Discussion Paper

Financial Reporting Council

October 2012

Thinking about disclosures in a broader context

A road map for a disclosure framework

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Disclosure framework: FRC discussion paper

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Foreword

We note that concerns about the increasing complexity and decreasing relevance of financial reports have been growing in recent years. We are committed to improving the quality of corporate reporting. We believe that there is a need for a disclosure framework and this was one of the recommendations in the Financial Reporting Council's (FRC) 2009 Discussion Paper (DP) *Louder than Words.*

“We are committed to improving the quality of corporate reporting.”

By publishing this paper, our aim is to:

- Recognise that a disclosure framework should consider disclosures in the financial report as a whole.
- Curtail the piecemeal approach to disclosures that is likely to continue as a result of future developments in disclosures, such as the forthcoming EC proposal on non-financial information and integrated reporting.
- Provide a framework to influence others addressing disclosure.
- Influence the International Accounting Standards Board (IASB) before it starts its recently announced project on a disclosure framework. We have set out a list of possible action points for the IASB on page 58.

In this DP, we present a road map for a disclosure framework. When suggesting any new concepts, it is helpful to be able to visualise what is meant at each stage. Therefore, we discuss a number of ideas for what a disclosure framework might include. These ideas have evolved over the period the FRC has been working with European Financial Reporting Advisory Group (EFRAG) and Autorité des normes Comptables (ANC) on a disclosure framework for the notes.

The ideas that we have put forward in this paper are not intended to be the final conclusions on a disclosure framework. They are presented as a starting point for debate. We do not intend this paper to be a 'straitjacket' but a basis to encourage innovation and experimentation.

Roger Marshall
Director, Financial Reporting Council

Thanks for the support

The ANC and Deutsches Rechnungslegungs Standards Committee e.V. (DRSC) support the issue of this DP. These bodies, while encouraging debate on the issues presented in the paper, do not express any opinion on those matters at this stage.

We would like to thank the staff of the ANC, DRSC, EFRAG and Organismo Italiano di Contabilità (OIC) for their comments during the development of this paper.

Joint EFRAG/ANC/FRC Discussion Paper

The FRC, in partnership with the EFRAG and the ANC, has recently published a DP *Towards a Disclosure Framework for the Notes* (referred to simply as 'joint DP' in this paper). The joint DP forms an essential part of the full disclosure picture but is deliberately limited in scope.

This paper complements the joint DP as it sets out the FRC's thinking on how a disclosure framework might apply in a broader context. In particular, this paper considers placement criteria, which in the FRC's view, are an integral part of a disclosure framework.

Introduction

The problem

Disclosure overload can make it difficult to see the 'wood for the trees'. In our view, the 'disclosure problem' is not just about quantity; the quality of disclosures, in terms of meeting the needs of users, is also an issue. Financial reports have become a disjointed collection of disclosures driven by different authoritative sources. The objective of financial reporting seems to have been forgotten as disclosures have become more about compliance than communication.

Who is this paper for?

We believe that improving disclosure is a shared responsibility. This paper is intended for standard setters, other regulators, preparers, auditors and users, although particular sections may be of more interest to specific groups. For example, the section addressing placement is primarily aimed at the regulators that set regulations governing the content of financial reports.

What is a disclosure framework?

We believe that a disclosure framework is a framework that draws together all the various strands of financial reporting that relate to disclosures. The aim is to develop a coherent framework within which standard setters and other regulators can set disclosure requirements and preparers and auditors can apply them. We anticipate that this will improve the quality of information provided to users.

"We believe that improving disclosure is a shared responsibility."

In this paper, we refer to:

- Regulators – all bodies involved in setting regulations.
- Regulations – all laws, accounting standards and other requirements that govern the content of financial reports.

What are the benefits of a disclosure framework?

We believe that the benefits of a disclosure framework are:

- The content of disclosures being more targeted to the needs of users;
- Ensuring that regulators only add disclosures to financial reports where those disclosures meet the objective of financial reporting;
- More consistent setting of disclosure requirements across standards;
- A reduction in the burden of disclosures arising from setting proportionate disclosure requirements;
- The elimination of duplicate information within financial reports;
- Better organisation of disclosures, which will make financial reports easier to navigate, as information fulfilling set objectives will be positioned within the same section of a financial report;
- Empowering preparers to apply materiality more robustly to disclosures; and
- Elimination of boilerplate disclosures.

Ultimately we believe that these benefits will lead to improved communication.

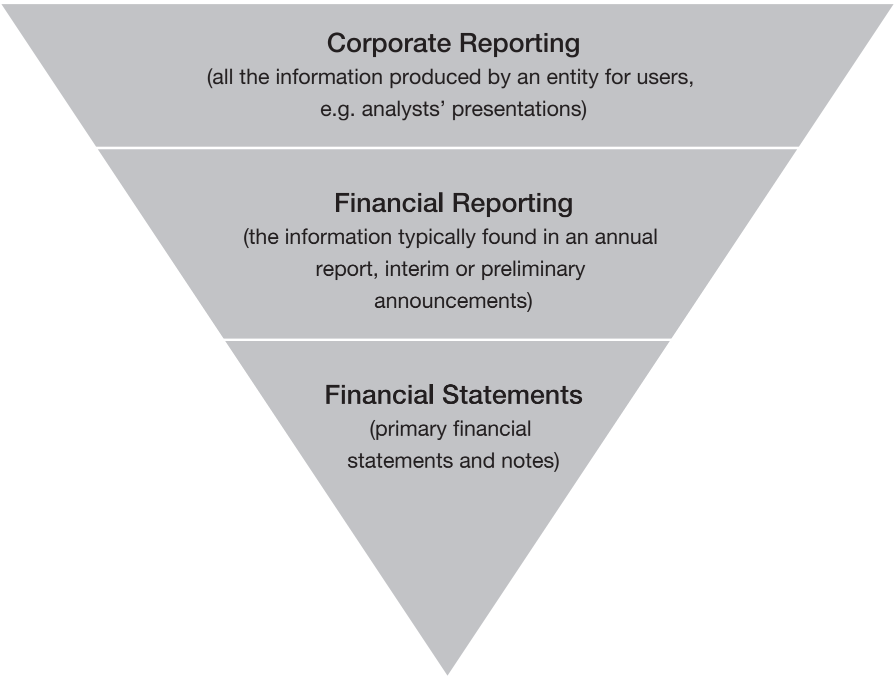
“Ultimately we believe that these benefits will lead to improved communication.”

What is financial reporting?

The IASB's Conceptual Framework covers financial reporting, although that term has not yet been defined.[1,2] We believe that this is one of the gaps in the Conceptual Framework that needs to be filled.

Financial reports communicate financial information to users and financial information takes many different forms.[3] For the purposes of this paper, we distinguish between corporate reporting, financial reporting and financial statements as illustrated below.

"For the purposes of this paper, we distinguish between corporate reporting, financial reporting and financial statements…"



Objective of financial reporting

In this paper we focus on disclosures that meet the objective of financial reporting, which is to provide information that is useful to users.[4] The objective assists in determining the boundary of a financial report.[5] We take the view that disclosures that do not meet the objective of financial reporting should be excluded from the financial report. We consider that this would be a step towards making annual reports shorter and more relevant.

