationship between some disclosures more understandable', entities should preserve a neutral depiction of

financial information. In EFRAG's view, the order of the notes that the entity chooses should not be detrimental to the presentation of financial information that faithfully represents all the phenomena that affected its financial position, its cash flows and its performance.

**Disclosure of accounting policies**

*Notes to constituents*

*32 The IASB acknowledged that the use of an income taxes accounting policy in paragraph 120 of IAS 1 as an example of a policy that users of financial statements would expect to be disclosed is not helpful because the example does not illustrate why an accounting policy on income taxes is significant.*

*33 Therefore, the IASB proposes to remove paragraph 120 of IAS 1 that includes potentially unhelpful examples.*

**EFRAG's response**

**EFRAG welcomes the proposed amendment, which removes examples of accounting policies that entities felt compelled to disclose even if it did not result in relevant information.**

34 EFRAG welcomes the IASB's proposals to delete paragraph 120 of IAS 1 that was read to be an overly prescriptive requirement.

35 However, we believe 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.

36 EFRAG understands that some believe that it should be possible to read financial statements as a self-contained document, i.e. including all significant accounting policies, regardless of whether they result from a choice. However, when an entity merely reproduces parts of the existing Standards this sometimes has little or no information value.

37 Finally, we welcome that the IASB is allowing entities in paragraph 113A to group accounting policies together with the other disclosures that relate to them. In EFRAG's view, this may help users in reading and understanding financial information also when it is disclosed in a detailed fashion.

**Question to Constituents:**

38 Do you agree that an entity should disclose only those accounting policies for which the entity was allowed a degree of discretion in choosing and applying the policy? Please explain.

**Presentation of items of other comprehensive income arising from equity-accounted investments**

> **Question 2 – Presentation of items of other comprehensive income arising from equity-accounted investments**
>
> Do you agree with the IASB's proposal to amend IAS 1 for the presentation of items of other comprehensive income arising from equity-accounted investments amendments (see paragraphs 82A, BC1-BC6 and the Guidance on implementing IAS 1).
>
> If not, why and what alternative do you propose?

*Notes to constituents*

*40 The IASB was requested to revise the presentation requirements in paragraph 82A of IAS 1 to clarify whether the share of items of other comprehensive income arising from equity method investments should be presented separately by nature, or in aggregate as a single line item (classified by whether or not the items will be reclassified (recycled) to profit or loss). This issue resulted from the amendments to IAS 1 that were issued in June 2011.*

*41 The IASB proposes amending paragraph 82A of IAS 1, to clarify that entities shall present the share of other comprehensive income of associates and joint ventures accounted for using the equity method:*

(a) *Separately between items that will be subsequently reclassified to profit or loss, and those that will not;*

(b) *In aggregate as a single line item within those classifications*

**EFRAG's response**

> **EFRAG agrees with the proposed amendments. However we recommend the IASB to use defined terms that are consistent with current Standards in order to avoid the need for future amendments.**

42 EFRAG agrees with these proposed amendments. However, we note that the IASB is currently addressing the issue of reintroducing the option to use the equity method of accounting in separate financial statements also to measure investments in subsidiaries together with associates and joint ventures. Therefore, we believe that the IASB should use the term 'investee' currently in IAS 28 *Investments in Associates and Joint Ventures* and in IFRS 10 *Consolidated Financial Statements* rather than the terms 'associates and joint ventures' in order to avoid future amendments to IAS 1.

**Transition requirements**

> **Question 3 – Transition provisions and effective date**
>
> Do you agree with the proposed transition provisions for the amendments to IAS 1 as described in this Exposure Draft (see paragraphs 139N and BC23-BC25)?
>
> If not, why and what alternative do you propose?

*Notes to constituents*

*44 The IASB proposes that the amendments included in the ED should be applied from their effective date. Early application is permitted; however, entities should disclose that fact. The IASB notes that paragraph 38 of IAS 1 requires an entity to present* *comparative information for all amounts reported in the current period financial statements and for narrative or descriptive information* 'if it is relevant to understanding the current period's financial statements*'. If an entity alters the order of the notes or the information disclosed compared to the previous year, it also adjusts the presentation and disclosure of comparative information to align with the current period presentation and disclosure. Therefore, the IASB believed that IAS 1 already provides sufficient guidance that ensures comparability of financial information.*

**EFRAG's response**

**EFRAG agrees with the proposed transition requirements.**

45 EFRAG agrees with the IASB's proposals.