

# AGENDA PAPER

IFRS Foundation Trustees meeting—Due Process Oversight Committee

MEXICO CITY 8 OCTOBER 2014

Agenda ref 3F

PRESENTER DAVID LOWETH

AUTHOR MICHELLE SANSON

## Correspondence: update

### Introduction

1. The purpose of this paper is to provide an update on whether any correspondence has been received on due process issues since the DPOC's meeting held on 8 July 2014 in Sydney.
2. At the time of writing (26 September), no new correspondence requiring the DPOC's attention has been received.

### EFRAG Draft letter

3. At the last DPOC meeting we brought one potential item to the Committee's attention (Agenda Paper AP 3G for that meeting refers). We reported that the European Financial Reporting Advisory Group (EFRAG) had issued on its website a draft letter *EFRAG Invites comments on proposal to enhance IFRS quality control*. The draft letter was open for comment until 15 August 2014.
4. Members may recall that the draft letter called for a change to the final stage of the IASB standard-setting process. In summary, the letter stated:
  - (a) Recent experience shows that despite efforts, final requirements can be difficult to understand and implement by the public at large. In EFRAG's view this is evidence that the IASB should improve its standard-setting process at the stage of finalising a Standard.
  - (b) Difficulties in understanding the Standard increase implementation costs, feed the views of those that consider IFRS to be complex and encourage the questioning of the quality of IFRS.
  - (c) Those currently involved in the private fatal flaw review have a prior understanding of the intended outcomes and therefore the review is likely to miss shortcomings in the drafting.

- (d) EFRAG, in its response of 20 September 2012 to a public invitation to comment on revisions to the *Due Process Handbook*, called for the due process in relation to the review drafts to be further developed.
- (e) If the IASB does not implement a fatal flaw public Exposure Draft, it ‘could’ consider inserting a new ‘implementation stage’. This stage would be after the publication of the Standard and would require the IASB to set up a dedicated team to respond to difficulties encountered in practice. The team would have sufficient authority to handle understandability and implementation issues, in a similar way to the issue of agenda decisions by the IFRS Interpretations Committee. Before the end of the implementation stage, an amended version of the final Standard would be approved by the IASB and published without supplementary due process. This amended version would to reflect all tentative drafting changes that had been decided upon and published throughout the implementation stage.

### **Staff comment**

- 5. EFRAG received 14 responses to the consultation. At its meeting on 19 September 2014, the EFRAG Supervisory Board reviewed a summary of the comment letters received.
- 6. The comment letters indicate support for EFRAG’s view the in the IASB’s standard-setting process at the stage of finalising a standard can be improved. EFRAG also notes that difficulties in understanding a standard increase the implementation costs, feed the views of those who feel that IFRS are too complex and encourage the questioning of the quality of IFRS. That said respondents do not support EFRAG’s proposal to introduce an ‘implementation stage’.
- 7. Respondents expressed a number of reasons for agreeing with EFRAG’s view that the IASB’s standard-setting process at the stage of finalising a Standard can be improved. These reasons include:
  - (a) in some cases, amendments have been issued shortly after the Standard has been issued; and
  - (b) reduced understandability of recently issued Standards.
- 8. The reduced understandability includes a concern that Standards are not written in plain English and that there is a lack of clarity about new and existing terms.
- 9. Alternatives to the implementation stage that had been proposed by EFRAG were also suggested. These include:
  - (a) improving the transparency of the current ‘fatal flaw’ procedures; and
  - (b) improving outreach both in the early stages of a project and in the finalisation stages, such as by field testing and conducting an effects analysis.

10. A number of respondents also noted that improvements had been made by the IASB and some referred to the Transition Resource Groups that have been established by the IASB for revenue and impairment of financial assets as being an example of an improvement.
11. At its meeting the EFRAG Supervisory Board agreed with the EFRAG staff recommendation to remove from the draft letter to the IASB the proposal for an implementation stage to be inserted, because of the lack of support for the proposal from EFRAG's constituents. The Supervisory Board, however, agreed to send a letter calling for a public fatal flaw review prior to finalising any major amendments or new Standards.
12. As noted above, EFRAG raised the issue of a public fatal flaw review in its response to the IFRS Foundation's 2012 review of the *Due Process Handbook*. The DPOC considered this at its meeting in October 2012, as part of its consideration of the issues raised by responses to the proposals to revise the *Due Process Handbook*. The report of that meeting<sup>1</sup> noted that:

“The DPOC considered the suggestions made by some respondents that review drafts should in effect become a systematic step in the due process and be published on the website for public fatal flaw reviews and field testing. It was noted that the purpose of a review draft was unclear. The IASB saw review drafts as a final ‘housekeeping check’ to ensure that the draft document was clear and reflected accurately the technical decisions made by the Board. It was not a document used to consider the appropriateness of the Board’s decisions. The DPOC accepted that having a review draft for external review should not become a mandatory due process step, but thought that the DPH should clarify the purpose of a review draft and what a review draft was not”.

13. This view was reflected in the *Due Process Handbook: Feedback Statement* that accompanied the issue of the revised *Due Process Handbook* in February 2013:

“We do not think that a review draft should become a mandatory due process step. The *Due Process Handbook* clarifies what the purpose is of such a draft and what it is not, noting that it does not constitute a formal step in the due process, and it is not a substitution for a formal due process step. It has a limited purpose, representing an editorial ‘fatal flaw’ review in which reviewers are asked whether the draft is clear and reflects the technical decisions made by the IASB. To reflect this, the *Due Process Handbook* uses the term ‘draft for editorial review’<sup>2</sup>.

14. The *Due Process Handbook* (paragraph 3.31) does give the IASB flexibility as to whether it makes available on the website a draft for editorial review. The IASB also has discretion as to the nature of the external review. But the *Due Process Handbook* (paragraph 3.32) does go on to specify the limited purpose of the draft for editorial review and the fact that it

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<sup>1</sup> Available at: <http://www.ifrs.org/DPOC/meetings/Documents/DPOCmeetingreportOct12.pdf>.

<sup>2</sup> The Feedback Statement can be accessed at: <http://www.ifrs.org/DPOC/Documents/2013/Feedback-Statement-Due-Process-HB-February-2013.pdf>.

does not constitute, nor is it a substitute for, a formal step in the due process. EFRAG's draft proposal would imply the introduction of another formal step.

**Action**

15. At the time of writing we have not received the letter from EFRAG and are therefore not in a position to make specific recommendations to the DPOC. However, we note that the DPOC is considering the final report on the Effect Analyses at this meeting—the use of effect analyses was noted by respondents as a potential way to improve the quality control of Standards.
16. The staff will circulate the letter to DPOC members when it is received. The staff will discuss the contents of the letter, together with specific recommendations that they could make for a possible response. Such a response could be cleared either by email, in a conference call or at the DPOC meeting in February 2015.