

Roger Harrington

Vice President & Chief Accounting Officer

BP p.l.c.
1 St. James's Square
London
SW1Y 4PD



18 February 2013

European Financial Reporting Advisory Group - EFRAG
35 Square de Meeûs
B-1000 Brussels
Belgium

Submitted via email: commentletters@efrag.org

Dear Sir or Madam,

Invitation to Comment – Discussion Paper: Towards a disclosure framework for the notes

We welcome the opportunity to comment on EFRAG, the French Autorité des Normes Comptables and the UK Financial Reporting Council Accounting Committee's Discussion Paper: Towards a disclosure framework for the notes (the "DP"). I am pleased to respond on behalf of BP p.l.c. to the invitation to comment.

Focus on users' needs

We agree with the approach set out in the DP that a disclosure framework should begin with a consideration of user's needs, and that standard setters, preparers, auditors and regulators should approach disclosure with users' needs in mind. The focus should be on providing information that is necessary, and only information that is necessary, for users to assess the entity's performance, financial position and cash flows, and management's stewardship of the entity. We agree that providing information that allows investors to project future cash flows as inputs to valuation models addresses user needs, but we also think that assessing management's past performance and running of the business is also important.

We agree that there are often excessive disclosures – disclosure of relatively insignificant details – which are intended more to comply with detailed requirements of the standards in a box-ticking exercise than to provide useful information to users. We believe that a significant amount of cultural change is necessary in order to eliminate excessive disclosure and focus on what is important to users. Annual reports are, we believe, increasingly subject to legal review as part of the preparation process and this can sometimes be a barrier to eliminating disclosures. The DP raises a number of interesting points in relation to the promotion of cultural change, which echo some of the comments we made in our responses to the IASB's 2011 Agenda Consultation, to ESMA's 2011 consultation on materiality, and to the IAASB's consultation on the future of auditor reporting.

A further question to be addressed when assessing users' needs is what role the annual financial statements, and annual report more broadly, should play in the context of companies which report quarterly, or who issue their earnings releases before the annual financial statements. The interaction between the various components of the suite of communications with investors (press releases, webcast slides, etc) should, we believe, be considered as part of the debate on the content of the annual report.

Direct 01932 758701
Main 020 7496 4000
Fax 01932 738216
harrro@bp.com
www.bp.com

For whom is a disclosure framework intended?

We believe that a disclosure framework should be intended for standard setters, preparers, auditors and regulators to use. It is important that it serves as a framework for standard setters as they frame the disclosures which should be provided, but equally should be referred to by preparers as they identify which disclosures are sufficiently significant to be published in their financial statements.

Because of the tendency towards "disclosure-by-checklist", we do not believe that individual standards should contain detailed lists of requirements which appear to be mandatory without regard to materiality considerations. Without a significant cultural shift, detailed lists of requirements, even if only strictly applicable when material, may lead preparers to disclose such items as a matter of course to minimize regulatory risk. We agree that it is helpful, if not essential, that the standard setters provide some guidance as to the types of disclosures that might be appropriate, but that some level of judgement is then applied depending on the individual entity's particular context. In this regard, examples of how the standard setters envisage the application of materiality should be applied would be helpful. Preparers should be able to refer to the disclosure framework in order to identify the disclosures that it is appropriate to provide; auditors and regulators should recognize that judgement is a fundamental part of financial reporting and acknowledge decisions to disclose, or not to disclose, made in good faith.

A disclosure framework for the notes, or a broader approach

Attempting to define the purpose of the notes to the financial statements risks excluding from consideration other information included in a company's financial reporting that is of value to users. We appreciate that different jurisdictions around Europe, and indeed around the world, have differing requirements and traditions regarding narrative and governance reporting, but we do believe that considering the annual report as a whole makes for a more meaningful discussion of disclosures.

