STAFF PAPER

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Project	**Conceptual Framework**
Paper topic	Draft discussion paper Presentation and disclosure (general)

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This paper is a very early draft of part of the Conceptual Framework discussion paper. It has been prepared by the staff for discussion by the IASB. Issues discussed and conclusions reached will be subject to change.

What does this section cover?

This section discusses presentation and disclosure issues. Specifically the paper discusses:

- What is meant by the terms financial statements, financial reports, presentation and disclosure;
- Presentation in the primary financial statements, including:
  - Purpose of primary financial statements
  - The concepts of aggregation, classification and offsetting
  - The relationship between primary financial statements;
- Disclosures in the notes to the financial statements, including:
  - Scope of information to be included in the notes
  - What is relevant information for disclosures in the notes, including a discussion of comparatives and materiality
  - Communication principles
  - Form of disclosure requirements
  - Cost benefit considerations.

Why is this section important? What problems will this section help address?

The *Conceptual Framework* does not currently have a section on presentation and disclosure. This is seen as having had the effect that disclosure requirements in IFRS are not always focused on the right disclosures and are too voluminous.

Purpose of the section

1. Presentation and disclosure are the mechanisms by which a reporting entity communicates information about its financial position and financial performance to users. Some aspects of presentation and disclosure are prescribed by IFRSs, whilst others are driven by consideration of the reporting entity's specific facts and circumstances.

2. The purpose of this section of the [draft] discussion paper is to discuss the principles that should underlie decisions the IASB makes about presentation and disclosure. This section will discuss:

   (a) What is meant by the terms presentation, disclosure, financial reporting and financial statements;

   (b) What are primary financial statements, including a discussion of their purpose and the relationship between primary financial statements;

   (c) How items should be presented, including a discussion about aggregation, classification and offsetting;

   (d) What is the purpose of disclosures in the notes to the financial statements, including a discussion of what information is relevant for the notes and how this should be communicated. The concept of materiality is also addressed as part of this discussion; and

   (e) What the IASB should consider in setting disclosure requirements, including cost benefit considerations.

What is the problem?

3. Presentation and disclosure are not currently addressed in the *Conceptual Framework.* Some believe that this has led to disclosure requirements in IFRSs that are not always focused on the right disclosures and are too voluminous. It is also seen as contributing to the lack of clarity around presentation of profit or loss and OCI. Section 8 [Agenda paper 10H(a)] deals with presentation of profit and loss and OCI. This paper deals with presentation and disclosures more broadly.

4. In terms of disclosures, many respondents to the *Agenda Consultation 2011* told the IASB that they think a framework for disclosures is needed. They think it is needed to ensure that information disclosed is more relevant to investors and to reduce the burden on preparers. Responses suggested such a framework would:

   (a) provide a structured way to review the need for disclosure, simplify the disclosure process and reduce the costs to preparers;

   (b) consider the costs and benefits of disclosure;

   (c) include a discussion of materiality in order to ensure that only material and/or relevant amounts are disclosed;

   (d) contain clear communication objectives so that disclosure is understandable and relevant.

5. As part of its feedback on the consultation, the IASB communicated that it would consider disclosures in the *Conceptual Framework* project.

Previous discussions

6. In 2008, the IASB and the US Financial Accounting Standards Board (FASB) published a discussion paper *Preliminary Views on Financial Statement Presentation*[1]. In 2010, the IASB and the FASB posted on their websites a staff draft of an exposure draft *IFRS X Financial Statement Presentation*[2]. Where relevant, this [draft] discussion paper incorporates principles developed during the financial statement presentation project. The IASB's current work plan does not include a project to develop a standard based on the work in that project. However, some of the issues discussed in the Financial Statement Presentation project are being considered in the Conceptual Framework project. The IASB is also assessing, in the light of the feedback on its shorter

[1] http://www.ifrs.org/Current-Projects/IASB-Projects/Financial-Statement-Presentation/Phase-B/DP08/Pages/DP08.aspx

[2] http://www.ifrs.org/Current-Projects/IASB-Projects/Financial-Statement-Presentation/Phase-B/Pages/Staff-draft-of-proposed-standard.aspx

term review of disclosure[3], the extent to which it should consider undertaking a broader standards level review of presentation and disclosure.

