CRUF
CORPORATE REPORTING USERS' FORUM

18 December 2019

FAO: IFRS Foundation
Columbus Building
7 Westferry Circus
Canary Wharf, London
E14 4HD

Via email: commentletters@ifrs.org

Dear Sir/Madam,

RE: Exposure Draft on Disclosure of Accounting Policies – Proposed Amendments to IAS 1 and IFRS Practice Statement 2

We will begin by reiterating that the current accounting policy disclosure is not ideal. We desperately need to contain the sort of boilerplate 'disclosure' that is of limited value to users.

The Corporate Reporting Users' Forum supports the Board's Better Communication in Financial Reporting project efforts; in particular the reduction of boilerplate accounting information in financial statements.

As such, the CRUF welcomes the opportunity to comment on the exposure draft: Disclosure of Accounting Policies: Proposed amendments to IAS 1 and IFRS Practice Statement 2.

We recognise that the core objective of the IFRS, as cemented in paragraph 1.2 of the Conceptual Framework, is the provision of financial information that is useful to primary users and do not exist primarily to drive good corporate governance behaviours. But we stress that the nature of the proposed changes to IAS 1 and IFRS Practice Statement 2 could impact broader corporate governance processes, and the potential effects should not be underplayed.

The concept of materiality is not isolated to traditional financial reporting. The requirements set forth in IAS 1 and IFRS Practice Statement 2 may influence a preparer's Board and Executive Committee's broader application of materiality principles as pertains to financial, integrated and sustainability reporting. As users, we place reliance on the corporate governance processes, and underlying control fabric that ensures the production of reliable financial and non-financial disclosures.

Broadly, the CRUF believes that the proposed amendments are supportive of establishing a reporting environment where preparers follow a robust materiality assessment process in the determination of which accounting policies are relevant and useful to users. We believe such process is underpinned by the success factors identified by the IFRS foundation in *"Better Communication in Financial Reporting: Making disclosures more meaningful"* which included:

- Senior management engagement and support;
- Engagement with the investment community to identify and understand information needs;
- Participation across departments; and

- Auditor, regulator and national standard setter support

Above all, we recognise that the IASB, through the addition of paragraph 117A, seeks to address:

1. Unnecessary duplication of IFRS Standards in disclosed accounting policies; and
2. Verbose and immaterial accounting policy information that overwhelms useful information.

We agree that paragraph 117A acts as the instrument through which non-useful accounting policy disclosure can be eliminated. To the extent that a standard is highly prescriptive, with limited subjectivity or optionality baked into a standard, we see paragraph 117A as necessary to "remove the clutter".

Caution is required in terms of the prominence paragraph 117A is given in the standard. As well as how the guidance contained in surrounding paragraphs and IFRS Practice Statement 2 are positioned and constructed. We believe this is of critical importance as the proposed amendments significantly influence the process preparers follow to delineate between material and immaterial accounting policy disclosures – the materiality assessment process.

The CRUF's opinion is that a materiality assessment of accounting policy disclosures is informed by the underlying entity-specific circumstances, complexities and subjectivities involved in accounting for particular events of economic phenomena. And while preparers may argue for the establishment of an enduring static materiality threshold to limit disruption to existing reporting processes, we see materiality as fluid in nature. We believe that where subjective judgements are applied, these are important behavioural signals, even when the numbers involved are small. Hence, the need for both users and non-executive directors to be in a position to challenge the robustness of preparers' materiality process and not solely the outcomes to deliver optimal policy disclosures.

A materiality assessment, itself, is an exercise of management judgement, and users have no explicit "voice" in a preparers materiality assessment process. Given this dynamic, we support changes that both:

- Drive an outcome that allows users and non-executive directors to critically challenge management's materiality assessment process; and
- Support preparers in narrowing accounting policy disclosures to those that are material either at a point-in-time, or are material over a period of time (on a forward-looking basis).

In addition, where accounting policy disclosures meet materiality thresholds, there is no explicit guarantee that the accounting policy content is useful to users. The CRUF believes useful accounting policies and associated information supports users in better understanding how:

- The impact of economic phenomena is disclosed in the financial statements both at a point in time and over periods of time; and
- Management judgements evolved with respect to accounting treatments requiring significant management judgement.

