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The Disclosure Initiative - IASB amends the accounting policy requirements

What you need to know

- On 12 February 2021, the IASB issued amendments to IAS 1 and the PS to provide guidance on the application of materiality judgements to accounting policy disclosures.
- The amendments to IAS 1 replace the requirement to disclose 'significant' accounting policies with a requirement to disclose 'material' accounting policies.
- Guidance and illustrative examples are added in the PS to assist in the application of the materiality concept when making judgements about accounting policy disclosures.
- The amendments to IAS 1 will be effective for annual periods starting on or after 1 January 2023.

Highlights

In February 2021, the International Accounting Standards Board (IASB or the Board) issued amendments to IAS 1 *Presentation of Financial Statements* in which it provides guidance and examples to help entities apply materiality judgements to accounting policy disclosures. The Board also issued amendments to IFRS Practice Statement 2 *Making Materiality Judgements* (the PS) to support the amendments in IAS 1 by explaining and demonstrating the application of the 'four-step materiality process' to accounting policy disclosures.

In particular, the amendments aim to help entities provide accounting policy disclosures that are more useful by:

- Replacing the requirement for entities to disclose their 'significant' accounting policies with a requirement to disclose their 'material' accounting policies; and
- Adding guidance on how entities apply the concept of materiality in making decisions about accounting policy disclosures.

Background

In an attempt to enhance communication in financial reporting, the IASB has made 'Better Communication in Financial Reporting' a central theme of its standard-setting activities in recent years. The Disclosure Initiative is part of the IASB's Better Communication theme and aims to address how the effectiveness of disclosures in IFRS financial statements can be improved. The 2021 amendments to IAS 1 and the PS are part of the Disclosure Initiative.

The PS represents non-mandatory guidance that was first issued by the IASB in September 2017 to help entities to make materiality judgements. The PS describes a four-step process for applying materiality and includes guidance on how to make materiality judgements in specific circumstances.

In assessing the materiality of accounting policy information, both quantitative and qualitative aspects need to be considered.

The amendments

Replacement of the term 'significant' with 'material'

In the absence of a definition of the term 'significant' in IFRS, the Board decided to replace it with 'material' in the context of disclosing accounting policy information. 'Material' is a defined term in IFRS and is widely understood by the users of financial statements, according to the Board. Material accounting policy information is defined as follows in paragraph 117 of IAS 1 "Accounting policy information is material if, when considered together with other information included in an entity's financial statements, it can reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements."

Application of the materiality definition

The Board has added guidance to help entities determine when accounting policy information is material and, therefore, needs to be disclosed. In assessing the materiality of accounting policy information, entities need to consider both the size of the transactions, other events or conditions and the nature of them.

The Board also amended the PS to clarify that the materiality assessment for accounting policy information should follow the same guidance that applies to materiality assessments applicable to other information, that is to consider both qualitative and quantitative factors. A diagram illustrating how entities should incorporate the different factors in an assessment of the materiality of accounting policy information has been added.

The Board explained that, although a transaction, other event or condition to which the accounting policy information relates may be material, it does not necessarily mean that the corresponding accounting policy information is material to the entity's financial statements. On the other hand, the amended IAS 1 highlights that other disclosures required by IFRS may be material despite the corresponding accounting policy information being immaterial. For example, if an entity determines that accounting policy information for income taxes is immaterial to its financial statements, other disclosures required by IAS 12 *Income Taxes* may be material.

The Board added examples of circumstances in which an entity is likely to consider accounting policy information to be material when:

- A change of accounting policy results in a material change to the information in the financial statements
- A choice of accounting policy is permitted by IFRS
- An entity develops an accounting policy in accordance with IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors in the absence of an IFRS that specifically applies
- Application of accounting policy requires significant judgements or assumptions
- It is difficult to understand material transactions, other events or conditions because they require complex accounting, e.g., when more than one IFRS is applied

The Board clarified that the list of examples is not exhaustive, but it believes that they will help an entity to determine whether accounting policy information is material or not.

The amended IAS 1 explicitly acknowledges that disclosure of immaterial accounting policy information may be acceptable, although it is not required. However, if an entity decides to disclose accounting policy information that is not material, it needs to ensure that immaterial information does not obscure material information, for example, by giving the immaterial accounting policy information more prominence.

Disclosure of standardised information

Entity-specific accounting policy information is more useful for users of financial statements than standardised information.

Entities often need to disclose information to describe how they have applied the requirements of a specific standard and provide "standardised information, or information that only duplicates or summarises the requirements of the IFRSs" (paragraph 117C of IAS 1). The Board acknowledged that, generally, such information is less useful to users than entity-specific accounting policy information. However, the Board also agreed that, in some circumstances, standardised accounting policy information may be needed for users to understand other material information in the financial statements. In those situations, standardised accounting policy information is material, and should be disclosed.

The amended standard highlights that it is generally more useful to provide information that reflects an entity's own specific circumstances, rather than just repeating what the applicable IFRS generally requires. Similarly, the PS was amended to emphasise that entities should focus on providing accounting policy information that is entity specific. Tailoring accounting policy information is particularly relevant when judgement is applied.

The amendments to the PS also provide examples of situations when generic or standardised information summarising or duplicating the requirements of IFRS may be considered material accounting policy information:

- The information is necessary for the users to understand other material information provided in the financial statements.
- The entity reports in a jurisdiction where entities also report under local accounting standards.
- Complex accounting is required by IFRS and the standardised information is needed to understand the accounting (e.g., where more than one IFRS is applied).

In addition, the amended PS provides two examples to illustrate the difference between making materiality judgements by focusing on entity-specific information, while avoiding standardised (boilerplate) accounting policy information (Example S) and providing accounting policy information that only duplicates requirements in IFRS (Example T).

Removal of reference to 'measurement basis'

In the amended standard, references to 'measurement basis' are removed; they were deemed redundant following the introduction of the guidance on the materiality of accounting policy information. Information about the measurement basis may be material, but this requires judgement similar to that which applies to other accounting policy information.

Transition and effective date

The amendments to IAS 1 are applicable for annual periods beginning on or after 1 January 2023. Earlier application is permitted as long as this fact is disclosed.

Since the amendments to the PS provide non-mandatory guidance on the application of the definition of material to accounting policy information, the Board concluded that transition requirements and an effective date for these amendments were not necessary.

How we see it

The replacement of 'significant' with 'material' accounting policy information in IAS 1 and the corresponding new guidance in IAS 1 and the PS may impact the accounting policy disclosures of entities. Determining whether accounting policies are material or not requires greater use of judgement. Therefore, entities are encouraged to revisit their accounting policy information disclosures to ensure consistency with the amended standard.

The use of boilerplate disclosures for accounting policy information has been observed in practice. Entities should carefully consider whether "standardised information, or information that only duplicates or summarises the requirements of the IFRSs" is material information and, if not, whether it should be removed from the accounting policies disclosures to enhance the usefulness of the financial statements.