A more holistic approach to financial reporting, such as the UK FRC's document "Thinking about disclosures in a broader context", which also considers the "front half" of the annual report, focuses on the key question of whether information is useful to investors (whether it should be included at all) rather than whether the information is shown in the notes or the front half.

Responses to the detailed questions raised in the discussion paper are included in the appendix to this letter.

* * *

If you would like to discuss any of the comments in this letter, we would be happy to do so. Please do not hesitate to contact myself or Martin Perrie (martin.perrie@uk.bp.com).

Yours faithfully



Roger Harrington

Cc: Deepa Raval, UK Financial Reporting Council (disclosure@frc.org.uk)

APPENDIX – Responses to the Invitation to Comment

Question 1.1 – Key principles

The Discussion Paper sets out a number of key principles that should underpin a Disclosure Framework. Do you agree with these key principles? If not, what alternative principles would you propose?

We broadly agree with the key principles set out in the DP, although in our view it does not focus on the key objective, which is that the information provided should be of relevance to users of the financial statements to enable them to understand and assess the entity's financial position, performance and cash flows, and management's stewardship of it.

There appears to us to be an inherent assumption in the principles listed under the heading "Setting the disclosure requirements" that a Disclosure Framework ("DF") is primarily intended as guidance for standard setters as to how to mandate required disclosures rather than for other stakeholders such as preparers, auditors and regulators. We believe that there should be an explicit statement in a DF that the principles set out are intended to be used by standard setters, preparers, auditors and regulators.

Additionally, it is important that principle 13 is clarified so that disclosure requirements are "applied, **audited and regulated** with a view to communicating information to users rather than a compliance exercise."

Question 1.2 – Understanding the problem

This Discussion Paper suggests that there are two main areas for consideration to improve the quality of disclosures:

- (a) avoiding disclosure overload, which may be caused both by excessive requirements in the standards, and by ineffective application of materiality in the financial statements;
- (b) enhancing how disclosures are organised and communicated in the financial statements, to make them easier to understand and compare.

Do you agree that these are the two main areas for improvements?

We agree that area (a), the avoidance of disclosure overload, is an important area of focus for improving financial reporting. However, this does raise a fundamental question as to the role of general purpose financial statements – who is the principal audience and how do those users read and obtain useful information from them? To some extent disclosure overload is mitigated by the fact that very few, if any, users will read our financial statements from start to finish, and users are able to electronically search pdf versions of our financial statements in order to locate specific information of interest to them. However, taken to an extreme, this could result in financial statements increasingly becoming a data dump to be searched through by users for any information of relevance to them. We do not believe that this should be the future of general purpose financial statements, and that there is a role for management judgement in providing disclosures that provide an appropriate level of focus through a robust preparation process.

While organization and communication of disclosures in the financial statements are important, we are not convinced that they are currently one of the more important obstacles to clarity in financial reporting, and so we would not identify area (b) as one of the most important for improvement. The structure of the financial statements will depend on the entity – while some principles might be useful we would not advocate rules that would be required to be applied across different entities. In our experience investors value consistency of reporting from period-to-period within an entity as well as consistency between entities.

Question 2.1

In chapter 2 a definition of the purpose of the notes is proposed to assist in deciding what financial information should be required in the notes. Do you think that there is a need to define the purpose of the notes? If not, please provide your reasoning.

We do not consider it necessary to define the purpose of the notes. As the DP recognizes, the purpose of financial statements is defined in IAS 1: "Presentation of Financial Statements" as:

"to provide information about the financial position, financial performance and cash flows of an entity that is useful to a wide range of users in making economic decisions. Financial statements also show the results of the management's stewardship of the resources entrusted to it."

and in our view the purpose of the notes is a natural extension of this. As we describe below in our response to Question 2.2, attempting to define the purpose of the notes in a more restrictive manner risks excluding information that is potentially valuable to users.

