Five Steps to Simplifying Financial Statements — Today

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FINANCIAL REPORTING

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What's the Big Picture? —Executive Summary

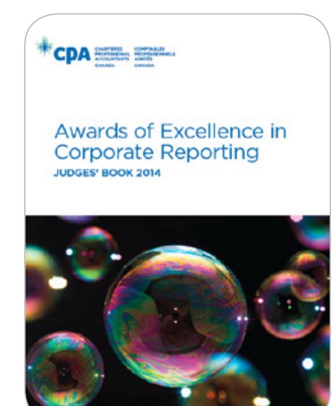
This publication sets out a principled five-step approach to simplifying financial statements by reducing disclosure overload and streamlining disclosure while achieving both more effective communication and full compliance with the intent of disclosure requirements.

These steps can be taken *now* by management, with reference to the standards and requirements currently in place. They provide an opportunity to add immediate value to an entity's financial statements, without requiring significant investments of money, time or resources.

The five steps, described in more detail on the following pages, are:

1. MAKE FINANCIAL REPORTING A STRATEGIC MATTER
2. FOCUS ON MATERIALITY
3. REFINE FORMATTING AND PRESENTATION
4. APPLY A TRULY CONDENSED APPROACH TO INTERIM REPORTING
5. KEEP LOOKING AHEAD

To provide practical assistance in moving through these steps, Appendix A sets out 20 questions management may want to ask. These question aim to assist management in developing and implementing a plan to simplify their financial statements.



Many examples used in this publication were taken from actual financial statements of Canadian entities, some of which were the recipients of CPA Canada's 2014 Awards of Excellence in Corporate Reporting — a program that showcases some of the best corporate reporting models in Canada.

To learn more about the CPA Canada Awards of Excellence in Corporate Reporting and to view a list of winners in a range of categories, visit www.cpacanada.ca/CRawards.

Disclosure Overload —Is It Today's Reality?

The term "disclosure overload" has been defined in various ways. These definitions typically reference the growing volume and increased complexity of financial statement disclosures, which are perceived to inhibit a user's ability to identify and understand the most important information.

Although different commentators might express their concerns about disclosure overload in different ways, they share a common theme: in one way or another, the volume of information contained in financial statements and the way the information is presented are often counterproductive. Although each individual item contained in the notes to the financial statements may, in theory, help a user understand those statements, the value of the item is often lost in the volume of information as a whole.

Some users and preparers of financial information argue that, over time, financial reporting has become a burdensome compliance exercise of decreasing relevance to investors. Simply put, many stakeholders feel financial statements are too long, confuse rather than inform, obscure relevant information and can result in undue cost to preparers.

Some financial statement users and preparers argue that, over time, financial reporting has become a burdensome compliance exercise of decreasing relevance to investors. Simply put, many stakeholders believe financial statements are too long, confuse rather than inform, obscure important information and result in undue cost to preparers.

In part, this criticism probably reflects constraints on time and resources: users with sufficient skill and knowledge to understand what is disclosed lack the time to do so. As such, disclosure overload might contribute to suboptimal investing decisions because it can result in a failure by investors to understand important information.

Many companies, regulators and auditors are perceived as having a "checklist mentality" towards financial reporting, creating the urge to provide each and every disclosure mentioned in IFRS.

For a specific entity, this might result in some or all of the following:

- **Immaterial disclosure:** disclosing immaterial information makes it difficult for users to easily identify information important to their decision making
- **Ineffective formatting and design:** poor formatting or design makes it difficult for users to locate or piece together information important to their decision making
- **Boilerplate disclosure:** boilerplate or generic wording makes it difficult for users to understand the entity's specific circumstances
- **Static financial reporting processes:** merely updating information and not eliminating, condensing or improving previous disclosures.

Management of some entities are likely aware that their disclosures reflect some or all of these weaknesses, but prefer this to bearing the perceived regulatory and legal risks of perhaps disclosing too little.

