



Basel Committee on Banking Supervision

BANK FOR INTERNATIONAL SETTLEMENTS

Chairman

Via e-mail: commentletters@ifrs.org

Mr Hans Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

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Discussion Paper on the Disclosure Initiative – Principles of Disclosure

Dear Mr Hoogervorst

The Basel Committee on Banking Supervision welcomes the opportunity to comment on the International Accounting Standards Board's Discussion Paper ("DP") Disclosure Initiative – Principles of Disclosure.

The Committee supports the IASB's objective to improve the effectiveness of disclosures in financial statements. This is consistent with the Committee's response to the IASB's 2015 Agenda Consultation, which supported the development of a disclosure framework that not only ensures an appropriate level of disclosure, but also supports the rationalisation of and improvements to the quality of disclosure requirements in existing standards.¹

The Committee largely supports the views expressed in Sections 1 through 6 in the DP and we encourage the IASB to move in the direction proposed, with the following detailed comments:

- Section 4, paragraph 4.11 – we agree with the advantages of reducing duplication via cross-referencing; however, we believe that allowing cross-referencing for both similar and identical information could improve users' understanding of the links between financial statement disclosures. Accordingly, we encourage the IASB to develop additional guidance on cross-referencing to enable users to link both identical and similar information disclosed in and outside the primary financial statements. In this regard, the IASB might find it helpful to consider "signposting", as described in the Committee's Pillar 3 disclosure requirements.² We note that the IASB will also need to consider guidance clarifying whether references to similar information that is not necessary to comply with IFRS

¹ Available at www.bis.org/bcbs/commentletters/iasb46.pdf.

² Please see paragraphs 20 through 22 of the Committee's Pillar 3 disclosure requirements available at www.bis.org/bcbs/publ/d309.pdf

and which is located outside the financial statements means that the information becomes part of the IFRS financial statements and subject to audit.

- Section 6, paragraphs 6.6 and 6.7 – we agree that the issues described are relevant and important and we recommend that the IASB explore the additional issue that disclosures of accounting policies tend to be fragmented. For example, high-level disclosures on significant accounting policies are often provided upfront in the notes to the financial statements, whereas critical accounting policy choices or judgments could appear throughout the notes to the financial statements. That being so, we encourage the use of cross-referencing to enable users to link significant judgments and assumptions that are not adjacent to significant accounting policies in the financial statements. We are most concerned by the placement of standard-level accounting policy disclosures that involve significant judgment, such as IFRS 7 *Financial Instruments: disclosures*.

Our further substantive comments are on Sections 7 and 8 and are set out below.

Section 7 – Centralised disclosure objectives

Responses to questions 11 and 12

The Committee sees merit in developing a central set of disclosure objectives that can be used as a basis for developing specific disclosure objectives and requirements in IFRS Standards. A central set of disclosure objectives can help improve the understanding of the purpose of disclosures, make it easier for the IASB to develop new disclosure objectives and requirements, and assist entities in making decisions on what information to disclose. This approach could contribute to more effective and consistent disclosure requirements between IFRS Standards, and could reduce excessive and redundant disclosures. This might also help auditors and financial statement regulators to enforce against those objectives.

Supporting disclosure objectives by examples

We believe it would be helpful if each disclosure objective were governed by principles and accompanied by examples of specific disclosures that could meet the objective. Otherwise, disclosure objectives alone could lead to generic disclosures which are unlikely to achieve the disclosure of an effective and comparable set of information. In this regard, you might find it helpful to refer to the Committee's guiding principles for banks' Pillar 3 disclosures³ when developing a set of centralised disclosure objectives. In addition, it might be helpful to refer to the Enhanced Disclosure Task Force's reports, which developed both principles and practical recommendations on bank disclosures. In our view, disclosure objectives that are sufficiently focused and granular, accompanied by explanations of why information is likely to be useful and industry-specific examples, will help to drive disclosures that are complete and relevant.

