STAFF PAPER

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Project	**Disclosure Initiative–Principles of Disclosure (POD)**		
Paper topic	Drafting of disclosure requirements - cover paper		
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Introduction

1. Since November 2014, staff of the New Zealand Accounting Standards Board (NZASB) have been working with IASB staff to develop a new approach to drafting the disclosure requirements for standards. This work is being undertaken as part of the Principles of Disclosure (POD) project. More specifically, the work involves reviewing two existing standards (IAS 16 *Property, Plant and Equipment* and IFRS 3 *Business Combinations*) to develop proposals for inclusion in the POD Discussion Paper, to illustrate how a proposed new approach to drafting disclosure requirements could be applied to two existing standards.

2. This agenda item consists of three papers:

Agenda Paper 11G	This paper illustrates the application to IAS 16 of a proposed new approach to drafting disclosure requirements.
Agenda Paper 11H	This paper illustrates the application to IFRS 3 of a proposed new approach to drafting disclosure requirements.
Agenda Paper 11I	This paper is for background information only. This paper sets out the disclosure principles and objectives used for developing proposed new disclosure sections for IAS 16 and IFRS 3 in Agenda Papers 11G and 11H.

Overall approach

3. In order to address perceived problems with existing disclosure requirements in a consistent and coherent way, we considered it helpful to first develop some general (or broadly-applicable) disclosure principles and objectives, based upon the IASB's *Conceptual Framework for Financial Reporting* and discussions to date in the Conceptual Framework and Disclosure projects.

4. Therefore, there is overlap between the broader principles and objectives we have used in our work and these projects. However, as our work is focused more specifically on developing a new approach to drafting disclosure requirements in accounting standards, we are not seeking feedback on the broader disclosure principles and objectives we developed for our work. Therefore, these broader principles and objectives have been provided as background information only in agenda paper 11I.

5. The focus for this agenda item is on the proposed approach to drafting disclosure sections of standards that resulted from applying those broader principles and objectives to IAS 16 and IFRS 3. The application of those broader disclosure principles and objectives to develop disclosure sections for IAS 16 is summarised in the table following paragraph 11 of agenda paper 11G and, for IFRS 3, is summarised in a table following paragraph 8 in agenda paper 11H.

6. In some cases, the proposed approach may result in the redrafted disclosure section for a standard being longer than the current disclosure section. This is because, as explained further below, the proposed new approach includes objectives and sub-objectives to provide users with the reason why certain disclosures may be necessary, and may include more examples of the types of information that could be disclosed to meet the disclosure objectives and sub-objectives. For example, see the redrafted disclosure section for IAS 16 in agenda paper 11G.

7. In other cases, the proposed approach may result in the redrafted disclosure section of a standard being shorter than the current section. For example, see the redrafted disclosure section for IFRS 3 in agenda paper 11H.

8. Regardless of whether redrafted disclosure sections are longer or shorter, entities are unlikely to need to include in their financial statements disclosures that follow

all of the examples provided. Therefore, the amount of information disclosed in financial statements could be less in comparison to what is currently reported.

9. The two main aspects of the proposed approach on which feedback is sought are:

(a) The inclusion in each standard of overall disclosure objectives, and sub-objectives for groups of possible disclosures.

(b) The emphasis on the exercise of judgement to determine the extent and mix of information to be provided to meet disclosure objectives, rather than prescriptive disclosure requirements.

Main aspects of the overall approach

Disclosure objectives and sub-objectives in standards

10. The lack of clear objectives for disclosure requirements, especially in older standards such as IAS 16, can make it more difficult for preparers to make judgements about whether a particular item of information is material and therefore should be disclosed, because it could be unclear why the item of information might be useful to users of the entity's financial statements—ie what purpose the information is aiming to achieve.

