AGENDA PAPER

IFRS Advisory Council Meeting

LONDON	18–19 June 2012	**Agenda ref 3**
TOPIC	Summary of the Disclosure discussions at the February 2012 Council meeting	
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This paper has been prepared for discussion at a public meeting of the IFRS Advisory Council. The views expressed in this paper are those of the authors. Comments made in relation to the application of an IFRS do not purport to be acceptable or unacceptable application of that IFRS.

Overview

1. At the February 2012 meeting of the IFRS Advisory Council, there were presentations on five projects that relate to disclosure.
2. Two of the projects that were presented focused mainly on reducing disclosure requirements in IFRSs. These were presentations on the recommendations of the New Zealand Institute of Chartered Accountants and The Institute of Chartered Accountants of Scotland *Losing the excess baggage–reducing disclosures in financial statements to what is important* and a proposal by the French standard setter Autorité des Normes Comptables *Simplify accounting obligations for 'small listed companies' in Europe*.
3. The next two projects that were presented focus on developing a framework for disclosures. The European Financial Reporting Advisory Group (EFRAG) along with the French and the UK standard-setters is developing a framework for the notes to the financial statement and the US standard-setter, the Financial Accounting Standards Board, is working on a project to develop a disclosure framework to help it improve its process for developing new disclosure requirements.
4. The fifth project that was presented was the UK Financial Reporting Council's paper *Cutting clutter–Combating clutter in annual reports*, which is not focused removing disclosures, but has proposals that should lead to better communications between constituents.

5. Finally, the Council was updated on what the IASB has been doing on disclosures, which has mostly been monitoring the other projects. Disclosures are also included in the agenda consultation that the IASB is currently undertaking.
6. After listening to the presentations on disclosures, the Council was divided into four groups to discuss questions developed by IASB staff.
7. The four groups were mostly based on stakeholder representation:
   (a) Group 1 (Investor/user/academics) led by Jeff Mahoney.
   (b) Group 2 (Preparers) led by Jerry de St. Paer.
   (c) Group 3 (Mixed) led by April Mackenzie.
   (d) Group 4 (Mixed) led by Richard Thorpe.

Questions for the break-out sessions

8. In the break-out sessions the Council was asked to focus its discussions on the following matters:
   (a) 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?
   (b) 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:
      (i) Remove specific disclosures (eg ICAS-NZICA).
      (ii) Modify (add) disclosure requirements for targeted areas (eg CRUF).
      (iii) 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).
      (iv) Clarify or provide additional guidance on how to assess relevance (materiality), either generally or in individual standards.
   (c) 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?

9. These questions focused mainly on shorter-term developments. The IASB expects that the broader projects being undertaken by EFRAG/ANC France/UK ASB and the FASB will help it in developing a disclosure framework.

Reports back

10. The results of the break-out groups were reported on in a full Council session. The reports back revealed a high level of agreement on a number of key points. Council reached consensus that:

- Improving the quality of footnote disclosures, and reducing the clutter in them, should be addressed as a matter of urgency.
- Quick fixes should be resisted. The topic is complex. A holistic, structured approach is required, including agreement on the purpose/role of footnote disclosures. The assistance of other organisations is needed. It is probably more realistic to aim for a medium-term solution.
- Differential disclosure requirements based on the size of the reporting entity is not supported. Solutions should be sought that would apply to all reporting entities using IFRSs.
- In the near term, guidance on the application of materiality to footnote disclosures would be useful. This might usefully build on the distinction between the materiality of line items in the primary financial statements and the evaluation of related information disclosed in the footnotes.
- The IASB should take a leadership role. Convening a forum of interested parties could be a useful start. The IASB might form a Working Party.

Group 1

11. Jeff Mahoney reported back for the group. On the first question, the group took a vote on each of the projects, with a grading system of 1-3, with 1 being very helpful, 3 not being helpful and 2 something in between. On the first project *Losing the excess baggage*, the group vote was that four member thought it was very helpful, five member thought it was helpful and two members thought it was not helpful. The comments made on the project

were that is was helpful in providing one view on how you might reduce the volume of disclosure. However, concerns were raised that the project focused too much on reducing the volume of disclosures and that there was not enough emphasis on enhancing clarity. There were also concerns that the starting point of the project was not right: it should start by evaluating what the user needs are and then going from there. Finally, the basis for various decision points in the model that is being used needs strengthening to give the IASB an approach that it could use going forward.

12. On the UK FRC project, the group vote was the same as for the previous project. The comments made on this project included that it was helpful in defining the term ‘clutter’ and in describing the behavioural influences on disclosure overload. There was concern that there was not enough user focus, and there was disagreement with some of the clutter examples (governance material and some explanatory material).

13. For the ANC project for simplifying accounting for small listed companies, the whole group thought that it was unhelpful. The consensus was that if you are a listed company you get certain benefits that come with certain obligations, such as more disclosures. There may however be multiple tiers in certain exchanges and the exchanges or the regulators may reduce the disclosure requirements for the lower tiers. This should, however, not be an issue for the IASB.

14. On question 2, the group thought that all the listed options in the question had some merit, but the group agreed that there are no ‘short-term fixes’. The group also thought that each of the items should be considered within a broader disclosure framework project. The most difficult of the suggestions relates to how clarify or provide additional guidance on assessing materiality.

15. On question 3, the group agreed that the IASB should bring the stakeholders together. The approach that could be used to do this might involve:

    (a) collect and analyse all of the existing research on the issue, from the:

        (i) World Bank, Financial Stability Board, individual companies and academic research.

    (b) pull together all the interested parties (critical that there be user involvement);

(i) what can be done under the existing framework;

(ii) what changes do we need to make to the framework in order to improve clarity and reduce unnecessary disclosures.

