STAFF PAPER

June 2018

IASB Meeting

Project	**Disclosure Initiative: Definition of Material**
Paper topic	Project redeliberations

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Objective

1. The objective of this paper is to present staff analysis and recommendations to the Board about next steps on the Definition of Material. In light of strong support for the project from respondents, we think that the Board can move forward with finalising amendments to the definition of material. Consequently, this paper contains staff analysis and recommendations on all aspects of the project.

2. Throughout this paper, references to the *Conceptual Framework* refer to the revised *Conceptual Framework* published on 29 March 2018.

Overview

3. This paper is structured as follows:
   (a) Background (paragraphs 4-8);
   (b) Summary of staff recommendations (paragraphs 9-13);
   (c) Including 'obscuring information' in the definition of material (paragraphs 14-40);
   (d) Location of the definition of material and explanatory paragraphs (paragraphs 41-44);

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(e) Existing terminology in the *Conceptual Framework* (paragraphs 45-49);

(f) Replacing the threshold 'could influence' with 'could reasonably be expected to influence' (paragraphs 50-53);

(g) Effective date (paragraphs 54-58);

(h) Other considerations (paragraphs 59-70);

(i) Appendix A—Aligning terminology with the *Conceptual Framework*;

(j) Appendix B—Extracts from IFRS Standards, Interpretations and the Materiality Practice Statement which use the terms 'immaterial' and 'not material'; and

(k) Appendix C—Extract from ISA 320 *Materiality in Planning and Performing an Audit*.

Background

4. The Board published the *Definition of Material—Proposed amendments to IAS 1 and IAS 8* Exposure Draft in September 2017.

5. The proposed amendments to IAS 1 *Presentation of Financial Statements* and IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* refine the definition of material and clarify its application to:

   (a) align the wording of the definition in IFRS Standards and the definition in the *Conceptual Framework*—the wording is currently similar but not identical—and make some minor improvements to that wording;

   (b) incorporate some of the existing supporting requirements in IAS 1 into the definition to give them additional prominence; and

   (c) improve the clarity of the explanation accompanying the definition of material.

6. Consequently, the proposals aim to clarify the definition of material by:

   (a) aligning the wording of the definition of material in IAS 1 and IAS 8 with the *Conceptual Framework*. This includes clarification that the users to whom the definition refers to are 'primary users' of an entity's financial statements. This clarification responds to concerns that the term 'users' may be interpreted too widely;

(b) replacing the threshold 'could influence' with 'could reasonably be expected to influence'. This clarification responds to concerns that the threshold 'could influence' is too low and might be applied too broadly;

(c) including 'obscuring information' in the definition of material. This clarification responds to concerns that the existing definition of material is sometimes perceived by stakeholders to focus only on information that cannot be omitted (material information), and does not indicate that including immaterial information may be unhelpful; and

(d) relocating the description of material misstatements, and other wording that explains rather than defines material, from the definition into the explanatory paragraphs accompanying the definition.

7. The comment period for the Exposure Draft closed on 15 January 2018. The staff presented a summary of all comment letter feedback to the Board at its April 2018 meeting (see ***April 2018 Agenda Paper 11A***).

8. Almost all respondents supported the proposed amendments to IAS 1 and IAS 8. However, respondents also expressed concerns about some of the specific components of the proposals and suggested amendments for the Board to consider. These primarily related to the following:

(a) including the concept of 'obscuring information' in the definition of material (paragraphs 14-40);

(b) the location of the definition of material and explanatory paragraphs (paragraphs 41-44);

(c) the existing terminology in the *Conceptual Framework* (paragraphs 45-49); and

(d) replacing the threshold 'could influence' with 'could reasonably be expected to influence' (paragraphs 50-53).

Summary of staff recommendations

9. With respect to the concept of 'obscuring information', we recommend that the Board:

    (a) retains the proposal to include the concept of 'obscuring information' in the bold definition of material (paragraphs 27-31); and

    (b) replaces the proposed wording explaining 'obscuring information' in the explanatory paragraphs with a clearer description and examples (paragraphs 32-37).

10. We also recommend that the Board replaces the definition of material and explanatory paragraphs in IAS 8 with a reference to the definition of material and explanatory paragraphs in IAS 1 (paragraphs 41-44).

