

CONSULTATIONS

FINANCIAL REPORTING COUNCIL DISCUSSION PAPER “THINKING ABOUT DISCLOSURES IN A BROADER CONTEXT”

INTRODUCTION

These comments are submitted by the Association of International Accountants (AIA), with input from a Technical Committee and members of the Association.

ABOUT AIA

The Association of International Accountants (AIA) was founded in the UK in 1928 as a professional accountancy body and from conception has promoted the concept of ‘international accounting’ to create a global network of accountants in over 85 countries worldwide.

AIA is recognised by the UK government as a recognised qualifying body for statutory auditors under the companies act 2006, across the European Union under the mutual recognition of professional qualifications directive and as a prescribed body under the companies (auditing and accounting) act 2003 in the Republic of Ireland. AIA also has supervisory status for its members in the UK under the money laundering regulations 2007.

AIA promotes and supports the advancement of the accountancy profession both in the UK and internationally. The AIA exams are based on international financial reporting and international auditing standards and are complimented by a range of variant papers applicable to local tax and company law in key jurisdictions together with an optional paper in Islamic accounting.

AIA members are fully professionally qualified to undertake accountancy employment in the public and private sectors.

AIA RESPONSE

SUMMARY

AIA supports the discussion of disclosure related issues in financial reporting, believing that the Discussion Paper (DP) issued by the Financial Reporting Council (FRC) should prompt a much needed debate. We note that the European Financial Reporting Advisory Group (EFRAG) and the International Accounting Standards Board (IASB) have also recently begun work on this issue and that the UK's Financial Reporting Lab also is looking into how disclosures can be made as useful as possible to the users of financial reports.

AIA is particularly interested in the debate surrounding the volume of information that is currently provided in disclosure notes, and in how a boundary can be established to eliminate information that is deemed irrelevant or immaterial to the main user groups.

QUESTION 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?

AIA believes that a disclosure framework as outlined in the DP is needed as a basis for discussion around disclosures. Without determining the information needs of users it is hard to see how a disclosure framework can be developed. Therefore the first question is of paramount importance and is possibly the hardest question to answer, given the wide range of users of financial reports as identified in the IASB's Conceptual Framework. We agree that the development of a disclosure framework will require input from users in order for the debate not to become a wasted opportunity in terms of clarifying and prioritising the key information needs of users, which should then form part of the disclosure framework. We also consider that this consultation with users should strive to identify the information currently given in financial reports that is NOT considered useful, as determining the information that can safely be excluded from financial reports could play a large role in de-cluttering financial disclosures.

AIA believes that a disclosure framework should result in the benefits as outlined on page 5 of the DP, with the expectation that, in particular, the disclosure of duplicate information will be avoided, and that information can be better organised, and provided in a layout which is easy for the users to navigate. We share the view of many that in recent years the volume of information provided to users has multiplied, and that this may well detract from the usefulness of information, rather than add to it.

QUESTION 2

DO THE DISCLOSURE THEMES SET OUT ON PAGE 16 OF THIS PAPER CAPTURE THE COMMON TYPES OF DISCLOSURES THAT USERS NEED?

AIA considers that the disclosure themes broadly capture the information needs of users. We believe that information around risk and uncertainty is very important to most users, and that there is potential for development of a robust framework in relation to disclosures of this type.

We also consider that some users may welcome the inclusion of financial information that is not a specific disclosure requirement of the applicable financial reporting framework. Such measures should, if included in the financial report, be consistently calculated and presented, adequately explained, and if necessary reconciled to required disclosures in order for them to be useful.

AIA agrees with the comment on page 17 that there is a need for a debate around the types of non-financial information that users would like to see included in a financial report. However care must be taken here to ensure that materiality can be applied to such information, and to ensure the proper placement of such information in the financial report, as it is likely to be less relevant and useful to most users than financial information.

QUESTION 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?

AIA agrees that the components of the financial report, as discussed in the DP, is a useful way to differentiate between the types of information provided to users. We feel that identifying a structure for the financial report and clarifying the information to be contained in each component of that structure should make the financial report easier to navigate and help comparability.