(c) develop proposals;

(d) consult on the proposals and obtain feedback; and

(e) move the best ideas into the IASB's project for disclosure framework.

Group 2

16. Jerry de St. Paer reported back for the group. On the first question the group thought that the work on these projects was helpful. The fact that a number of major projects are under way demonstrates that this is a major issue. It also demonstrates the need to deal with disclosure in a structured and systematic way and also the complexity of the challenge.

17. There is a need to define 'users'. Are they investors (equity, debt or hybrid)? Are they regulators, or rating agencies which may have access to private data?

18. The group also noted that disclosures are more than the notes. The include MD&A, directors' report, press releases and other supplemental reports. There is also a need to define 'relevance' and 'materiality' for the notes. In addition to that, the group also thinks that there is a need to decide on the role of the notes, on the analogy of a dictionary versus a novel. Should they be all-encompassing and should they explain movements in the balance sheet and the profit or loss statement?

19. The group also thought that once you are a listed company, you have accessed the capital markets and have the obligation to disclose, and so there should be no differentiation based on size.

20. Disclosure should be a part of the conceptual framework and should be strategic, not tactical. There should be a disclosure statement for each standard and the bar should be higher for including new notes than for removing existing notes. Finally, there is a need to recognise that this is behaviour-related and so it requires changes to behaviour.

21. On question 2, the group thought that it might be possible to remove specific disclosures (eg as suggested in the ICAS-NZICA project). It might also be possible to modify (or

add) disclosure requirements for targeted areas (eg CRUF). There should also be the possibility of consolidating some of the disclosure requirements (such as introducing a more general requirement for reconciliations rather than have such a requirement in individual standards).

22. There is a need to clarify, or to provide additional guidance, on how to assess relevance (materiality), either generally or in individual standards. However, using the existing projects does not fit into the IASB due process. There is a need for a more holistic process. Doing many different projects is a diversion of energy.

23. On question 3, the group thought that the IASB should try to bring these groups together. There is a need for a more holistic process and for recognising the overall disclosure environment.

24. There must be full formal due process, which would include:

(a) interactive collaboration of preparers (including audit committees), auditors, regulators (financial, auditing (IFAC), etc);

(b) round tables; and

(c) a working group.

25. Finally, the group noted that, for example, IAASB/IFAC 'non-trivial' requirements in some cases are the cause of immaterial detail being provided in notes.

Group 3

26. April Mackenzie reported on behalf of the group. On the first question, there was a high degree of consensus that there is an issue regarding disclosures. The IASB should show leadership and provide co-ordination on this project—not 'start from scratch' but to build on the existing projects (ESMA's project on materiality needs to be considered within this context).

27. A project on disclosure should be a high priority: The length of the project is likely to make it a medium-term project. The group thinks that there are no quick wins on this project and that it should be started as soon as possible. The project should be on a disclosure framework, with special emphasis on the materiality, relevance and quality of

the disclosure. It should acknowledge the range of user of financial statements and the group observes that the project is also about behaviour.

28. The quantity of the disclosures may reflect the increased complexity of business and the goal should not be to simply cut down volume but to look at the quality of the disclosure. There is also a timing tension between developing a framework and solving the disclosure problem now. The framework that would result from the project could therefore be tested, while being developed against existing standards such as IAS 2, IAS 7 and IAS 36.

29. There is also a need to acknowledge the behavioural issues and how preparers are under pressure to read things very legalistically. Part of this behavioural change is going to have to be tackled at a local level.

30. There was no support in the group for the French proposal to have different disclosures for smaller listed companied than for large listed companies

31. On question 2, there was an agreement that the IASB should start with the existing projects and recognise the work done. The disclosure project is a high priority, but it is not a quick-fix project, specifically because of the need to develop principles and find common ground. The IASB should start the development of a framework immediately, but at the same time it should be conscious of the ideas that are being developed in the framework and the ideas that are being raised in the existing projects.

32. The IASB should double-check the disclosures proposed in its four major projects (eg offsetting) and try to start applying the new thinking now so as not to overload the new standards, given that the problem of possibly excessive disclosures has een identified.

33. On question 3, the group thought that the IASB should establish a focus group drawn from existing disclosure projects, because those working on them have already given this matter a lot of thought. The IASB should organise a meeting soon on this issue. That meeting should not be a ‘talkfest’—the IASB staff should provide a stimulating general orientation of what a disclosure framework might be.

34. Stakeholders also need to look at their own role and be willing to change (regulators; auditors, preparers).

Group 4

35. Richard Thorpe reported back on behalf of the group. The group focused on questions 2 and 3. On question 2, the group thought that there were not many quick wins for the IASB on this issue. The group considered this issue in relation to relevance, materiality and communication. On communication, the group noted that with more electronic communication, there is less pressure than there was on resolving disclosure issues, but communication issues remain highly relevant.

36. There is value in accelerating work on materiality as the beginning of a wider project on disclosure. That would address the issue of materiality in the financial statements themselves versus the materiality in the notes. Any work on this issue should be done with the IAASB. Some members of the group thought that the work by ESMA on materiality is not helpful and that this is not a job for securities regulators; it should be left to the standard-setters.

37. The group also debated whether some of the proposals in the ICAS-NZICA paper could be accelerated, especially the proposal to reduce the number of reconciliations and comparatives.

38. This is an issue about behaviour; preparers get into a mindset of producing disclosures and if challenged by regulators they find it easier just to provide the information, rather than saying that 'this is not relevant'. A change of behaviour can only be achieved through some form of symposium or working party in which all the relevant stakeholder would be represented.

39. One option would be to look at best practice. HBSC has done a lot to reduce the length of their accounts. What were they doing and what have others done?

40. There was also not much support for smaller listed companies being treated differently.