A more holistic approach to financial reporting, such as the UK FRC's document "Thinking about disclosures in a broader context", which also considers the "front half" of the annual report removes some of these issues as it allows the question to be whether the information is useful to investors (whether it should be included at all) rather than whether the information is shown in the notes or the front half.

Question 2.2

Is the proposed definition of the purpose of the notes helpful in identifying relevant information that should be included in the notes? If not, how would you suggest it should be amended?

Despite our response to Question 2.1, we largely agree with the definition of the purpose of the notes set out in the DP, and the related discussion. However, it is not clear to us whether the information required to be presented by IFRS 8: "Operating Segments", or any other information that is provided "through the eyes of management", would meet the proposed definition of the purpose of the notes set out in the DP:

"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."

The segment amounts do not provide further description of the amounts presented in the financial statements when the measures used by management differ from the "GAAP" amounts.

While not wanting to pre-empt the post-implementation review of IFRS 8 currently under way, there were clearly persuasive arguments made during the development of IFRS 8 that segment information should be provided using the measures which management uses. We would therefore expect a definition of the notes to capture the disclosures required by IFRS 8 as they are clearly of value to, and provide relevant information to, users.

Question 3.1

In chapter 3, it is proposed to identify specific users' needs that the notes should fulfil. Those users' needs are drawn from the Conceptual Framework. It is also suggested that a Disclosure Framework should include indicators to assist the standard setters to decide when additional information is required to fulfil those users' needs.

(a) Is the description of the approach clear enough to be understandable? If not, what points are unclear?

(b) If you do not support this approach, what alternative would you support and why?

(c) Do you think that a category on "information about the reporting entity as a whole" should be included? If so, why?

We believe that the descriptions of users' needs in paragraphs 1 to 24 of Chapter 3 is clear and understandable, and agree that considering users' needs is an essential first step in determining what information should be disclosed. As stated above, in our view the DF should not only apply to standard setters, and so preparers, auditors and regulators should also consider users' needs.

"Information about the reporting entity as a whole" should be provided in the notes to the financial statements to the extent that it is necessary to allow the user to understand the context in which the entity operates. However, the amount of information that it is appropriate to present in the notes will depend on the nature of the entity. There is clearly less need for a listed entity that produces a comprehensive annual report and maintains a website with extensive information about its business to provide this context in the financial statements than a private company that does neither of these.

Applying the going concern assumption is fundamental to the basis of preparation of financial statements, and so it is appropriate that any significant uncertainty as to the entity's ability to continue as a going concern is disclosed as this information is clearly relevant to users of the financial statements.

Question 3.2

Are the proposed users' needs and indicators in chapter 3 helpful to identify relevant information? If not, how would you suggest amending them, or what other basis would you suggest to identify relevant information to be included in the notes?

As we suggest in our response to Question 3.1, we do not believe that the financial statements should be viewed in isolation, rather they should be considered as part of a broader context including the entity's other communications with investors and stakeholders, and should assume that users possess a reasonable level of knowledge of the applicable financial reporting framework. To the extent that information is provided or available elsewhere (and cross-referenced where appropriate), and can appropriately be considered to be "assumed knowledge" of a reasonably well informed investor, we would not require it to be reproduced in the notes, for example certain types of standing data.

Paragraph 8(c) of Chapter 3 identifies reconciliations of balance sheet items as useful because they assist in understanding related cash flows. While the "inner-auditor" in us understands the appeal of such reconciliations from an ability to cross-check or cross-reference other items shown in the financial statements, we question the extent to which they provide valuable information to users wanting to understand the entity's financial performance and cash flows. As we commented to the IASB in response to their 2011 Exposure Draft "Revenue from contracts with customers", the incremental introduction of balance sheet reconciliations should not be a substitute for an open debate on the merits and drawbacks of requiring the presentation of a direct cash flow statement.

It is also important that each of the user needs identified be subject to the caveat “to the extent necessary to make economic decisions about the entity and assess management’s stewardship.” We appreciate that this relates to the discussion in Chapter 4 on the application of materiality, but we believe it important to reinforce this concept throughout.