11. To address this problem, the proposed approach includes an overall disclosure objective for each standard. For example, the proposed overall objective for IAS 16 is as follows (see paragraph 1 of the redrafted disclosure section for IAS 16 in agenda paper 11G):

> This Standard requires an entity to disclose sufficient relevant and representationally faithful information about property, plant and equipment to enable users of its financial statements to understand and evaluate the effect property, plant and equipment has on the financial position, financial performance and cash flows of the entity.

12. The suggested overall objective for IFRS 3 is as follows (see paragraph 1 of the redrafted disclosure section for IFRS 3 in agenda paper 11H):

> This Standard requires an entity to disclose sufficient relevant and representationally faithful information about

> business combinations to enable users of its financial statements to understand and evaluate the effect business combinations have on the financial position, financial performance and cash flows of the entity.

13. The proposed approach also includes sub-objectives for groups of disclosures. Each sub-objective attempts to clearly answer the "why" question, that is, why users would want particular types of information? For example, for IAS 16, the suggested sub-objective for disclosure of information about measurement bases and related uncertainties associated with property, plant and equipment is as follows (see paragraph 8 of the redrafted disclosure section of IAS 16 in agenda paper 11G):

> Consistent with the disclosure objective, an entity considers disclosing information about the basis for measuring property, plant and equipment and any associated uncertainties of that measurement. <u>This information helps users understand how the amounts recognised have been determined and any significant measurement uncertainties that are associated with that determination.</u>

14. For IFRS 3, the suggested sub-objective for disclosure of information about measurement bases and related uncertainties associated with business combinations is as follows (see paragraph 9 of the redrafted disclosure section of IFRS 3 in agenda paper 11H):

> Consistent with the overall disclosure objective, an entity considers disclosing information about the basis for measuring assets acquired, liabilities assumed, non-controlling interests in the acquiree and consideration transferred in business combinations during the reporting period and any associated uncertainties of that measurement. <u>This information helps users understand how the amounts recognised have been determined and any significant measurement uncertainties that are associated with that determination.</u>

Questions 1 to 3
1) Does the IASB agree with the overall approach of providing a disclosure objective for each standard and sub-objectives for particular groups of disclosures? 2) Does the IASB consider that the sub-objectives in each standard are sufficiently linked to the overall disclosure objective for that standard? 3) Does the IASB consider that the overall disclosure objectives and the sub-objectives explain why the information could be important to users?

Use of judgement to meet disclosure objectives

15. The wording used in existing disclosure requirements, such as "the entity shall disclose…" and "as a minimum" is prescriptive. This prescriptive wording could encourage preparers to adopt a compliance or checklist approach to disclosure requirements. The wording could also give the impression that the specified disclosures must be provided, notwithstanding the guidance in IAS 1 *Presentation of Financial Statements* explaining that an entity need not provide a specific disclosure required by a standard if the information resulting from that disclosure is not material.

16. To address this problem the redrafted disclosure sections for IAS 16 and IFRS 3 in agenda papers 11G and 11H:

    (a) encourage an entity to use its judgement to determine the extent and appropriate mix of quantitative and qualitative information to disclose in order to meet the disclosure objective and sub-objectives and list factors for entities to consider in exercising their judgement;

    (b) use less prescriptive language;

    (c) allow for different amounts of information to be disclosed depending on the relative importance of property, plant and equipment or business combinations to the entity.

Use of judgement

17. Paragraph 2 of the redrafted disclosure sections for both IAS 16 and IFRS 3 in agenda papers 11G and 11H respectively, state the following:

> To achieve the disclosure objective, an entity uses its judgement to determine the extent and appropriate mix of quantitative and qualitative information to disclose, including the extent of aggregation or disaggregation of that information. Assessments about the amount of information to provide depends on the relative importance of [property, plant and equipment to / the effects of business combinations on] the entity. Assessments therefore should take into account the extent to which the entity's financial position, financial performance or cash flows [(and associated risks and uncertainties)] are affected by [(a) property, plant and equipment and claims against property, plant and equipment (and changes in those); and (b) risks and uncertainties about property, plant and equipment or claims against property, plant and equipment (and changes in those) / business combinations] during the reporting period.