Description of terms

7. Before going into a detailed discussion about presentation and disclosure, it is worthwhile discussing what is meant by the following terms used in this section:

    (a) "presentation" and "disclosure" (paragraphs 8-14); and

    (b) "financial statements" and "financial reports" (paragraphs 15-18).

What is meant by the terms "presentation" and "disclosure"?

8. In the context of financial reporting, the term *presentation* attracts different meanings. IAS 1 *Presentation of Financial Statements* prescribes "the basis for presentation of general purpose financial statements to ensure comparability both with the entity's financial statements of previous period and with the financial statements of other entities." [4]

9. Others think that the term *presentation* has a more specific meaning ie the depiction of financial information in words and by monetary amounts on the face of an entity's primary financial statements.

10. In this discussion paper, we have used the term *presentation* as meaning the disclosure of financial information on the face of an entity's primary financial statements (see paragraphs 18-21 for more information on primary financial statements).

11. Disclosure has a broader meaning than presentation. *Disclosure* is the process of providing relevant financial information about the reporting entity to users. The entire financial report is a form of disclosure including amounts and descriptions presented in the primary financial statements and information included in the notes to the financial statements.

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[3] Refer to Feedback Statement *Improving Disclosure in Financial Reports* [April] 2013

[4] IAS 1 paragraph 1

12. It is often an entity's own facts and circumstances that determine what information is presented in the primary financial statements and what information is disclosed in the notes to the financial statements.

13. The notes to the financial statements disclose relevant information which is not presented on the face of the primary financial statements, for example:

    (a) Unrecognised assets and unrecognised liabilities of the entity;

    (b) Further disaggregation of items presented in the primary financial statements;

    (c) An entity's financial exposure to risks and uncertainties arising from its recognised and unrecognised resources and obligations.

14. How an entity presents and discloses information in its financial statements is critical to how effectively that information is communicated.

What is meant by the terms "financial statements" and "financial reports"?

15. The *Conceptual Framework* seeks to meet the objective of "general purpose financial reporting"[5] by addressing the concepts underlying the information presented in general purpose financial statements.[6]

16. General purpose financial reports ("financial reports") include general purpose financial statements ("financial statements") and other financial reporting. Other forms of financial reporting, for example, management commentary assists in the interpretation of a complete set of financial statements or improves users' ability to make economic decisions.

17. Collectively, financial statements depict a view of the financial position and financial performance of an entity. Financial statements comprise the primary financial statements and the notes to the financial statements. Currently the primary financial statements are:

    (a) the statement of financial position;

[5] OB2

[6] *Preface to IFRSs* paragraph 8

(b) the statement of profit or loss and other comprehensive income (or the statement of profit or loss and the statement of comprehensive income);

(c) the statement of changes in equity; and

(d) the statement of cash flows.[7]

18. Primary financial statements convey summarised information that communicates a financial picture of an entity. Each primary financial statement communicates a different facet of that financial picture.

Primary financial statements

Purpose of primary financial statements

19. IFRSs provide the following guidance on the objectives of financial reporting and financial statements:

(a) The objective of *financial reporting* is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity.[8] [In making these decisions], existing and potential investors, lenders and other creditors need information to help them assess the prospects of future net cash inflows into an entity[9].

(b) The objective of *financial statements* is to provide information about the financial position, financial performance and cash flows of an entity that is useful to a wide range of users in making economic decisions. [10]

(c) To assess an entity's prospects for future net cash inflows, existing and potential investors, lenders and other creditors need information about the resources of the entity, claims against the entity, and how efficiently

[7] IAS 1.10

[8] OB2

[9] OB3

[10] IAS 1.9

and effectively the entity's management and governing board have discharged their responsibilities to use the entity's resources.[11]

20. Based on the above, this [draft] discussion paper proposes that the objective of primary financial statements is to depict summarised information about recognised assets, liabilities, equity, income, expenses and cash flows that has been classified and aggregated in a manner that is useful to users in their assessment of the entity's financial position and financial performance.

21. Primary financial statements provide information about:

    (a) the resources of the entity and the claims against the entity; and

    (b) how efficiently and effectively the entity's management and governing board have discharged their responsibilities to use the entity's resources.

