

International Financial Reporting Standards

Purposes of the primary financial statements and the notes

Principles of Disclosure Project

The views expressed in this presentation are those of the presenter, not necessarily those of the IASB or the IFRS Foundation.

Agenda

- Background
- Objective of financial statements
- Purpose of the primary financial statements
- Purpose of the notes
- Questions

Background

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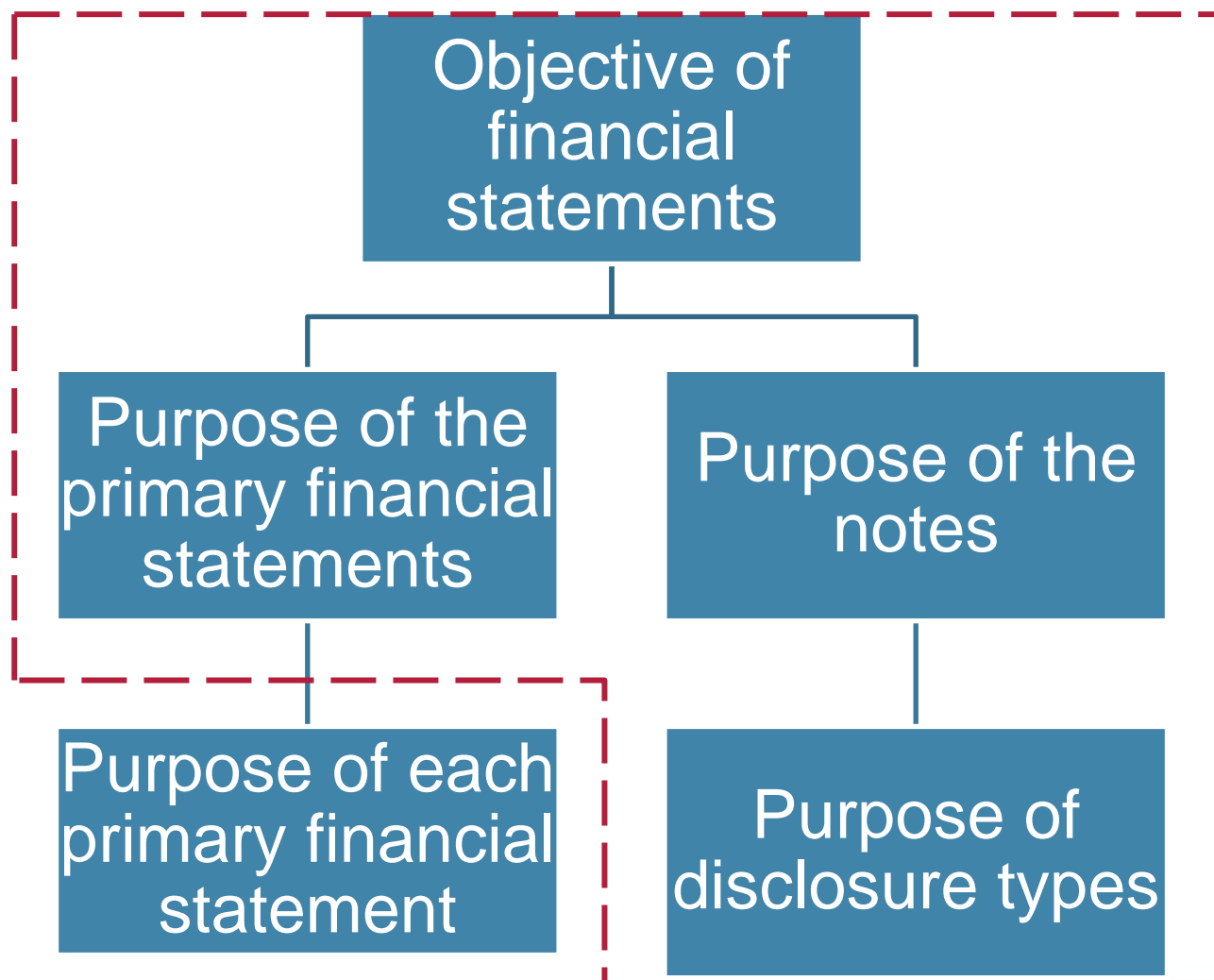
What we have heard, what we will cover

- Requests to clarify the purpose of the notes reflect the need for help:
 - making decisions about placement in financial statements (generally the notes) or in management commentary;
 - making decisions about placement between notes and information on the face of the primary financial statements; and
 - setting better disclosure objectives in IFRS (ie the context for determining what information is useful).
- IASB staff think a discussion about the purpose of the notes needs to include a discussion about the purpose of the primary financial statements.

- The *Conceptual Framework* Discussion Paper described the primary financial statements as:
 - the statement of financial position;
 - the statement of profit or loss and other comprehensive income (or the statement of profit or loss and the statement of comprehensive income);
 - the statement of changes in equity; and
 - the statement of cash flows.
- We will use the collective term ‘primary financial statements’ for the purposes of this presentation (for want of a better term).

What we will cover in this presentation

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Objective of financial statements

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Objective of the financial statements

- *Conceptual Framework* project (tentative decision):

Financial statements provide information about an entity's assets, liabilities, equity, income and expenses that is useful to users of financial statements in assessing the prospects for future net cash inflows to the entity, and in assessing management's stewardship of the entity's resources. As a result, financial statements provide information about the financial position, financial performance and cash flows of an entity.

