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Topic **Disclosure**

Background

1. At the IFRS Advisory Council session on Tuesday you will hear presentations on five projects that relate to disclosure.

2. Two of the projects focus mainly on removing disclosure requirements from IFRSs. The ICAS-NZICA report looks at the suite of IFRSs, identifying disclosures that the authors think should be removed, as well as making other recommendations including adding references to materiality to many IFRSs. The ANC report is focused more on smaller listed entities.

3. Two of the projects relate to creating a disclosure framework. EFRAG/ANC France/UK ASB have a project to develop a framework for the notes to the financial statements. Their objective is to stimulate debate on how disclosures should be made more relevant for users while also ensuring that only useful information is disclosed. The FASB has a project to develop a disclosure framework to help the FASB improve its process for developing new disclosure requirements, to help preparers decide when and to what extent disclosures should be made and to establish principles for the organisation and formatting of disclosures that promote clear communication.

4. The UK FRC paper on reducing clutter is not focused on removal of disclosures, but instead has proposals that it thinks should lead to better communication between constituents. The report includes ideas and guidance for better readability as well as guidance to identify information that is not material.

IASB work

5. The IASB has been monitoring these projects. In some cases our staff are liaising with the sponsoring bodies. In other cases the Board has discussed related reports in public meetings.

6. The Board has also been considering disclosures, which is why it encouraged the IFRS Advisory Council to discuss this important topic. In its agenda consultation document, the Board stated that it thinks that work on disclosure matters is a priority.

7. Most respondents to the agenda consultation believe that IFRSs impose too many disclosure requirements. Those respondents suggest that it is difficult to target clear communication to users when the message is obscured by high levels of boilerplate disclosure.

8. There was support for the development of a disclosure framework. Many respondents suggested that a disclosure framework could provide a structured way to review the need for disclosure. It could simplify the disclosure process and reduce the costs to preparers. In their view, the disclosure framework should contain clear communication objectives so that disclosure is understandable, easily accessible and relevant and it should include a discussion of materiality in order to ensure that only material amounts are disclosed. Development of a disclosure framework could be part of the work on the conceptual framework.

Investors

9. As part of the agenda consultation, the Board undertook extra and focused consultation with investors. The feedback we received was that simply reducing the volume of disclosure requirements was not the solution.

10. Among the investor community there is a general concern that financial reporting has become more complex, and that even sophisticated users of financial

statements have trouble understanding them. There is a concern that the increased complexity makes them less able to assess management's accountability. On the other hand, some investors note that the economic environment in which companies operate has become more complex and believe that the accounting is merely reflecting that additional complexity.

11. Investors want to see improvements in the relevance of the information provided and they want us to examine ways to stop important information from being obscured. Investors generally think that the concept of materiality should dictate the information and level of detail disclosed.

12. There is also a widely shared perception that financial reports (in particular, the note disclosures) are too long, and that they contain information that is not always useful or do not contain basic information that is relevant. Many stated that they want *relevant* and higher quality disclosure, regardless of whether that means more or less disclosure. In other words, there is a view in the investor community that management are simply 'checking the box' (often providing boilerplate information) rather than telling their shareholders a 'story' about their business, such as the risks that the company faces, its prospects, what has happened during the period, the judgements made by management in developing the financial statements and how those judgements affect reported amounts.

13. Many of the investors we spoke to doubt the assertions made by preparers of financial statements that being more descriptive risks them revealing competitive or proprietary information. To the contrary, they assert that providing investors with more transparency would actually decrease a company's cost of capital and would increase shareholder returns because existing and potential shareholders would be more confident that management is not hiding material information.

14. Investors generally tend to support the development of a presentation and disclosure *framework* rather than a disclosure *standard*. In fact, there is some concern about the suitability of a disclosure standard because:

    (a) it might focus on reducing the volume of disclosures rather than aiming to enhance the information content; and

(b) the disclosures needed for any particular asset or liability are often related to the recognition and measurement requirements of the particular asset or liability.

15. Some investors would like to see the Board do more work on integrated reporting. In their view, investors cannot fully understand the financial statements without understanding the environmental, social and governance risks and opportunities that a company faces. They note that investment decisions are not made solely on financial information and think that it would be useful to bring together the financial statements (eg performance) and key non-financial information (eg business model and strategy) so that investors can see the entire picture. Those investors support the IASB's involvement with the International Integrated Reporting Council (IIRC). On the other hand, others are concerned that work on a topic such as integrated reporting, which is not central to the IASB's work, can become too political while using valuable and limited resources.