11. In all other respects, we recommend that the Board retains the amendments proposed in the Exposure Draft. In particular, we recommend that the Board:

    (a) retains the proposed amendments that align terminology in the definition of material with existing terminology in the *Conceptual Framework* (paragraphs 45-49);

    (b) retains the proposed amendment to replace the threshold 'could influence' with 'could reasonably be expected to influence' in the definition of material (paragraphs 50-53);

    (c) should not take any further action in response to feedback about the use of the terms 'immaterial' and 'not material' (paragraphs 59-61);

    (d) should not incorporate any of the Materiality Practice Statement in IAS 1 or the Conceptual Framework, including via reference, at this time (paragraphs 62-64);

    (e) should not take any further action in response to feedback about the varying use of the term 'material' (paragraphs 65-67); and

    (f) should not take any further action in response to feedback about the interaction between the definition of material and the description of

Materiality in the Context of an Audit in ISA 320 *Materiality in Planning and Performing an Audit*.

12. With respect to the effective date of the amendments, we recommend that the Board:

    (a) sets an effective date of application of the amendments as accounting periods beginning on or after 1 January 2020 (paragraphs 54-58); and

    (b) permits early application of the amendments (paragraphs 55-56).

13. If the Board agrees with all of the staff recommendations in this paper, we anticipate the bold definition of material in IAS 1 being that proposed in the Exposure Draft:

    'Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of a specific reporting entity's general purpose financial statements make on the basis of those financial statements.'

Including 'obscuring information' in the definition of material

Feedback

14. Many respondents thought the proposed definition of material and explanatory paragraphs did not sufficiently explain the concept of 'obscuring information' in the context of determining whether or not information is material. Consequently, these respondents asked the Board for a clearer definition of the concept and to supplement this with illustrative examples and application guidance.

15. These respondents added that there are many examples of different ways in which information might be obscured. They added that the proposals in the Exposure Draft and the existing use of the concept of 'obscuring information' in IFRS Standards do not sufficiently explain what does and does not constitute 'obscuring information' in all circumstances. For example, at what point do excessive aggregation or disaggregation, and vague or unclear descriptions apply to the concept of 'obscuring information' in the definition of material? Similarly, should the question of whether or not information is material if it is obscured be considered in the context of the financial statements as a whole, or with regard to individual notes or disclosures?

16. In addition, a few respondents said that ‘obscuring information’, ‘omitting’ and ‘misstating’ are all concepts which relate to whether information provides a faithful representation or the communication of information, and not to whether that information is material in the first place. These respondents thought that ‘obscuring information’, ‘omitting’ and ‘misstating’ should be removed from the definition of material.

Staff analysis

Overview

17. In the Basis for Conclusions on the Exposure Draft, the Board explained that obscuring information can have a similar effect to omitting it. By including the concept of ‘obscuring information’ the Board hoped to address concerns that the existing definition could be perceived by stakeholders to focus only on information that cannot be omitted (material information), and not also on why it is unhelpful to include immaterial information.

18. Furthermore, in its April 2018 meeting, the Board reiterated that the purpose of including ‘obscuring’ alongside ‘omitting’ and ‘misstating’ is to give these concepts equal prominence. This is because some stakeholders think it is more important to avoid ‘omitting’ and ‘misstating’ material information than it is to avoid ‘obscuring’ material information. Some Board Members described achieving equal prominence of these three concepts as the ‘added value’ of the project.

19. In order to achieve the objective of giving equal prominence to ‘omitting’, ‘misstating’ and ‘obscuring’ in the definition of material staff have analysed the following two options:

    (a) removing ‘omitting’, ‘misstating’ and ‘obscuring’ from the definition of material and retaining these concepts within the explanatory paragraphs (paragraphs 21-26); and

    (b) retaining ‘omitting’, ‘misstating’ and ‘obscuring’ in the definition of material and explanatory paragraphs (paragraphs 27-31).

20. We have also considered alternative options in which the Board could exclude the concept of ‘obscuring’ information from the bold definition of material but include it in the explanatory paragraphs. However, we think that this approach would fail to achieve the objective of giving the concepts of ‘omitting’, ‘misstating’ and ‘obscuring’ information equal prominence.

Removing ‘omitting’, ‘misstating’ and ‘obscuring information’ (ie removing the concepts of ‘omitting’ and ‘misstating’ from the existing definition of material)

21. Staff agree with the few respondents who said that ‘omitting’, ‘misstating’ and ‘obscuring’ are all concepts that relate to the presentation of information and not whether that information is material in the first place. Consequently, we think that the suggestion to remove all of these concepts from the definition of material has merit.

22. However, we believe that removing the concepts of ‘omitting’ and ‘misstating’ may constitute a substantive change to the existing definition of material. This is because it may be perceived by some to result in an increase of what information is deemed to be ‘material’ by removing the context in which a preparer can determine what may and may not be material (ie removing the context in which to identify whether or not information may affect user decisions may result in preparers disclosing more information).

23. Further, if the Board were to remove the concepts of ‘omitting’ and ‘misstating’ from the definition, we think that other bodies may want to consider, and provide feedback on, this in the context of their own definitions of material. This would include bodies, such as the International Auditing and Assurance Standards Board (‘IAASB’).

