

Issues paper: Clarification of Tier 2 Disclosure Principles

Objective

1. The objective of this paper is to consider improvements to the drafting of the guidance for applying 'Tier 2 Disclosure Principles'. The improvement come from our experiences in applying the principles to Standards issued after the *IFRS for SMEs* publication.

Background

2. In determining Tier 2 disclosure requirements, the AASB decided to use the same principles that the IASB used in determining disclosures under the *IFRS for SMEs*. The disclosures required by the *IFRS for SMEs* are substantially reduced compared with those in full IFRSs on the basis that some disclosures are excluded:
 - (a) because they relate to topics covered in full IFRSs that are omitted from the *IFRS for SMEs*;
 - (b) because they relate to recognition and measurement requirements in full IFRSs that are not available in the *IFRS for SMEs*;
 - (c) because they relate to optional accounting policies in full IFRSs that are not included in the *IFRS for SMEs*; and
 - (d) due to users' needs or cost-benefit considerations.
3. 'Tier 2 Disclosure Principles' is a reference to 'user need' and 'cost benefit' principles and the related operational guidelines facilitating the application of those principles.

Existing Tier 2 Disclosure Principles

4. Paragraph 1 of the existing Tier 2 Disclosure Principles notes:

"The disclosures proposed under Tier 2 are determined by:

 - (a) drawing directly on the IFRS for SMEs when Tier 2 recognition and measurement requirements are the same as those under the IFRS for SMEs; and*
 - (b) using the 'user need' and 'cost-benefit' principles applied by the IASB in developing its IFRS for SMEs when Tier 2 recognition and measurement requirements are not the same as those available under the IFRS for SME."*
5. In terms of recognition and measurement requirements, the *IFRS for SMEs* differs from full IFRSs in a number of ways:
 - (a) some topics in full IFRSs are omitted from the *IFRS for SMEs*. Examples are earnings per share, interim financial reporting, and segment reporting;
 - (b) SMEs are limited to particular accounting policy options — either one option in full IFRSs is mandated or a 'new' accounting policy is required. Examples are no option to revalue property, plant and equipment, or intangibles, a cost-depreciation model for investment property unless fair value is readily available without undue cost or effort and fair value model for investments in associates and jointly controlled entities; and

6. other recognition and measurement differences. Examples are no available-for-sale or held-to-maturity classes of financial assets and amortisation of goodwill. In cases when the recognition and measurement accounting policies under Tier 2 and those under the *IFRS for SMEs* are the same, under the Tier 2 Disclosure Principles we rely on the IASB's judgement, rather than directly applying the 'user need' and 'cost benefit' principles to full IFRS disclosure requirements to arrive at Tier 2 disclosure requirements. This approach was termed as 'benchmarking' in the AASB Discussion Paper *Differential Financial Reporting – Reducing Disclosure Requirements* (February 2010). Paragraph 8.2 of the Discussion Paper explains that:

“This approach [the approach noted in paragraph 5(a) above] does not necessarily use the IFRS for SMEs disclosures directly; rather it benchmarks the disclosures under the Reduced Disclosure Regime to those under the IFRS for SMEs which are seen as the minimum disclosures required to satisfy the objective of [general purpose financial statements]GPFSS. This approach would help minimise the cost of determining and maintaining disclosures under the proposed Reduced Disclosure Regime. Satisfying the objective of GPFSS would be the basis for determining the disclosures under the Reduced Disclosure Regime whether or not the recognition and measurement accounting policy options available under that regime align with those provided under the IFRS for SMEs.”

7. The following points regarding the approach are relevant.
- (a) Benchmarking reduces the cost of determining and maintaining disclosures by drawing on the judgements made in determining disclosures under the *IFRS for SMEs*.
 - (b) Benchmarking does not necessarily involve the direct use of *IFRS for SMEs* disclosures.
 - (c) The *IFRS for SMEs* notes that its disclosure requirements constitute the minimum disclosures required to GPFSS.
 - (d) Tier 2 disclosures should satisfy the objective of GPFSS irrespective of whether the recognition and measurement accounting policies available under Tier 2 align with those provided under the *IFRS for SMEs*.
8. This last point is of particular significance since it contemplates disengagement from the *IFRS for SMEs* disclosure requirements when satisfaction of the objective of GPFSS would warrant it.