18. These proposals are consistent with the intention behind the recent amendments to IAS 1. In particular:

(a) the fact that a standard is applicable does not necessarily mean that all the disclosures listed in that standard must be provided in all cases; and

(b) the fact that specific disclosures in a standard are presented in a list does not necessarily mean that all the disclosures listed must be provided.

19. However, it should be noted that the redrafted disclosure sections for IAS 16 and IFRS 3 in agenda papers 11G and 11H cover disclosure for property, plant and equipment in its entirety and business combinations in their entirety, without consideration of where those requirements might be placed in specific standards. At this stage, we are not seeking feedback on where certain requirements are best placed, for example, in IAS 16 / IFRS 3 or in IAS 1.

Less prescriptive language

20. The redrafted disclosure sections for IAS 16 and IFRS 3 use less prescriptive language such as "Consistent with the disclosure objective…, an entity considers disclosing information about…" and "the type of information that is likely to be helpful could include…". For example, refer to paragraph 8 of the redrafted disclosure section for IAS 16 in agenda paper 11G and of the redrafted disclosure section for IFRS 3 in agenda paper 11H.

21. This language is intended to illustrate how a less prescriptive, principles-based approach to drafting disclosure requirements could be applied. We note that a key consideration for the IASB is whether this aspect of the proposed approach is:

    (a) workable in various jurisdictions, especially those that are more used to a less judgemental, more prescriptive approach to disclosure requirements; and

    (b) will result in acceptable outcomes, as there is a risk that some might take advantage of such a principles-based approach to omit material information from the entity's financial statements on the grounds that it is not explicitly required to be disclosed.

22. The above points would be key matters to consider in the proposed field testing (see paragraph 25). Note that, at this stage, we are not seeking feedback on the specific examples of information listed under the proposed sub-objectives that may be useful to users. Rather, we are seeking feedback on the language used in the drafting.

Extent of disclosure depending on relative importance

23. The redrafted disclosure sections for IAS 16 and IFRS 3 are divided between "general" and "additional" information. They require that entities:

    (a) first consider disclosing some general information about the relative importance of property, plant and equipment or business combinations to the entity in order to provide the context that users need to understand and evaluate the effect of property, plant and equipment or business combinations on the entity; and

(b) consider disclosing additional information depending on the relative importance of property, plant and equipment or business combinations to the entity. The greater the relative importance and the greater the amount of judgement involved in accounting for property, plant and equipment or business combinations, the more information an entity is expected to disclose.

See paragraphs 7 to 12 of the redrafted disclosure section for IAS 16 in agenda paper 11G and paragraphs 7 to 13 of the redrafted disclosure section for IFRS 3 in agenda paper 11H.

24. The relative importance of an item to an entity is considered to depend on the nature and size of the item as well as the risk associated with that item.

Questions 4 to 7
4) Does the IASB consider it helpful to use less prescriptive language, whereby entities are required to exercise judgement to determine what information should be provided to meet objectives and sub-objectives, rather than prescriptive disclosure requirements? 5) Does the IASB consider it helpful to split disclosures between general information and additional information? 6) Does the IASB agree that the extent of disclosure about particular items (such as property, plant and equipment or business combinations) should depend on their relative importance to the entity? 7) Does the IASB agree that relative importance of particular items (such as property, plant and equipment or business combinations) depends on their nature, size and associated risks?

Next Steps

25. If the IASB are broadly comfortable with exploring the proposed approach further, the next steps would be to field test the proposed approach with preparers, auditors, regulators and users in different jurisdictions. This would enable feedback to be gathered on the workability of the approach in practice. It is

proposed that this field testing be undertaken before publication of the Principles of Disclosure Discussion Paper, currently planned for Q4 2015.