24. The objective of the proposed amendments was to make minor amendments to clarify the definition of material (see paragraph 5). The Board did not intend to make a substantive change to the definition. Consequently, we think that if the Board does consider making a substantive change to the definition of material, it may need to revise the objective of the project and consider whether, in accordance with the Due Process Handbook, to re-expose revised amendments to IAS 1 and IAS 8 for comment (see paragraphs 22 and 23).

25. In addition to the reasons discussed in paragraphs 21 to 24, the Board has also received feedback that many stakeholders support the existing definition of material

which includes the terms ‘omitting’ and ‘misstating’ (see paragraph BC3 of the Exposure Draft). Those stakeholders think that substantive changes to the definition are unnecessary. This is also consistent with the feedback from almost all respondents to the Exposure Draft that they supported the objective and general direction of the proposed amendments. As a result, staff think that there may be unintended consequences of removing the concepts of ‘omitting’ and ‘misstating’ from the definition of material.

26. Consequently, we do not recommend removing the concepts of ‘omitting’ and ‘misstating’ information from the definition of material.

Retaining ‘omitting’, ‘misstating’ and ‘obscuring information’ (ie retaining the proposed amendment to include the concept of ‘obscuring information’)

27. In light of discussions at the April 2018 Board meeting (see paragraph 18), we have analysed examples of fact patterns in which increasing the prominence of the concept of ‘obscuring information’ would be beneficial. Staff note that there are many examples in which a piece of information is included in the financial statements (not omitted) and measured at the correct amount (not misstated), but may not have necessarily been communicated in a manner that allowed users to determine the full effect of that information. We also considered examples of ‘obscuring information’ for which some respondents requested further clarification (ie excessive aggregation, disaggregation, insufficient explanation or other means). In these examples, user decisions may also be affected and we therefore think that the Board’s reasons for proposing this amendment remain valid. Raising the prominence of ‘obscuring information’ will help regulators, auditors and others to prioritise the concept of ‘obscuring information’ more than they are able to do today.

28. Nevertheless, we agree with those respondents who said the concept of ‘obscuring information’ is complex and highly subjective and, as a result, requires the exercise of significant judgement. We think that making judgements about what constitutes ‘obscuring information’ is more difficult than making judgements about what constitutes ‘omitting’ or ‘misstating’ information. Consequently, staff also tried to identify examples of fact patterns in which applying the definition of material is more difficult because of the inclusion of the concept of ‘obscuring information’. We were

unable to identify any such example fact patterns. This is because we could not identify any examples in which 'omitting' and 'misstating' information would not influence the decisions of users of financial statements but 'obscuring' that same information would.

29. The definition of material as proposed in the Exposure Draft effectively asks entities to consider whether user decisions could be influenced by the absence of a piece of information, *irrespective of the cause of that absence*. We could not identify any circumstance in which deciding exactly what constitutes 'obscuring' is the decision-marker for whether or not information is material.

30. As a result, we think that, despite the concerns regarding the application of the concept of 'obscuring information', there is no indication that the proposed amendment will alter the underlying concept of materiality in IFRS Standards. Instead, making this amendment will elevate the concept of 'obscuring' to be of equal prominence to the concepts of 'misstating' and 'omitting' when entities are considering *how to communicate* material information. This is in line with the objective of the amendments which stated that the amendments 'are not intended to alter the underlying concept of materiality in IFRS Standards'. In practical terms, entities will need to:

    (a) consider whether information is material on the basis of whether that information being obscured (or omitted, or misstated) by *any* means could affect user decisions; then

    (b) consider how it communicates information in the financial statements to ensure that material information is not obscured. This is already required by paragraph 30A of IAS 1 today.

31. Consequently, we recommend retaining the proposed amendment to include the concept of 'obscuring information' in the bold definition of material.

Application guidance and illustrative examples for the concept of 'obscuring information' as it applies within the concept of materiality

32. In light of requests by respondents (see paragraph 14), staff have considered whether the Board could provide any application guidance or illustrative examples to help entities to apply the concept of 'obscuring information'.

33. We think it would be difficult for the Board to develop illustrative examples or application guidance that would be effective in addressing all of the concerns raised by respondents about applying the concept of 'obscuring information' (see paragraph 15). For example, we think the Board would not be able to define the point at which over-aggregation becomes 'obscuring', or the point at which an unclear explanation becomes 'obscuring'.

34. However, as described in paragraph 29 and 30 above, we think that applying the proposed definition of material does not in itself require an entity to determine the exact point at which information becomes obscured. Nevertheless, by raising the prominence of this concept, we think that communicating material information in a way that does not obscure it could receive more focus from auditors, regulators and others. There is a risk that this increased prominence will be challenging for entities and others to comply with. This is because of the significant level of judgement involved in deciding what constitutes 'obscuring information'. Consequently, to the extent possible, we think the Board should provide a more detailed explanation of this concept than was proposed in the explanatory paragraphs of the Exposure Draft.