Benchmarking to the IFRS for SMEs

9. Benchmarking to the *IFRS for SMEs* is not meant to be to the *IFRS for SMEs* issued as of a certain date (such as July 2009), rather to a notional *IFRS for SME* that is updated for changes in full IFRSs. In other words, in determining Tier 2 disclosures the main principles used by the IASB in determining disclosures under the *IFRS for SMEs*, that is 'user need' and cost-benefit' principles, are drawn upon to the extent the disclosures under a revised/improved IFRS diverge from those under the IFRSs extant at the time the *IFRS for SMEs* was published.
10. Benchmarking as explained above is consistent with the premises underlying the Reduced Disclosure Requirements (RDR). In explaining the reasons for the AASB's preference for an RDR over the *IFRS for SMEs*, the Discussion Paper, paragraph 5.2(b) notes the AASB's concern that :

“entities applying the IFRS for SMEs would be deprived of improvements and simplifications as they become available at the full IFRS level because the IASB has stated that it will only update the IFRS for SMEs once there have been two years of broad adoption and, thereafter, every three years.”

11. Paragraph 5.2(b) of the Discussion Paper foresees issues arising in the intervening period between the two versions of the *IFRS for SMEs*. It goes on to clearly envisage a process under RDR where Tier 2 entities would not be deprived of improvements and simplifications as they become available at the full IFRS level. Such improvements are not confined to the recognition, measurement or presentation requirements and encompass the disclosure requirements too.
12. Periodic reviews of the *IFRS for SMEs* leads to ‘double handling’, in the sense that the same topic is dealt with at different times under different Tiers. In contrast, the RDR avoids double handling by dealing with the same topic under the two Tiers simultaneously. The above notion of benchmarking is consistent with the latter.
13. Another consideration corroborating the notion of benchmarking described in paragraph 9 would be the direct application of user need and cost benefit principles in situations where the recognition and measurement accounting policies under a full IFRS and the *IFRS for SMEs* differ. In such situations, Tier 2 disclosures are determined using ‘user need’ and ‘cost-benefit’ principles directly (see paragraphs 5 and 6 of Tier 2 Disclosure Principles, Appendix 1). The approach in such cases is akin to the notion of benchmarking described above. It may be argued that confining benchmarking to the *IFRS for SMEs* as of a certain date could lead to inconsistencies in determining Tier 2 disclosures in situations where there are no recognition and measurement differences compared with situations where there are such differences.
14. Benchmarking becomes a prominent tool for determining Tier 2 disclosures each time the *IFRS for SMEs* is updated. However, its usefulness as a basis for determining disclosures decreases as new or revised full IFRS disclosures become available. At the same time, direct use of ‘user need’ and ‘cost benefit’ principles increases until the next version of the *IFRS for SMEs* is published.
15. To clarify the operational guidance on benchmarking, staff have marked up the Tier 2 Disclosure Principles for the minimum changes required (see Appendix 1).
16. The clarifications would help remove ambiguities about the application of Tier 2 Disclosure Principles in circumstances such as when new or revised disclosures are introduced by an IFRS without a change in related recognition and measurement accounting policy option.

Consistency of application

17. Tier 2 Disclosure Principles and related operational guidance should be applied consistently so that disclosures relating to analogous circumstances are not significantly different (see paragraph 10, appendix 1).

18. While the ‘consistency of application’ guidance helps ensure that similar Tier 2 disclosure decisions are made in similar situations, it also makes it possible to rely on similar previous decisions (‘analogising’) in analysing IFRS disclosure requirements for Tier 2 purposes.
19. Exclusion or retention of full IFRS disclosures by analogy is not intended to be a new principle; rather it is a tool that facilitates communication between different parties engaged in analysing IFRS disclosures for Tier 2 purposes. Accordingly, analogising does not relieve these parties from making independent decisions in the circumstances of each case, rather it provides corroborative evidence for the decisions made and helps ensure ‘consistency of application’ is achieved. A recent example of employing this tool is in analysing disclosure requirements under AASB 13 *Fair value Measurement*. Appendix 2 includes relevant examples of this analysis.
20. More generally, analogising has been explicitly or implicitly used in relation to disclosures in the following areas:
 - Risk management
 - Sensitivity analysis
 - Reconciliations
 - Fair value measurement assumptions
21. Staff believe that providing information about analogous situation(s) in the comment column of the ‘Analysis of Disclosure Requirements’ may be as useful to external readers as it has been to those performing the analyses. However, care will need to be taken to ensure this information is presented in a way that enhances the external parties’ understanding of the process involved and assists them in providing more informed comments.
22. ‘Analogising’ is not limited to the Board’s previous Tier 2 decisions in relation to similar disclosures. Its application may be extended to analysing full IFRS disclosures by relying on the IASB decisions in relation to similar disclosures under the *IFRS for SMEs*, albeit those disclosures are included in a section of the *IFRS for SMEs* that does not correspond to the topic covered by the full IFRS.