While we hold a cautious view, this is grounded in our thinking around the need to mitigate against emergent "principal-agent" issues. In particular, where preparers make unilateral decisions, under the ambit of paragraph 117A, to eliminate accounting policy disclosures to support reporting process optimization efforts. Under this dynamic, the risk exists that resource gains from the simplification of reporting processes are achieved at the expense of the usefulness of policy information.

We expect such action to be a natural consequence of the stressed reporting environment preparers operate within. We recognise that companies already find it challenging to meet the increasing number and rising complexity of disclosure requirements set out by global and national standard setters, regulatory authorities, and the capital markets industry.

Our detailed responses to the questions raised in the exposure draft that relate to the issues that concern analysts and investors are set out in the appendix.

APPENDIX – CRUF's responses to the questions raised in the ED

Question 1:
The Board proposes to amend paragraph 117 of IAS 1 to require entities to disclose their 'material' accounting policies instead of their 'significant' accounting policies.

Do you agree with the proposed amendment? If not, what changes do you suggest and why?

The CRUF supports the amendment to substitute "material" for "significant" in paragraph 117 of IAS 1 as "significant" is not defined in IFRS. However, the CRUF does not believe the wording alone will have an impact on the selection of accounting policies disclosed.

Question 2:
The proposed new paragraph 117A of IAS 1 states that not all accounting policies relating to material transactions, other events or conditions are themselves material to the financial statements.

Do you agree with the proposed statement? If not, what changes do you suggest and why?

The CRUF supports the introduction of this wording in particular where accounting policies relate to standards that are highly prescriptive, with limited subjectivity or optionality baked into them. In such instances, we recognise the incremental benefit of paragraph 117A as a necessary instrument to remove boilerplate disclosures.

But, as explained in the covering letter, we are cautious in terms of the application of paragraph 117A by preparers. The CRUF must highlight the potential risk of broad reductions in useful accounting policy disclosures under the ambit of paragraph 117A. Preparers may see the commercial benefit of reduced disclosure (e.g. reduced costly reporting staff; faster reporting processes) outweighing the usefulness of accounting policy disclosures to users. Under this dynamic, we believe preparers are more inclined to establish enduring static materiality thresholds in an effort to optimise reporting processes. This discounts the "organic" nature of materiality and the need to regularly test whether established materiality assessment processes remain relevant considering the entity-specific developments.

The CRUF reiterates that users of financial statements would like as much useful information as possible about material transactions and balances. We agree with the characteristics of what constitutes useful accounting policy disclosures stated in the Basis for Conclusions under BC9.

As such, we believe that any amendments, holistically, should stress the importance of testing accounting policy disclosures and information against those characteristics as part of a robust materiality assessment process. We believe that placing paragraph 117A ahead of paragraph 117B and 117C gives greater importance to activities of removal above activities focussed on testing whether accounting policy disclosures are indeed useful to users.

We believe the current positioning of paragraph 117A, and the implicit statement of its importance, should be reconsidered by the board. We suggest placing paragraph 117A after 117B and 117C.

Question 3:
The proposed new paragraph 117B of IAS 1 lists examples of circumstances in which an entity is likely to consider an accounting policy to be material in its financial statements.

Do the proposed examples accurately and helpfully describe such circumstances? If not, what changes do you suggest and why?

We assume that the list of examples is not exhaustive and merely an indication of circumstances where an accounting policy can be considered material. The board should make it clear that the proposed list is not an exhaustive list of circumstances where an accounting policy is considered to be material in order to mitigate against a check-list compliance attitude amongst preparers.

The proposed list may indicate to users' that reference to "material' should be considered narrowly, which we do not believe to be the case.

There may be cases where the impact of a change in accounting policy is immaterial in the current year but represents a change in business strategy. Users would benefit from receiving this information to understand the impact of financial statements in future periods. For example, the risk management strategy of management may have changed near year-end where management now choose to hedge certain foreign exchange positions, that had not previously been hedged. Users' would benefit from understanding this change in strategy together with the accounting policy underlying the hedge strategy, as this will impact on the future cash position of the entity, whether or not hedges have been entered into at year-end.

IAS 8 paragraphs 30 and 31 requires disclosure of the impact of new accounting standards that the entity has not yet adopted. In the years leading up to the adoption of the new standards, users would benefit from understanding the new accounting policy that will be effective in the next reporting periods and also how that policy differs from the present policy. Since IAS 8 considers disclosure of the future change in accounting policy to be useful information to users, it seems inconsistent for this not to be included in the proposed paragraph 117B.