We request regulators to consider what their objectives are when setting disclosure requirements and whether those objectives are in line with the objective of financial reporting and the needs of the users of those financial reports.

Annual financial reports sometimes contain carbon emissions disclosures or some disclosures required by prudential regulators. Recently, the EU consulted on country-by-country reporting for extractive industries, including a proposal to include additional disclosures in the financial statements.[6,7] Some would say that these are examples of disclosures that may be better placed outside the annual financial report, as they do not meet the objective of financial reporting.

In this paper, we focus on disclosures that are contained within the annual financial report. We note that financial reporting refers to a wider information set than just the annual financial report, but we use the annual financial report to provide structure to our discussion. Where it is informative to the debate, we also consider disclosures in other types of financial reports such as preliminary announcements.

Joint DP – Objective of a disclosure framework

In our joint DP, we have expressed the general objective of a disclosure framework in the context of the financial statements as: "To ensure that all and only relevant information is disclosed in an appropriate manner, so that detailed information does not obscure relevant information."

We believe that this general objective applies in the broader context of financial reporting as well.

Components of a financial report

Once we have established the boundaries of financial reporting, we need to identify the components of a financial report. While the boundary has not been formally established, the IASB is clear that it includes management commentary as well as the financial statements.[8]

Further, there are specific components of the financial reporting package that have evolved in practice.

Management Commentary	Corporate Governance	Financial Statements

The existence of these three components is reinforced by the EU Accounting Directives, which require each of these components within an annual financial report.[9]

> "We hope that this paper will be a catalyst for change."

Next steps

We hope that this paper will be a catalyst for change. While improving disclosures is a shared responsibility, we believe that the IASB could take the lead in developing a disclosure framework as they are an international body. We are pleased to note that the IASB has stated its intention to add a disclosure framework to its future agenda. We also believe that a disclosure framework should not be developed in isolation, but should be considered as part of the reinvigorated Conceptual Framework project. Determining the boundaries and components of financial reports, as well as developing a definition of disclosure, as distinct from presentation, would be key first steps that would contribute to the development of a disclosure framework.

Distinguishing presentation from disclosure is an aspect of the disclosure framework that is specific to financial reporting standard setters. We have set out some thoughts for developing a definition of disclosure as compared to other considerations in standard setting, i.e. recognition, measurement and presentation, in Appendix A.

As well as considering disclosure explicitly within the Conceptual Framework, we believe that there are other steps that the IASB can take that will enable preparers and others to more critically assess which disclosures they include in financial reports. All our suggestions for the IASB are set out on page 58.

"As a starting point… we set out a road map for the development of a disclosure framework. We have framed this around four questions."

What do you think?

When you have read this paper, we would like to know what you think. As a starting point, on the next page we set out a road map for the development of a disclosure framework. We have framed this around four questions.

Is what we are suggesting a logical and sensible way forward? What other suggestions do you have for the development of a disclosure framework? To help frame your views, we have raised a number of questions which are set out on page 60 of this paper.

So let us know what you think. We would appreciate your comments by 31 January 2013, by post or email to:

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We have structured our road map for a disclosure framework around four questions:

1.

What information do users need?

Aim: to ensure that disclosures are relevant and targeted to meet the needs of users.

The first step in the journey to a disclosure framework is to establish principles for the content of disclosure requirements.

To develop our thinking, we have identified a set of 'disclosure themes'. We believe that these represent the common types of information that users need.

Our idea is that these 'themes' would provide a guide when setting disclosure requirements.

Principles for: Content

2.

Where should disclosures be located?

Aim: use placement criteria to provide a structure for the financial report so that disclosures are organised in a way that is more informative to the reader and can be consistently applied.

In order to develop placement criteria, we have identified the components of a financial report and then we discuss how to draw boundaries between each of the components.

Placement

3.

When should a disclosure be provided?

Aim: to reduce the disclosure burden through the application of the concepts of proportionality and materiality.

We use the term proportionality in this paper to refer to the steps regulators can take to ensure that disclosure requirements are proportionate for a particular group of entities in line with the needs of users.

We then discuss what materiality means from a disclosure perspective. Materiality is entity-specific. Preparers apply materiality to disclosure requirements set by regulators so that financial reports only provide disclosures that are relevant to the entity.

Proportionality and Materiality

4.

How should disclosures be communicated?

Aim: to develop a set of principles for good communication that will assist in improving the quality of disclosures.

We have developed some principles for the communication of disclosures. These principles are aimed at preparers and provide a practical approach to applying the qualitative characteristics of financial information.[10]

This is one of the areas where we would continue to encourage innovation and experimentation.

Communication

1.

We believe that the starting point for determining the content of disclosures is to identify what information users need. However, that question itself raises a few issues.

- Who are the users?
- What are the sources of information users need?
- What are users' information needs?

In our view, the development of a disclosure framework requires input from users. Comprehensively establishing users' needs is beyond the scope of this paper. However, we consider a number of tools to identify what information users need and set out a number of questions for users (page 60) to start the debate.

Who are the users?

We believe that there is a need for disclosures contained within financial reports to be re-focused on their purpose – providing investors with information that is useful for making their resource allocation decisions and assessing management's stewardship.[11] Our view of 'users' is consistent with 'users' as set out in the IASB's Conceptual Framework.[12]

By understanding the needs of users, we establish the boundary of a financial report. This is essential, because it determines what information should be included and, just as importantly, what information should be excluded from a financial report.

Other stakeholders, such as prudential regulators, may require specific disclosures. However, regulators need to consider the boundaries of the financial report in determining the best place for these specific disclosures to be located.

What are the sources of information users need?
As illustrated in the visual on page 6, we believe that users need information that extends beyond the financial report. In our opinion, a disclosure framework should focus on user needs that can be met by financial reporting. It may be that the principles established for a disclosure framework for the financial report may be capable of broader application, say to corporate reports; however, the initial focus should be on developing a disclosure framework for the financial report.

What information do users need?
We appreciate that identifying the needs of users is not an easy task. There are different types of users and, if users are asked what information they need from financial reports, some would come up with a long list of requirements. We believe that disclosure in the financial report needs to be

"We believe that there is a need for disclosures… to be re-focused on their purpose – providing investors with information…"

sufficient so that it provides information that is common to most investors (as this information will tend to satisfy the needs of other user groups as well) rather than a 'phone book' of all disclosures that satisfy the specific needs of different types of users.

> "We believe that disclosure… needs to be sufficient… rather than a 'phone book' of all disclosures that satisfy the specific needs of different types of users."

Content principles

We have set out some 'disclosure themes' on page 16. These identify the common types of information users may need. From the disclosure themes we have developed a number of principles for the content of disclosures.

Disclose information that provides:

- Context for understanding the performance, position and development of the entity.
- The specific risks to which an entity is exposed, including their context as well as management's approach to those risks.
- An explanation of the corporate governance arrangements in place including setting out the responsibilities of the board.
- A disaggregation of amounts at a level that enables the key components of primary financial statements to be understood.[13]
- An explanation of the basis for recognition and measurement of line items in the primary financial statements.
- Information relating to items not recognised in the balance sheet that, if or when recognised, would have a significant effect on future cash flows.

As part of the development of this paper, we reviewed a sample of disclosures in preliminary announcements to obtain an insight into the types of disclosures that are important for users. We have included the results of that review in Appendix B.

Disclosure themes

We have identified some common themes for the types of information that users may need.