35. The proposed amendment explained that *'[m]aterial information might be obscured if it is not communicated clearly—for example, if it is obscured by immaterial information.'* We agree with respondents who described this explanation as circular and unhelpful.

36. Consequently, staff recommend replacing the proposed amendment (see paragraph 35), with a more clear and concise explanation which would help stakeholders understand how 'obscuring information' may affect the decisions that primary users make on the basis of those financial statements.

37. For example, the paragraphs supporting the bold definition of material would explain that information is obscured if it is communicated in a way that has a similar effect for primary users of financial statements to omitting or misstating that information. The paragraphs would also explain that the following circumstances have the potential to result in material information being obscured:

(a) information regarding a material item, transaction or event being disclosed in the financial statements but the language used to explain it is vague and unclear;

(b) information regarding a material event being presented piecemeal across various notes in the financial statements so that a primary user is unable to determine the effect of the event on the financial statements as a whole;

(c) inappropriate aggregation of dissimilar items or transactions;

(d) inappropriate disaggregation of similar items or transactions; and/or

(e) material information being hidden, or clouded, by immaterial information to the extent that a primary user is unable to determine what that material information is.

Summary of staff recommendations about 'obscuring information'

38. The staff recommend that the Board retains the concept of 'obscuring information' in the definition of material, as was proposed in the Exposure Draft. This is because we believe that including this concept will address concerns that 'obscuring' material information has a similar effect to 'omitting' or 'misstating' material information and as a result should be of equal prominence. Furthermore, having considered the feedback from respondents, we have not been able to identify any scenarios in which including the concept of 'obscuring information' alters the underlying concept of materiality in IFRS Standards.

39. Staff also recommend that the concepts 'omitting' and 'misstating' are not removed from the definition of material. This is because we believe that removing these terms would constitute a substantive change in the definition of material which is outside the scope of this project (see paragraph 5). Further, we believe that removing these concepts may result in unintended consequences.

40. Finally, staff recommend replacing the proposed wording in the explanatory paragraphs in relation to 'obscuring information' with an explanation that information is obscured if it is communicated in a way that has a similar effect for primary users of financial statements to omitting or misstating that information. In addition, staff

recommend that this explanation be accompanied by a list of examples which detail circumstances where material information may be obscured.

Question for the Board

Question 1
Does the Board agree with the staff recommendations that the Board should: a) retain the proposal to include the concept of 'obscuring information' in the bold definition of material (paragraphs 27-31); and b) replace the proposed wording explaining 'obscuring information' in the explanatory paragraphs with a clearer description and examples (paragraphs 32-37)?

Location of the definition of material and explanatory paragraphs

41. Many respondents thought that the definition of material should not be repeated in multiple locations within the Standards. Instead, they thought the definition should be in IAS 1 only, and other Standards, including IAS 8, should make reference to the definition in IAS 1 as required. Further, a few respondents expressed confusion over why the wording in IAS 8 differed to the wording in IAS 1.

42. We think that locating the definition of material within a single Standard will have the following advantages:

    (a) reduce repetition throughout the Standards which was identified as a concern in the Principles of Disclosure project;

    (b) eliminate any confusion about different wording in IAS 8 and IAS 1; and

    (c) eliminate the risk of any inconsistencies arising across different Standards from changes to the definition of material in future.

43. The primary disadvantage to replacing the definition of material and explanatory paragraphs in IAS 8 with a reference to IAS 1 is that materiality is a fundamental concept for consideration in applying the requirements of IAS 8. Consequently, some think having the definition of material in IAS 8 itself helps entities to apply the

requirements of that Standard. However, because materiality is a fundamental concept across *all* IFRS Standards, the staff think it can be more confusing than helpful to repeat the definition in some, but not all, Standards. For example, if the definition is repeated in IAS 8, what does that mean about the application of materiality to Standards in which the definition is not repeated?

44. Consequently, the staff recommend that the Board replace the definition of material and explanatory paragraphs in IAS 8 with a reference to the definition of material and explanatory paragraphs in IAS 1.

Question for the Board

Question 2
Does the Board agree with the staff recommendation that the Board should replace the definition of material and explanatory paragraphs in IAS 8 with a reference to the definition of material and explanatory paragraphs in IAS 1?