In some cases, the value of certain instruments may fluctuate from positive to negative and vice versa. The quantum of the amount may not be material to warrant accounting policy disclosure in terms of paragraph 117B, but the impact of the swings from positive to negative, or vice versa might be material to the users understanding of the risk of the instrument and potential cash outcomes. In these cases, an accounting policy would benefit the users understanding of the recognition and measurement of the instrument.

Question 4:
The Board proposes to add to IFRS Practice Statement 2 two examples that illustrate how the concept of materiality can be applied in making decisions about accounting policy disclosures. Are these examples useful and do they demonstrate effectively how the concept of materiality can be applied in making decisions about accounting policy disclosures? If not, what changes do you suggest and why?

The practice statement does not form part of IFRS. The CRUF is of the opinion that the examples are better placed within IAS 1.

We agree with example S albeit that the example appears incomplete. The policy relating to the allocation of the transaction price to the identified components will be material in terms of paragraph 117B(d) and should be disclosed. However, this is excluded from the example. We recommend that the example be updated to explain that the allocation of the transaction price to the two identified performance obligations will also be material.

We note that Example T intends to illustrate a material accounting policy under para 117B(d) as it involves significant estimation of a material amount, however the conclusion is that separate disclosure of the accounting policy is not required. Whilst the example explains that the disclosures under IAS 1 and IAS 36 have been provided, we believe that the accounting policy that is recommended to be removed should not be removed and rather the information should be made more specific to the entity in the accounting policy.

Question 5:
Would any wording or terminology introduced in the proposed amendments be difficult to understand or to translate?

No comments.

Question 6:
Do you have any other comments about the proposals in this Exposure Draft?

We note the Disclosure Initiative – Targeted Standards-Level Review of Disclosure is in discussion. We are concerned that it may be premature to issue this amendment prior to the finalisation of the Targeted Standards-Level Review of Disclosure. If the Board chooses to issue the amendment to IAS 1 and Practice Statement 2, we are concerned that the decisions made here to reduce disclosure may impact on the decisions made in the Targeted Standards-Level Review of Disclosure project.

The Board should consider whether or not alternative ways of presenting existing accounting policies may be appropriate, for example by including the accounting policies as an appendix to the IFRS financial statements.

We think if the comments above are taken into account, that the flowchart diagram in the Practice Statement will need to be deleted as it does not lead to appropriate conclusions, being that accounting policies for immaterial amounts are not provided.

About the Corporate Reporting Users' Forum (CRUF)

The CRUF was set up in 2005 by users of financial reports to be an open forum for learning about and responding to the many accounting and regulatory changes that affect corporate reporting. In particular, participants are keen to have a fuller input into the deliberations of accounting standard setters and regulators. CRUF participants include buy and sell-side analysts, credit ratings analysts, fund managers and corporate governance professionals. Participants focus on equity and fixed income markets. The Forum includes individuals with global or regional responsibilities and from around the world, including Australia, Canada, France, Germany, Hong Kong, India, Japan, New Zealand, South Africa, UK and USA.

The CRUF is a discussion forum. Different individuals take leadership in discussions on different topics and in the initial drafting of representations. In our meetings around the world, we seek to explore and understand the differences in opinions of participants. The CRUF does not seek to achieve consensus views, but instead we focus on why reasonable participants can have different positions. Furthermore, it would not be correct to assume that those individuals who do not participate in a given initiative disagree with that initiative. This response is a summary of the range of opinions discussed at the CRUF meetings held globally. Local country differences of opinion are noted where applicable.

Participants take part in CRUF discussions and joint representations as individuals, not as representatives of their employer organisations. Accordingly, we sign this letter in our individual capacity as participants of the Corporate Reporting Users' Forum and not as representatives of our respective organisations. The participants in the Forum that have specifically endorsed this response are listed below.

(Signatures)

Kevin Harding
Investec Bank Ltd

Biharilal Deora
Director - Abakkus Asset Manager LLP

Larissa van Deventer

Peter Parry
UKSA

Charles Russell
Citi

Peter Reilly
Tempest Concepts

Jed Wrigley
Senior Investment Officer
Eight Roads