³ Please see paragraphs 12 and 13 of Committee's Pillar III disclosure requirements available at www.bis.org/bcbs/publ/d309.pdf

Approach to developing a central set of disclosure objectives

The IASB has identified two methods of, and a hybrid approach to, developing a central set of disclosure objectives. Method A focuses on the types of information disclosed, while Method B focuses on the information about an entity's activities. The hybrid approach (see DP paragraphs 7.34 to 7.37) combines Methods A and B and is at an early stage of development.

We support the IASB in exploring the hybrid approach, by considering when Method A or Method B disclosures alone, or a mix of the two, are appropriate. In our view, consideration of *how an item is accounted for* and *how it is used* in a business will drive relevant disclosures. The hybrid method could take the form of a combination of accounting and business model information (type 1) and management information (type 2). The first type of information should be linked to the line items included in the primary financial statements. The second type of information should be linked to information produced for an entity's board, such as information on the risks and activities of the entity, as well as its capital structure and capital management. There will also need to be appropriate linkages between the two types of information.

We encourage the IASB to also consider disclosures based on different types of information and uncertainties that are embodied in different types of assets and liabilities and explanations of the different measurement bases to assist users' understanding of an entity's current and future financial performance and position.

As an example of the application of the hybrid approach, let us consider Expected Credit Loss (ECL) disclosures of financial assets held at amortised cost under IFRS 9 *Financial Instruments* (please note that this is an example intended to illustrate our thought process, and not a comprehensive proposal on disclosures for IFRS 9 – ECL):

- The objective could be that an entity should provide disclosures that help users understand how the entity is managing its financial assets, the impact on current and future income and expense, and the risks and uncertainties around current and future income, expense and recoverability of carrying amounts.
- Further to these objectives, the entity would need to consider disclosing information about the data, methodologies and assumptions in its ECL impairment models, how these have changed since the prior period and how these relate to the impairment charge in the income statement. This could be accompanied by disclosures that allow users to assess the uncertainties around future income, expense and cash flows, including the effects of management judgments on the ECL estimate.

The hybrid approach should be underpinned by strong principles that focus on users' needs, and aid preparers to make decisions on the types of disclosures that are relevant.

Response to question 13

Location of disclosure objectives

With regard to locating all IFRS disclosure objectives and requirements within a single Standard, or set of Standards for disclosures, we believe the decision may follow from the outcome of the IASB's thinking on how disclosure objectives and

requirements are determined. Currently, the IASB has standards that contain principles for recognising, measuring and disclosing information, and standards that deal only with disclosures. Examples of the latter type are the IFRS 7 *Financial instruments: Disclosures*, which complement IAS 32 *Financial Instruments Presentation* and IFRS 9 *Financial Instruments*; and IFRS 12 *Disclosure of interests in other entities*, which covers IFRS 10 *Consolidated Financial Statements*, IFRS 11 *Joint Arrangements* and IAS 28 *Investments in Associates and Joint Ventures*.

We understand that there may be different approaches, such as having an overarching disclosure standard with guiding principles for disclosure objectives applicable to all IFRS Standards. This could be followed by a set of disclosure standards that include disclosure objectives and requirements relevant to specific standards and supplemented with guidance that includes industry-specific examples. Irrespective of the approach taken, in our view it is important that the resulting disclosures fit together, are consistent and meaningful, do not overlap and, when taken together, are not excessive. We encourage the IASB to review existing and new disclosure requirements to ensure that, taken together, these objectives are achieved.

Section 8 – New Zealand Accounting Standards Board (“NZASB”) staff’s approach to drafting disclosure requirements in IFRS Standards

Response to question 14

There are four aspects to the NZASB’s approach set out in paragraph 8.2, and we comment on each in turn.

Disclosure objectives and sub-objectives: Please see our response to questions 11 and 12, where we set out our views on supporting disclosure objectives with examples. In addition, we recommend that the IASB develop a hierarchy of objectives, starting from the objective of financial statements through to identifying more specific disclosure objectives for individual items or activities. The specific objectives could be ranked based on information considered essential for the understanding of the particular item or transaction followed by information which is considered meaningful but not central to the analysis. In addition, the use of a two-tier approach to disclosing information could make it easier for entities to apply disclosure requirements, following a principle of proportionality.