Classification and aggregation

22. A key aspect of financial statement presentation is effective communication and making information understandable. Classifying, characterising and presenting information clearly and concisely makes it *understandable*.[12]

23. Classification is sorting of items based on shared qualities. Aggregation involves the adding together of individual items within those classifications. To present information in the primary financial statements that is understandable an entity classifies and aggregates information about recognised elements and presents it on a summarised basis.

24. As indicated above, the main advantage of aggregation is that it allows an entity to disclose the breadth of its activities in an understandable and accessible way. In essence it is a mechanism by which an entity can highlight those items, and relationships between items, that are important to an assessment of its financial position and financial performance.

[11] OB4

[12] QC30

25. However, aggregation loses detailed information. Applied appropriately, aggregation has advantages that outweigh the cost of losing this detail. Applied inappropriately, aggregation can obscure useful information or even result in misleading information, for example when dissimilar items are aggregated.

26. At the highest level, the primary financial statements classify and aggregate information about the recognised elements (including changes in elements and components of elements). In particular:

    (a) The statement of financial position presents information about assets, liabilities and equity.

    (b) The statement of profit or loss and other comprehensive income (or the statement of profit or loss and statement of comprehensive income) presents information about income and expense.

    (c) The statement of changes in equity presents information about income less expenses, contributions to equity and distributions of equity, transfers between classes of equity, as well as the opening and closing amounts of equity.

    (d) The statement of cash flows presents information about cash inflows and cash outflows, as well as the opening and closing cash balances.

27. Within each of the above statements, an entity presents separate groups of recognised items as separate lines (‘line items’). Each line item represents that group by providing a description of the aggregated group of recognised elements (or components of elements) and a monetary amount. Line items, sub-totals and totals derived from those line items, should be presented when they provide useful information.

28. In order to provide information about the resources of the entity, the claims against the entity and how efficiently and effectively the entity’s resources have been used, classification and aggregation into line items and sub-totals (where relevant) should be based on similar properties such as:

    (a) the function of the item;

    (b) the nature of the item; and

(c) the measurement basis of the item.

29. In this context "function" refers to the primary activities (and assets and liabilities used in those activities) in which an entity is engaged, such as selling goods, providing services, manufacturing, advertising, marketing, business development or administration. "Nature" refers to the economic characteristics or attributes that distinguish items that do not respond similarly to similar economic events, such as wholesale revenues and retail revenues; materials, labour, transport and energy costs; or fixed-income investments and equity investments. Section 6 of this [draft] discussion paper discusses measurement bases of an item.

30. In many cases an entity will determine what line items, sub-totals and totals to present in its primary financial statements based on its individual facts and circumstances and its assessment of what is relevant at a summary level.

31. In some case the IASB may decide to require a particular item to be presented in the primary financial statements if it is material to the entity. A particular line item may be required to be presented where the IASB considers that information about that item would be essential to providing a summary depiction of the financial position and financial performance of an entity that is useful to a wide range of users.

Offsetting

32. Because offsetting aggregates dissimilar items (assets/liabilities, income/expense), offsetting will generally not provide the most useful information for assessing an entity's financial position and financial performance.

33. However the IASB may choose to require offsetting where such presentation provides a more faithful representation of a particular position, transaction or other event.[13]

[13] FSP Staff Draft paragraphs 54-56

Relationship between primary financial statements

34. No primary financial statement has primacy over the other primary statements but should be looked at as a group. The way items are presented in primary financial statements help users take that overall view of an entity's financial position and performance. This could be achieved by ensuring that relevant relationships between the statements and among items presented in them are clear.

Disclosures - Notes to the financial statements

Scope of information that should be included in the notes to the financial statements

35. The notes to the financial statements are inextricably linked to the primary financial statements. Therefore, based on the objective of financial reporting (see paragraph 19) and the objective of primary financial statements proposed earlier in this paper (see paragraph 20), this [draft] discussion paper proposes that the purpose of the notes to the financial statements is to supplement and complement the primary financial statements and to provide additional information that is useful to users for their assessment of the entity's financial position and financial performance.

36. To be useful, information about an entity's financial position and financial performance (including information that complements and supplements the primary financial statements) must be relevant and faithfully represent the entity's financial position and financial performance.