Management commentary

Provides context for understanding the financial statements and commentary that supplements and complements the financial statements *(including non-financial information*)* addressing areas such as:

Unrecognised amounts

Provides information about those items that are not currently recognised but may be in future as they impact future cash flows:

- Commitments and contingencies
- Off balance sheet arrangements
- Non-adjusting post balance sheet events

Risks

Provides information about factors that could adversely affect amounts in the primary financial statements:

- Principal risks (e.g. credit, foreign exchange)
- Valuation uncertainty
- Liquidity
- Solvency
- Use of derivatives

Primary financial statements

Present an entity's financial results in accordance with Generally Accepted Accounting Practice (GAAP) on a comparable basis

Disaggregation

Provides disaggregation of amounts in the primary financial statements:

- Segmental information
- Type of financial instrument
- Components of aggregated items

Explanatory material

Provides information on recognition and measurement of items in the primary financial statements and linkage between financial statements:

- Business model
- Resources, risk and relationships
- Objectives and strategies
- Results of operations and prospects
- External environment
- Critical performance measures and indicators both financial and non-financial

Uncertainties

Provides information about key assumptions and uncertainties:

- Key assumptions
- Sensitivities to assumptions
- Use of estimates (e.g. provisions)

- Accounting policies
- Basis of valuation
- Reconciliations (e.g. bad debt or net debt reconciliations)
- Recurring vs. non-recurring items

Corporate Governance

Provides information about the responsibilities of the board.

Board composition and effectiveness:

- Strategy
- Stewardship
- Committees
- Procedures and decisions
- Risk management

Accountability to shareholders:

- Control environment
- Related party disclosures
- Audit function
- Dialogue with shareholders
- Remuneration

**Non-financial information*

We use the term 'non-financial' to refer to information such as resources and relationships, environmental matters and management's expectations of future performance. This type of information is often included in management commentary.

Financial reports contain a mixture of both financial and non-financial information. We believe there is a need for a debate around the types of non-financial information that users need to be included in a financial report.

2.

Where should disclosures be located?

The regulations governing the disclosures required within financial reports are set by a number of regulators, and these differ by country. We do not envisage that this will change, in that there will continue to be multiple regulators governing the content of financial reports. However, it is essential that there is a principles-based disclosure framework, within which all regulators can operate.

Given that the IASB will be setting the boundaries of financial reporting as part of their Conceptual Framework project, and have already considered placement within an earlier project on Management Commentary, they would appear to be the most logical body to set the principles-based disclosure framework, including placement principles.

We acknowledge that there may be barriers to moving information to a different place in the financial report, such as legal constraints, audit considerations, or the mandate of standard setters. However, we have not let these limit our thinking.

What are placement criteria?

Placement is about geography. Placement criteria assist with determining where disclosures should be located in a financial report.

Why do we need placement criteria?
We believe that having placement criteria as part of the IASB's Conceptual Framework would provide a method for organising disclosures. We believe that this would encourage regulators to work together and co-ordinate disclosure requirements. Placement criteria would also enable users to locate information more easily as similar information is grouped together.

Currently, the location of disclosures in financial reports tends to be driven by which regulator set the requirement. For example, disclosures that are required by the IASB are generally included in the notes to the financial statements. As disclosures in the financial report have expanded, we believe that there is a need to re-think how disclosures are organised.

We believe that having a structure for a financial report and criteria for where disclosures should be located are likely to result in financial reports being more cohesive. It may even be a step towards eliminating duplication and inconsistency that often exists in the front and the back halves of the financial report, often as a result of similar requirements being set by different regulators.

Components of a financial report

We believe that the first step in developing placement criteria is to identify the components of a financial report. We identified these components as:

Management Commentary	Corporate Governance	Financial Statements

"We believe that [having placement criteria] would encourage regulators to work together and co-ordinate disclosure requirements."

Objective of the components
The second step is to determine the content of the disclosures that should be included in each of the components; to achieve this, we believe it is necessary to consider the objective of each of the components:

Component	Objective
Management Commentary	Provides context for the related financial statements.[14]
Corporate Governance	Provides information about the responsibilities of the board in setting the company's strategic aims, supervising the management of the business and reporting to shareholders on their stewardship.[15]
Financial Statements	
Primary Financial Statements	Present an entity's financial position, performance and development in accordance with GAAP on a comparable basis.
Notes	Amplify and explain the financial statements.[16]

Placement criteria

This paper builds on the placement criteria that were considered in the IASB's DP 'Management Commentary'.[17] That paper contains two criteria to differentiate between information in management commentary and the notes.

Information would be disclosed:

(1) In management commentary if it provides an investor with information that puts the financial statements into the context of the entity and its operating environment; and

(2) In the notes if it is essential to an understanding of the primary financial statements and its elements.

The Management Commentary DP suggested that all unrecognised items should be disclosed in the notes; as an example, under the IASB's criteria disclosures about proven and probable mineral reserves would be provided in the notes.[18] Whilst we agree that there should be some disclosure of unrecognised items in the notes, we believe that there is a need to draw a boundary around those that are provided in the notes and those that are provided elsewhere in the financial reporting package.

> **"… we have identified corporate governance as an integral component of a financial report."**

In this paper, we have identified corporate governance as an integral component of a financial report. Therefore, we require a third criterion for governance:

(3) In governance if it provides information about the responsibilities of the board in setting the company's strategic aims, supervising the management of the business and reporting to shareholders on their stewardship.

Where do we draw the boundary?

Developing placement criteria inevitably leads to drawing a line between different components of a financial report. We do not think that this is clear cut and we believe that experimentation in this area would be helpful. However, thinking about the content of information in each of the components can assist in the application of placement criteria.

The placement criteria identified above can be linked back to the 'disclosure themes' (page 16), which we used to identify the content of disclosures.

Management Commentary	Corporate Governance	Financial Statements		
Management Commentary	Corporate Governance	Disaggregation	Explanatory Material	Unrecognised Items
Risks and Uncertainties				

As we have illustrated, the 'themes' for management commentary and corporate governance map directly to the equivalent components. However, we believe that setting a boundary for the other 'themes' requires more thought.

Management commentary
There are a couple of features of information contained in management commentary that distinguish disclosures in management commentary from those in other parts of the financial report.

Information in management commentary generally provides management's view. This is in contrast with financial statements that are prepared up to the reporting date. Management commentary may also include forward-looking information that may not relate to past transactions and other events existing at the reporting date.

Corporate governance
Corporate governance involves a set of relationships between a company's management, its board, its shareholders and other stakeholders.[19] Corporate governance disclosures set out the responsibilities of the board.

Financial statements
When developing placement criteria for the notes, we believe it is helpful to consider how the disclosures are used. Note disclosures assist users with:

- Understanding whether the numbers in the primary financial statements reflect the economics of the business; and
- Making judgements on the sustainability of reported profits and cash flow.

Joint DP – Definition of the purpose of the notes

Our joint DP defines the purpose of the notes as: "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."

More details on this definition are included in Chapter 2 of the Joint DP.

Disclosures required by accounting standard setters tend to be placed in the notes to the financial statements. We believe that some of those disclosures, whilst useful, may be better placed elsewhere in the financial report. Disclosures that are usually found in the notes can be grouped into the following 'themes':

- Disaggregation
- Explanatory material
- Unrecognised amounts.

