Dear IASB members,

Invitation to comment - Exposure Draft ED/2019/6/Disclosure of Accounting Policies Proposed amendments to IAS 1 and IFRS Practice Statement 2

Ernst & Young Global Limited, the central coordinating entity of the global EY organisation, welcomes the opportunity to offer its views on Exposure Draft Disclosure of Accounting Policies - Proposed amendments to IAS 1 and IFRS Practice Statement 2 (the ED).

We appreciate the objective of the Board to provide specific guidance on which accounting policies to disclose in order to direct the preparers to more entity-specific disclosure behaviours. We believe that additional guidance on disclosure of accounting policies will be helpful in directing the attention of the preparers to the material accounting policies, which, in turn, will allow users to more effectively focus on decision-useful information.

We agree with the clarification in the proposed amendments that not all accounting policies relating to material transactions, other events or conditions are themselves material to the financial statements.

We support the Board’s effort to provide guidance in the IFRS Practice Statement 2 Making Materiality Judgements (the PS) on how to apply the concept of materiality to accounting policy disclosures. This will help to raise awareness of the issue of disclosure overload and encourage management to more actively pursue disclosure effectiveness by applying the materiality concept. However, we do not think that the two examples are sufficiently clear in guiding preparers to determine what information about an accounting policy is material and needs to be disclosed.

In general, there is the risk of entities providing standardised and boilerplate information. We suggest that the Board should also consider providing additional guidance on how to prepare entity-specific and tailored accounting policy disclosures, in order to achieve the behavioural change among preparers that is sought after.
Our detailed responses to the questions are set out in the Appendix to this letter.

Should you wish to discuss the contents of this letter with us, please contact Leo van der Tas at the above address or on +44 (0)20 7951 3152.

Yours faithfully

Ernst & Young Global Limited
Appendix - Responses to specific questions

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 this proposed amendment? If not, what changes do you suggest and why?

We support the proposal to require entities to disclose their material accounting policies. We believe that the proposed requirement for accounting policy disclosures will be helpful to direct the attention of the users to the material accounting policies, and thus, potentially will result in more effective communication. Furthermore, consistency on how to determine whether a piece of information is relevant or not, is desirable. Currently, accounting policies are to be disclosed under a different threshold (“significant”) from other types of information (“material”), which is somewhat confusing, particularly considering that the current threshold is not defined anywhere in IFRS (at least, not in the context of disclosures).

However, the proposal is not clear as to whether the proposed change is intended to represent a change in threshold, or if it is simply a change in terminology. Our reading suggests that it is in fact a change in threshold, in that “significant” policies includes all policies that regards material transactions and items, while “material” policies are only those that must be disclosed in order to provide the users with decision useful information. We believe the Board should clarify the impact of the change in wording.

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 an entity’s financial statements.

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

We agree with the clarification that not all accounting policies relating to material transactions, other events or conditions are themselves material to the financial statements. Furthermore, we agree that “accounting policies that relate to immaterial transactions, other events or conditions are themselves immaterial and need not be disclosed”. However, we encourage the Board to consider highlighting the concept of ‘obscuring information’, i.e., that disclosing immaterial policies may have the effect of obscuring material information.
We also believe it would be helpful to provide guidance on how to determine whether accounting policies applied in comparative periods, but not in the current period, are material, as per the disclosure requirement in paragraph 38 of IAS 1. In our view, the same guidelines as prescribed in paragraph 117B of the ED would apply. To clarify this, the proposed introduction to paragraph 117B could be amended by adding “...relates to material transactions, other events or conditions in the current period or any comparative period(s) included in the financial statements and ...”. Also, the guidance in paragraphs 66-69 in the PS may be considered.

It is not clear whether material accounting policies would only relate to transactions, other events or conditions in the periods covered by the financial statements. For example, it is unclear whether an entity would need to disclose accounting policies for a business combination that occurred in prior periods, but not included in the current or the comparative periods, when an entity recognised material goodwill from that business combination. Therefore, we believe that the Board also needs to clarify whether accounting policies are only limited to those transactions, other events or conditions in the periods covered by the financial statements.

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

We agree that the list of examples of circumstances enumerated in paragraph 117B is relevant in determining whether an accounting policy is material to the financial statements. However, the wording of the requirement suggests that the list is not exhaustive, and thus, a policy not captured in the list may still be considered material. Contrary to the proposed requirement, we are not able to identify other circumstances in which disclosure of an accounting policy would be material. Therefore, we believe the Board should consider revisiting the wording.