Existing terminology in the *Conceptual Framework*

45. Almost all respondents supported aligning the terminology in the definition of material with terminology in the *Conceptual Framework*. However, they also expressed several concerns over existing terminology in the *Conceptual Framework* that was used in the Exposure Draft:

    (a) the definition of material in the *Conceptual Framework* uses the term ‘general purpose financial report’, whilst the Exposure Draft uses the term ‘general purpose financial statements’. Some respondents thought these should be aligned, and preferred the term ‘general purpose financial statements’ as was used in the Exposure Draft;

    (b) the scope of the term ‘primary users’;

    (c) the use of the terms ‘economic decisions’ and ‘decisions’;

    (d) the use of the term ‘specific reporting entity’ as opposed to ‘reporting entity’; and

(e) the interpretation of the term ‘information’.

46. The revised *Conceptual Framework* was issued on 29 March 2018. For each of the terminology concerns listed in paragraph 45 above, we have reviewed:

    (a) relevant Board Papers from the Conceptual Framework project; and

    (b) relevant Basis for Conclusions paragraphs from both the *Conceptual Framework* and the Exposure Draft.

47. Details of this review can be found in Appendix A. In summary, we have concluded that all of the terminology concerns raised by respondents have been previously deliberated by the Board, either as part of the Conceptual Framework project or when developing the Exposure Draft. We think that the feedback received from respondents about terminology does not highlight any new information. When making decisions about terminology in the *Conceptual Framework* and the Exposure Draft, we think the Board has already given due consideration to the points raised.

48. Furthermore, we think that re-considering terminology that is aligned with the recently published *Conceptual Framework* would not be helpful to stakeholders at this time. The objective of these proposals in the Exposure Draft was to align wording and improve clarity. We think that adjusting existing terminology in the *Conceptual Framework* falls outside the scope of the Definition of Material project.

49. Consequently, staff recommend that the Board retain the proposed amendments that align terminology in the definition of material with existing terminology in the *Conceptual Framework*.

Question for the Board

Question 3
Does the Board agree with the staff recommendation that the Board should retain the proposed amendments that align terminology in the definition of material with existing terminology in the *Conceptual Framework*?

Replacing the threshold 'could influence' with 'could reasonably be expected to influence'

50. Some respondents were concerned about the inclusion of the term 'reasonably' within the definition. These respondents thought that this term might be interpreted differently, particularly across different jurisdictions, and that this may result in inconsistencies in how the definition of material is understood and applied in practice. These respondents suggested that the Board further explain the term 'reasonably'.

51. In the Basis for Conclusions on the Exposure Draft, the Board explain that feedback has been received from stakeholders that the existing definition of material is too broad and hence may result in entities disclosing immaterial information in their financial statements. The Board proposed replacing the threshold 'could influence' with 'could reasonably be expected to influence' in response to this feedback. We think the Board's reasons for proposing this amendment remain valid, and note that many respondents supported this proposed amendment.

52. Furthermore, the proposed amendment clarifies and clearly incorporates existing requirements from IAS 1 paragraph 7 which states: '*Therefore, the assessment needs to take into account how users with such attributes could reasonably be expected to be influenced in making economic decisions*'. There are also many other uses of the term 'reasonable' throughout IFRS Standards that are not supplemented with additional explanation and are applied by stakeholders today. Therefore, we think that further defining the use of 'reasonable' in this context could have unintended consequences.

53. Consequently, the staff recommend that the Board retain the proposed amendment to replace the threshold 'could influence' with 'could reasonably be expected to influence' in the definition of material.

Question for the Board

Question 4
Does the Board agree with the staff recommendation that the Board retain the proposed amendment to replace the threshold 'could influence' with 'could reasonably be expected to influence' in the definition of material?

Effective date

54. If the Board agree with all of the staff recommendations in this paper, we anticipate the final amendments to the definition of material being ready for publication in the fourth quarter of 2018. The proposed amendments to the definition of material do not represent a substantive change to the requirements in IFRS Standards. Instead, they are intended to clarify and improve understanding of the existing requirements. Consequently, we continue to think that prospective application is appropriate, as was proposed in the Exposure Draft. Furthermore, we do not think that a long implementation period is required.

55. In order to ensure there is enough time for translation and other adoption processes to take place, the staff recommend an effective date of annual periods beginning on or after 1 January 2020. We think that if an entity would like to early apply the amendments, they should be permitted to do so.

56. Some respondents thought the Board should not require an entity to disclose early application of the proposals. This is because they thought the nature of the amendments means there should be no impact on judgements made in the preparation of financial statements. However, the staff think this fact should not affect disclosure of any early application and that, if an entity does choose to early apply the amendments, that fact should be disclosed. This approach is consistent with the early application requirements in other new IFRS Standards and amendments.