Short term actions—the 'quick win'

16. We have heard many calls for the IASB to make some short-term changes to disclosure requirements to reduce the disclosure burden. They see this as a 'quick win' with the IASB fixing some obvious problems with the disclosure requirements in IFRSs. The ICAS-NZICA report is an example of such a suggestion, with claims that, if it were to be implemented, financial reports could be reduced by about 30 per cent.

17. Another example came to the IASB in the agenda consultation. In its submission, the Corporate Reporting Users' Forum (CRUF) included an appendix with five 'quick wins' that it believes would greatly improve the relevance of reported information, which could be implemented in advance of any work done on a disclosure framework. All of these 'quick wins' are for matters for which the CRUF wants *more* information, not less. Their focus is not on simply removing

disclosures, but on getting more relevant information.[1] What one party sees as a quick win will not always be seen by others as being positive.

Collective action

18. It is clear that when it comes to improving the quality of financial information, many parties have a role to play. We have heard that the disclosure process is affected by the enforcement environment. Preparers have told us they adopt a checklist approach because it is more costly to apply judgement and have to justify their decisions firstly with their auditor and then, sometimes publicly, with regulators who question the absence of a particular disclosure. In other words, preparers using their judgement and applying materiality to disclosures face greater scrutiny from auditors and regulators than preparers who disclose everything on their 'checklist'.

19. The chain of events starts with IFRSs. The IASB needs to ensure that it provides the right tools for preparers, auditors and regulators to work with. Preparers need to apply their judgement and to keep the needs of investors in mind. We know that preparers can reduce the size of their reports within the current framework of IFRS requirements. In 2011 HSBC reduced the size of its financial statements by about 20 per cent, by taking a fresh look at what information it thought should be presented. My impression is that HSBC thinks this improved its report and the changes were well received.

20. Auditors need to ensure that they are applying the same materiality principles as the preparers. We are told that some preparers simply disclose information

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[1] The CRUF itself acknowledges that its 'quick wins' do not eliminate disclosures, and they are aware of the danger of adding, or being perceived as adding, to the disclosure burden. The CRUF observes: "The intention is to focus on the pragmatic rather than rehearse conceptual debates. It is hoped that areas identified could be addressed by most companies without significant incremental cost. However, the CRUF recognises that this will not be universally true. Similarly, it recognises that there will be companies for whom elements of this list will not be relevant. And so the Forum wishes to stress that it does not wish companies to view this as yet another check list; its ambition is simply to offer some feedback on the effectiveness of some areas of reporting today."

because their auditors are following check-lists. And, of course, regulators clearly influence preparers, and auditors, by how they ‘enforce’ disclosure requirements.

Next steps

21. At its March meeting the Board will discuss its general strategy for developing its new work plan. As the agenda consultations papers at this Advisory Council meeting indicate, the strategy will include building a more formal and extensive network of standard-setters and others to assist the IASB in developing projects. The feedback we receive from this meeting will be considered when the staff develop their recommendations.

22. Everything that the Board has heard so far supports the addition of a project to examine disclosure. The staff will be recommending to the Board that it should give priority to the development of a project on disclosures that would have at least two parts—the development of a disclosure framework and the assessment of potential short-term improvements that would not need to wait for the introduction of such a framework.

23. In addition, the staff are looking at ways by which the IASB could facilitate more public dialogue between the Board, securities regulators, auditors, investors and preparers. Possibilities include the IASB hosting a special symposium on disclosure, in public.

Questions for the break-out sessions

24. In the break-out sessions we would like you to consider the following matters:

- How helpful did you find the ICAS-NZICA, ANC and UK FRC reports? What are the main messages that the IASB should take from those reports?

- What short-term ‘fixes’ to IFRSs do you think are most likely to address concerns about the clarity (and length) of financial reports? Among the suggestions made to the Board are:
    - Remove specific disclosures (eg ICAS-NZICA).
    - Modify (add) disclosure requirements for targeted areas (eg CRUF).
    - Consolidate some of the disclosure requirements (such as introducing a more general requirement for reconciliations rather than having such a requirement in many individual standards).
    - Clarify or provide additional guidance on how to assess relevance (materiality), either generally or in individual standards.
- Should the IASB bring together regulators, auditors, investors and preparers to assess strategies for improving the quality of financial reports? Do you have suggestions about what you think is the best way to do this?

25. These questions focus mainly on shorter-term developments. We expect that the broader projects being undertaken by EFRAG/ANC France/UK ASB and the FASB will help the IASB in developing a disclosure framework.