We have identified the objective of the notes to the financial statements on page 21 as to 'amplify and explain the financial statements'. Therefore, it seems a logical step that the starting point for placement criteria for the notes are the numbers reported in the primary financial statements.

Disaggregation and Explanatory material
Disclosures that disaggregate and explain are linked to the numbers reported in the primary financial statements. Therefore, those disclosures would be placed in the notes.

Unrecognised amounts
We believe that drawing the boundary for disclosures relating to unrecognised amounts is more difficult.

One principle might be:

Disclosures that are linked to or are likely to affect a user's understanding and perception of the numbers reported in the primary financial statements should be placed in the notes.

Joint DP – Unrecognised amounts

The joint DP draws the line for disclosure of unrecognised amounts at those that relate to events that exist at the reporting date. One of the implications of this approach is that disclosures of non-adjusting post balance sheet events would be placed outside the notes.

Under that approach, disclosures on post balance sheet events would still be considered useful to users but may be better placed outside of the notes.

A disclosure is placed in the notes when non-disclosure might make the primary financial statements misleading.

While this principle may have appeal, as it seems to include essential information in the notes to the financial statements, it is so broad that it is easy to argue that potentially any disclosure could affect a user's understanding and perception of the number.

> "There is already a precedent for locating risk disclosures outside the financial statements. IFRS 7… allows such disclosures to be located… in management commentary…"

Risks and Uncertainties
Risk disclosures appear in different places in the financial report. They are an example of how the placement criteria identified above might apply.

Management Commentary	Corporate Governance	Financial Statements
Management's view on risk exposures and how they are managed day to day	The nature and extent of risks the Board is willing to take and ensuring that the system of internal control is effective	Maturity analysis Disaggregation of balance by risk exposure

There is already a precedent for locating risk disclosures outside the financial statements. IFRS 7 *Financial Instruments: Disclosures* is a standard that allows such disclosures to be located outside the notes to the financial statements in management commentary or a risk report.[20]

We have heard that some investors favour grouping all risk disclosures together in one place, in a risk report. This is the approach to risk reporting in Germany, and is adopted by a number of banks in the UK.

Implications of placement criteria

One of the implications of the placement criteria that we have identified is that some of the disclosures in financial reports will be located in a different place to where they are currently. Some examples are set out in the following pages.

Non-GAAP measures
Applying the placement criteria identified previously, non-GAAP measures that are linked to the primary financial statements would be placed in the notes. As an example, the net debt reconciliation is produced from the numbers in the primary financial statements. We note that IAS 1 does not prevent such disclosures being provided in the notes.

We believe that non-GAAP measures can provide relevant information for users and that the placement criteria above may promote consistency in reporting in this area. For example, where entities are disclosing information based on adjusted profit figures, it may be appropriate for these to fall under the regulator that has responsibility for the notes.

Related party disclosures
Related party disclosures provide valuable information on stewardship.[21] Applying the third placement criteria, we consider that related party disclosures should be provided in the corporate governance component of the financial report.

"Applying the first placement criteria… non-GAAP measures that are linked to the primary financial statements would be placed in the notes."

Non-adjusting post balance sheet events
Non-adjusting post balance sheet events are unrecognised as they relate to conditions that did not exist at the balance sheet date. For example, the destruction of a major production plant by a fire after the balance sheet date.

Applying the first placement criteria, this disclosure provides context for the financial statements and relates to a future reporting period. Therefore, the disclosure would be provided in management commentary.

"We believe that placement criteria still have a role in an online reporting format."

Role of placement criteria in an online format

We believe that placement criteria still have a role in an online reporting format. In our view, the criteria would enable users to know where to find the disclosures they need as there would be a consistent structure for the financial report.

Others believe that placement criteria become irrelevant as users make use of search functions in online reports and with developments such as XBRL. We believe that these are the tools to report the information, and whilst they make navigation easier, they do not solve the problems relating to cohesion and duplication of information.

3.

When should a disclosure be provided?

In this paper and the joint DP, we refer to proportionality as steps taken by standard setters to set disclosure requirements that are proportionate to users' needs for a specified group of entities. In this paper we briefly address how proportionality could be considered within a disclosure framework.

Materiality is a much more difficult subject when it comes to disclosure. There appears to be a need for guidance on what materiality means from a disclosure perspective. The concept of materiality is set in accounting standards but applied by preparers and auditors as it is entity-specific.

Proportionality

Disclosures need to be proportionate to the nature of an entity taking into account the needs of the users of those financial reports.

IFRSs are accounting standards designed with large listed companies, whose equity or debt is traded on the capital markets, in mind. However, in some jurisdictions regulators have decided to permit or require the use of IFRSs for unlisted entities. Consequently, the level of disclosure required by IFRSs may not be appropriate for the needs of the users of those financial reports.

We believe that there are a number of ways in which standard setters can address the issue of proportionality for disclosures:
- Simplify the disclosure requirements for all entities;
- Set principles-based disclosure requirements that allow preparers the flexibility to determine the level of disclosure that is appropriate for the entity; or
- Develop a differential disclosure regime with different levels of disclosure.

Differential disclosure regimes
A number of standard setters have been considering differential reporting regimes which have the effect of simplifying or reducing the disclosure burden for certain entities.

We have provided a summary of the various approaches on the next page. As illustrated, the determination of which entities are eligible to apply different disclosures can be based on different dimensions: public accountability; size; industry; or where there is a group relationship. We consider that each of these approaches has their advantages and drawbacks.

“We believe that there are a number of ways in which standard setters can address the issue of proportionality for disclosures…”

We believe that there should be two main drivers of a proportionate disclosure regime:

- Relevance of the information contained in the disclosure requirement for users of the financial reports for that entity; and
- Cost of providing the information justified by the benefits to users.

Standard setter	Publication	Effect on disclosures	Comments
Approaches based on public accountability			
IASB	*IFRS for SMEs*	Simpler disclosures for non-publicly accountable entities.	Principles based approaches requiring the application of judgement.
Australian Accounting Standards Board (AASB)	*Reduced Disclosure Regime*	Exemptions from some disclosure requirements in IFRS.	
Approaches based on size			
ANC	Proposal: *Simplify accounting obligations for "small listed companies" in Europe*	Simplify IFRS disclosure requirements and reduce volume of notes.	Sized-based approaches are simple to apply but generally require quantitative thresholds to distinguish between small, medium and large entities.
Approaches based on industry			
FRC	FRS 102 *The Financial Reporting Standard applicable in the UK and Republic of Ireland*	Complex financial instrument disclosures limited to financial institutions only.	Ensures that non-financial institutions are not burdened with disclosures designed for financial institutions, but there are difficulties in defining a financial institution.
Other approaches – group relationships			
FRC	FRS 101 *Reduced Disclosure Framework*	Disclosure exemptions for ultimate parents and subsidiaries.	Objective is that, where equivalent disclosures are available at a consolidated level; these are not duplicated in individual financial statements of group entities.

Materiality

Materiality as a concept in relation to recognition and measurement is well-established. However, what materiality means from a disclosure perspective is less clear. Therefore, it is not surprising that materiality is not being applied as robustly to disclosures. Some would say that we have a principles-based model for recognition and measurement, but a compliance-based model for disclosures. The overall result is disclosure of immaterial information that leads to clutter.