Aligning the effective date to other changes being made in IAS 8

57. Some respondents suggested that the Board align the effective dates for amendments to the definition of material with the effective date for other amendments to IAS 8. The Board has two other maintenance projects on its Agenda relating to IAS 8:

    (a) Accounting Policy Changes (Amendments to IAS 8). The Exposure Draft for this project is out for comment, with a feedback deadline of 27 July 2018; and

    (b) Accounting Policies and Accounting Estimates (Amendments to IAS 8). The Board is deciding project direction in light of comment letter feedback received.

58. The effective date for any amendments that might arise as a result of these projects has not yet been determined. Staff do not believe that the amendments to the definition of material should be deferred to align the effective date of all amendments being proposed to IAS 8. However, in light of the relative project stages, we think it is unlikely that either of the projects listed in paragraph 57 would result in amendments with an effective date of 1 January 2019. Consequently, we think that the proposed effective date for amendments to the definition of material of 1 January 2020 means there remains a possibility of aligned effective dates for all potential changes to IAS 8.

Staff recommendation and question for the Board

Question 5
Does the Board agree with the staff recommendation that the effective date of amendments be for annual periods beginning on or after 1 January 2020 with early application permitted?

Other considerations

'Immaterial' and 'not material'

59. Some respondents were concerned that both the terms 'immaterial' and 'not material' are used across IFRS Standards and additional guidance (such as the Materiality Practice Statement). Respondents questioned whether the two terms have the same meaning.

60. In light of this feedback, we have reviewed all uses of the terms 'immaterial' and 'not material' throughout the Materiality Practice Statement and the authoritative guidance in IFRS Standards (see Appendix B). Based on this review, we think the terms are used interchangeably—ie they have the same meaning.

61. The staff recommend that the Board does not take any action in response to feedback about the use of the terms 'immaterial' and 'not material'. This is because we do not think it is necessary to do so.

Materiality Practice Statement

62. Some respondents provided feedback on the effect of the recently published Materiality Practice Statement. These respondents thought the Materiality Practice Statement is useful, and asked the Board to consider incorporating elements of the guidance into the *Conceptual Framework*, IAS 1 or both.

63. In the March 2018 Board meeting the Board decided that it would consider whether to perform further activity relating to materiality when it has more information about the practical effect of all recent Board publications about the application of materiality, including the Materiality Practice Statement. As described in ***Agenda Paper 11A*** at that meeting, we recommend waiting until 2019 to perform this work. By this time, many entities will have been through two complete reporting cycles since the Materiality Practice Statement was issued.

64. Consequently, in line with the decision made in the March 2018 Board meeting, the staff recommend that the Board does not incorporate any of the Materiality Practice Statement in IAS 1 or the *Conceptual Framework*, including via reference, at this time. We note that the Board may consider doing this as part of its future work on the Principles of Disclosure project.

Use of the term 'material'

65. A few respondents expressed concern over the varying use of the term 'material' in IFRS Standards. These respondents identified that the term 'material' is used inconsistently across the Standards and is sometimes used in other, narrower contexts (ie not in relation to the financial statements as a whole). For example—IAS 16 *Property, Plant and Equipment* says that sometimes residual value does not have a material effect on the calculation of depreciation.

66. The staff note that the purpose of the amendments to IAS 1 and IAS 8 is to align the definition of material between the IFRS Standards and the *Conceptual Framework*, and to improve clarity. Further, many stakeholders supported the existing definition of material.

67. We think that redeliberating the use of the term 'material' in other Standards is beyond the scope of this project. Furthermore, we are not aware of any practical

consequences of the two uses of the term ‘material’ as described in paragraph 65 such that it would be helpful for the Board to address. Consequently, the staff recommend that the Board does not take any action in response to feedback about the use of the term ‘material’.

International Auditing and Assurance Standards Board (IAASB)

68. A few respondents suggested that the Board liaise with the IAASB as they have a more detailed definition of materiality (see Appendix C). These respondents thought that it would be helpful if the Board’s definition and the IAASB’s definition aligned. The IAASB did not submit a comment letter.

69. Staff think that it would be beneficial to consider whether the proposed amendments to the definition of material have any consequences in terms of interaction with the IAASB’s literature. Consequently, we have reviewed the description of Materiality in the Context of an Audit (as per ISA 320 – see Appendix C) in light of the Board’s proposed changes to the definition of material and the staff recommendations in this paper. We think that the interaction between the Board’s and the IAASB’s literature are not changed by the proposed amendments, or by the staff recommendations in this paper. This conclusion is supported by the objectives of the project and the staff analysis in paragraph 30—both of which conclude that the proposed amendments do not alter the underlying concept of materiality in IFRS Standards.

70. We think that if the Board agrees with the staff recommendations in this paper, it does not need to take any further action in respect of aligning the definition of material with the IAASB.