Questions for the Board:

- (a) Does the Board agree in principle with staff clarifications of Tier 2 Disclosure Principles as shown in mark up in Appendix 1?
- (b) If so, does the Board agree to staff finalising the redrafted Tier 2 Disclosure Principles?

APPENDIX 1:

TIER 2 DISCLOSURE PRINCIPLES (MARKED UP)

The ‘user need’ and ‘cost-benefit’ principles that underlie the determination of disclosure requirements in the *IFRS for SMEs* are applied in determining disclosures under Tier 2 (Reduced Disclosure Requirements). The following operational guidance is intended to facilitate the application of those principles:

~~The following principles are applied in determining disclosures under Tier 2:~~

General guidance

1 The disclosures proposed under Tier 2 are determined by:

~~drawing directly on benchmarking to the *IFRS for SMEs* disclosures when Tier 2 recognition and measurement requirements-accounting policies are the same as those under the *IFRS for SMEs* unless the relevant full IFRS disclosure is a new or revised disclosure that did not exist when the *IFRS for SMEs* was published or last updated. In such cases the ‘user need’ and ‘cost-benefit’ principles (used by the IASB in developing its *IFRS for SMEs*) are applied to new or revised disclosures; and~~

(b) ~~using applying~~ the ‘user need’ and ‘cost-benefit’ principles ~~applied by the IASB in developing its *IFRS for SMEs* when Tier 2 recognition and measurement requirements are not the same as those available under the *IFRS for SMEs*.~~

Specific guidance

Approach when Recognition and Measurement Requirements are the Same

Identical or similar disclosures

2 Where the disclosure requirements under a full IFRS as adopted in Australia and the *IFRS for SMEs* are the same or similar (that is, result in the same disclosures), those disclosure requirements are retained as part of Tier 2 requirements, using the wording of the relevant full IFRS as adopted in Australia.

Dissimilar disclosures

3 Where the disclosure requirements under a full IFRS and the *IFRS for SMEs* are dissimilar, the following procedure is followed:

(a) Where the *IFRS for SMEs* does not require a disclosure that is required in the relevant full IFRS, Tier 2 does not retain that disclosure unless the relevant full IFRS disclosure requirement is a new or revised disclosure requirement and the application of user need and cost-benefit principles warrants otherwise.

(b) ~~Furthermore, w~~Where the *IFRS for SMEs* disclosure is less onerous than the relevant full IFRS, the less onerous disclosure is adopted unless the relevant full IFRS disclosure requirement is a new or revised disclosure requirement and the application of user need and cost benefit principles warrants otherwise.

Benchmarking to the *IFRS for SMEs* in cases where a new or revised disclosure is not involved This is on the basis that, in developing the *IFRS for SMEs*, the IASB has already applied the user needs and cost benefit considerations-principles and concluded that an exemption or reduced disclosure is appropriate.

Although the *IFRS for SMEs* has been developed to apply to for-profit private sector entities, broadly it is considered reasonable to rely on the judgements made in developing the *IFRS for SMEs* in respect of both for-profit and not-for-profit (including public sector) entities in Australia given that IFRSs are generally applied to all types of Australian entities. The AASB uses its *Process for Modifying IFRSs for PBE/NFP* in assessing the need for specific requirements relating to not-for-profit entities.

In most cases, the structure of the words in the relevant full IFRS enables the use of shading to show that a relevant disclosure is excluded or reduced so as to match the *IFRS for SMEs* disclosure outcome. In the few cases where this is not feasible, the wording in the *IFRS for SMEs* is used as the basis for an RDR paragraph as a substitute for the relevant full IFRS wording.

- 4 In the few cases where the *IFRS for SMEs* has an additional disclosure requirement that is not included in the full IFRS, that disclosure is not included in Tier 2 requirements.