> **"… what materiality means from a disclosure perspective is less clear."**

Materiality in accounting standards
The concept of materiality is clear as described in the IASB's Conceptual Framework as:

> QC 11 "Information is material if omitting it 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."

This clearly states that information can be material by size or nature.

The ASB's Statement of principles for financial reporting describes materiality in a similar way, but it also provides clarity on immaterial information:

> 3.29 "... when immaterial information is given in the financial statements, the resulting clutter can impair the understandability of the other information provided. In such circumstances, the immaterial information will need to be excluded."

IFRSs also include a clear statement on materiality for disclosures.

> IAS 1.31 "An entity need not provide a specific disclosure required by an IFRS if the information is not material."

Materiality from a disclosure perspective
We believe that there needs to be debate around:

- What materiality means from a disclosure perspective as compared to recognition and measurement; and
- Whether there are different levels of materiality for disclosure purposes.

Some have suggested that there should be a higher level of materiality for disclosures within the notes to the financial statements. The rationale for this is that more weight is given to the primary financial statements over the notes.

> **"We believe that there needs to be debate around: what materiality means from a disclosure perspective… and whether there are different levels of materiality…"**

Further, we believe that within the financial report as a whole, different levels of materiality from a disclosure perspective may apply. We have identified three levels of materiality to formulate the ideas:

(1) Top level – these are disclosures that would be of interest to the 10-minute reader. In *Cutting clutter*, we noted that a number of descriptors are used in IFRS and Company law in the context of disclosures and could be interpreted as an attempt to define this top level of materiality.

(2) Middle level – the concept of materiality as described in accounting standards.

(3) Bottom level – this refers to items that are considered to be insignificant or trivial, which is a term that is often used in auditing standards.

Descriptors used in IFRS and Company Law

- Critical
- Essential
- Fundamental
- Important
- Key
- Main
- Major
- Primary
- Principal
- Significant

Joint DP – Materiality

More details on the application of materiality are included in Chapter 4 of the joint DP.

Determining the order of magnitude of these different terms can be difficult. We have ranked the terms below as a basis for discussion, with significant being the most important and insignificant being the least:

- Significant
- Material
- Not material
- Immaterial
- Insignificant.

We appreciate that defining the different terms is not an easy task, but we recommend that the IASB considers this point and as a minimum uses the terms consistently. For example, IAS 1 requires a 'summary of significant accounting policies'. Currently, as noted above, different words are used to describe similar concepts.

Application of materiality to disclosures
We believe that there is a need for guidance on how materiality should be applied to disclosures. We have set out some thoughts on how materiality could be applied to different components of the financial report in Appendix C to this paper.

"We believe that there is a need for guidance on how materiality should be applied to disclosures."

4.

How should disclosures be communicated?

We believe that the problems with disclosures are not just about quantity. As preparers navigate their way through the myriad of disclosure requirements applying a checklist is often the 'easier' option. To address this, we have developed some principles for communication namely, disclosures should be:

- Entity-specific
- Clear, concise, and written in plain language
- Current
- Explaining the substance of a transaction.

Also, in applying these principles, information contained in the financial report should provide a clear link between an entity's business, financial performance and position.

In the following pages, we expand on each of these communication principles by setting out:

The principle

Application of the principle

Providing a further explanation

Describing an example of how applying the principle may impact disclosures

Principle:	**Disclosures should be entity-specific.**
Application of principle:	• Each disclosure should be assessed for its applicability to the entity and tailored as appropriate. • Only include disclosures that are relevant to the entity.
Explanation:	Financial reports are often prepared from a template. The result is generic boilerplate disclosures that do not provide information specific to the entity. There is a tendency to comply with all the disclosure requirements rather than to identify only those disclosures that are applicable to the entity.
Example:	Accounting policies, which simply repeat information in accounting standards, may not provide any new information to a user. A user may be more interested in understanding areas of accounting policy choice, and changes in accounting policies.

Principle:	**Disclosures should be clear, concise, and written in plain language.**
Application of principle:	• The use of a glossary is encouraged where industry-specific or accounting terms are used. • In certain circumstances, it may be appropriate to use tables to present disclosures. • Consider the style of writing where disclosures contain large amounts of text.
Explanation:	Disclosures are often written or presented in a style that makes them difficult to read and understand. As a consequence, they fail to provide an adequate explanation of the subject matter.
Example:	Roll-forward tables may be the clearest and most accessible format for users to obtain information on movements.

Principle:	**Disclosures should be current.**
Application of principle:	• Disclosures should be reviewed to ensure that they are relevant to the current reporting period. • Delete disclosures that are no longer useful.
Explanation:	Disclosures may be carried forward from prior periods. Consequently, some disclosures may become less useful over time.
Example:	Disclosures on sovereign debt provide useful information during the current crisis. However, in a few years' time, these disclosures may be less relevant.

Principle:	**Disclosures should explain the substance of a transaction, going beyond the IFRS requirements if necessary.**
Application of principle:	• Information provided should enable users to understand the economic substance of transactions.
Explanation:	Disclosures in the notes are often prepared using a checklist so although a particular disclosure may 'tick the box', the disclosure may not adequately explain the substance of a transaction or series of transactions.
Example:	A sale and repurchase agreement may, in substance, be a financing arrangement rather than a sale. It is therefore important that a user understands the business rationale behind this type of transaction, which may require a preparer to go beyond the requirements in IFRS.

Principle:	**Information contained in the financial report should provide a clear link between an entity's business, financial performance and position.**
Application of principle:	• Disclosures should be linked to the business model of the entity where appropriate. • There should be clear reconciliations between amounts in the primary financial statements and notes. • Where non-GAAP numbers are disclosed, there should be a clear reconciliation to the amounts contained in the primary financial statements. • Cross-references should be provided to link items and avoid duplication.
Explanation:	Disclosures often seem disconnected from the entity's business and it is often difficult to see the relationships between items.
Example:	The FRC's *UK Corporate Governance Code* requires disclosures of an entity's business model, strategy and risk management. It would be helpful to link this information together to demonstrate the accountability of the board in these areas.

Alternative methods for communicating information

We believe that communication of disclosures is an area where entities have an opportunity to innovate and experiment. We have set out our thoughts for improving communication below.

Presenting disclosures outside the annual financial report
We believe there is a need for a debate around including some disclosures outside the annual financial report, which in the UK, is usually a printed document.

Standing data
We believe that there is a case for suggesting that some explanatory information that remains unchanged from one year to the next could be included on a website. This is our vision, but currently there are legal barriers that prevent these disclosures being included outside the printed annual report.

We have identified three types of information:
- Entirely new each year
- Refreshed to reflect changing circumstances; and
- Unchanged or where changes are trivial.

An example would be the summary of significant accounting policies that are required by IAS 1 *Financial Statement: Presentation*, and corporate governance disclosures, which are required to demonstrate compliance.

Re-thinking the organisation of information
We note that users value being able to find disclosures consistently in the same place and we are not suggesting that the order of disclosures is changed every year but there may be ways in which information can be organised so that it is more useful.

Joint DP – Communication

The structure and order of information in the notes is discussed in more detail in Chapter 5 of the joint DP.

For example, disclosures around share-based payments may be organised so that the share-based payment note starts with a disaggregation of the profit and loss charge, which includes the most important scheme first and focusing the narrative disclosures on the most important schemes.

