



European Securities and Markets Authority (ESMA)
103 Rue de Grenelle
75007 Paris

Deutsche Bank AG
Taunusanlage 12
60325 Frankfurt am Main
Germany
Tel +49 69 9 10-00

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Dear Sirs

Consultation Paper: Considerations of materiality in financial reporting

Deutsche Bank welcomes the opportunity to comment on the European Securities and Markets Authority's (ESMA) Consultation Paper "Considerations of Materiality in Financial Reporting" (the Consultation Paper).

Applying the concept of materiality is fundamental to our financial reporting process. It provides the framework for ensuring that information presented and disclosed in financial statements is relevant to users. The Consultation Paper has prompted a useful and focused discussion about this concept.

Overall, we consider that the concept of materiality is clearly understood and consistently applied in the context of IFRS-based financial reporting. However materiality needs to be a single concept that can be applied globally. Likewise, any guidance on materiality must have the potential to be consistently adopted in all jurisdictions in which we operate. Therefore if the discussions arising from the Consultation Paper highlight potential areas for improvement, it is our view that any future development in this area should be the responsibility of the International Accounting Standards Board (IASB).

These overall comments are supported by individual responses to the questions in the Consultation Paper as set-out below.

Q1: Do you think that the concept of materiality is clearly and consistently understood and applied in practise by preparers, auditors, users and accounting enforcers or do you feel more clarification is required?

We recognise that decisions about materiality require judgement and necessarily relate to entity-specific facts and circumstances. That said, when preparing our financial reports, we assess materiality in accordance with IFRS, statutory and other regulatory requirements. In particular, we consider materiality when assessing the impact of current and prior year omissions and misstatements on our financial statements and related disclosures. In this context we consider that the concept of materiality is clear and understandable and consistently applied within our financial report and across periods.



One area where further debate may be warranted is in relation to disclosure overload. Removing immaterial disclosures has proven to be difficult in practice and in this regard we support recent projects that seek to develop a Disclosure Framework (e.g. EFRAG and FASB). We would urge the IASB and ESMA to consider the output of these projects.

Q2: Do you think ESMA should issue guidance in this regard?

As indicated above, we consider that, the concept of materiality is clearly and consistently understood and applied and therefore, for the most part, further guidance is not needed. As a result, we do not think ESMA should issue guidance in this regard.

However we do support the development of a Disclosure Framework. In our view this should ultimately be issued by the IASB representing a global approach to disclosures. We think ESMA and other regulators should input into this development via the relevant due process.

Q3: In your opinion, are ‘economic decisions made by users’ the same as users making ‘decisions about providing resources to the entity’? Please explain your rationale and if possible provide examples.

An important aspect of these definitions is what is meant by the term ‘user’ (see our response to Question 4). In our view, applying the objective of general purpose financial reporting in the Conceptual Framework for Financial Reporting, the term ‘users’ in IFRS means primary users e.g. existing and potential investors, lenders and other creditors. By their nature, these users have or will provide resources to the reporting entity. As such economic decisions made by primary users (in that capacity) will either directly or indirectly relate to the provision of resources. Therefore in our opinion ‘economic decisions made by users’, in the context of IFRS, has the same meaning as users making decisions about providing resources to the entity.

Q4: Is it your understanding that the primary user constituency of general purpose financial reports as defined by the IASB in paragraph 13 includes those users as outlined in paragraph 16 above? Please explain your rationale and if possible provide further examples.

In paragraph 16 of the Consultation Paper you list the following primary users:

- existing and potential investors;
- existing and potential lenders and other creditors; and
- present and past employees.

We agree that the above constituents are primary users for the purposes of IFRS and we cannot think of other primary users that would fall outside one of these broad categories. We agree with the view, as embodied in the Conceptual Framework, that financial reporting should be to provide useful information to these primary users. That does not mean that we think financial reports cannot provide useful information to other users, but that the preparation of financial reports should have a clearly defined audience with one clear objective.

We note that the list in paragraph 16 of the Consultation Paper could be seen as limiting the types of information that is relevant to particular users. Information that is useful to a user would be virtually unlimited and therefore there seems little point in defining it using an exhaustive list of examples.



Q5a: Do you agree that the IASB's use of the word 'could' as opposed to, for example, 'would' implies a lower materiality threshold? Please explain your rationale in this regard.

A decision about materiality requires the preparer to put itself "in the shoes" of a user. It would be generally impracticable to substantiate whether an omission or misstatement *would* influence a user's economic decision. This is because the preparer is using its own judgement to determine how an investor would or would not be influenced by a future presentation or disclosure item. We consider that the term 'could' takes into account the nature of this hypothetical decision and make the definition of materiality workable rather than necessarily implying a higher or lower threshold.

Q5b: In your opinion, could the inclusion of the expression 'reasonably be expected to' as per the Auditing Standards, lead to a different assessment of materiality for auditing purposes than that used for financial reporting purposes. Have you seen any instances of this in practice?

Not applicable.

