



EFRAG Draft Comment Letter on ED/2017/6 Definition of Material - Proposed amendments to IAS 1 and IAS 8

ICAEW welcomes the opportunity to comment on EFRAG's Draft Comment Letter on *ED/2017/6 Definition of Material - Proposed amendments to IAS 1 and IAS 8* published by IASB on 14 September 2017, a copy of which is available from this [link](#).

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MAJOR POINTS

1. We are currently in the process of finalising our response to the IASB's Exposure Draft ED/2017/6 *Definition of Material – Proposed Amendments to IAS 1 and IAS 8*. Although we are not yet able to confirm our detailed comments on the IASB's proposals, we do not expect to make substantive changes at this stage. On this basis we are pleased to provide comments on EFRAG's Draft Comment Letter.
2. In our draft response to the IASB, we agree with the overall objective of aligning the definition of material in the *Conceptual Framework* with that in the Standards, and ensuring it is consistent wherever it appears. We also support a number of the key proposed amendments to IAS 1 *Presentation of Financial Statements* and IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*, including replacing the threshold 'could influence' with 'could reasonably be expected to influence'.
3. In our draft response to the IASB, we express the view that changing the subject of the assessment of materiality from the 'error' (the omission, misstatement or degree to which information is obscured) to the information itself is highly problematic in relation to misstatements. We therefore agree with EFRAG that the references to omitting, misstating and obscuring should be removed from the core definition, but we consider they should be retained in the accompanying explanation. In addition, while we agree with the inclusion of the concept of obscuring in the accompanying explanation, we agree with EFRAG that it needs much clearer explanation before it is to be helpful.
4. Overall, we think the proposals need significant improvement before they can be regarded as helpful to preparers.

RESPONSES TO EFRAG'S SPECIFIC QUESTIONS

Do you agree with EFRAG's suggestion that the terms 'obscuring', 'misstating' and 'omitting' from the definition should not be included in the definition of 'material' as these concepts relate to principles of fair communication? Can you identify specific areas where the proposed exclusion might create legal issues in the specific context of your jurisdiction?

5. In our draft response to the IASB, we express the view that the references to omitting, misstating and obscuring should be removed from the core definition of material. However, we consider that they should be retained in the accompanying explanation.

Obscuring

6. We understand that the concept of obscuring has been given greater prominence in order to assist with decisions in respect of aggregation and disaggregation, and to encourage more targeted disclosures. While we support this objective, we consider that the added emphasis may cause concerns for preparers trying to find the appropriate balance between the risks of omitting and obscuring information if the accompanying explanation and any related guidance are insufficiently clear.
7. We do not consider that the proposed explanatory sentence adds significantly to an understanding of the concept. The explanation seems somewhat circular ("... information might be obscured ... if it is obscured..") and we agree with EFRAG that more extensive explanations should be provided.

Misstatements

8. The proposed revised definition changes the subject of the assessment of materiality from the error (the omission, misstatement or degree to which information is obscured) to the information itself. In our draft response to the IASB we agree with this change in focus for omissions and obscuring information as we consider that it supports the wider *Disclosure Initiative*. However, we do not think it works in the context of misstating. Any information could be material if the misstatement were sufficiently large. Equally, information might be inherently material but if it is misstated to only a very small extent, then the misstatement could not reasonably be expected to influence the decisions of primary users. In other words, material information could be misstated without that being material. The critical issue in this context is whether the misstatement is material, not whether the information itself is material. We note that the same issue applies to the wording in the revised *Conceptual Framework* as currently drafted.
9. The first paragraph in the proposed accompanying explanation to the IAS 1 and IAS 8 definitions contains the following sentence: "A misstatement of information is material if it could reasonably be expected to influence decisions made by the primary users." This sentence appears to address the issue highlighted in the previous paragraph, but in our view it would be preferable to ensure the core definition worked in all circumstances.

Legal issues arising from EFRAG's proposal in the context of the UK?

10. We are not aware of any legal issues that might arise in the context of the UK jurisdiction from the exclusion of the terms 'obscuring', 'misstating' and 'omitting' from the definition.

OTHER POINTS

Aligning the definition

11. In our draft response to the IASB we agree with the Board's proposal to align the definition of material in the *Conceptual Framework* with that in IFRS. It is important that there is consistency across all authoritative statements to minimise the risk of confusion and inconsistency in application.
12. However, we agree with EFRAG that consideration should be given to including the definition and accompanying explanation in only one Standard. Other Standards could simply use the word 'material', with no requirement for definition or further explanation.
13. In addition, we consider that the part of the accompanying explanation dealing with the characteristics of users and identifying the primary users should be included only in the *Conceptual Framework*.

Primary users

14. We agree with the IASB's proposal to specify that the users to whom the definition refers are the primary users as defined in the *Conceptual Framework*.

The threshold for determination of material

15. We agree with replacing 'could influence' with 'could reasonably be expected to influence' for the reasons set out in the ED's Basis of Conclusions.

Clarifying the accompanying explanation

16. Our draft response to the IASB states that we do not consider that the accompanying explanation should include all the additional text included in the Exposure Draft. Specifically,

the explanations concerning users and their characteristics appear out of place in a definition in a Standard and we do not consider it necessary to repeat guidance that is contained in the *Conceptual Framework*. If the term ‘primary users’ is defined and explained in the *Conceptual Framework*, then there is no need to repeat it in Standards.

17. In particular, the last sentence in the proposed accompanying explanation (“At times, even well-informed and diligent users ...”) seems wholly out of place in a Standard. It is not clear why this sentence is required or how it is relevant to the definition of material.

Wording and terminology

18. In our draft response to the IASB we set out some concerns in respect of the wording used in the ED. We have highlighted some of these concerns in the following bullet points:

- The term ‘obscuring’ may not translate easily into other languages and, as noted above, consider that further explanation would be useful of how material information might be obscured. However, we consider that such clarification would be better placed in the *Conceptual Framework* than in a Standard, and that it would be useful to include examples in the Materiality Practice Statement.
- We consider that the phrase “judged in the entity’s circumstances” may be difficult to understand in the context of the consideration of the ‘characteristics’ of primary users. In our view it is not clear what this means in practice. We consider that it would be more helpful and understandable to refer to primary users’ information requirements rather than to their ‘characteristics’. Again, any further explanation of this element of the definition would be better placed in the *Conceptual Framework*, with examples in the Materiality Practice Statement.
- The first sentence of the proposed accompanying explanation reads: “Materiality depends on the nature or magnitude of information, or both.” We do not consider that the phrase ‘magnitude of information’ is wholly clear. First, it is not clear whether the word ‘magnitude’ means size or importance, or possibly both. Second, if intended as a direct replacement of the original word ‘size’, it is not clear that ‘information’ itself can have a size or numerical quantity or value. In this respect we consider that the wording in the current draft *Conceptual Framework* works better: “materiality is an entity-specific aspect of relevance based on the nature or magnitude, or both, of the items to which the information relates.”

Effective date

19. The proposed text in respect of the effective date requires an entity to disclose, where applicable, that it has early applied the amended definition of material. In our draft response to the IASB we note that this seems an unusual requirement given the Board believes the proposed amendments are not substantive changes and are unlikely to affect how materiality judgements are made; that is, knowledge of early adoption would not be material information. In fact, a statement in financial statements that the revised definition had been early adopted might lead users to think that this had had an impact on judgements made. If an entity decided to change disclosures in the financial statements then presumably the reasons for the change would be disclosed as appropriate in the normal course of events.