To the extent a problem exists, it is not caused solely by management. The public pronouncements of standard setters may be interpreted (rightly or wrongly) as promoting adherence to the letter of disclosure requirements, without regard for specific circumstances. Auditors may also foster this impression. Even though accounting standards are subject to the overriding concept of materiality, the very fact that standard setters include such extensive disclosure requirements in the various standards may seem to imply that the safest approach is to treat those requirements as a checklist.

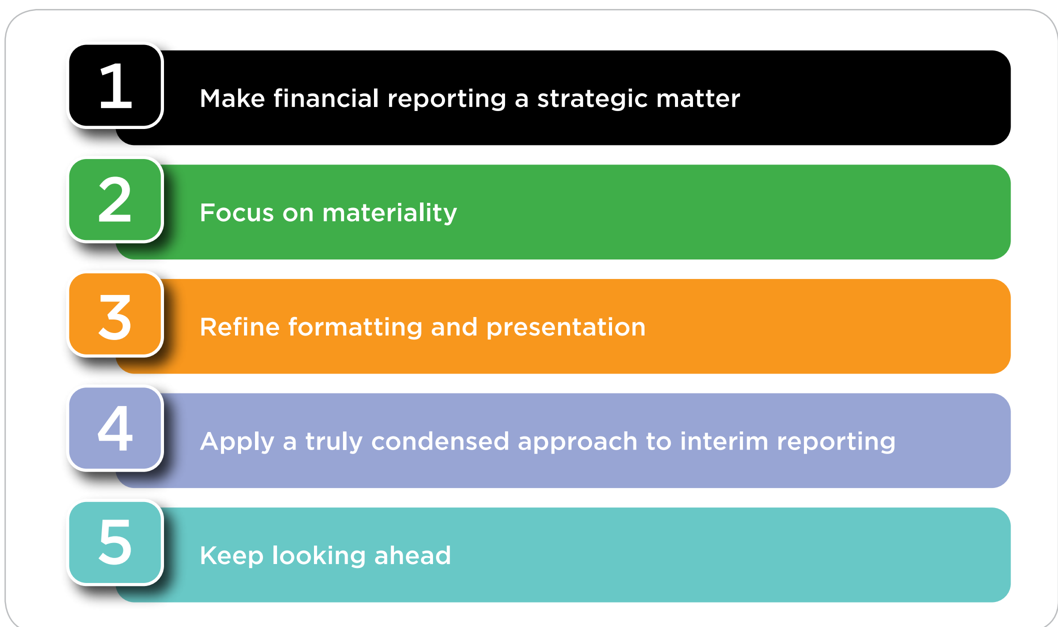
Regulators, auditors and standard setters are all aware of the growing concern over disclosure overload and are considering their response to it. However, financial statements are the responsibility of management and therefore management has the authority and motivation to begin the process of simplifying its financial statements today.

What Are the Five Steps to Simplifying Financial Statements?

This publication sets out a principled five-step approach to simplifying financial statements by reducing disclosure overload and streamlining disclosure while achieving both more effective communication and full compliance with the intent of disclosure requirements.

These steps can be taken *now* by management, with reference to the standards and requirements currently in place. They provide an opportunity to add immediate value to an entity's financial statements, without requiring significant investments of money, time or resources.

The five steps are identified in the illustration below.



Many parties, with an interest in effective financial reporting, have made suggestions on how disclosure overload might be addressed by changes to standards, regulatory actions or other means outside the control of financial statement preparers. This publication focuses, however, on steps that can be taken now by management using today's standards and requirements.

In addition, this publication focuses on actions that can be taken quickly to add immediate value to an entity's financial statements. The suggestions in this publication should generally not require significant investments of money, time or resources. They do, however, require a modest collective determination on the part of those involved in an entity's financial reporting process.

