BUSINESSEUROPE

International Accounting Standards
Board (IASB)
30 Cannon Street
London EC4M 6XH
United Kingdom

26 February 2016

Dear Board Member,

Re: Exposure Draft ED/2015/8 IFRS Practice Statement: Application of Materiality to Financial Statements

BUSINESSEUROPE is pleased to have the opportunity to comment on ED/2015/8 (the ED or the Practice Statement).

We think that guidance in this area will be helpful both to users and preparers, provided that it remains non-mandatory. We therefore object to the clear message of paragraphs BC10 to BC15 that the Board actually thinks that the document should be made mandatory by jurisdictions. In addition, we would request that in drafting and presenting the Practice Statement, the Board bears in mind that the document may nonetheless become mandatory in some jurisdictions and therefore should be drafted in such a way as to avoid expanding its scope beyond the financial statements and creating procedural practice which would be both onerous for entities and contradict the spirit of the Disclosure Initiative.

We think that the Practice Statement might be made more effective by removing the majority of the duplication of existing mandatory guidance extracted from various IFRS documents and focusing on the following:

- Clarifying the scope of the guidance to ensure that it does not stray outside the boundaries of financial reporting.
- A brief explanation of the relevance and pervasiveness of the concept of materiality in IFRS, along with its definition.
- An explanation that the assessment of materiality is a qualitative analysis more than a quantitative one, and requires the application of judgement in the context of the entity's specific circumstances.
- The guidance should focus on areas where the assessment of materiality presents the most difficulty (disclosure in the notes, interim reporting, etc.) rather than the better-understood areas of the primary financial statements; it

should avoid guidance which could result in boiler-plate disclosures or anything which could be taken as a checklist.

- The single most helpful element would be to provide illustrative examples of both poor and good assessment of materiality with sufficient context to facilitate their comprehension.

The Practice Statement should remain non-mandatory indefinitely, or at the very least, it should be non-mandatory until the guidance has been proved through experience to be helpful, practical and free from unforeseen adverse consequences. The post-implementation review of the amendments resulting from the Disclosure Initiative will be an essential source of such information.

Our detailed comments and responses to the question in the ED are set out in the appendix to this letter.

Please do not hesitate to contact us should you wish to discuss these issues any further.

Yours sincerely,

P.P.

Jérôme P. Chauvin
Deputy Director General

APPENDIX

Question 1—Form of the guidance

A Practice Statement is not a Standard. The IASB's reasoning for issuing guidance on applying the concept of materiality in the financial statements in the form of a non-mandatory Practice Statement is set out in paragraphs BC10-BC15.
(a) Do you think that the guidance should be issued as non-mandatory guidance? Why or why not?
(b) Do you think that a Practice Statement is the appropriate form for non-mandatory guidance on applying the concept of materiality? Why or why not? If not, what alternative(s) do you propose and why?

We are of the view that the Practice Statement as currently drafted should not be made mandatory.

However, the discussion in paragraphs BC10 to BC15 states three times that the relevant authorities could choose to require compliance with it, thus making it clear that the IASB actually would prefer that the guidance were mandatory but refrained from proposing this only because of the concern that it might cause conflicts with national legal frameworks. The IASB then contradicts this concern by going on to state its view that "even though some jurisdictions have legal or regulatory requirements about materiality, this should not necessarily result in a conflict with the guidance." We do not think that the current text is suitable to be made mandatory and therefore these comments should be removed from the text.

Materiality is a concept that is pervasive throughout current IFRS and assessment of whether information is material is generally accepted to be mandatory. However, there is little guidance at present as to how to make judgements about materiality and so the IASB's project to fill this gap is welcome.

There is a danger that the Practice Statement be seen as "best practice" and this would, in our view, be undesirable since some of the suggestions made in the ED cannot be applied to all entities without generating additional but unnecessary processes and procedures within those entities. The examples listed in paragraph 22 represent procedures which would be a burden in some entities if made mandatory. It is important not to force entities down a particular route but to allow them to consider their own circumstances and apply judgement to decide on the most suitable approach for them.

We also recognise that if the guidance were to be provided in the form of "educational material" it may not be given the appropriate weight that it deserves. A Practice Statement is a relatively new form of document in the body of IFRS, and constituents might need time and help in coming to terms with its status. However, we agree that the status of a Practice Statement is probably the best approach in the first instance. This should be reviewed at a later stage to see whether a change of status is justified in the light of practical experience. .

We are also aware that this ED forms an early part of the "Disclosure Initiative", and that further developments in that project might have a bearing on the guidance provided here. The most efficient way to review the Practice Statement would be as part of the post-implementation review of the amendments resulting from that project. Overall therefore, we agree that non-mandatory status is appropriate at present.

Question 2—Illustrative examples

Do you find the examples helpful in the [draft] Practice Statement? Do you think any additional practical examples should be included? If so, what scenarios should the examples address? Please be as specific as possible and explain why those example(s) would be helpful to entities.

We think that the provision of examples to help entities understand how materiality should be assessed is probably the single most important element that the ED should provide.

The examples in the current draft tend to be obscured by long tracts of text, including extracts from the existing IFRS literature on materiality. It would be more "user-friendly" if the examples were highlighted and the duplicated existing text eliminated, thus making it clear which text represents new implementation guidance. This would also have the advantage of making the Practice Statement more easily digestible by reducing its volume.

It should be clearly stated that the examples are intended to be non-mandatory and that they should not be regarded as a "check-list" of elements to consider or actions to be undertaken.

One area in particular in which we think examples are lacking is that of how materiality should be considered in the context of interim financial statements.