Approach when Recognition and Measurement Requirements are not the Same

- 5 The disclosures under Tier 2 are determined by drawing on the ‘user need’ and ‘cost-benefit’ principles applied by the IASB in developing its *IFRS for SMEs* when Tier 2 recognition and measurement requirements-accounting policies are not the same as those under the *IFRS for SMEs*.
- 6 The principles applied by the IASB in developing its *IFRS for SMEs* are grounded in the view that users of financial information of non-publicly accountable for-profit entities are particularly interested in knowing information about:
- (a) short-term cash flows and about obligations, commitments or contingencies, whether or not recognised as liabilities;
 - (b) liquidity and solvency;
 - (c) measurement uncertainties;
 - (d) the entity’s accounting policy choices;
 - (e) disaggregations of amounts presented in the financial statements; and
 - (f) transactions and other events and conditions encountered by such entities.

Guidance

- 7 Guidance relating to a disclosure that is retained in Tier 2 requirements is also retained in Tier 2 requirements on the grounds that it assists entities in making that disclosure and would not add to the disclosure burden. Guidance that relates to a disclosure that is not retained in ~~the~~ Tier 2 requirements is also not retained in Tier 2 requirements. Text in the nature of contextual material is not treated as guidance. Such text is retained in Tier 2 on the basis that its retention does not add to the disclosure burden.

Disclosure Encouraged

- 8 Where a disclosure is encouraged, whether under the full IFRSs as adopted in Australia or the *IFRS for SMEs*, it is not included.

Presentation vs Disclosure

- 9 Tier 2 does not involve amending the presentation (sometimes used interchangeably with classification) requirements of Tier 1 and is concerned only with reducing the disclosure burden. Sometimes judgement is required as to whether a particular requirement relates to presentation or disclosure. The following criteria-guidance are is used to distinguish between presentation and disclosure:

‘Presentation requirements are limited to requirements that specify the broad structure of financial statements including the basis of classification of items. Specifications relating to subclassifications or line items to be shown on the face of financial statements, or in the notes, are treated as matters of disclosure.’

Clarification in relation to Not-For-Profit and Public Sector Entities

- 10 Although the *IFRS for SMEs* has been developed to apply to for-profit private sector entities, broadly it is considered reasonable to rely on the judgements made in developing the *IFRS for SMEs* in respect of both for-profit and not-for-profit (including public sector) entities in Australia given that IFRSs are generally applied to all types of Australian entities. Accordingly, paragraphs 3 and 6 are relevant to all types of entities, since the same transactions are generally accounted for in the same manner for all types of entities under the AASB’s policy of transaction neutrality. The AASB uses its *Process for Modifying IFRSs for PBE/NFP* in assessing the need for specific requirements relating to not-for-profit entities.

— However, there are a For the limited number of disclosure requirements in full IFRSs as adopted in Australia that are specific to the circumstances of not-for-profit and public sector entities – In relation to these disclosures, the Tier 2 disclosures are determined by drawing on applying the user need and cost-benefit principles applied by the IASB in developing its *IFRS for SMEs* in the context of the specific needs of users of not-for-profit and public sector entity financial statements.

- (a) drawing directly on the *IFRS for SMEs* when Tier 2 recognition and measurement requirements are the same as those under the *IFRS for SMEs*; and
- (b) using the ‘user need’ and ‘cost-benefit’ principles applied by the IASB in developing its *IFRS for SMEs* when Tier 2 recognition and measurement requirements are not the same as those available under the *IFRS for SMEs*.

Consistency of application

- 11 Tier 2 Disclosure Principles and related operational guidance are applied consistently so that disclosures relating to analogous circumstances are not significantly different.

APPENDIX 2:

Examples of 'Analogising' to previous Tier 2 Disclosure Decisions

Analysis of Disclosure Requirements in AASB 13 *Fair Value Measurement* (May 2011) with a View to Determining Corresponding Tier 2 Disclosure Requirements

AASB 13 *Fair Value Measurement* is a new Standard that provides guidance for measuring fair value and includes disclosures about fair value measurement. AASB 13 includes some new disclosures and some disclosures carried forward from existing Standards (and those Standards have been amended accordingly). All disclosure requirements under AASB 13 are included in this analysis.

Note to Sub-committee:

In determining the Tier 2 disclosure requirements for those disclosures that have been carried forward from existing Standards, the existing Tier 2 disclosure requirements of other relevant Standards are considered and used as a basis.