Although the criteria in (a) to (d) of paragraph 117B are already included in the current standard, organising them in a list format significantly improves clarity. Criterion (e) is new. However, the nature of item (e) is somewhat different from the others. Item (e) arguably refers to policies applied by an entity in which choices and/or judgement has been made, and as such is an incremental addition to the list. However, such policies would often fall within criterion (d). Item (e) also addresses what disclosures should be made about material accounting policies, i.e., the disclosures should be specific to the facts and circumstances of the entity, and, as such, it is not helpful in determining whether an accounting policy is material or not. Furthermore, item (e) could also refer to the level of granularity of accounting policy disclosures in the financial statements. Therefore, we believe the “what disclosures” dimension of item (e) should rather be included in the guidance in paragraph
If the Board believes there are accounting policies that are material by reference to item (e) only, then we believe item (e) needs to be clarified. We also suggest that the Board clarifies the level of granularity of accounting policy disclosures in the financial statements. This can be achieved by providing illustrative examples (also refer to our response to question 4).

**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?

We agree that providing illustrations in the PS would be useful for entities applying the concept of materiality to accounting policy disclosures. However, we do not think that the two examples are sufficiently clear. The examples try to focus on the fact that an entity should provide entity-specific information and avoid standardised accounting policies and duplication of the requirements in the standards. We believe that the examples in the PS could be further improved by providing additional guidance and illustrations of the contents of material accounting policy disclosures.

Furthermore, we believe that the two examples intended to illustrate the difference between material and immaterial accounting policies are not achieving their objective, since the difference between the two examples is unclear, combined with the above-mentioned confusion between “when to disclose” and “what to disclose”.

Therefore, we encourage the Board to revisit the examples with the intention to clarify: (a) when an accounting policy would need to be disclosed in the financial statements; and (b) what information about the accounting policy would need to be disclosed (or does not need to be disclosed).

For instance, Example S only provides the reason why disclosure of accounting policy for revenue recognition is likely to be material (i.e., because the entity has made significant judgements in applying the accounting policy and it had to consider how the requirement of the standard applies to its own circumstances). However, the example provides no guidance on which information about the accounting policy the entity will need to disclose. Considering that IFRS generally are principle-based, all policies prescribed by the standards have to be applied to entities’ own circumstances. Thus, Example S does not provide any guidance on how to distinguish between material and immaterial policies. The handset-data issue illustrated by this example is quite common in the telecommunications industry. The judgement applied in determining the applicable performance obligations and the timing of the revenue in these contracts is fairly consistent across most entities. Therefore, we are not
convinced that Example S is particularly helpful in providing guidance as to how to distinguish between material and immaterial policy disclosures.

Nevertheless, Example T fails to distinguish between the accounting policies an entity needs to include in the financial statements and the information about those accounting policies that should be disclosed. The example seems to focus more on highlighting the need to avoid accounting policies that duplicate the requirement of the standard. It is clear from the example that certain information about impairment of non-financial assets is “material” (e.g., the discount rate used in impairment testing). However, it is unclear how the Board believes the interaction between specific information that is considered to be material and the assessment of whether policy disclosures are material, works, and why the disclosure of the applicable accounting policies reflecting the entity’s specific facts and circumstances is not material, when comparing to the analysis in Example S. For instance, information about the cash generating units identified by the entity applying the policies prescribed by IAS 36 Impairment of Assets could be material in accordance with the proposed paragraph 117B(e).

**Question 5**

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

In general terms, we appreciate the Board’s concerns about understandability of the concept of materiality and translation into other languages. More specifically, the ED uses the terms “material accounting policies” and “information about accounting policies that are material”. In reference to our comments above, we believe that a two step-approach is needed: 1) to identify material accounting policies; and 2) to determine appropriate disclosures in respect of the material accounting policies. The Board should ensure that the terminology used is consistent, such that the former wording is only used when referring to 1), and the latter is consistently used in the context of 2).

**Question 6**

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

The Board suggests that the proposed amendments should be applied prospectively. The Board notes in paragraph BC17 “that retrospective application of the proposed amendments would not be possible because the proposed amendments affect only the disclosure of accounting policies”. This adds additional confusion on the disclosure of accounting policies with regards to prior periods (see our response to Question 2 above).
The left side of the “Diagram – determining whether an accounting policy is material” in the PS includes a broken line that suggests an entity would still need to consider whether other disclosure requirements have been met for immaterial transactions, other events or conditions. We suggest that this line be deleted as the disclosure requirements of other standards are not required for immaterial transactions, other events or conditions.