We believe that placement criteria are one method for organising disclosures in financial reports but there may be others. We are pleased to see that entities are already experimenting in this area.

One financial services company has prepared an 'integrated' financial report. Disclosures that are typically found in the notes are split into two groups – those that are considered most important (these were included in their preliminary announcements) and others that have been moved into an Appendix. The first group of disclosures together with the primary financial statements are embedded in the financial review.

Another financial services company presents accounting policies with the relevant note disclosure, as well as the narrative relating to the Financial Review with the primary financial statements.

The Financial Reporting Review Panel's (FRRP) 2012 Annual Report published by the FRC notes that there is evidence of entities eliminating unnecessary detail and giving greater prominence to material disclosures. A few entities have also changed the order of the content.

In addition, the FRC's Financial Reporting Lab is also working with companies and investors to identify ways to improve corporate reporting in specific areas. Topics addressed in the Lab's first year have included net debt reconciliations, debt and cash flow disclosure, and remuneration reporting.

"The… FRRP… notes that there is evidence of entities eliminating unnecessary detail and giving greater prominence to material disclosures."

Glossary

ASB	UK Accounting Standards Board
AASB	Australian Accounting Standards Board
ANC	Autorité des normes Comptables (France)
Corporate reporting	All the information produced by an entity for users.
Disclosure	To provide additional information that is not generally known to users to enable them to understand an entity's business model, governance and financial performance.
Disclosure framework	A structure to support the development and application of disclosures.
DRSC	Deutsches Rechnungslegungs Standards Committee e.V. (Germany)
EFRAG	European Financial Reporting Advisory Group
Financial reporting	Information typically found in an annual report, interim report or preliminary announcements.
FRC	Financial Reporting Council
FRRP	Financial Reporting Review Panel
GAAP	Generally Accepted Accounting Practice
IAS	International Accounting Standard
IASB	International Accounting Standards Board
IFRS(s)	International Financial Reporting Standard(s)
Material	Information is material if omitting or misstating it could influence decisions that users make on the basis of financial information about a specific reporting entity.
Notes	Notes to the primary financial statements.
OIC	Organismo Italiano di Contabilità (Italy)
Placement	Principles for determining where disclosures are located.
Presentation	The display of information for comparability purposes.
Primary financial statements	Profit or loss account, other comprehensive income, balance sheet and cash flow statement.
Proportionality	Setting disclosure requirements based on the size or nature of a group of entities and the needs of users.
Regulations	All laws, accounting standards and other requirements that govern the content of corporate reports.
Regulators	All bodies involved in setting regulations.
Users	Existing and potential investors, lenders and other creditors.

Appendix A: Objective for disclosure

What is disclosure?

The objective of disclosure is not defined in accounting standards. We believe that understanding the objective of disclosure is a helpful starting point for a disclosure framework. To begin to develop an objective, we think that it is necessary to step back and consider the different aspects of accounting standard setting – recognition and measurement; presentation; and disclosure.

Recognition and Measurement	Presentation	Disclosure

Recognition and measurement
In our view, recognition and measurement deals with how items are accounted for in the primary financial statements. We believe that recognition and measurement tend to be the main focus of standard setters and accordingly the IASB's Conceptual Framework contains some material on recognition and measurement. There is little on presentation and disclosures, and we believe that the line between the two is hazy.

Presentation
Presentation is a term that is commonly used to refer to items 'displayed' on the face of the primary financial statements (PFS) or required to be displayed in the notes. The objective of presentation is stated in IAS 1 *Financial Statement Presentation* and is associated with the provision of information for comparability purposes.

We have noted that the terms presentation and disclosure are often used interchangeably. IAS 1 mentions presentation, present, presenting and presents a total of 253 times, with disclose (or derivations thereof) being mentioned 120 times.

We believe that it is necessary to distinguish between presentation and disclosure as they have different objectives.

"We have noted that the terms presentation and disclosure are often used interchangeably."

Presentation is an overused term and can mean different things to different people, such as presentation on the face of the primary statements, how information is organised, which information is given greater prominence, down to the colour or font used. For the purposes of this paper, presentation is defined as 'the display of information for comparability purposes'.

Disclosure

Financial reporting disclosures have evolved over time. Disclosures started off as being footnotes that amplified and explained items in the primary financial statements.

Reflecting the increased complexity of the underlying financial transactions, the information contained within financial reports has become more complex. Disclosure in financial reporting has now come to refer to a wider set of information than was the case historically. To reflect this change, we think it would be helpful to define disclosure. We believe that there are two steps in establishing what the purpose of disclosure is:

(1) First, as with the term 'presentation', define what we think the purpose of disclosure is with regard to financial reporting. With this in mind we have come up with the following definition:

> To provide additional information that is not generally known to users to enable them to understand an entity's business model, governance and financial performance.

(2) Second, once a definition of disclosure is agreed, and with this definition in mind, develop a disclosure objective for each of the components of a financial report. For example, a disclosure objective for management commentary. We considered objectives for each of the components of a financial report in the placement section of this paper.

"Disclosure in financial reporting has now come to refer to a wider set of information than was the case historically."

As part of the process of developing both the definition of disclosure and the objectives for the components of financial reports, we thought that it is also informative to the debate to discuss what disclosure is not. We do not believe that disclosure should be:

- A substitute for inadequacies in recognition and measurement; we recognise that disclosures are required to 'amplify and explain' the primary financial statements, but the aim should be to get to the 'right' answer on recognition and measurement rather than using disclosure as a 'quick fix';[22]
- A mechanism to reconcile different positions where there is a lack of agreement on recognition, measurement or presentation, unless the additional information would help users (for example, disclosures have recently been used by the IASB to facilitate convergence with the Financial Accounting Standards Board (FASB) for offsetting financial assets and financial liabilities); or
- A basis for re-calculation.

> "… we thought that it is also informative to the debate to discuss what disclosure is not."

Behavioural aspects of disclosures in the financial reporting process

We believe that disclosures are often considered at the last stage in the financial reporting process. Standard setters tend to focus more on recognition and measurement aspects, which often results in disclosures being added on to the end of standards. A similar approach is taken by preparers and auditors, which often results in checklists being followed and materiality not being applied as robustly to disclosures compared to other areas of the financial statements. The process is also influenced by users who often demand more and more information, as well as by regulators. With all these forces in action, we think that it is unsurprising that the volume of disclosures has grown.

Appendix B: Review of preliminary announcements

We believe that analysing preliminary earnings announcements is one quick way to form an understanding of the needs of users. Preliminary announcements are relatively concise and focus on information that is important to investors. Financial statements are much longer, and there is a perception that their preparation is driven by the need to comply rather than the desire to inform.

"Financial statements are much longer, and there is a perception that their preparation is driven by the need to comply rather than the desire to inform."

Requirements relating to preliminary announcements

In the UK, there is no longer a regulatory requirement to publish a preliminary announcement. However, where a company chooses to produce such an announcement, it must follow the requirements in the Listing Rules. The Listing Rules requirements are procedural in nature, rather than specifying the content of such announcements.

Insights from review of preliminary announcements

We have made the following comments based on our review of a sample of UK preliminary announcements.