Staff recommendations and questions for the Board

Question 6

Does the Board agree with the staff recommendations that the Board:

(a) should not take any further action in response to feedback about the use of the terms ‘immaterial’ and ‘not material’;

(b) should not incorporate any of the Materiality Practice Statement in IAS 1 or the *Conceptual Framework*, including via reference, at this time;

(c) should not take any further action in response to feedback about the varying use of the term ‘material’; and

(d) should not take any further action in response to feedback about the interaction between the definition of material and the description of Materiality in the Context of an Audit in ISA 320?

Appendix A—Aligning terminology with the *Conceptual Framework*

A1. This Appendix summarises the concerns raised by respondents about proposals in the Exposure Draft that relate to existing terminology in the *Conceptual Framework*. It also summarises the previous deliberations by the Board which support the staff's recommendation that the Board should retain the proposed amendments that align terminology in the definition of material with existing terminology in the *Conceptual Framework*. These concerns related to:

(a) the definition of material in the *Conceptual Framework* uses the term 'general purpose financial report', whilst the Exposure Draft uses the term 'general purpose financial statements' (paragraphs A2-A4);

(b) the scope of the term 'primary users' (paragraphs A5-A6);

(c) the inconsistent use of the terms 'economic decisions' and 'decisions' (paragraphs A7-A8);

(d) the use of the term 'specific reporting entity' as opposed to 'reporting entity' (paragraphs A9-A10); and

(e) the interpretation of the term 'information' (paragraphs A9-A10).

'General purpose financial report' and 'general purpose financial statements'

A2. The definition of material in the *Conceptual Framework* uses the term 'general purpose financial report', whilst the Exposure Draft uses the term 'general purpose financial statements'. Some respondents did not agree with using different terms. They suggested that the Board use consistent terminology by adjusting the *Conceptual Framework* definition to refer to 'general purpose financial statements'.

A3. Chapter 3 (in particular paragraph 3.1) of the *Conceptual Framework* provides clear guidance that 'general purpose financial statements' are a particular form of 'general purpose financial reports.' In other words, the term 'general purpose financial reports' has a broader scope than the term 'general purpose financial statements'. The *Conceptual Framework* discusses the information in general purpose financial reports and general purpose financial statements separately—it is clear that these terms are not used interchangeably and do not mean the same thing.

A4. Consequently, the Board proposed using the term 'financial statements' rather than 'financial reports' in the Exposure Draft because the requirements in IAS 1 and IAS 8 specifically relate to general purpose financial statements and not to general purpose financial reports. Similarly, the use of the two different terms in the *Conceptual Framework* appropriately reflected their different meanings.

'Users' and 'primary users'

A5. Some respondents did not agree with the change of the term 'users' to 'primary users' in the definition of material. This was because, in their view, 'primary users' is too narrow. These respondents thought that financial statements should provide information to a wider range of users such as regulators, government agencies, policy makers and internal stakeholders.

A6. The change of terminology from ‘users’ to ‘primary users’ was considered in detail by the Board in May 2014 as part of the Conceptual Framework project. At that time, the Board considered similar concerns about the change in terminology as the concerns raised by respondents to the Exposure Draft and it was determined that primary users was appropriate.

‘Economic decisions’ and ‘decisions’

A7. A few respondents thought that the word ‘economic’ should not be removed from the definition. These respondents said that ‘economic decisions’ is a more precise term than ‘decisions’ and would therefore be more consistently applied.

A8. As described in paragraph BC15 of the Exposure Draft, the Board clarified in paragraph 1.5 of the *Conceptual Framework* that these terms are intended to be interpreted the same way. Further, both terms have been used interchangeably throughout the *Conceptual Framework*.

Other terms

A9. Some respondents expressed confusion about the use of the terms:

(a) ‘specific reporting entity’ as opposed to ‘reporting entity’—these respondents suggested that the Board provide clarification as to the difference between these terms; and

(b) ‘information’ as opposed to ‘financial information’.

A10. The four terms described in paragraph A9 are each used throughout the *Conceptual Framework*, including within the definition of material as it appears in the *Conceptual Framework*. There was no feedback received during the Conceptual Framework project for which issues were raised in relation to the use or application of these terms.

Appendix B—Extracts from IFRS Standards, Interpretations and the Materiality Practice Statement which use the terms 'immaterial' and 'not material'

IFRS 4, paragraph 39J

'*If an entity applied the temporary exemption from IFRS 9 when accounting for its investment in an associate or joint venture using the equity method (for example, see paragraph 20O(a)), the entity shall disclose the following, in addition to the information required by IFRS 12 Disclosure of Interests in Other Entities:*

…

(b) the quantitative information described by paragraphs 39B–39H in aggregate for all individually immaterial associates or joint ventures. The aggregate amounts:

(i) disclosed shall be the entity's share of those amounts; and

(ii) for associates shall be disclosed separately from the aggregate amounts disclosed for joint ventures.'