Question 3.3

Do you agree with the way risk and stewardship are addressed in the Discussion Paper? If not, what are your views about how risk and stewardship information that should be provided in the notes?

We agree with the fairly broad manner in which the concept of risk is discussed in the DP and believe that it would be likely to lead to somewhat more balanced disclosures in the financial statements than is currently the case, if properly applied. For non-financial institution entities we consider that the current disclosure requirements in IFRS place undue emphasis on risks associated with financial instruments.

However, we are not persuaded that the notes to the financial statements are an appropriate location for discussion of the entity’s operating objectives or market conditions, other than to the extent they could directly impact the amounts presented in the financial statements. In the UK reporting regime it would usually be more appropriate to include these discussions as part of the discussion of the business model and the associated principal risks and uncertainties.

Similarly, an entity’s risk appetite would be difficult to describe, let alone quantify, in a consistent manner across entities, so we question whether this would be a suitable matter to be disclosed in the notes.

As discussed above, to the extent information in relation to stewardship is provided elsewhere we do not see a need for it to be repeated in the notes to the financial statements.

Question 3.4

Standard setters frequently mandate detailed disclosure requirements in each standard. In chapter 3, it is suggested that the way in which disclosures are established influences behaviours, and alternative approaches are discussed. Do you think that standard setters should change their practice of mandating detailed disclosure requirements in each standard? If so, which of the alternative approaches discussed do you think will be the most effective in improving the quality of information in the notes?

We understand that standard setters intend detailed lists of disclosure requirements to be applied where material. We are not convinced that there is a common understanding of materiality between standard setters, preparers, auditors and regulators in the context of disclosures. We would therefore encourage EFRAG to work together with the IASB, the IAASB, preparers, users, auditors and regulators to form a common understanding as to what is material and what is not, and to develop examples which show how materiality should be applied in cases which are not clear.

We do believe that lists of detailed requirements in each standard influences behaviour, even when each party recognizes that there is an overarching statement in IAS 1 that specific disclosures required by IFRS need not be provided if the information is not material. We believe that this is therefore as much a cultural or behavioural problem as an inherent problem with the disclosures that would be required were the related transactions or balances material.

We are not uncomfortable with the current approach of the standard setter providing detailed guidance on the disclosures that are required where material; this provides clarity for preparers, users, auditors and regulators and promotes a degree of consistency between entities. Our concern is as to how the concept of materiality is applied in practice.

Question 3.5

Some standard setters have established, or have proposed establishing, differential reporting regimes on the basis that a 'one size fits all' approach to disclosures is not appropriate. They consider that reporting requirements should be more proportionate, based on various characteristics such as entity size, or whether they relate to interim or annual financial statements? Do you think that establishing alternative disclosure requirements is appropriate?

Within IFRS there are already differential reporting regimes depending on the nature of the reporting entity: IAS 33: "Earnings per share" and IFRS 8 "Operating segments" are only applicable by listed companies. And of course IFRS for SMEs is available to be applied by certain entities in certain jurisdictions. We supported the UK FRC's proposals to allow reduced disclosures in financial statements of certain entities which otherwise use IFRS recognition and measurement criteria (subject to compliance with EU accounting directives). We believe that for privately owned companies, including wholly or nearly-wholly owned subsidiaries of listed companies, there is less need to provide extensive disclosures as users – both owners and providers of finance – will often have access to the relevant information through channels other than general purpose financial statements. Consideration could also be given to developing a separate reporting regime for banks and other regulated financial institutions.

We agree that the disclosure requirements related to interim financial statements should be reduced compared with annual financial statements, and support the principle that interim financial statements should be viewed as an update of the last annual financial statements rather than seen as a stand-alone document. We believe that this principle is entirely consistent with the objective of providing useful and relevant information to users.