Most preliminary announcements are structured as follows:

- Summary data – key GAAP and non-GAAP measures
- Chief Executive's statement
- Management commentary – including forward-looking information
- Financial review, with a focus on earnings
- Primary financial statements
- Notes

We thought that it was interesting that the structure of preliminary announcements broadly follows that of the annual financial report.

Disclosures

We found that there are certain disclosures that were given in most preliminary announcements:

- Segmental information
- Non-recurring/ exceptional items
- Tax
- Dividends
- EPS
- Net debt
- Business combinations
- Pensions
- Capital structure
- Risk information

Those disclosures tend to appear in the financial review, where there is narrative on these items, and then in the notes, which provide the numbers.

We noted that:

- Accounting policies in preliminary announcements tend to be limited to the basis of preparation. We believe that this indicates that accounting policies are perhaps of limited use to investors;
- Few balance sheet notes are provided; we thought that this is unsurprising given that the focus of preliminary announcements tends to be on earnings;
- There are more entity-specific notes; and
- Often the notes in preliminary announcements go beyond those required by accounting standards. For example, the net debt reconciliation.

How does this help in the development of a disclosure framework?

We made a number of observations from our review of preliminary announcements that may assist in the development of a disclosure framework.

Content
Our review demonstrates that investors use a broad range of information including disclosures that are included in management commentary and the notes to the financial statements. This supports our view that the scope of a disclosure framework needs to go beyond the financial statements.

Materiality
We believe that preliminary announcements provide an insight into the key information that users require. They focus on 'big picture' items so we think that these can help preparers determine the most important information for the user.

Communication
In our view, disclosures in preliminary announcements can assist in better communication of information. We believe that they provide a method of prioritising information or identifying the 'core' information that users need.

We consider that the content of preliminary announcements can be used as a building block that provides the first layer of disclosures that users need. Different users may require a different depth of disclosure requirements. We suggest that one approach is to have two layers of disclosure and have one shorter, simpler version of the financial report with the first layer of disclosures and then signpost this to a full version containing all the detailed disclosures.

Appendix C: Application of materiality

Different levels of materiality

As set out on page 34, we have suggested that there could be different levels of materiality for different types of disclosures. In this Appendix, we consider how these different levels might be applied.

Management Commentary
The concept of materiality covers both quantitative and qualitative aspects and therefore covers management commentary. In the UK, current regulations covering management commentary use terms such as ‘key’ and ‘principal’, which suggests that a higher level of materiality should be applied.

Example: there is a requirement to disclose ‘principal risks and uncertainties’.

In this context, the use of the word principal implies that companies ought to be disclosing the most important risks.

In February 2011, the FRRP issued a press release noting that as accounting enforcers they were seeking to understand the ‘principal’ risks and uncertainties, rather than searching for a long list of all the risks and uncertainties. The FRC recently published the *FRRP’s Annual Report 2012*, and noted there was evidence of improvement in the reporting of principal risks and uncertainties.

Corporate Governance
In our opinion, governance reporting should include:
- Corporate governance disclosures, for example, those required by the *UK Corporate Governance Code* (the Code);
- Remuneration reporting as required by various regulations; and
- Reporting on other factors relevant to the board’s stewardship, such as related party disclosures.

“… we have suggested that there could be different levels of materiality for different types of disclosures.”

Most EU markets have a Corporate Governance Code, which contains two categories of disclosure – disclosures that are required, and disclosures that only need to be provided by 'exception'. Despite the 'comply or explain' philosophy at the heart of the Code, practice by many entities seems to be to explain everything.

> **Despite the 'comply or explain' philosophy at the heart of the Code, practice by many entities seems to be to explain everything.**

As noted in *Cutting clutter*, demands by others, who are not the primary users of financial reports as defined in this paper, has led to the inclusion of disclosures that represent standing data that does not change much, if at all, from year to year.

We believe that there are two types of corporate governance disclosures:

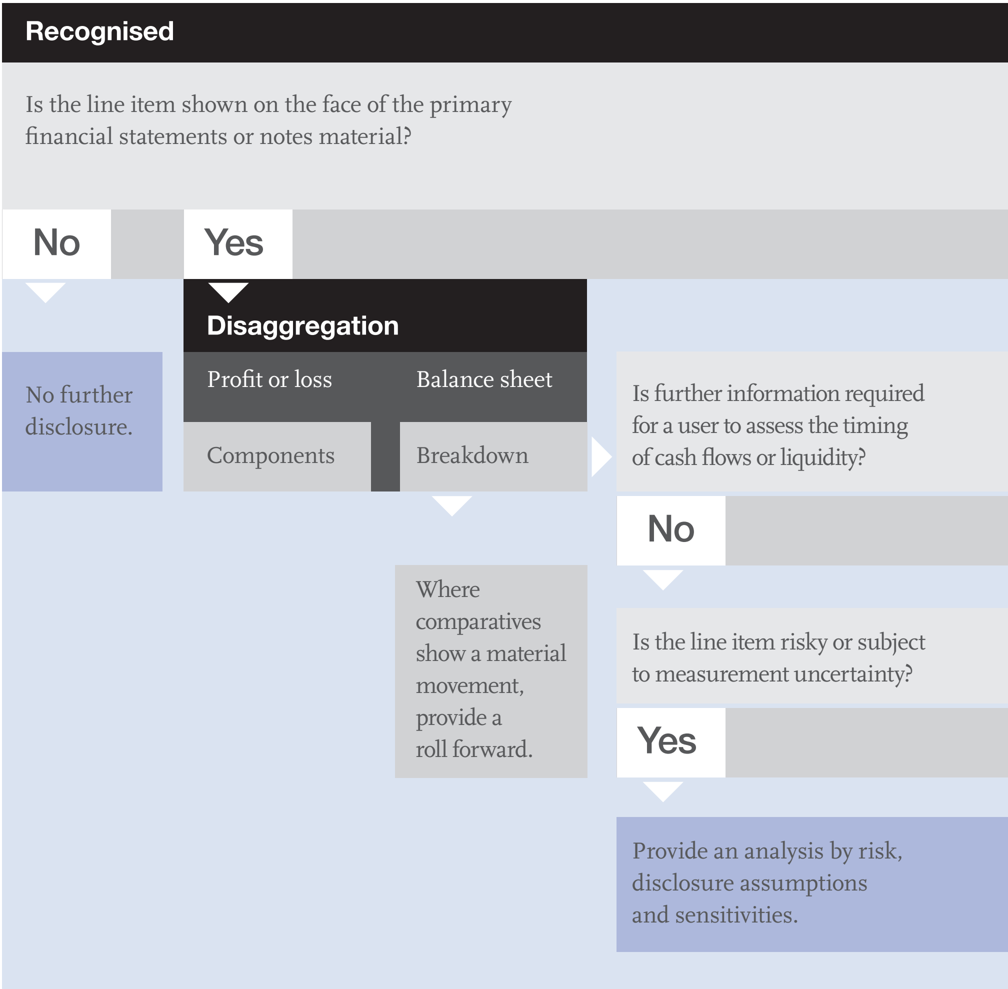
- Those disclosures that demonstrate compliance with the Code which are provided regardless of materiality.
- Other disclosures, such as those required by accounting standards, which also provide investors with information on stewardship (e.g. related party disclosures), where the materiality principle applies. Some would say that a lower level of materiality should apply to these types of disclosures.