IFRS 4, paragraph 39M

'*If an entity applied the overlay approach when accounting for its investment in an associate or joint venture using the equity method, the entity shall disclose the following, in addition to the information required by IFRS 12:*

…

(b) the quantitative information described by paragraphs 39K–39L(d) and 39L(f), and the effect of the reclassification described in paragraph 35B on profit or loss and other comprehensive income in aggregate for all individually immaterial associates or joint ventures. The aggregate amounts:

(i) disclosed shall be the entity's share of those amounts; and

(ii) for associates shall be disclosed separately from the aggregate amounts disclosed for joint ventures.'

IFRS 12, paragraph 21

'*An entity shall disclose:*

…

(c) financial information as specified in paragraph B16 about the entity's investments in joint ventures and associates that are not individually material:

(i) in aggregate for all individually immaterial joint ventures and, separately,

(ii) in aggregate for all individually immaterial associates.'

IAS 1, paragraph 29

'*An entity shall present separately each material class of similar items. An entity shall present separately items of a dissimilar nature or function unless they are immaterial.*'

IAS 1, paragraph 31

> '*... An entity need not provide a specific disclosure required by an IFRS if the information resulting from that disclosure is not material...*'

IAS 2, paragraph 14

> '*... Most by-products, by their nature, are immaterial. When this is the case, they are often measured at net realisable value and this value is deducted from the cost of the main product. As a result, the carrying amount of the main product is not materially different from its cost.*'

IAS 8, paragraph 8

> '*…Those policies need not be applied when the effect of applying them is immaterial. However, it is inappropriate to make, or leave uncorrected, immaterial departures from IFRSs to achieve a particular presentation of an entity's financial position, financial performance or cash flows.*'

IAS 8, paragraph 16

> '*The following are not changes in accounting policies:*
>
> *…*
>
> *(b) the application of a new accounting policy for transactions, other events or conditions that did not occur previously or were immaterial.*'

IAS 8, paragraph 41

> '*…Financial statements do not comply with IFRSs if they contain either material errors or immaterial errors made intentionally to achieve a particular presentation of an entity's financial position, financial performance or cash flows…*'

IAS 16, paragraph 53

> '*The depreciable amount of an asset is determined after deducting its residual value. In practice, the residual value of an asset is often insignificant and therefore immaterial in the calculation of the depreciable amount.*'

IAS 17, paragraph 17

> '*For a lease of land and buildings in which the amount that would initially be recognised for the land element, in accordance with paragraph 20, is immaterial, the land and buildings may be treated as a single unit for the purpose of lease classification and classified as a finance or operating lease in accordance with paragraphs 7–13. In such a case, the economic life of the buildings is regarded as the economic life of the entire leased asset.*'

Materiality Practice Statement, paragraph 8

> '*... However, it is inappropriate for the entity to make, or leave uncorrected, immaterial departures from IFRS Standards to achieve a particular presentation of its financial position, financial performance or cash flows.*'

Materiality Practice Statement, paragraph 28

> '*… In such circumstances, providing information to meet local legal or regulatory requirements is permitted by IFRS Standards, even if that information is not material according to the materiality requirements in the Standards…*'

Appendix C—Extract from ISA 320 *Materiality in Planning and Performing an Audit*

Materiality in the Context of an Audit

2. Financial reporting frameworks often discuss the concept of materiality in the context of the preparation and presentation of financial statements. Although financial reporting frameworks may discuss materiality in different terms, they generally explain that:

    - Misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements;
    - Judgments about materiality are made in light of surrounding circumstances, and are affected by the size or nature of a misstatement, or a combination of both; and
    - Judgments about matters that are material to users of the financial statements are based on a consideration of the common financial information needs of users as a group. The possible effect of misstatements on specific individual users, whose needs may vary widely, is not considered.

3. Such a discussion, if present in the applicable financial reporting framework, provides a frame of reference to the auditor in determining materiality for the audit. If the applicable financial reporting framework does not include a discussion of the concept of materiality, the characteristics referred to in paragraph 2 provide the auditor with such a frame of reference.

4. The auditor's determination of materiality is a matter of professional judgment, and is affected by the auditor's perception of the financial information needs of users of the financial statements. In this context, it is reasonable for the auditor to assume that users:

    a) Have a reasonable knowledge of business and economic activities and accounting and a willingness to study the information in the financial statements with reasonable diligence;

    b) Understand that financial statements are prepared, presented and audited to levels of materiality;

    c) Recognize the uncertainties inherent in the measurement of amounts based on the use of estimates, judgment and the consideration of future events; and

    d) Make reasonable economic decisions on the basis of the information in the financial statements.