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Secretary
Financial Reporting Council
c/ The Treasury
Langton Crescent
PARKES ACT 2600

31 July 2012

Dear Madam

Re: MANAGING COMPLEXITY IN FINANCIAL REPORTING

Deloitte is pleased to provide the Financial Reporting Council (FRC) our comments on the FRC's report "Managing Complexity in Financial Reporting" (the Report). Our detailed comments have been presented on a basis consistent with your request, however we would like to open our comments with some general observations.

In its discussion of the sources of reporting complexity the FRC rightly notes that the current regulatory framework is not optimal and has identified that many regulators, in Australia and elsewhere, sometimes require General Purpose Financial Reporting for entities or circumstances for which such reports were not created. This is consistent with our comments in our letter of 13 October 2011 to the FRC Reducing Complexity Taskforce. Further, the Report cites a KPMG report as finding some 41% of Australian businesses nominated 'rules and regulation changes' as the biggest driver of rising business complexity in the past two years.

If real progress is to be made in managing complexity in financial reporting in Australia an essential first step is a comprehensive review of who reports what - in other words a review of the requirements and application of the differential financial reporting framework. To achieve progress in this area will require robust debate among many stakeholders.

We note the Australian Accounting Standards Board is currently undertaking a research project on differential reporting and we believe that the progression of this project should act as an initiator for a broader public debate on this subject. We encourage the FRC to seize this opportunity to create a practical, meaningful financial reporting framework that is responsive and relevant to the needs of the various users of financial statements whilst acknowledging that one size does not fit all.

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We also note that the Report does not explicitly address whether its observations and strategies are focused at publicly accountable entities (i.e. mainly listed entities) alone or at all entities. Whilst some observations appear to have broader implications, such as the need to urge the IASB to undertake reforms, it appears that other observations and suggested strategies are more focused on those entities that are publicly accountable, for example the discussion on presentation of results, possible impacts arising from developments in Integrated Reporting and the ability to use information technology to deliver information to the end user. The development of practical solutions and strategies to reduce complexity in financial reporting requires clear delineation between the various categories of reporting entity as what is suitable to a large listed company may not be appropriate to a small charitable organisation or a large government agency.

We believe that the Task Force's efforts are better served in concentrating on strategies to reduce this complexity. In the interest of key stakeholders, the primary objective should still be to improve the effectiveness of financial reporting and thus reduce the complexity. We do not believe that by *managing* the complexity in the short term we will alleviate many of the concerns expressed by users or preparers of financial reports. In order to achieved this and bring about change, we strongly encourage the Task Force to further stimulate debate and support the AASB in its calls for the IASB to establish a framework for presentation and disclosure.

Additional sources of reporting complexity

Pursuant to the Corporations Act 2001, accounting standards have the force of law. Consequently, regulators in enforcing their interpretation of the law can (and do) influence the behaviour of both preparers of financial statements and their auditors. In reacting to the regulators' actions, preparers and auditors more often than not lean towards providing more disclosure rather than applying judgement to determine whether such disclosure is appropriate for the information needs of the report's users. It is the absence of an adequate framework to allow preparers to use their judgement to determine the relevance of disclosures, especially when reacting to the regulators' focus areas, which contributes to the overload of irrelevant and boilerplate disclosures. It is the existence of such disclosures, and the multiple pages thereof, which often in practice result in criticism of the unnecessary complexity of today's financial statements.

Hence it is important that the IASB and influential regulatory bodies acknowledge and provide a framework which allows for preparers to adopt judgement (and the use of materiality with respect to disclosures) and to better tailor their disclosures and financial reports to the needs of their users. Not all disclosures will be relevant, or of equal importance across organisations and this will allow preparers to focus on the more relevant disclosures and in turn, deliver a more meaningful financial report to its users.

We note that the International Auditing and Assurance Standards Board (IAASB) have responded to this matter and have undertaken a project to explore the issues and concerns around the audit of disclosures. The objective of this initiative is to assist the IAASB to gain a robust understanding of the views and perspectives on issues relevant to auditing disclosures in a financial statement audit.

Complexity is inevitable in the short term

As we noted in our letter of 13 October 2011, we believe that complexity in financial reporting reflects numerous factors which we categorised as those arising from the environment in which business is conducted; those arising as a result of the internal entity structure itself; and those arising from the accounting setting and regulatory environment. We see no reason why those factors creating complexity in financial reporting arising from the business environment in which an entity operates or from the entity structure itself will dissipate, and, therefore, we believe that efforts to manage complexity in financial reporting should be driven by consideration of the accounting standard framework to be applied and the regulatory framework to which the entity is subject.