Financial Statements

We have developed a framework for applying materiality within the primary financial statements and notes, which is set out in the visual on the next page. The framework contains two levels of materiality to address disclosures relating to items that are:

- Recognised on the face of the primary financial statements; and
- Unrecognised, but may be in future as they impact future cash flows.

We believe that it would be helpful to develop a framework for the application of materiality to disclosures. We have used disclosures in the financial statements as an example for how this might work.



Unrecognised

Are the items not currently recognised on the balance sheet (but that will affect future cash flows) likely to be very important to users?

No

No further disclosure.

Yes

Describe the item and the effect on future cash flows.

Yes

Provide a maturity analysis.

Footnotes

1. IASB: *The Conceptual Framework for Financial Reporting 2010.*
2. In the absence of a formal IASB definition of 'financial reporting', we have relied on the EU Accounting Directives (Fourth Directive), which contain three components: management report (Article 46); corporate governance statement (Article 46a); and accounts (Article 2).
3. Paragraph 6, ASB: *Statement of Principles for Financial Reporting.*
4. IASB's *Conceptual Framework for Financial Reporting 2010,* paragraph OB2 defines the objective of financial reporting as "to provide financial information about a reporting entity that is useful to existing and potential investors, lenders and other creditors about providing resources to the entity."
5. The IASB has acknowledged that it will consider this as part of its Conceptual Framework Project.
6. EC: *Country-by-Country Reporting for Multinationals.*
7. The United States Securities and Exchange Commission requires similar disclosures but such disclosures would be provided outside the financial report.
8. Paragraph IN 4 IASB Practice Statement *Management Commentary.*
9. As noted in footnote 2, EU Accounting Directives (Fourth Directive) contain three components: management report (Article 46); corporate governance statement (Article 46a); and accounts (Article 2).
10. Chapter 3 IASB: *Conceptual Framework for Financial Reporting 2010.*
11. Page 10, FRC *Louder than Words.*
12. IASB's *Conceptual Framework for Financial Reporting 2010*, paragraph OB2 defines users as "Existing and potential investors, lenders and other creditors."
13. 'Disaggregation' and 'explanation' were identified as principles for the content of the notes to the financial statements in our joint DP.
14. Paragraph 9, IASB *Management Commentary* Practice Statement.
15. Based on the OECD definition of Corporate Governance.
16. Paragraph 7.4, ASB: *Statement of Principles for Financial Reporting.*
17. Paragraph 169, IASB *Management Commentary* DP.
18. Paragraph E8, IASB *Management Commentary* DP.
19. Page 11, OECD: *Principles for Corporate Governance.*
20. Paragraphs B6 and B43-B46, IFRS 7 *Financial Instruments: Disclosures.*
21. Page 70, Joint DP.
22. Chapter 7 ASB: *Statement of Principles for Financial Reporting.*

Sources and further reading

ASB: *Statement of Principles for Financial Reporting* (1999)

ASB: *Rising to the challenge* (2009)

ASB: Financial Reporting Exposure Drafts 46, 47 and 48: *The Future of Financial Reporting in the UK and Republic of Ireland* (2012)

ANC: Proposal: *Simplify accounting obligations for small listed companies in Europe* (2011)

AASB: *1053 Application of Tiers of Australian Accounting Standards and AASB 2010-2 Amendments to Australian Accounting Standards arising from Reduced Disclosure Requirements* (2010)

EC: *Consultation of Financial Reporting on a Country-by-Country Basis by Multinational Companies* (2010)

EFRAG/ANC/FRC: Discussion Paper: *Towards a Disclosure Framework for the Notes* (2012)

European Securities and Markets Authority (ESMA): Consultation Paper: *Considerations of materiality in financial reporting* (2011)

ESMA: Summary of Responses: *Considerations of materiality in financial reporting* (2012)

Financial Accounting Standards Board: Discussion Paper: *Disclosure Framework* (2012)

FRC: *Louder than Words* (2009)

FRC: *Cutting clutter* (2011)

FRC: *Financial Reporting Review Panel Annual Report 2012*

FRC: *UK Corporate Governance Code* (2012)

IASB: *Discussion Paper: Management Commentary* (2005)

IASB: *IFRS for SMEs* (2009)

IASB: Practice Statement: *Management Commentary* (2010)

IASB: *The Conceptual Framework for Financial Reporting* (2010)

International Auditing and Assurance Standards Board (IAASB) Discussion Paper: *The Evolving Nature of Financial Reporting: Disclosure and Its Audit Implications* (2011)

New Zealand Institute of Chartered Accountants and The Institute of Chartered Accountants of Scotland: *Losing the excess baggage* (2011)

OECD: *Principles of Corporate Governance* (2004)

Action points

In writing this paper, we have identified a number of action points, which are summarised below.

IASB

There are a number of steps that regulators could take that would contribute to the development of a disclosure framework. Among others, the IASB, as an international body, could set the principles, for example, as part of developing its Conceptual Framework. For this purpose, the IASB should:

1. Define the boundaries of financial reporting for their purposes.
2. Develop placement criteria for establishing where information should be disclosed.
3. Develop a clear objective for disclosure, as well as a distinct objective for presentation.

In addition, there are other steps that the IASB can take that will enable preparers and others to critically assess the disclosures they should provide within financial reports. The IASB should:

1. Engage with users at an early stage in the development of a disclosure framework.
2. Provide guidance on what materiality means from a disclosure perspective.
3. Reduce and define the terms used within IFRSs, e.g. significant, key, critical, and then use the defined terms consistently.
4. Provide overarching principles for disclosures and present these within one standard.
5. Update IAS 1 so that presentational and disclosure aspects are clearly separated.

6. Make it clear that measures not defined within IFRSs (e.g. net debt) and adjusted measures (e.g. EBITDA) can be disclosed within the notes to the financial statements (as a type of disaggregation) as long as these measures are:
   a. Defined
   b. Reconciled back to IFRS figures
   c. Include a comparable figure for the prior year
   d. Consistently calculated and presented.
7. Where disclosure requirements within individual standards are not mandatory, these should be moved into implementation guidance that is not part of the standard.

All Regulators

1. Ensure that new disclosures that are proposed to be included in the financial report meet the objective of financial reporting as previously defined.
2. Regulators and enforcers need to agree that disclosures are not required for immaterial items.

Preparers and Auditors

1. Critically assess what materiality means from a disclosure perspective to cut clutter.

Questions to consider

1. Would a disclosure framework that addresses the four questions identified below help address the problems with disclosures?
   - What information do users need?
   - Where should disclosures be located?
   - When should a disclosure be provided?
   - How should disclosures be communicated?
2. Do the disclosure themes set out on page 16 of this paper capture the common types of disclosures that users need?
3. Do you agree with the components of the financial report as identified on page 20? Are there any other components that should be identified?
4. Do you believe that the placement criteria identified in this paper are appropriate?
5. How should standard setters address the issue of proportionate disclosures?
6. Do you agree with the framework for materiality set out in this paper? How could it be improved?
7. Are there other ways in which disclosures in financial reports could be improved?

Additional questions for users

8. What type of user are you?
9. Which disclosures are important to you?
10. What disclosures do you use the least?
11. How do you use the information in the following disclosures?
   – Management commentary.
   – Governance.
   – Notes to the financial statements.

We would appreciate your comments by 31 January 2013, by post or email to:

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