For the new disclosures in AASB 13, where appropriate, Tier 2 disclosure requirements relating to disclosures of a similar nature in other Standards have been considered by analogy in determining the Tier 2 disclosure requirements. For new disclosures in AASB 13 that are not analogous, in nature, to disclosures in other Standards, 'user need' and 'cost benefit' principles are applied in determining the Tier 2 disclosure requirements. In this exercise, the specific needs of users of financial statements of Tier 2 entities such as information about short-term cash flows and about obligations, commitments or contingencies, liquidity and solvency; measurement uncertainties; entity's accounting policy choices; disaggregations of amounts presented in the financial statements; and transactions and other events and conditions encountered by such entities are considered.

Analysis of Disclosure Requirements

Disclosure requirements in AASB 13 <i>Fair Value Measurement</i>	Disclosure requirements in IFRSs for SMEs Section 11 <i>Basic Financial Instruments</i> , Section 14 <i>Investments in Associates</i> , Section 15 <i>Investments in Joint Ventures</i> , Section 16 <i>Investment Property</i> , Section 34 <i>Specialised Activities</i>	Comments
<p>91. An entity shall disclose information that helps users of its financial statements assess both of the following:</p> <p>(a) for assets and liabilities that are measured at fair value on a recurring or non-recurring basis in the statement of financial position after initial recognition, the valuation techniques and inputs used to develop those measurements.</p> <p>(b) for recurring fair value measurements using significant unobservable inputs (Level 3), the effect of the measurements on profit or loss or other comprehensive income for the period.</p>	<p>The disclosure requirement in paragraph 11.43 relates to financial instruments and also applies to section 14 <i>Investments in Associates</i> and section 15 <i>Investments in Joint Ventures</i> where the references to financial instruments are to be read to include the type of assets covered by those sections.</p> <p>11.43 For all financial assets and financial liabilities measured at fair value, the entity shall disclose the basis for determining fair value, eg quoted market price in an active market or a valuation technique. When a valuation technique is used, the entity shall disclose the assumptions applied in determining fair value for each class of financial assets or financial liabilities. For example, if applicable, an entity discloses information about the assumptions relating to prepayment rates, rates of estimated credit losses, and interest rates or discount rates.</p> <p>16.10 An entity shall disclose the following for all investment property accounted for at fair value through profit or loss (paragraph 16.7):</p> <p>(a) the methods and significant</p>	<p>Paragraph 91(a) of AASB 13 and paragraphs 11.43, 16.10 and 34.7 of the <i>IFRSs for SMEs</i> correspond.</p> <p>Based on paragraph 2 of Tier 2 disclosure principles, paragraph 91(a) should be retained in the Tier 2 disclosure requirements.</p> <p>[Note: Paragraph 75(d) of AASB 140 <i>Investment Property</i> corresponds to paragraph 16.10 of <i>IFRS for SMEs</i>, paragraph 47 of AASB 141 <i>Agriculture</i> corresponds to paragraph 34.7 of <i>IFRS for SMEs</i> and paragraph 27 of AASB 7 <i>Financial Instruments: Disclosures</i> corresponds to paragraph 11.43 of the <i>IFRS for SMEs</i>. These paragraphs have been retained in the Tier 2 disclosure requirements, which corroborates the proposed retention of paragraph 91(a) in the Tier 2 disclosure requirements.]</p> <p>Paragraph 91(b) is a new disclosure requirement and has no equivalent in the <i>IFRS for SMEs</i>. Based on paragraph 3 of ‘Tier 2 Disclosure Principles’, paragraph 91(b) should be excluded from Tier 2 disclosure requirements.</p> <p>[Note to the Sub-committee: Paragraph 91(b) requires disclosures that are similar in nature to the disclosures in paragraphs 27B(c) and 27B(d) of AASB 7, which are excluded from the Tier 2 disclosure</p>

<p>Disclosure requirements in AASB 13 Fair Value Measurement</p>	<p>Disclosure requirements in IFRSs for SMEs Section 11 <i>Basic Financial Instruments</i>, Section 14 <i>Investments in Associates</i>, Section 15 <i>Investments in Joint Ventures</i>, Section 16 <i>Investment Property</i>, Section 34 <i>Specialised Activities</i></p>	<p>Comments</p>
	<p>assumptions applied in determining the fair value of investment property.</p> <p>34.7 An entity shall disclose the following with respect to its biological assets measured at fair value:</p> <ul style="list-style-type: none"> (a) a description of each class of its biological assets. (b) the methods and significant assumptions applied in determining the fair value of each category of agricultural produce at the point of harvest and each category of biological assets. 	<p>requirements. This corroborates the proposed exclusion of paragraph 91(b) from the Tier 2 disclosure requirements.]</p>