## IASB® meeting

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| Date | **December 2022** |
| Project | **Disclosure Initiative—Subsidiaries without Public Accountability: Disclosures** |
| Topic | **Proposed statement of compliance** |
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## Purpose of this paper

1. This paper discusses the feedback on the proposed statement of compliance with IFRS Accounting Standards (statement of compliance) and the statement that an eligible subsidiary has applied the proposed IFRS Accounting Standard (draft Standard) set out in Exposure Draft *Subsidiaries without Public Accountability: Disclosures* (Exposure Draft).

## Summary of staff recommendation

2. The staff recommend the IASB proceeds with its proposal to require an eligible subsidiary that elects to apply the Standard to disclose it has complied with IFRS Accounting Standards together with the fact it has applied the Standard.

## Structure of the paper

3. This paper is structured as follows:

   (a) background (paragraphs 4–6);

   (b) summary of feedback (paragraphs 7–8);

   (c) staff analysis (paragraphs 9–24); and

   (d) staff recommendation and question for the IASB (paragraph 25).

# Background

## Question in the Invitation to Comment

4. Question 8 of the Invitation to Comment on the Exposure Draft asked for feedback on the proposed disclosure requirements set out in paragraphs 22–213 of the draft Standard. Respondents were asked if they agreed with the proposals, or recommend any further reduction or additional disclosure requirements in the draft Standard. In responding to this question, some respondents commented on the proposed statement of compliance and the statement that an eligible subsidiary has applied the draft Standard.

## Statement of compliance[1]

5. In developing its proposals, the IASB observed that the financial statements of two similar subsidiaries that applied IFRS Accounting Standards could be different if only one subsidiary applied the draft Standard. The two subsidiaries' financial statements are unlikely to provide the same disclosures, but both subsidiaries would still be able to assert compliance with IFRS Accounting Standards.

6. The IASB proposed that an eligible subsidiary disclose the fact that it has applied the draft Standard as it would provide useful information to users of the subsidiary's financial statements. To aid comparability and understandability, the IASB proposed that this disclosure be located together with the statement of compliance. Extracts from the draft Standard are below:

   *Paragraph 22 of the draft Standard:*

   > An entity applying this [draft] Standard shall disclose that fact together with the statement of compliance required by paragraph 110 of this [draft] Standard.

   *Paragraph 110 of the draft Standard (which replaces paragraph 16 of IAS 1* Presentation of Financial Statements)*:*

   > An entity whose financial statements comply with IFRS Standards shall make an explicit and unreserved statement of such compliance in the notes. An entity shall not describe financial statements as complying with IFRS Standards unless they comply with all the requirements in IFRS Standards. An entity shall make this statement together with the fact that it has applied this [draft] Standard as required by paragraph 22 of this [draft] Standard.

[1] See paragraphs BC54–BC56 of the [Basis for Conclusions on the Exposure Draft](Basis for Conclusions on the Exposure Draft).

## Summary of feedback

7. In its April 2022 meeting, the IASB discussed the feedback on the Exposure Draft. Some respondents provided feedback on paragraphs 22 and 110 of the draft Standard[2]. Respondents supported paragraph 22 of the draft Standard that requires a subsidiary to disclose that it has applied the draft Standard together with the statement of compliance required by paragraph 110 of the draft Standard. These respondents noted that this provides useful information to users and provides comfort that recognition and measurement requirements of IFRS Accounting Standards have been applied with reduced disclosures.

8. Some respondents expressed concerns and said taken together paragraph 22 and paragraph 110 could be confusing or conflicting. These respondents said:

    (a) the subsidiary would not in fact apply 'all' requirements in IFRS Accounting Standards because the proposed disclosure requirements in the draft Standard are reduced.

    (b) making the statement might imply that overall disclosure objectives could be met in different ways—either through reduced or full disclosures. This respondent further suggested that the draft Standard should be a separate reporting framework.

    (c) consideration is needed on how the draft Standard would be referred to in audit reports.

## Staff Analysis

9. The staff analysis is structured as follows:

    (a) perceived conflict between applying the draft Standard and the statement of compliance (paragraphs 10–16);

    (b) disclosing the election to apply the draft Standard with the statement of compliance (paragraphs 17–20); and

    (c) other concerns (paragraphs 21–24).

[2] See Agenda Paper 31A *Feedback from comment letters* and Agenda Paper 31B *Feedback from outreach events* of the April 2022 IASB meeting.

## Perceived conflict between applying the draft Standard and the statement of compliance

10. The main concern from respondents is the perceived conflict of an eligible subsidiary asserting compliance with IFRS Accounting Standards when applying the draft Standard, because the draft Standard has reduced disclosures from IFRS Accounting Standards.

11. A subsidiary applying IFRS Accounting Standards and electing to apply the Standard would provide fewer disclosures compared to a subsidiary that does not apply the Standard. However, the subsidiary applying the Standard must state it has applied the Standard and state compliance with IFRS Accounting Standards.

12. The staff note that differences in the information reported by similar entities applying IFRS Accounting Standards already exist in practice. Differences not only arise from disclosure requirements, but also from recognition and measurement requirements. For example, different information may be reported as a result of:

    (a) applying the exemptions or practical expedients in IFRS Accounting Standards, such as:

        (i) IFRS 1 *First-time Adoption of International Financial Reporting Standards* allows an entity to elect to use one or more of the exemptions contained in Appendices C–E of IFRS 1 (see paragraph 18 of IFRS 1).

        (ii) IFRS 9 *Financial Instruments* allows an entity to apply a practical expedient when measuring expected credit losses (see paragraph B5.5.35 of IFRS 9).

