STAFF PAPER

November 2014

IASB Meeting

Project	**Disclosure Initiative—Principles of Disclosure (POD)**		
Paper topic	Cross-referencing—Disclosing IFRS information outside the financial statements		
CONTACT(S)	Holger Obst	obst@drsc.de	+49 (0)30 2064 1229
	Kristy Robinson	krobinson@ifrs.org	+44 (0)20 7246 6933

Purpose of this paper

1. This paper builds on the IASB's discussion on cross-referencing at its meeting in July.[1] In this follow-up paper we address the concerns and questions raised by some Board members about our initial proposals on when it might be appropriate to present information required by an IFRS outside the financial statements, and use cross-referencing to incorporate it into financial statements. The tentative views of the IASB will be used to develop a section on cross-referencing in the Principles of Disclosure Discussion Paper.

2. In this follow-up paper we do *not* provide any further discussion about guidance in IFRS for cross-referencing *within* financial statements (eg between notes). The IASB supported the staff recommendations on that subject.

[1] Agenda Paper 11E—http://www.ifrs.org/Meetings/MeetingDocs/IASB/2014/July/AP11E-Disclosure%20Initiative.pdf

Staff recommendation

3. The staff recommend a general principle for limiting the disclosure of IFRS information outside of the financial statements:

   (a) to information disclosed in the entity’s annual report; and

   (b) when disclosing it outside of the financial statements makes the annual report as a whole more understandable; and

   (c) the financial statements remain understandable and fairly presented.

4. Appendix A of this paper should help the IASB to understand the potential implications of the staff recommendations (comprising the recommendations in this paper together with the staff recommendation discussed with the IASB in July) for a general principle within the context of existing guidance in IAS 1 *Presentation of Financial Statements*.

Background

5. In July (Agenda Paper 11E) we proposed to introduce a general principle on a specific use of cross-referencing into IFRS. This principle proposed permitting entities to disclose information required by IFRS outside of financial statements and incorporate it into financial statements by using cross-referencing.

6. The staff developed this principle for dealing with the use of cross-referencing on the basis that sometimes the disclosure of information required by IFRS outside of financial statements can enhance the understandability of the information. Cross-referencing does this by:

   (a) linking related information so that the relationships between items of information are clear; and/or

   (b) preventing redundancy of information, ie making financial information more concise for users by avoiding unnecessary duplication.

7. The proposal was developed in the light of reports by constituents that the duplication of information contributes to the disclosure problem. It was also clear from current provisions in IFRS that currently permit the use of cross-referencing to place information in a report that accompanies financial statements, that some information required by a Standard may actually be more usefully disclosed and discussed in such a report.

8. The staff also considered the benefits of establishing a single general principle permitting disclosure of IFRS information outside of financial statements and incorporating it into financial statements using cross-referencing. The staff considered this idea in comparison to the current situation, in which explicit permission is given in particular Standards. These benefits included:

   (a) making the process of redeveloping cross-referencing guidance in particular Standards superfluous; and

   (b) clarifying the conditions for use of cross-referencing in IFRS and the disclosure about information that forms part of a complete set of financial statements.

9. In addition, we had heard questions from some constituents about the current guidance for the use of cross-referencing as a tool for incorporating information into financial statements. In particular, the questions related to what was meant by the requirement that information is made available to users 'on the same terms as the financial statements and at the same time'. In response, in July we proposed that a general principle to permit entities to disclose information required by IFRS outside of financial statements, and incorporate it by cross-reference, should be accompanied by additional guidance as follows:

   (a) The entity should disclose—together with the unreserved statement of compliance in accordance with paragraph 16 of IAS 1—a list of cross-referenced information placed outside the financial statements that forms part of a complete set of financial statements in accordance with IFRS.

(b) The cross-referenced information located 'outside' financial statements should be depicted as being information prepared in accordance with IFRS and forming part of the financial statements (and audited if applicable).