The example of the NZASB (please see paragraphs 8.9, 16.X1, 16.X5 and 16.X7) could be a good starting point; however, in our view, the example is not sufficiently focused to help preparers and others make decisions on what should be disclosed. In particular, objectives and sub-objectives that state that disclosures should help users understand “the effect of X or Y on the financial position, financial performance and cash flows of the entity” may not result in useful disclosures. In our view, an operable disclosure objective should drive a preparer to consider the sorts of disclosures that are relevant to users. The objective can do so by focusing the preparer on the informational qualities of different disclosures and how the disclosures relate to the fundamental objectives of assessing the potential future cash flows and the stewardship of resources. We note that paragraph 16.X6 of the example in Chapter 8 touches on this idea by requiring an entity to consider whether to disclose key risks and restrictions associated with property, plant and equipment so that a user can understand and evaluate how that might affect the entity’s ability to use, sell or otherwise derive economic benefits from the assets.

Two tiers of disclosure requirements: We agree with the NZASB's split of disclosure requirements into two tiers. Again, for both tiers, entities should be required to consider what information users will need to make decisions and what information they need to disclose in order to enable those decisions. We also agree with the objectives set out in paragraph 8.13 (eg ensuring a degree of consistency while providing flexibility on what information is needed to meet the overall disclosure objective). We encourage the IASB to consider whether the disclosure on key judgments currently required by IAS 1 can be enhanced to ensure that users can understand the judgments that management has made in determining what is and is not disclosed. This will be particularly important when principles are used and/or disclosures are optional rather than mandatory.

Greater emphasis on the need to exercise judgment: We agree that it will be helpful to emphasise that management needs to exercise judgment, whether in a single disclosure standard or in individual standards. However, an entity's ability to exercise judgment about information to be disclosed should be carefully assessed against the impact on the comparability and consistency of disclosures between entities' financial statements. Please also refer to our responses to questions 11 and 12 on the benefits of including examples and more granular disclosure objectives.

Less prescriptive wording in disclosure requirements: We agree that less prescriptive wording should help preparers to make objective-based judgments about what should be disclosed rather than encouraging an approach that leads to preparers taking a checklist approach (see also our response to question 15).

Response to question 15

We agree that the way disclosure requirements are drafted contributes to the disclosure problem, for the reasons identified in the question. We are concerned about disclosure objectives that do not sufficiently drive thoughtful and complete disclosures. This applies to standards that do not currently have a disclosure objective and those that do, but where that objective is at a very high level. An example of the latter includes IFRS 7, paragraph 7, which states that "[a]n entity shall disclose information that enables users of its financial statements to evaluate the significance of financial instruments for its financial position and performance", as well as the disclosure objectives included as examples in the NZASB approach.

We also agree with the view that a long list of "shall disclose" items in accounting standards could encourage a checklist approach without considering what is relevant to users. On the other hand, we note that it may be simpler to use specific disclosure requirements and that specific disclosure requirements can drive an appropriate level of comparability between entities' financial statements. Accordingly, we support the use of a judgment-driven approach, whereby disclosure objectives are supported by industry-specific examples (see our responses to questions 11 and 12). We recommend that a balance be struck between objectives that drive appropriate disclosures and the tiers of summary and additional information that are set out in the NZASB approach.

We hope that you find these comments constructive and helpful. The letter has been prepared by the Committee's Accounting Experts Group, chaired by Mr Fernando Vargas Bahamonde, Associate Director General, Bank of Spain. If you have any questions regarding these comments, please contact Mr Vargas (+34 91 338 8746) or Ms Ruby Garg of the Basel Committee Secretariat (+41 61 280 8463).

Yours sincerely

A handwritten signature in blue ink, appearing to read 'Stefan Ingves', with a stylized, cursive script.

Stefan Ingves