Q6a: Do you agree that the quantitative analysis of the materiality of an item should not be determined solely by a simple quantitative comparison to primary statement totals such as profit for the period or statement of financial position totals and that the individual line item in the primary statement to which the item is included should be assessed when determining the materiality of the item in question? Please explain your rationale in this regard.

We agree that the quantitative analysis of materiality of an item should not be determined solely by a simple quantitative comparison to primary statement totals. We also agree that the individual line item in the primary statement in which the item is included should also be assessed as well as the impact on any related footnote or other disclosures.

Q6b: Do you agree that each of the examples provided in paragraph 21 a – e above constitute instances where the quantitative materiality threshold may be lower? Are there other instances which might be cited as examples? Please explain your rationale.

We consider that an item can be material from either a quantitative or qualitative perspective or both. In our view a materiality 'threshold' is the line between whether an item is or isn't material. We agree that the transactions listed in paragraph 22 of the Consultation Paper have special characteristics that often make them material from a qualitative perspective. However we do not think these characteristics alone would merit a lower materiality threshold. For example although it may be necessary to consider whether there is something relevant about a transaction with a related party e.g. did an error arise because of the influence an entity has over one of its associates, we do not consider that all transactions with related parties are material per se.

However where an item is material primarily based on qualitative factors, we do not consider that it has a lower level of materiality. The qualitative aspects of these transactions may make information about them relevant to users, and make the quantitative assessment less likely to be considered separately.

As set-out in our response to Question 4, it would be impossible to create an exhaustive list of examples, since often materiality, in terms of both qualitative and quantitative assessments, depends on facts and circumstances that are neither static nor definable.



Q7: Do you agree that preparers of financial reports should assess the impact of all misstatements and omissions, including those that arose in earlier periods and are of continued applicability in the current period, in determining materiality decisions. Please explain your views in this regard.

See our response to Question 8 below.

Q8: Do you agree that preparers of financial reports should assess the impact of all misstatements and omissions as referred to in paragraphs 23 to 26 above in determining materiality? Please explain your views in this regard and provide practical examples, if applicable.

As stated in our response to Question 1, an assessment of materiality requires judgement and takes into account the particular facts and circumstances of the preparer. Determining whether a misstatement or omission is material requires an assessment of a range of information (both quantitative and qualitative). We do not see the relevance of guidance in the form of a definitive list.

Q9a: Do you believe that an accounting policy disclosing the materiality judgments exercised by preparers should be provided in the financial statements?

Q9b: If so, please provide an outline of the nature of such disclosures.

Q9c: In either case, please explain your rationale in this regard.

Materiality judgements are generally considered on an individual transaction basis or in relation to a group of similar or related transactions. The assessment can relate to an error, misstatement or omission. As a result the factors considered (quantitative and qualitative) can be extremely varied. Therefore a specific accounting policy disclosure about materiality would either be very general (i.e. boiler-plate) or overwhelmingly detailed (i.e. provides information on immaterial items and/or individual items). Neither level of disclosure would provide useful information to users of financial statements. In addition we feel that any disclosure would focus on the quantitative thresholds, which we have previously mentioned are often only part of an assessment of materiality.

Further we question whether users would find an accounting policy on materiality useful. We agree that users need assurance that financial statements are materially correct, but this should not be addressed by providing the user with information on materiality assessments in the form an accounting policy note. Users' assurance over the material accuracy of financial statements is provided by the internal and external (audit and regulatory) governance of an entity.



Q10: Do you agree that omitting required notes giving additional information about a material line item in the financial statements constitutes a misstatement? Please explain your rationale in this regard.

Whether omitting a required note about a material line item constitutes a misstatement depends on whether the additional information being provided by the note is itself material. If an entity assesses that information the disclosure provides is not relevant to users (i.e. it is not material) then the entity should not be required make a disclosure as set-out in an IFRS. This would be the case whether the line item to which the disclosure relates is material, although materiality assessments of the line item and disclosure would commonly align.

For example an industrial company may have a significant balance of customer receivables. These are financial assets under IFRS 7 “Financial Instruments: Disclosures”. It does not necessarily mean that all the disclosures related to financial assets are as relevant to users of that entity’s financial statements, as they would be for a financial institution.

Q11: Do you believe that in determining the materiality applying to notes which do not relate directly to financial statement items but are nonetheless of significance for the overall assessment of the financial statements of a reporting entity:

- (a) the same considerations apply as in determining the materiality applying to items which relate directly to financial statement items; or**
- (b) different considerations apply; and**
- (c) if different considerations apply, please outline those different considerations.**

The same considerations should apply.

Q12: In your opinion, how would the materiality assessment as it applies to interim financial reports differ from the materiality assessment as it applies to annual financial reports?

It should not change. The only difference is that the assessment of what is materiality (in terms of recognition and disclosure) needs to be considered in the context of the specific guidance in IAS 34 “Interim Financial Reporting”. The focus is on updating information at year-end, rather than providing financial statements on a stand-alone basis.

If you would like to discuss any aspect of our response in further detail, please do not hesitate to contact me on +49(69)910-31183 or at karin.dohm@db.com.

Yours faithfully

Karin Dohm
Chief Accounting Officer