(c) The cross-referencing must be direct and be precise as to what it relates to. In other words a direct cross-reference should take you to the ultimate location in one step and not detour via another location that holds a further cross-reference. A precise cross-reference indicates clearly the paragraphs or sections that contain the IFRS information instead of cross-referencing to another report or document as a whole.

(d) The cross-referenced information must remain available over time at the cross-referenced location.

10. Despite the accompanying guidance, some IASB members had the following concerns regarding the staff's recommendation for a general principle for cross-referencing in these circumstances:

(a) it increases the risk that cross-referencing will fragment information so that it impairs the usefulness of IFRS financial statements; and

(b) increased use of cross-referencing may make it more difficult to identify the IFRS financial statements, if information prepared in accordance with IFRS is commingled with other information. There is a risk of diminishing the IFRS 'brand'.

11. The IASB asked the staff to consider limiting this use of cross-referencing to information disclosed in the management commentary and to circumstances in which the discrete nature and magnitude of the disclosure justifies the use of cross-referencing.

Staff analysis

12. The staff analysis is structured as follows:

    (a) limiting the use of cross-referencing to information disclosed in the management commentary (paragraphs 13-20);

    (b) circumstances in which the discrete nature and magnitude of the disclosure justifies the use of cross-referencing (paragraphs 21-25);

    (c) potential areas for disclosing information required by IFRSs outside of financial statements (paragraphs 26-29); and

    (d) the use of a general principle, versus the use of criteria, for developing disclosure guidance (paragraphs 30-32).

Cross-referencing to information within management commentary

13. The staff considered whether it would be appropriate to limit where an entity is permitted to disclose information required by IFRS which is incorporated into financial statements by cross-reference to the management commentary. In our view limiting the use of cross-referencing in these circumstances would be narrower in scope than the existing cross-reference guidance in current Standards. For example, paragraph 21B of IFRS 7 *Financial Instruments: Disclosures* indicates that either the management commentary *or* the risk report are suitable statements in which to locate cross-referenced information. Consequently, we think that the use of cross-referencing should not be limited to information disclosed in the management commentary.

14. We therefore considered the basis for the request to limit where an entity may disclose information required by IFRS. We think narrowing the scope of ‘eligible reports’ would help to mitigate concerns that presenting information in different financial reports (albeit linked by cross-referencing) may impair access to information. This narrowing of the scope responds to a preference by users to

have all the relevant information in a single reporting package. Having information in one place should spare users from having to carry out a time intensive 'recollection exercise' to assemble financial information from different locations. It would also mitigate the risk that cross-referenced information is no longer available. Furthermore, the more disconnected and separate information is, the more likely it will be difficult to understand.

15. On the basis that users prefer to have all relevant information in one place, the staff believe that the location of information that could be incorporated into financial statements by cross-reference would be better described as being limited to information in the 'annual report'. We think the 'annual report' is a broader term than 'management commentary' and would more easily encompass the range of documents that may accompany the financial statements in a financial reporting package.

16. Current IFRSs include references to the 'annual report' but do not provide a more detailed description of this term. The staff think the 'annual report' could be described as a single reporting package of the entity with boundaries similar to those proposed by the IAASB in the Exposure Draft of ISA 720 (Revised) *The Auditor's Responsibilities Relating to Other Information - Proposed Consequential and Conforming Amendments to Other ISAs* (hereafter ED ISA 720).[2] The ED ISA 720 defines the annual report as follows:

> Annual Report - A document, or combination of documents, prepared typically on an annual basis by

[2] The proposals of ED ISA 720 require the auditor to read and consider the 'other information' that is included in an entity's annual report (but not part of financial statements). This is because other information that is materially inconsistent with the financial statements or with other knowledge that the auditor has obtained during the course of the audit may indicate that there is a material misstatement of the financial statements or that a material misstatement of the other information exists. Either of these types of misstatement may undermine the credibility of the financial statements and the auditor's report on them. The ED ISA 720 clarifies that the disclosures required by IFRS, but permitted to be located outside of financial statements but with cross-references, form part of financial statements and do *not* constitute 'other information'. See also https://www.ifac.org/sites/default/files/publications/files/IAASB-Proposed-ISA-720-April-2014_0.pdf

> management or those charged with governance in accordance with law, regulation or custom, the purpose of which is to provide owners (or similar stakeholders) with information on the entity's operations and the entity's financial results and financial position as set out in the financial statements. An annual report contains or accompanies the financial statements and the auditor's report thereon and usually includes information about the entity's developments, its future outlook and risks and uncertainties, a statement by the entity's governing body, and reports covering governance matters. The content of an annual report, and the name by which it is known, may vary by law, regulation or custom across jurisdictions.