        (iii) IFRS 10 *Consolidated Financial Statements* permits a parent not to present consolidated financial statements provided it meets all the conditions set out in paragraph 4(a) of the Standard (see paragraph 4 of IFRS 10).

        (iv) IFRS 16 *Leases* provides recognition exemptions to short-term leases and 'low value' leases (see paragraph 5 of IFRS 16).

(b) applying judgement in determining what disclosures to provide, such as:

(i) paragraph 17(c) of IAS 1 states that an entity is required to provide additional disclosures when compliance with the specific requirements in IFRS Accounting Standards is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance.[3]

(ii) paragraph 31 of IAS 1 states that an entity need not provide a specific disclosure required by an IFRS Standard if the information resulting from that disclosure is not material.

13. For the examples provided in paragraph 12, an entity that applied all or some of these exemptions and expedients may still assert compliance with IFRS Accounting Standards in its financial statements, as could an entity that did *not* apply those exemptions and expedients. Put simply, an entity's statement of compliance is not affected by whether it applied the exemptions and expedients permitted by IFRS Accounting Standards.

14. Furthermore, the staff observe that had the IASB decided to include the 'reduced' disclosure requirements proposed in the draft Standard within each IFRS Accounting Standard (instead of in a separate IFRS Accounting Standard) the question or concerns about the statement of compliance might not have arisen.

15. The Standard, if finalised, will be part of IFRS Accounting Standards. The proposals in the Standard provide relief from some disclosure requirements in IFRS Accounting Standards by not requiring those disclosures designed for users of the financial statements of publicly accountable entities. Therefore, the staff think that a subsidiary that elects to apply the Standard should be able to state compliance with IFRS Accounting Standards.

16. The IASB could consider requiring a different statement of compliance for subsidiaries electing to apply the Standard. For example, the IASB could require the subsidiary to state that it has complied with the recognition, measurement and presentation requirements of IFRS Accounting Standards and the disclosure requirements of the Standard. However, requiring a different statement of compliance for such subsidiaries could give the impression that the financial statements were prepared under a different financial reporting framework (that is, a different framework to IFRS Accounting Standards or the *IFRS for SMEs* Accounting Standard). As noted in the paragraph 15, the Standard, if finalised, will be part of IFRS Accounting Standards.

[3] This requirement is reiterated in paragraph 16 of the draft Standard. Feedback and comments on this aspect of the draft Standard will be discussed in a future IASB meeting.

## Disclosing the election to apply the draft Standard with the statement of compliance

17. Stakeholder concerns on the perceived conflict of a subsidiary asserting compliance with IFRS Accounting Standards when applying the draft Standard could be because of the proposal that a subsidiary disclose the statement of compliance together with the fact that it has applied the draft Standard. Locating the two disclosures together might have raised questions that otherwise might not have arisen. As noted in paragraph 6, to aid comparability and understandability, the IASB proposed that the two requirements be disclosed together.

18. The IASB could consider separating these proposed disclosures requirements. In other IFRS Accounting Standards, when an entity elects to apply an exemption or expedient, the fact that it has applied an exemption or expedient need not be disclosed together with the statement of compliance. For example, IAS 27 *Separate Financial Statements* requires a parent that elects not to prepare consolidated financial statements (in accordance with paragraph 4(a) of IFRS 10) and instead prepare separate financials statements to disclose the fact that the financial statements are separate financial statements and the exemption from consolidated has been used (see paragraph 16(a) of IAS 27). IAS 27 does not specify where such disclosure be located.

19. However, disclosing the election to apply the Standard and statement of compliance together provides useful information to users of financial statements about how an entity’s financial statements are prepared. Specifically, locating those disclosures together confirms that the financial statements, whilst providing reduced disclosures, are still compliant with IFRS Accounting Standards. It provides information to users of subsidiaries’ financial statements (particularly in the first few years of applying the Standard and in jurisdictions where a reduced disclosure standard is new) that applying the Standard has not impaired the subsidiaries’ ability to assert compliance with IFRS Accounting Standards.

20. Therefore, the staff thinks that the fact that a subsidiary applied the Standard should be disclosed together with the statement of compliance, as proposed in the Exposure Draft.

### Other concerns

#### *Disclosure objectives and separate financial reporting framework*

21. One of the other concerns noted on the statement of compliance is the proposed statement might imply that disclosure objectives could be met in different ways, either through reduced or full disclosures. The respondent raising this concern said because of this the draft Standard should be a separate reporting framework and not part of IFRS Accounting Standards.

22. In developing the proposed disclosure requirements in the draft Standard, the IASB decided to exclude disclosure objectives in IFRS Accounting Standards as an exception to the approach to developing the proposed disclosure requirements in the draft Standard. This is because including those objectives might result in subsidiaries being compelled to provide the same disclosures as if they had not applied the draft Standard, which would be contrary to the project objective (see paragraph BC41 of the Basis for Conclusions on the Exposure Draft).

23. The staff will consider this comment on disclosure objectives together with other feedback on disclosure objectives at a future IASB meeting.

#### *Interaction with audit reports*

24. A further concern raised relates to how to refer to the draft Standard in audit reports. Audit reports are prepared in accordance with auditing standards (for example, International Standards on Auditing issued by the International Auditing and Assurance Standards Board). The staff think this matter is best addressed by auditing regulatory bodies.

## Staff recommendation and question for the IASB

25. In light of the analysis in paragraphs 9–24, the staff recommend the IASB proceeds with its proposal to require an eligible subsidiary that elects to apply the Standard to disclose it has complied with IFRS Accounting Standards together with the fact it has applied the Standard.

| **Question for IASB members** |
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| Does the IASB agree with the staff recommendation in paragraph 25 of this paper? |