Question 4.1

Chapter 4 discusses the application of materiality to disclosures. Currently, IFRS state that an entity does not need to disclose information that is not material. Do you think that a Disclosure Framework should reinforce the application of materiality, for instance with a statement that states that immaterial information could reduce the understandability and relevance of disclosures ?

Yes, as stated above, we do not believe that the concept of materiality is particularly well applied, and agree that it needs to be reinforced as described in the DP.

Question 4.2

Chapter 4 also includes proposed guidance to assist in the application of materiality. Do you think that a Disclosure Framework should include guidance for applying materiality? If you disagree, please provide your reasoning.

Although we think that this is in part a cultural matter, we do believe that some guidance would be helpful. Cultural change can be promoted through education and discussion. Application guidance, examples or indicators, may be useful to frame the debate and to provide a more robust foundation for not providing immaterial disclosures.

Question 4.3

Is the description of the approach clear enough to be useful to improving the application of materiality? If not, what points are unclear or what alternatives would you suggest?

One of the inherent challenges facing preparers is how they can know whether something is material or not, given the wide range of interests of different investors. Some items may clearly be material or immaterial, but this is not always clear.

The principles behind the approach set out in the DP are clear and we largely agree with the direction of the discussion, in particular the summary in paragraphs 42 and 43 of Chapter 4: disclosures are not required if information is immaterial; and disclosures are not required for every line item presented in the primary financial statements unless the information would be material. However, we do find the detailed analysis rather overcomplicates a topic which in essence is addressing the question of whether the information is useful to users of the report. While we do not necessarily agree with all of the detail included, we find the decision tree set out in Appendix C to the UK FRC's "Thinking about disclosures in a broader context" a helpful tool which focuses on the right questions.

Consistent with our response to Question 3.2 above, we do not agree with the analysis in paragraphs 39 to 41 of when a balance sheet reconciliation is necessary. In each of the scenarios A, B and C it is likely that the acquisitions, depreciation and impairment will be shown in (or determinable from) the cash flow statement and possibly in other notes to the financial statements as well. Applying the principles in the remainder of the chapter on materiality, it is not clear to us that such a reconciliation would be required in those scenarios.

Question 5.1

Chapter 5 includes proposals for improving the way disclosures are communicated and organised. Would the proposed communication principles improve the effectiveness of disclosures in the notes? What other possibilities should be considered?

As we set out above in our response to Question 1.2, the importance of the manner in which disclosures are communicated and organized is lessened by the fact that very few, if any, users will read our financial statements from start to finish, and users are able to electronically search pdf versions of our financial statements in order to locate specific information of interest to them.

While organization and communication of disclosures in the financial statements are important, we are not convinced that they are currently one of the more important obstacles to clarity in financial reporting, and while we largely support the principles set out in Chapter 5, we believe they are less important than the cultural and behavioural issues related to the application of materiality set out in Chapter 4.

We are not sure that the "prioritization" described in paragraphs 34 to 37 will result in a better presentation of financial statements. An essentially stable structure from one year to the next helps preparers and users, even now that electronic searchability of financial statements is possible.

Question 5.2

Do any of the suggested methods of organising the notes improve the effectiveness of disclosures? Are there different ways to organise the disclosures that you would support?

We agree with the premise that disclosures should be made with a view to communicating information to users rather than a compliance exercise. The principles appear to be a good summary of existing best practice.

Question 6.1

Are there any other issues that you think need to be addressed to improve the quality of information reported in the notes to the financial statements? Please explain how you think these issues should be addressed and by whom.

We welcome the fact that EFRAG has been working together with the US FASB on developing their different discussion papers on this subject. As a company whose shares are listed in both London and New York we believe that it is important that the changes proposed are promoted on both sides of the Atlantic. While we do not believe in convergence for convergence's sake, we would appreciate a common approach to materiality in the territories that represent our two most significant investor bases.