17. In Appendix B of this paper we have included an extract from the IAASB's further explanation of the definition in ED ISA 720, with examples of documents or other forms of report that would or would not be covered by the definition.

18. The staff reviewed whether the definition of the annual report would exclude documents that are eligible sources for cross-referencing according to specific guidance in current Standards. Current Standards refer to the following statements or documents as sources for cross-referenced information:

    (a) management commentary or risk report (IFRS 7 *Financial Instruments: Disclosures*);

    (b) another published document (IFRS 1 *First-time Adoption of International Financial Reporting Standards*);

    (c) another group entity's financial statements (IAS 19 *Employee Benefits*); and

    (d) interim financial report (IAS 34 *Interim Financial Reporting*).

19. We think that from the list in paragraph 18, only (c), which refers to another group entity's financial statements, might not be covered by the definition of the entity's

annual report. Consequently, the cross-referencing guidance in IAS 19 would be considered as special guidance in addition to the general principle for cross-referencing.

20. We also think that the 'interim financial report' is identical to the annual report on an interim basis for the entity's single reporting package. Thus, the general principle for cross-referencing could also be applied to interim financial statements.

Cross-referencing to information of a discrete nature and magnitude

21. As proposed in July and described in paragraph 6 above, we think that entities should be permitted to disclose information required by IFRS in a report outside of financial statements and incorporate it into financial statements by cross-reference, but only if this placement enhances the understandability of the information. Such placement will enhance understandability if it:

    (a) links related information so that the relationships between items of information are clear; and/or

    (b) prevents redundancy of information, ie making financial information more concise for users by avoiding unnecessary duplication.

22. However, the request by some IASB members to limit the type of IFRS information permitted to be disclosed outside of financial statements to information that has a discrete nature and magnitude, highlights the risk that fragmenting disclosures too widely can also reduce the understandability of the financial statements.

23. We think that overuse of cross-referencing in financial statements, either within a single note or looking at the financial statements as a whole (including information incorporated by cross-references), can make those financial statements so fragmented that they are not understandable and therefore not fairly presented. This would be the case if the information in financial statements is so

widely dispersed that the overall picture of information being represented by a suite of disclosure objectives and requirements in a particular Standard or a about a particular matter is obscured. For example, one of the objectives of IFRS 7 is to provide information that helps entities evaluate the nature and extent of risks arising from financial instruments and how those risks are managed. Disclosing information about some risks in the financial statements and information about other risks in another part of the annual report could be confusing, and could dilute the overall view an entity's exposure to risk from financial instruments.

24. In addition, too much fragmentation of information required by IFRS throughout the annual report may make it difficult to identify what is IFRS information (which is potentially audited) and also difficult to identify and assess the financial statements as a whole.

25. For these reasons, we think that disclosing IFRS information outside of financial statements would generally only be appropriate when it brings IFRS and non-IFRS disclosures together for a particular matter, and disclosing it outside of the financial statements does not detract from, or reduce the understandability of, the financial statements.

Potential areas for disclosing information required by IFRSs outside of financial statements

26. The most common situation for an entity wanting to place information required by IFRS outside of the financial statements together with other information in the entity's annual report will be when the disclosures relate to the same topic, and the other disclosures are required by a different regulator or for a different purpose. In these circumstances, some disclosures might meet both purposes because the requirements overlap. In other cases they provide information about different perspectives of the same topic and the entity might consider that it is more

appropriate, and effective, to report all related information of the specific topic together.