We welcome the fact that the FRC's DP takes a broad approach, looking at several components of the financial report, unlike EFRAG's current discussion paper on disclosures, which focuses on the notes to the financial statements.

QUESTION 4

DO YOU BELIEVE THAT THE PLACEMENT CRITERIA IDENTIFIED IN THIS PAPER ARE APPROPRIATE?

AIA agrees that placement criteria are an important part of a disclosure framework. We also agree that a differentiation between management commentary, corporate governance and the financial statements is logical. The placement criteria approach should clarify the relationship between the components of the financial report.

We agree that disclosures in relation to disaggregation and explanatory material linked to the financial statements should be contained in the notes to the financial statements.

A concern is that moving disclosures, for example information in relation to unrecognised amounts, from the financial statements notes to management commentary could have implications for auditors and their report on financial statements. There will need to be a cohesive debate surrounding the audit of information contained in the financial statements as opposed to requirements in ISA 720 relating to “other information in documents containing audited financial statements” to ensure that information is audited where necessary, despite its placement within the financial report. This issue is also relevant to the placement of related party disclosures and non-adjusting post balance sheet events in a financial report, if such disclosures were moved to corporate governance and management commentary respectively.

AIA accepts that placement criteria can be used in deciding where a disclosure should be made, as illustrated with risks and uncertainties on page 25. However, a concern remains that this could result in duplication of information, resulting in unnecessary clutter. AIA encourages the FRC to explore the concept of a separate risk report, believing that this could provide a very user-friendly “one stop shop” by bringing all risk-related disclosures together, subject to the issue of auditing these disclosures as mentioned above.

QUESTION 5

HOW SHOULD STANDARD SETTERS ADDRESS THE ISSUE OF PROPORTIONATE DISCLOSURES?

AIA strongly believes that a proportionate disclosure regime is needed in order for de-cluttering of financial information to take place, especially for small and medium sized entities. We believe that the requirements of financial reporting standards in relation to disclosure should be principle-based and avoid a “checklist” approach, as this often results in over-disclosure.

It is difficult to comment on how standard setters should address this issue as there are many advantages and disadvantages to the various methods outlined in the DP. AIA would tentatively suggest that the issue of public accountability is of prime importance, and that type of industry should also be a factor in determining the level of disclosure required in a financial report. This is because we believe that the type of information needs of users is much more driven by the accountability and area of operation of a business than by its size.

QUESTION 6

DO YOU AGREE WITH THE FRAMEWORK FOR MATERIALITY SET OUT IN THIS PAPER? HOW COULD IT BE IMPROVED?

AIA believes that the disclosure framework should clarify how the concept of materiality is applied to disclosures. The definition of materiality is well understood but sometimes not well applied due to the number of descriptors as laid out in page 34 confusing the issue. In particular we would welcome a streamlining of terminology and a possibly the development of a hierarchy of materiality.

We strongly believe that if preparers of financial information are increasingly required to use judgment in determining whether a matter is sufficiently material to warrant disclosure then robust guidance must be given on the definitions or criteria used to make that judgment call. There should also be consistency where possible between definitions used in financial reporting and in auditing standards.

We consider the FRC's suggestion that materiality should be gauged with reference to risk and measurement uncertainty is sensible and relevant to most users, and that a maturity analysis would provide useful information.

Above all the disclosure framework should provide clear guidance on what information should be excluded on the grounds of immateriality – this is the only way to avoid information overload and to ensure that all information provided is in some way relevant.

QUESTION 7

ARE THERE OTHER WAYS IN WHICH DISCLOSURES IN FINANCIAL REPORTS COULD BE IMPROVED?

AIA encourages the discussion of whether some disclosure can be provided in appendices or in some other way made separate from the main body of disclosures. For example, "static" information such as statements of compliance with IFRS or national GAAP, and unchanged accounting policies could be provided for reference but are unlikely to be the main focus of users' attention. We note that accounting policies notes sometimes are little more than a word for word repetition of the financial reporting standards requirements, and therefore do not add much value to the financial report.

FURTHER INFORMATION

The above replies represent our comments upon this consultation document. We hope that our comments will be helpful and seen as constructive. AIA will be pleased to learn of feedback, and to assist further in this discussion process if requested.

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