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Date
30 March 2012

Re
Consultation paper
Considerations of materi-
ality in financial reporting

Our ref
KvH

Attachment

Direct dial nr
020-3010399

Dear Sir/Madam,

The NBA¹ appreciates the opportunity to comment on the ESMA Consultation Paper "Considerations of materiality in financial reporting". Please find enclosed our comments 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?

In our opinion, the concept of materiality is not clearly and consistently understood by the various parties involved. It should be noted that for different purposes different materiality could be used or different materiality levels can apply. However, all parties involved should have the same understanding of the concept of materiality. More clarification could be useful. The concept of materiality is described in the financial reporting framework. Judgment is important and the interpretation depends upon the specific context/situation. Therefore only general instructions can be given.

It would be useful to have more information from the users about what influences their materiality.

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

We consider it more appropriate for standard setters such as the IASB to issue guidance. The ESMA could issue a policy statement regarding their role of supervision of this issue.

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.

There could be some differences. If resources relate to capital and labor, this is more limited than making economic decisions. Investors can buy shares on the stock market which does not generate resources for the entity. Consumers –which can be users- buy products, but do not generate capital resources for 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.

It is our understanding that the primary user constituency of general purpose financial reports as defined by the IASB includes the users outlined in paragraph 16. The types of decisions described in paragraph 16 seem to be the type of decisions that should be supported by the financial statements. The focus should be on the primary users and their information needs in order to avoid an excess of information.

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¹ The Dutch Professional Accountancy Association (Dutch acronym: NBA) is an alliance between NIVRA and NOVAA

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.

We are not native speakers, but we got the feeling that 'could' implies a lower materiality 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?

No, the IASB also uses the expression 'reasonably be expected to' in IAS 24 paragraph 19. Furthermore, in practice there will be no differences. As both the preparer as well as the auditor should focus on a comparable user group, in principle there should be no important differences.

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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 with the first part of the question. Professional judgment and qualitative factors play an important role in this regard. We do not agree that the individual line item should always be assessed when determining the materiality of the item in question. The primary focus of the financial statements is the overall fair presentation and not the fair presentation of all individual line items therefore not all individual line items need to be assessed when determining the materiality.

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

We would like to mention first that the examples can never be exhaustive and might not be relevant in all situations and therefore should not be regarded as absolute. We agree with the examples provided. However, in the examples disclosures are missing. For example, disclosures regarding the performance of significant new activities, significant risks and assumptions related to estimations.

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.

In principle we agree. If the misstatements still have an impact on the current period, they should be taken into account unless they are clearly insignificant.

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.

We agree:

- An item that may not be material in one financial reporting period could become material in another and vice versa.
- Immaterial errors that are used to achieve a particular presentation should be corrected.
- Immaterial misstatements or omissions should be aggregated.
- The set-off of compensating error amounts does not necessarily render material misstatements immaterial.

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.

We believe that such a disclosure might be misunderstood or could lead to confusion by the users and as a result might lead to incorrect decision making by primary users. We are not per se against greater transparency regarding materiality, but feel that the impact on decision making should be investigated by academics before implementing new disclosure requirements. Further the internal assessment process might be difficult to explain externally and would lead to questions and discussions.

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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.

This does not necessarily always constitute a misstatement. The importance of the information element should be judged in the overall context.

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.*

In principle the same considerations apply (option A), but we also believe that qualitative aspects are more important in assessing materiality applying to notes. This is not very different from determining materiality to notes which do relate directly to financial statement items. However, we wonder why a different terminology (significance) is used.

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?

We refer to IAS 34 and paragraph 31 in the consultation. In general, the materiality for interim financial reports would be higher. Interim reports are shorter, more comprehensive and may rely on estimates to a greater extent than annual reports. Further interim reports have a different purpose than annual reports and have a lower level of accuracy. This will have an impact on materiality.

Closing remarks

We trust to have informed you sufficiently. If you have any questions, please do not hesitate to contact Karin van Hulsen – k.vanhulsen@nba.nl
Yours sincerely,

NBA
Dutch Ethics & Assurance Standards Board

SIGNED BY:

Prof. dr. Peter W.A. Eimers RA
Chairman

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The logo for the Nederlandse Beroepsorganisatie van Accountants (NBA) features a thick horizontal grey bar above the letters 'NBA' in a large, bold, sans-serif font.