27. For example, in some jurisdictions there is a significant overlap of related party disclosure in accordance with IFRS and other disclosures as part of the entity's annual report, eg the directors' remuneration report. An entity might consider that it is more effective to report key management personnel compensation in accordance with IAS 24 *Related Party Disclosures* together with the remuneration report—which usually provides more detailed information about management compensation schemes.

28. Disclosures about risk management, and disclosures about non-adjusting post-balance sheet events, are likely to be suitable candidates, because significant overlaps of disclosures with other parts of an entity's annual report exist in some jurisdictions.

29. Similarly, we consider that in some jurisdictions that management commentary and segment information are considered to be closely interlinked. The entity may conclude that reporting disclosures in accordance with IFRS 8 *Operating Segments* together with other segment information as part of the management commentary, would be a more effective way of reporting the related information, enhancing the understandability of the annual report.

Use of a general principle vs. use of criteria for developing disclosure guidance

30. The staff also reconsidered whether—instead of a general principle at a Standard level—the scope and circumstances identified above in paragraphs 13-29 should be used as common criteria by the IASB for developing or revising disclosure guidance on cross-referencing in a particular Standard.

31. The staff believe that a general principle at Standard level has the key benefit of being generic enough to be applicable in different and changing national reporting

environments. In other words, without a general principle, the IASB might need to constantly observe and respond to changes of entities' reporting environment in many different jurisdictions. In addition, the staff believe that a general principle would also help to streamline disclosure guidance across Standards and would therefore limit the risk of introducing inconsistencies in guidance in or between particular Standards. The staff have already observed slight differences in existing guidance about cross-referencing. Consequently, the staff conclude that overall it would be more useful to establish a general principle at Standards-level instead of criteria at a *Conceptual Framework* level.

32. Appendix A of this paper illustrates how a general principle on cross-referencing based on staff recommendation could be implemented into IFRS disclosure guidance.

Questions for the IASB

Question 1: The staff recommend to limit the general principle for disclosing IFRS information outside the financial statements to information in an entity's annual report. The annual report would be described as a single reporting package of the entity with boundaries similar to those proposed by the IAASB in ED ISA 720 (see paragraph 16). Do you agree? If not, how would you describe the scope of reporting package as eligible source for cross-referencing?

Question 2: The staff recommend that disclosing IFRS information outside of financial statements and incorporating it by cross-reference would only be appropriate when disclosing it outside of the financial statements makes the annual report as a whole more understandable; and the financial statements remain understandable and fairly presented (see paragraphs 21-25). Do you agree? If not, how do you describe the circumstances in which disclosure of IFRS information outside financial statements are appropriate?

Question 3: The staff recommend, instead of having various guidance for specific disclosures in particular Standards, a general principle for IFRS that would guide the preparer in judgement when disclosing IFRS information outside of financial statements and incorporating it by cross-reference is appropriate (see paragraphs 30-32). Do you agree?

Appendix A—Potential implementation of staff recommendation

IAS 1 *Presentation of Financial Statements*

Identification of the financial statements

49 An entity shall clearly identify the financial statements and distinguish them from other information in the same published document.

50 IFRSs apply only to financial statements, and not necessarily to other information presented in an annual report, a regulatory filing, or another document. Therefore, it is important that users can distinguish information that is prepared using IFRSs from other information that may be useful to users but is not the subject of those requirements.

51 An entity shall clearly identify each financial statement and the notes. In addition, an entity shall display the following information prominently, and repeat it when necessary for the information presented to be understandable:

(a) **the name of the reporting entity or other means of identification, and any change in that information from the end of the preceding reporting period;**

(b) **whether the financial statements are of an individual entity or a group of entities;**

(c) **the date of the end of the reporting period or the period covered by the set of financial statements or notes;**

(d) **the presentation currency, as defined in IAS 21; and**

(e) **the level of rounding used in presenting amounts in the financial statements.**

52 An entity meets the requirements in paragraph 51 by presenting appropriate headings for pages, statements, notes, columns and the like. Judgement is required in determining the best way of presenting such information. For example, when an entity presents the financial statements electronically, separate pages are not always used; an entity then presents the above items to ensure that the information included in the financial statements can be understood.