- Proposed objective is consistent with paragraph 9 of IAS 1

Additional tentative decisions:

- discussion about the disclosures that the IASB would normally consider requiring when setting Standards, including disclosures about the nature and extent of risks arising from the entity's assets and liabilities; and
- the IASB should require forward-looking information to be included in the notes to the financial statements only if it provides relevant information about the assets and liabilities that existed at the end of, or during, the reporting period.

Conceptual Framework project

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- The IASB also tentatively decided:
 - not to introduce the term ‘primary financial statements’ in the *Conceptual Framework*; and
 - not to add a separate definition of the purpose of the notes in the *Conceptual Framework*.
- We think these tentative decisions relate to the *Conceptual Framework* only.

Boundary of the financial statements

- Objective of financial statements (in the *Conceptual Framework*) describes their boundary.
- However, in the Principles of Disclosure project:
 - we will not seek to limit what the IASB determines is useful/relevant information (objective of financial reporting); and
 - we will develop guidance that helps determine placement in the financial report.

Distinct purposes – primaries and notes?

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Yes

- Distinct roles.
- Reflects practice.
- Could help the IASB develop disclosure objectives/requirements.
- Necessary for:
 - materiality decisions; and
 - placement decisions.

No

- No distinct role.
- Distinction may imply notes are not as important as 'primary financial statements'.
- Could be too vague to be useful.
- Arbitrary/unnecessary.

Purpose of the primary financial statements

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Purpose of the primary financial statements

- *Conceptual Framework* Discussion Paper:

‘The objective of the primary financial statements is to provide summarised information about recognised assets, liabilities, equity, income, expenses, changes in equity and cash flows that has been classified and aggregated in a manner that is useful to users of financial statements in making decisions about providing resources to the entity.’
[emphasis added]
- Some feedback that the objective was under-developed and vague.

Purpose of the primary financial statements

Representation
Window

Roadmap

Picture

Statement

Snapshot

Signpost

Index

Sheet

Overview

Outline

Summary

Synopsis

Mathematical sum

Characteristics and role of the primary financial statements

- Structured representation of an entity's financial position and financial performance:
 - classified and aggregated; and
 - mathematical sum—inclusive of recognised monetary amounts within a statement total.
- Comparable (high degree of standardisation).
- Both an index (starting point for analysis) and a stand-alone summary sufficient for:
 - overall assessment;
 - do I need to dig deeper? and
 - do I need to do further analysis?

Staff observations – primary financial statements

- A distinct purpose for the primary financial statements would provide a basis for determining:
 - what is a primary financial statement;
 - what should be a line item in the primary financial statements; and
 - materiality judgements in the context of the primaries, eg can an entity omit a primary financial statement?
- Debate about what should be a primary financial statement:
 - little debate that a statement of comprehensive income and the statement of financial position are primary.
- Debate about the terminology – primary infers that the remainder is secondary and therefore inferior.

Purpose of the notes

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- *Conceptual Framework* Discussion Paper

‘The objective of the notes to the financial statements is to supplement the primary financial statements by providing additional useful information about:

- (i) the assets, liabilities, equity, income, expenses, changes in equity and cash flows of the entity; and
- (ii) how efficiently and effectively the entity’s management and governing board have discharged their responsibilities to use the entity’s resources.’

- Feedback:

- clarify the boundary of financial statements; and
- a few noted that notes are of equal importance and do not just supplement the primaries.

Purpose of the notes – IAS 1

- IAS 1 definition of the notes:
 - ‘Notes provide narrative descriptions or disaggregations of items presented in those [primary financial] statements and information about items that do not qualify for recognition in those statements.’
(paragraph 7 of IAS 1)
- Definition appears to be incomplete (outdated) in the context of current IFRS requirements, eg risk disclosures.
- Link between general requirements in IAS 1 and specific disclosure requirements in Standards is unclear:
 - eg accounting policy disclosure in particular Standards vs summary of significant accounting policies.

Purpose of the notes – work of others

- EFRAG, FRC and ANC Discussion Paper:
The purpose of the notes is to provide a relevant description of the items presented in the primary financial statements and of unrecognised arrangements, claims against and rights of the entity that exist at the reporting date.
- FASB Exposure Draft:
The primary purpose of notes to financial statements is to supplement or further explain the information on the face of financial statements by providing financial information relevant to users.
- Other approaches exist among constituents to categorise or list all general types of disclosures in the notes with description of their objectives.

- Direct relationship with the primary financial statements:
 - provide further information about recognised amounts eg expand line items, different perspectives;
 - unrecognised assets and liabilities;
 - information relevant to an understanding of the above.
- Different purpose does not mean inferior.
- Do different types of disclosures have different purposes?
 - we think that detailed purposes by disclosure type could assist the IASB and entities make relevance/materiality judgements.
 - should the IASB specify the types of disclosures that form the notes?

Purpose of the notes – more detail needed?

- Possible information types (note may overlap with each other):
 - reporting entity;
 - additional information about line items;
 - information about other past events and current conditions and circumstances that can affect an entity's cash flows:
 - unrecognised assets or liabilities; and
 - risks.
 - methods, assumptions and judgements:
 - accounting policies.
 - alternative measurements in which this information would be relevant; and
 - control/stewardship.

Questions

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- Do the primary financial statements (as a group) and the notes have distinct purposes?

If yes:

- How would you describe those distinct purposes?
- What collective term would you use to describe the ‘primary financial statements’?
- Is the current set of primary financial statements (listed on slide 5) appropriate?
- Should the IASB specify the types of disclosures that form the notes?