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Dear Sir

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

We are pleased to comment on the above Exposure Draft (the ED). Following consultation with the BDO network[1], this letter summarises views of member firms that provided comments on the ED.

Although we agree that it is desirable to encourage entities to eliminate unnecessary disclosures of accounting policies, we consider that the proposals as drafted could result in useful information being excluded from financial statements. In particular, it would appear that for some entities the proposals could result in no requirement for the disclosure of any accounting policies. We believe that the boundary needs to be shifted and, consistent with a principles-based reporting framework, entities should be required to apply judgement when determining whether an accounting policy should be disclosed for transactions, other events or conditions that are either quantitatively or qualitatively material.

Our responses to the questions in the ED are set out in the attached Appendix A.

We hope that you will find our comments and observations helpful. If you would like to discuss any of them, please contact me at +44 (0)20 7893 3300 or by email at abuchanan@bdoifra.com.

Yours faithfully

Andrew Buchanan

Andrew Buchanan

Global Head of IFRS

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Appendix A

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 agree with the objective of the IASB in reducing 'boilerplate' disclosures and overly descriptive and lengthy accounting policies when the underlying transaction, event or circumstance is of little importance to the financial statements. However, we share some of the views expressed by IASB Board member Martin Edelmann in his alternative view, which was included in the exposure draft.

Our primary concern is that we believe that requiring an accounting policy to be material (as defined by the proposed paragraph 117B) in order for it to be disclosed has the potential to result in the removal of more disclosures than would be appropriate.

Consequently, we believe that if entities were to implement the amendments as proposed in the exposure draft, the usefulness of information contained in financial statements may be reduced. This is because the proposed amendments may be interpreted in a way that significantly reduces the disclosure of an entity's accounting policies to the detriment of the primary users of financial statements.

While we agree that disclosures of accounting policies are too often 'boilerplate' or overly descriptive in instances where no options or significant judgments exist, we are concerned that entities could apply the revised requirements and disclose very few, if any, accounting policies.

To illustrate our concern, we have provided the following example.

Entity A is a manufacturer of 'widgets'. Entity A has the following characteristics applicable to its preparation of financial statements for the year ended 31 December 2020 (unless otherwise noted, assume that all balances and transactions streams are quantitatively material):

- Revenue is recognised once widgets are shipped to customers;
- Property, plant and equipment consists manufacturing equipment and computers;
- Goodwill that arose from a previous business combination;
- Lease liabilities and right-of-use assets for its building;
- Accounts receivable are short-term in nature and expected credit losses are immaterial; and
- There are no complex financial instruments, only accounts receivable, accounts payable and a term bank loan.

Despite certain aspects of Entity A's transaction streams being quantitatively material, applying the proposed paragraphs 117A and 117B, Entity A may conclude that it has no accounting policies to disclose. That is because none of the policies applied by Entity A satisfy any of the conditions noted in 117B. None of the policies changed in the period, were chosen from an alternative within IFRS, were developed by applying the hierarchy in IAS 8 in the absence of an IFRS Standard, or relate to an area of significant judgment. We also believe that applying the proposed flowchart in IFRS Practice Statement 2 could result in the same conclusion. This same conclusion could be drawn for very common accounting and widespread accounting policies, such as accounting for income taxes. Very few accounting policies for how an entity applies IAS 12 would be 'material' based on paragraph 117B. While we agree that entities should be required to consider whether, and the extent to which, the disclosure of accounting policies for transactions with little to no judgment or choices made in their application should be made, we believe that for items that are quantitatively or qualitatively material the exclusion of any disclosure of a policy would not be appropriate.

While the conceptual framework presumes that primary users of financial statements have a reasonable level of financial knowledge, the conceptual framework also acknowledges that not all primary users of financial statements are accounting experts. A significant reduction in disclosed accounting policies could therefore be detrimental in the following ways:

- A significant reduction in disclosed accounting policies would make it more challenging for users who have a working knowledge, but are less familiar with certain detailed requirements, of IFRS to understand the requirements of IFRS compared to other GAAPs.
- Applying the proposed paragraph 117B(a) may result in an entity disclosing its policies for new IFRS Standards, only for those policies to be removed in subsequent periods once 117B(a) no longer applies. This could be challenging for primary users when accounting policies have recently changed.
- The requirements of IFRS differ substantially from many other GAAPs in fundamental and pervasive aspects (e.g. 'on balance sheet' lease accounting and the three stage expected credit loss impairment model for financial assets). Many primary users of financial statements base their fundamental knowledge of accounting principles from their national GAAP, which may differ substantially from IFRS. A lack of explanation in an entity's accounting policies may make it difficult to understand how financial statements prepared in accordance with IFRS differs from other GAAPs.

We believe that amendments to IAS 1 and IFRS Practice Statement 2 should focus on encouraging entities to reduce the length of disclosure relating to accounting policies that have little optionality or judgment in their application, as noted in BC10(a) of the exposure draft. For example, the requirements of IAS 12 and IAS 21 apply very consistently for most entities; however, we observe that disclosures relating to the accounting policies for income taxes and foreign currency translation are often very lengthy. Our proposed approach to address this concern is discussed in our response to question 3.

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?

Our concern relating to the proposed new paragraph 117A relate to how it would be applied given the proposed new definition of material in proposed new paragraph 117B. See our response to question 3 below.

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 do not agree with the proposed paragraph 117B, for the reasons explained in our response to question 1. If the proposed amendments are made, we suggest additional guidance be added that establishes a requirement for entities to 'step back' and evaluate whether the disclosed accounting policies provide sufficient information for a primary user, with characteristics as defined in the conceptual framework, to understand the material balances and transactions. We understand that this is the intention of the proposed amendments; however, we believe that drafting of the exposure draft may not have the intended effect. We also note that the amendments might be interpreted as focussing only on those items that are quantitatively material, rather than extending to include those for which amounts may be small, but are qualitatively material.

In order to address our concerns, we suggest that the following changes are made to the proposed amendments:

Paragraph 117A

Delete the second sentence, so that this paragraph deals only with the factual question of accounting policies relating to immaterial items.

Paragraph 117B

Add a new second sentence and amend what will become the third sentence:

> 'An entity applies judgement in determining whether an accounting policy, that relates to quantitatively or qualitatively material transactions, other events or conditions, is itself material. An entity may consider an accounting policy to be material to its financial statements if that accounting policy relates to material transactions, other events or conditions, and is likely to consider it material when in addition (for example) an accounting policy:

Amend subparagraph (e) to read:

> 'results from the application of the requirements of an IFRS Standard......'

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 believe that the examples provide a useful illustration of more informative disclosures of accounting policies, however, our concerns relate to how the proposed amendments describe how an entity determines which accounting policies should be disclosed by applying the definition of 'material' in proposed new paragraph 117B (see our responses to questions 1 and 3).

Question 5 *- Would any wording or terminology introduced in the proposed amendments be difficult to understand or to translate?*

As noted in our responses above, we believe the drafting of the proposed amendments may result in unintended outcomes, therefore, we have suggested amendments, as noted earlier in our response. Our primary concern relates to how the proposed new paragraph 117B defines 'material' accounting policies.

Question 6 *- Do you have any other comments about the proposals in this Exposure Draft?*

We have no other comments.