53 An entity often makes financial statements more understandable by presenting information in thousands or millions of units of the presentation currency. This is acceptable as long as the entity discloses the level of rounding and does not omit material information.

X1 An entity may disclose information required by IFRSs outside of its financial statements but within the annual report if:

(a) locating the information outside of its financial statements enhances the understandability of the annual report as a whole and the financial statements remain understandable and fairly presented;

(b) the information is incorporated into the financial statements by cross-reference; and

(c) the information is available to users of the financial statements on the same terms as the financial statements and at the same time.

X2 Disclosing information required by IFRSs outside of financial statements and incorporating it into financial statements by cross-reference enhances understandability of financial statements if it:

(a) links related information together so that the relationships between items of information are clear; and/or

(b) reduces duplication of information.

X3 Disclosing information as required by IFRSs outside of financial statements and incorporating it by cross-reference can fragment information so that it makes it difficult to understand and may mean that the financial statements are not fairly presented. It may also make it difficult to identify a complete set of financial statements. For example disclosing closely related information in a widely dispersed way throughout the annual report may not only make it difficult to identify the complete set of financial statements, it may obscure information and relationships between information needed to meet disclosure objectives and requirements a particular Standard. For this reason, disclosing IFRS information outside of financial statements and incorporating it by cross-reference would generally only be appropriate when it brings IFRS and non-IFRS disclosures together for a particular matter.

X4 If an entity applies cross-referencing in accordance with paragraph X1, it shall:

(a) disclose, together with the unreserved statement of compliance in accordance with paragraph 16 of IAS 1, a list of cross-referenced disclosures placed outside the financial statements in the entity's annual report that form part of a complete set of financial statements in accordance with IFRS;

(b) depict the cross-referenced information located outside financial statements as being information prepared in accordance with IFRS (and audited if applicable);

(c) make the cross-referencing direct and precise as to what it relates to; and

(d) ensure the cross-referenced information remain available over time at the cross-referenced location.

Appendix B—Extract from ED ISA 720—Further explanation of proposed definition of the term 'Annual Report'

A1. Law, regulation or custom may define the content of an annual report, and the name by which it is to be referred, for entities in a particular jurisdiction. In some cases, an entity's annual report may be a single document and referred to by the title "annual report" or by some other title. In other cases, law, regulation or custom may require the entity to report to owners (or similar stakeholders) information on the entity's operations and the entity's financial results and financial position as set out in the financial statements (i.e., an annual report) by way of a single document, or by way of two or more separate documents that in combination serve the same purpose. An annual report contains or accompanies the financial statements and the auditor's report thereon. For example, depending on law, regulation or custom in a particular jurisdiction, one or more of the following documents may form part of the annual report:

- Management report, management commentary, or operating and financial review or similar reports by those charged with governance (for example, a directors' report).
- Chairman's statement.
- Corporate governance statement.
- Internal control and risk assessment reports.

A2. An annual report may be made available to users in printed form, or electronically, including on the entity's website. A document (or combination of documents) may meet the definition of an annual report, irrespective of the manner in which it is made available to users.

A3. An annual report is different in nature, purpose and content from other reports, such as a report prepared to meet the information needs of a specific stakeholder group or a report prepared to comply with a specific regulatory reporting objective. Examples of reports that, when issued separately, are not typically part of the combination of documents that comprise an annual report (subject to law, regulation or custom), and that are, therefore, not other information within the scope of this ISA, include:

- Separate industry or regulatory reports, such as may be prepared in the banking, insurance, and pension industries.
- Corporate social responsibility reports.
- Sustainability reports.
- Diversity and equal opportunity reports.
- Product responsibility reports.
- Labor practices and working conditions reports.
- Human rights reports.

A4. Documents that are referred to as integrated reports may or may not be the entity's annual report, or part of the combination of documents that comprise the entity's annual report, depending on their nature, purpose and content, and whether such documents contain or accompany the financial statements and the auditor's report thereon.