Question 3—Content of the [draft] Practice Statement

The [draft] Practice Statement aims to propose guidance in three main areas: (a) characteristics of materiality; (b) how to apply the concept of materiality in practice when presenting and disclosing information in the financial statements; and (c) how to assess whether omissions and misstatements of information are material to the financial statements. It also contains a short section on applying materiality when applying recognition and measurement requirements.
Please comment on the following and provide any suggestions you have for improving the [draft] Practice Statement:
(a) Do you think that any additional content should be included in the Practice Statement? If so, what additional content should be included and why?

As mentioned above, guidance about interim reporting seems to repeat the guidance of IAS 34. It should be developed further to make it clear what is the relevant context in which materiality should be assessed. For example, in the case of quarterly reporting, it should be made clear whether the relevant period is the discrete quarter or the year to date, or both. It would also be helpful to have examples of information about changes from the annual statements which would be material.

There is a presumption in accounting that all basic transactions (cash movements, expense invoices, sales invoices, etc.) will be recorded in the books underlying the financial statements. In the context of tight reporting deadlines and interim reporting, for example, it is acceptable to make estimates of the amount of transactions. It may be helpful to provide a discussion of how the consideration of materiality affects such procedures.

(b) Do you think the guidance will be understandable by, and helpful to, preparers of financial statements who have a reasonable level of business/accounting knowledge and IFRS? If not, which paragraphs/sections are unclear or unhelpful and why?

We think that the bulk of the difficult decisions about materiality arise in the context of the notes to the financial statements rather than in respect of the aggregation or disaggregation of items on the face of the primary financials. The guidance should focus on this.

In addition, the quantitative aspect of the assessment of materiality is better understood than the qualitative aspect. Further focus on the qualitative aspect would therefore help.

Detailed actual examples of what is meant by the notion of the obscuring of material information by immaterial information would be useful. Users may be able to provide examples drawn from financial statements they have examined.

Paragraph 11 states that "Requirements in IFRS must be applied if their effect is material to the complete set of financial statements". Paragraph 62 reiterates this in respect of the recognition and measurement requirements. In contrast, paragraph 43 states that "Management considers whether an item is material by considering it relative to individual line items, subtotals and totals on the face of an individual statement as well as to each overall individual statement". This is potentially confusing, particularly in view of the expectation mentioned above that all transactions are recognised, even if immaterial. The relationship between these different areas needs to be better articulated to help comprehension.

In a similar vein, paragraph 29 states, quite rightly in our view, that the assessment of whether an item is material should be undertaken on both an individual and a collective basis. Further discussion and illustration of this would be helpful. Paragraphs 56 to 58 touch on these matters but insufficiently.
As an overall comment, we think that the guidance should be better articulated by highlighting examples illustrating each concept developed.

(c) Are there any paragraphs/sections with which you do not agree? If so, which paragraphs/sections are they and why?

We think that the section about omissions and misstatements does not in its place in this Practice Statement. IAS 8 makes it clear that any intentional error made by management in order to achieve a particular outcome is, by its very nature and purpose, material. If the Board considers that more clarification is required, IAS 8 would be the more appropriate place for this.

We do not agree with the inclusion of paragraph 36. The underlying principle of financial reporting should be that management has considered all the potential information for disclosure and has made the judgement that certain information need not be disclosed because it is not material and its inclusion would not be helpful. We think that the interpretation of this paragraph could be that negative assurance is best practice in many or all circumstances and this could lead to uncertainty about whether important information has not been disclosed. We think it would be clearer not to include this discussion but just to rely on management's assessment of what needs to be disclosed. Paragraphs 34 and 35 are sufficient in this respect.

(d) Do you think any paragraphs/sections are unnecessary? If so, which paragraphs/sections are they and why?

We feel that the guidance should be made more concise by eliminating those sections which only duplicate the guidance that already exists in IFRS.

(e) Do you think any aspects of the guidance will conflict with any legal requirements related to materiality within your jurisdiction, or a jurisdiction in which you file financial statements?

We are not aware about any such conflict.

Question 4—Timing

The IASB plans to issue the Practice Statement before the finalisation of its Principles of Disclosure project.

The IASB has tentatively decided to include a discussion on the definition of materiality, and whether there is a need to change or clarify that definition within IFRS, in the Discussion Paper for its Principles of Disclosure project (expected to be issued early in 2016). Nevertheless, the IASB thinks that to address the need for guidance on the application of materiality, it is useful to develop the Practice Statement now.

The IASB does not envisage that the discussion about the definition of materiality or any other topics in its Principles of Disclosure project will significantly affect the content of the Practice Statement. Nevertheless, the IASB will consider whether any consequential amendments to the Practice Statement are necessary following the completion of the Principles of Disclosure project. Do you agree with this approach?

Please refer to the discussion about the format of the guidance in our response to question 1. We agree that it is useful to develop the Practice Statement now, but that for the reasons discussed above, it should be published as "work in progress" pending finalisation of the Principles of Disclosure project and in the light of the experience of using the Statement in practice.

Question 5—Any other comments
Do you have any other comments on the [draft] Practice Statement? As mentioned in Question 4, a discussion about the definition of materiality will be included in the Discussion Paper in the Principles of Disclosure project, so the IASB is not asking for comments on the definition at this time.

Scope

We think that the remit of the IASB is to produce guidance for the preparation of the financial statements. The scope of the Practice Statement should reflect this and there should be no suggestion that it applies to other areas, such as the management report. Example of areas where the guidance seems to be going beyond the financial statements are paragraphs 22, 28 (a) and (b) and 57.

However, some of the areas dealt with in these paragraphs are relevant to explain past performance depicted in the financials or financial performance in the foreseeable future and/or are specifically required under certain standards (such as IFRS 3). It would therefore be useful to explain how entities should make the assessment of materiality in the context of the financial statements and with regard to management's accountability for decisions and actions taken and the financial consequences of these (stewardship).

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