Arises from past and current conditions, transactions and events

37. Given that financial statements reflect a reporting period, to be relevant the information they contain must arise from past and current conditions, transactions and events.

38. By limiting the notes to the financial statements to information arising from past and current conditions, transactions and events, this discussion paper proposes to

limit the type of forward-looking information presented in financial statements. Forward-looking information is information about the future (eg information about prospects and plans) that may later be presented as historical information (ie results).[14]

39. Many types of forward-looking information are disclosed outside of financial statements, for example in management commentary if the entity prepares one. However, forward-looking information would be included in financial statements to the extent that it relates to an entity's assets, liabilities, equity, income and expenses. For example, forward looking information that relates to the measurement of an asset or liability would be included in the notes to the financial statements. However, how the amount of that asset or liability (or a change in that amount) compares to an entity's stated strategies and targets would be included in management commentary, if the entity prepares one.

40. Given that financial statements provide information about financial position and financial performance, financial statements should also include information about financial impact of risk that arises from an entity's assets and liabilities.

41. One issue caused by scoping the notes to the financial statements in this way relates to non-adjusting events after the reporting date. Non-adjusting events after the reporting period are those events that occur between the end of the reporting period and the date when the financial statements are authorised for issue and that are indicative of conditions that arose after the end of the reporting period.[15]

42. Applying the principle in paragraph 37 above, non-adjusting events after the reporting period would not be disclosed in the notes to the financial statements. To include them in financial statements the IASB would need to treat them as an exception to this principle. This would be on the basis that, although the information is not related to the reporting period, it provides information that is otherwise relevant.

[14] IFRS Practice Statement *Management Commentary: A framework for presentation* – see the Appendix

[15] IAS10.3

Relevant information

43. Relevant information is capable of making a difference in the decisions made by users. Information is relevant if it has predictive value, confirmatory value or both.[16]

44. To meet the purpose of the notes to the financial statements, an entity may use different types of disclosures to communicate relevant information to users of financial statements. For example an entity may disaggregate line items in the primary financial statements as well as provide additional description and amounts for certain unrecognised assets and liabilities. Disclosures may also describe the basis, scope and context for the amounts, transactions and events disclosed in the financial statements.

45. This [draft] discussion paper proposes that the type of information that is generally relevant to a user's understanding and assessment of an entity's financial position and financial performance can be grouped as follows:

    (a) The reporting entity as a whole;

    (b) The recognised and unrecognised assets of the entity;

    (c) The recognised and unrecognised liabilities of the entity;

    (d) Transactions and other changes in assets and liabilities;

    (e) The financial impact of risks arising from those assets and liabilities; and

    (f) Methods and assumptions used to account for the above.

46. Using these groups, the table below provides some examples of the types of disclosures that may provide relevant information. A single note in the financial statements may combine two or more of these types of disclosures. In addition, one disclosure might provide two types of relevant information. For example a maturity analysis of a liability provides further information about the obligation, but also provides information about liquidity risk. Similarly, a single note might

[16] QC6-7

provide information about a group of assets, transactions relating to those assets, risks arising from them and methods used to account for them.

Table 1: Examples of disclosures split by type of relevant information

Type of relevant information	Examples of disclosures
Reporting entity	• General information about the reporting entity • Information about subsidiaries, associates, parent etc • Business model • Going concern

Assets, liabilities and changes in those assets and liabilities	• Disaggregation of line items in the primary financial statements including:
	  o Analysis of a single amount (line item, item, transaction or event);
	  o Analysis by function, nature or measurement where different to that provided in the primary financial statements;
	  o Maturity analysis;
	  o Roll-forwards
	  o Operating segments
	  o Related party transactions
	• Disclosure of unrecognised assets and liabilities
	• Relationship between line items (eg hedging, offsetting)

Risks	• The types of financial risks faced by the entity including its sources and exposures • How the entity has managed those risks • How management of risks has impacted its financial statements
Methods and assumptions	• Accounting policies • Alternative measurements • Measurement uncertainty

Comparatives

47. A complete set of IFRS financial statements includes comparative information in respect of the preceding period. Presentation of additional comparative information is permitted and, in some circumstances, required. [17] Comparative information provides a basis from which to assess the financial statements of the

[17] IAS1.10(ea), 38-44

current period and therefore provides relevant information. It follows that comparative information is an integral part of an entity's current period financial statements.

