18 January 2013

Ms Deepa Raval
Financial Reporting Council
5th Floor, Aldwych House
71-91 Aldwych
London WC2B 4HN
United Kingdom

Email: disclosure@frc.org.uk

Dear Ms Raval

Discussion Paper: Thinking about disclosures in a broader context

Thank you for the opportunity to comment on the above. CPA Australia and the Institute of Chartered Accountants in Australia (the Institute) have considered the Discussion Paper (DP) and our comments follow.

CPA Australia and the Institute represent over 200,000 professional accountants in Australia. Our members work in diverse roles across public practice, commerce, industry, government and academia throughout Australia and internationally.

We appreciate the 'disclosure problem' that motivated the Financial Reporting Council (FRC) to publish its DP. The issue of 'voluminous' and 'boilerplate' disclosures and their effect on the quality of the information in terms of meeting the needs of users is evidenced by the many other global consultation papers on disclosure and complexity in reporting.

Some of those consultation papers have a narrow scope in that they look only at the disclosure components of general purpose financial statements. In contrast, this DP has a broader scope and explores the need to develop a disclosure framework for application to that information the DP categorises as financial reporting (being, the information typically found in an annual report, interim or preliminary announcements).

Given the broad scope of this project, we consider that some linkages could be made to the Integrated Reporting Framework currently being developed by the International Integrated Reporting Council due for release in December 2013.

The DP identifies three components of the financial report: management commentary, corporate governance and financial statements and suggests that a 'single' disclosure framework could be developed to apply to the financial report. Further, the proposal for a single disclosure framework appears to be founded on the proposition that the relationship of the three components of the financial reporting package (management commentary, corporate governance and financial statements) is one of equals.

We have some problems with the approach taken. We do not see the relationship of the components of the financial reporting package in this way. Rather, we see financial statements as playing an important role in corporate governance. In that role, the financial information in the financial statements is a product of the governance process and an input to the governance mechanisms that help alleviate the agency problem that results from the separation of management and financing. Accordingly, we believe it might be more appropriate to use corporate governance as the basis for developing a disclosure framework to apply to the financial report as defined by the DP.

Where the disclosure framework is limited to financial statements only, we consider the International Accounting Standards Board (IASB) best placed to lead the project. However, should corporate governance be used as the basis there may be other bodies with more suitable expertise and experience to develop this much broader framework. We consider the action points suggested for the IASB on page 58 of this paper, would be useful in the development of the disclosure framework as part of their Conceptual framework project they have already commenced. Some commentators consider that good corporate governance should have the maximisation of shareholders' wealth as its objective, while others focus on social responsibility or sustainability. At the very least before undertaking a project on disclosure we believe there is a need to better understand the meaning attributed to corporate governance by those stakeholders with an interest in financial reporting, the interactions of the various parts of the information categorised in the DP as financial reporting and the impacts of each information type on the overall quality of the information available to users.

The Appendix to this letter contains our answers to the 'Questions to consider'. We have not responded to the 'Additional questions for users'.

If you have any questions regarding this submission, please do not hesitate to contact either Mark Shying (CPA Australia) at mark.shying@cpaaustralia.com.au or Kerry Hicks (the Institute) at kerry.hicks@charteredaccountants.com.au.

Yours sincerely

Alex Malley
Chief Executive Officer
CPA Australia Ltd

Lee White
Chief Executive Officer
Institute of Chartered Accountants Australia

Appendix

Questions to consider

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 disclosure be provided?**

   The DP acknowledges that prior to answering the question 'What information do users need?' it is necessary to understand who are the users? The DP limits users to investors. In contrast, we think of the financial report as providing people who are interested in a company – such as current and prospective shareholders, lenders, analysts and employees – with information about the financial performance and position about the company. Aside from that issue, we agree that a disclosure framework that addresses those four questions would help to address the problems with disclosure.

2. **Do the disclosure themes set out on page 16 of this paper capture the common types of disclosures that users need?**

   The disclosure themes identified for the primary financial statements and management commentary seem reasonable.

   We believe the disclosure themes set out for corporate governance represent one view of what constitutes corporate governance and the view taken by directors about for whom they govern. Some commentators consider that good corporate governance should have the maximisation of shareholders' wealth as its objective, while others focus on social responsibility or sustainability. While the disclosure themes set out for corporate governance appear to be consistent with a shareholder wealth objective it is not clear why the corporate governance component is being developed in this restricted way.

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?**

   The components of the financial report are listed as management commentary, corporate governance and financial statements. Early on the DP notes that these three components are reinforced by the EU Accounting Directives, which require each of the components within an annual report.

   What is considered to be part of the financial report differs widely across different countries. In Australia the *Corporations Act 2001* defines the financial report as consisting of the directors' declaration that the financial statements and notes comply with accounting standards, give a true and fair view and there are reasonable grounds to believe the company is solvent, the financial statements and the notes that accompany the financial statements. The Australian law does not consider management commentary and corporate governance to be part of the financial report.

   We do not consider a strong case for the financial report to consist of the three components has been made.

4. **Do you believe that the placement criteria identified in this paper are appropriate?**

   We do not agree that any placement principles relevant for financial statements would necessarily be relevant for the whole financial report, as envisaged by the DP. In the letter to this submission, we state our position that it might be more appropriate to use corporate governance and not financial statement reporting as the basis for developing a disclosure framework to apply to the financial report as defined in the DP.

The criteria in the IASB's DP 'Management Commentary', outlined on page 21, do provide adequate differentiation between the management commentary and the notes to the accounts.

In the context of financial statements, disclosure is typically understood as referring to the notes that accompany the information that is presented on the face of the financial statements. The themes identified for the notes on page 24 do some have relevance and could be worthy of further analysis by the IASB.

The experience of the International Public Sector Accounting Standards Board in its conceptual framework project suggests that when the information is not financial statements, the reasons for disclosure and the attributes of that information might be different – an outcome that may make a single disclosure framework problematic.

5. How should standard setters address the issue of proportionate disclosures?

We support a need for differential disclosures for non-listed entities, as we expect the user needs for the financial reports of those entities are different to that of listed company users. We also support the use of IFRS for SMEs to provide differential disclosures as well as differential recognition and measurement in the financial statements of non-listed small and medium entities

6. Do you agree with the framework for materiality set out in this paper?

We have observed an increase in an 'if in doubt, disclose' behaviour amongst preparers and auditors. Whilst the IASB has some reference to materiality in the conceptual framework, we consider that more can be done in this area. As part of the Conceptual Framework project, we would like the IASB to expand guidance in this area. This should be done in full consultation with all stakeholders including the International Auditing and Assurance Standards Board and the International Organization of Securities Commissions. They could contribute to the development of different terminology to be used to describe orders of magnitude.

7. Are there other ways in which disclosures in financial reports could be improved?

We have no other comments.