Strategies to better manage complexity

As commented above, we believe that the first strategy to manage complexity is to clarify the information reporting requirements of entities. Complex businesses will inevitably create complex reporting. However, we would like to comment on some of the strategies suggested by the Task Force.

Make better use of developments in information technology and delivery

Although the use of technology may assist in the delivery of information, for example, reducing the physical volume of financial reports by allowing some of the information such as governance and accounting policies, to be contained on the organisation's website, it does not reduce the sheer volume of information that needs to be prepared. The "unbundling" of the Annual Report to allow users to filter information merely provides an alternative method of delivery and may not actually improve the *quality* of information provided to users.

Address the legal impediments to preparers determining relevant material disclosures

We agree with the Task Force's comment that the challenge is to find a "*mechanism that encourages directors and preparers to properly consider whether or not a disclosure is material, rather than the simple option of including all disclosures*". We also agree that a key strategy would be to better educate directors, preparers and the Australian Securities and Investments Commission (ASIC) on the concept of materiality relating to financial statement disclosures, which may assist in the reduction of boilerplate financial disclosures. We note that the IASB is increasing its focus on its role as educator in financial reporting in the international environment and we support and will continue to support similar initiatives being undertaken by the AASB in Australia.

Empower users through the delivery of financial information via XBRL

While the adoption of XBRL may offer the potential to provide users with the ability to more readily extract and use information, by allowing users to manage, arrange and compare data, we feel that the success of this method as a short term management strategy will be hindered by adoption (or lack of) and acceptance of this method on a widespread basis in Australia. We believe that for a strategy to empower users through delivery of financial information via XBRL to be successful a policy of regulator intervention to require mandatory use of XBRL will be required. Any such move towards mandatory implementation should be made in consultation with both preparers and users of financial information.

Develop guidelines that encourage more use of financial reporting terms and definitions

We agree with the Task Force's comment that there is no value in constraining the use of relevant industry-specific financial or non-financial information and we believe that over time there will be continued emergence of industry specific reporting terms and usage in particular industry segments. We also believe that future developments in projects such as Integrated Reporting and Service Performance reporting will underpin the development of such reporting terminologies.

We do however have reservations over the development of glossaries of financial reporting terms as in our experience they can be time consuming and cumbersome to develop and are frequently at risk of becoming obsolete relatively quickly. We recommend that if the FRC is to consider this strategy further it consults with industry groups to ascertain their experience. For example we are aware that the Property Council of Australia has carried out research projects in this area.

Urge the IASB to undertake reforms

We endorse the FRC's comments for the IASB to establish a framework for presentation and disclosure and progress the accounting for total income and the differentiation between net income in the Income Statement and Other Comprehensive Income. We note the continued quality of the AASB's responses to the IASB, those of the professional accounting bodies, the large professional accounting firms and the continued involvement in the comment letter process and outreach organisations of Australian corporate entities, whether participating directly or through Australian or global industry forums. The Australian business community continues to be an active participator in the international accounting standard setting arena and we believe that this legacy of active standard setting participation can and should continue. We do not believe that any specific action is required of the FRC in this respect.

Consider better ways of influencing the IASB

We concur with the comments made in the Report about the growing importance of the regional accounting standard setting groups and consider that it is vital that the AASB continues its efforts in this area.

We also note that Jeffrey Lucy's appointment as an IFRS Foundation Trustee ends in December 2013 and those of Charles Macek and Judith Downes as members of the IFRS Advisory Council end in December 2014 and December 2012 respectively. We encourage the FRC to ensure that suitable replacements to these appointments are made.

Q4. Suggestions for Financial Reporting terms and definitions that should be encouraged for development

Financial reporting terminology contained within the International Financial Reporting Standards should be sufficient. It is not clear from the Report how the FRC envisages such glossaries. Please refer to our comments above with respect to the use of financial reporting terms and definitions.

Q.5 Quick wins which could be achieved in the current Australian legislative framework

We believe that in the long run the quick win will be a timely and comprehensive review of the requirements and application of a robust differential reporting framework.

Q.6 Any other issues

None noted.

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We thank you for the opportunity to continue to contribute to this very important debate. Please do not hesitate to contact Anna Crawford on 02 9322 7177 if you would like to discuss any of the matters raised in this letter further.

Yours faithfully

Anna Crawford
Partner
Deloitte Touche Tohmatsu