Materiality

48. Chapter 3 of the *Conceptual Framework* states that:

> [i]nformation is material if omitting or misstating it could influence decisions that users make on the basis of financial information about a specific reporting entity. In other words, materiality is an entity-specific aspect of relevance based on the nature or magnitude, or both, of the items to which the information relates in the context of an individual entity's financial report. Consequently, the Board cannot specify a uniform quantitative threshold for materiality or predetermine what could be material in a particular situation."[18]

49. In addition, IAS 1 provides that an entity need not provide a specific disclosure required by an IFRS if the information is not material.[19]

50. The IASB believe that the concept of materiality is clear and is generally well understood. Therefore the IASB proposes not to amend or provide additional guidance on materiality in the *Conceptual Framework*.

51. However, how the concept of materiality is applied in practice is seen by many as a major cause of the current disclosure problem in financial reporting. That problem is often identified as a failure to use professional judgement when considering materiality that has resulted in both the disclosure of too much irrelevant information and not enough relevant information. As a result the IASB is considering additional work to address the application of materiality at a standards or application guidance level.

[18] QC11

[19] IAS1.31

Faithful representation of relevant information

52. To be a faithful representation, a depiction needs to be complete, neutral and free from error.[20] A key characteristic of information in the notes to the financial statements is that it is neutral.

53. As discussed earlier, disclosure is a mechanism by which an entity communicates with its users. Financial statements, including the notes to the financial statements, communicate neutral information. Information about management's view of the entity's performance, position and progress belongs outside financial statements, for example in management commentary.[21] It follows that information with these types of characteristics should not be required to be disclosed in the financial statements.

Communication principles

54. For disclosures to communicate effectively, they should have the following characteristics:

    (a) Disclosures should be clear, balanced and understandable. Disclosures should be written as simply and straightforwardly as possible without:

        (i) loss of useful information; and

        (ii) unnecessarily increasing the length of the financial statements;

    (b) Disclosures should be entity-specific. Where possible, disclosures should highlight information that is relevant to an entity and not include 'boilerplate' or generally available information that is not specific to the entity;

    (c) Disclosures should be organised in a manner that highlights to a user what is important. This principle may be considered when determining

[20] QC12

[21] IFRS Practice Statement *Management Commentary: A framework for presentation* paragraphs 12-13. In addition, the Appendix: defines forward-looking information as "… information about the future … [that] is subjective and its preparation requires the exercise of professional judgement."

what order to make disclosures or the emphasis given within a single disclosure;

(d) Disclosures should be linked. As with primary financial statements, disclosures should show the relationship between items in the primary financial statements and information disclosed in the notes. Where appropriate, disclosures should also show the relationship between notes and, where possible, with other disclosures elsewhere in the financial report. Cross-referencing should be used where possible and appropriate;

(e) Disclosures should not be duplicated in different parts of the financial report; and

(f) Disclosures should be comparable among entities and across reporting periods.

Form of disclosure requirements

55. Each IFRS that proposes disclosure and presentation requirements should have a clear objective. This objective should guide entities to identify the best disclosures and presentation to meet the objective. The language used to describe additional specific disclosure requirements should enable an entity to determine whether the specified information would be useful in meeting the stated disclosure objective. This may result in some disclosures not being made on the basis they are not material, or conversely alternative or additional disclosures being made.

56. In setting disclosure requirements, it is proposed that the IASB should consider the communication principles described in paragraph 54 above.

Cost benefit of disclosure requirements

57. In setting a disclosure requirement, the IASB should consider that the benefits of making the disclosure outweigh the costs that an entity will incur to make that disclosure. In making that determination, the IASB should consider the extent to which a wide range of users will find the information useful.

Questions for respondents

58. Do you have any comments on:

    (a) The description of the relationship between “presentation”, “disclosure”, “financial reporting” and “financial statements”;

    (b) The proposed approach to presentation in the primary financial statements; or

    (c) The proposed approach to disclosures in the notes to the financial statements.