Step 1 — Make Financial Reporting a Strategic Matter

Strategy for Informing Users

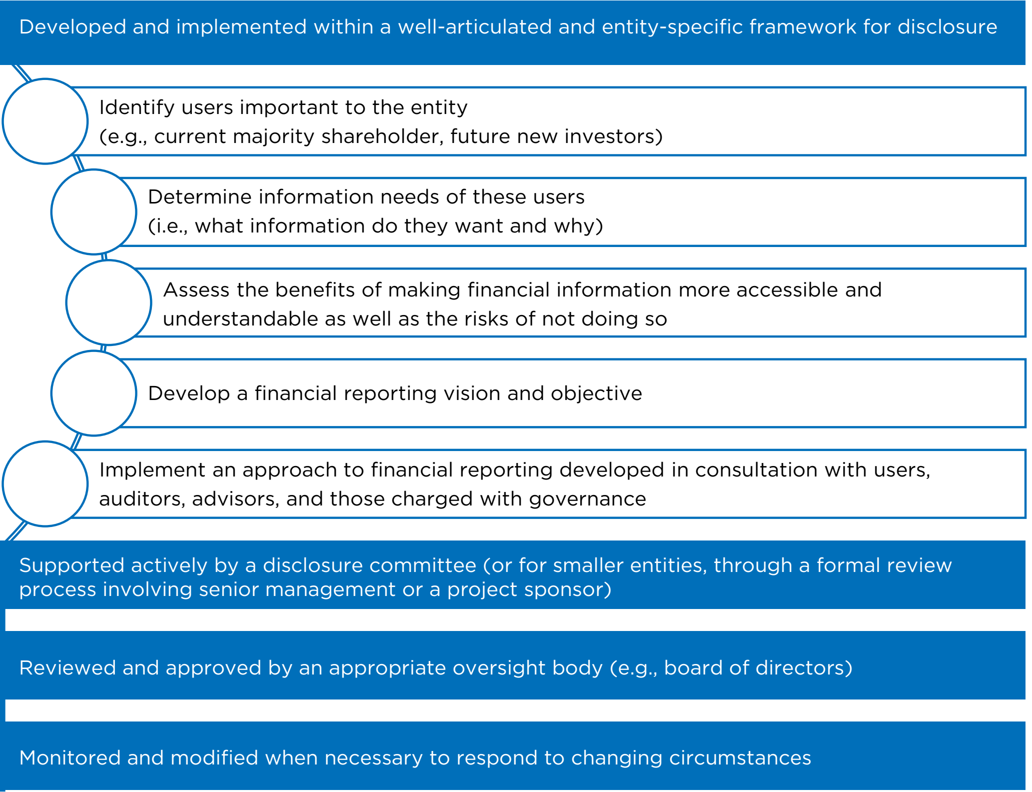
When financial reporting is perceived as a strategic matter, steps can be taken to integrate financial reporting into strategy.

Good financial reporting benefits both the users and preparers of the information and is most effective when it responds to user needs. These needs vary from entity to entity in line with their objectives and strategies.

A good strategy for informing users includes an entity-specific disclosure strategy. Optimum disclosure practices depend on the particular entity's stage of development, nature of operations, transactions, financial position, expectations based on the disclosure practices of competitors (in Canada or internationally), the particular demands of users, and on a range of other matters (e.g., a desire to attract investors, to be seen as transparent, willingness to go beyond minimum requirements, etc.).

When developing a disclosure strategy, consideration of the points in the table below is suggested.

Table — Disclosure Strategy Considerations



An entity's disclosures will be most effective if users have been consulted about their needs.

When an entity chooses to disclose different information than its competitors it would benefit users to have an explanation of the entity's approach to disclosure, generally outside the financial statements, such as within the Management Discussion and Analysis (MD&A).

In some cases, consultation with users coupled with an internal assessment might suggest a need for *more* disclosure in some areas—although this will often relate to information to be provided in the MD&A rather than in the financial statements. In other cases, however, focusing on user needs may result in financial statements that contain less, rather than more, disclosure (see "Focus on Materiality" below). In all cases, management's conclusions should be tested against the expectations of regulators and discussed thoroughly with auditors to avoid the risk of time-consuming disagreements about disclosure at a late stage in the audit process.

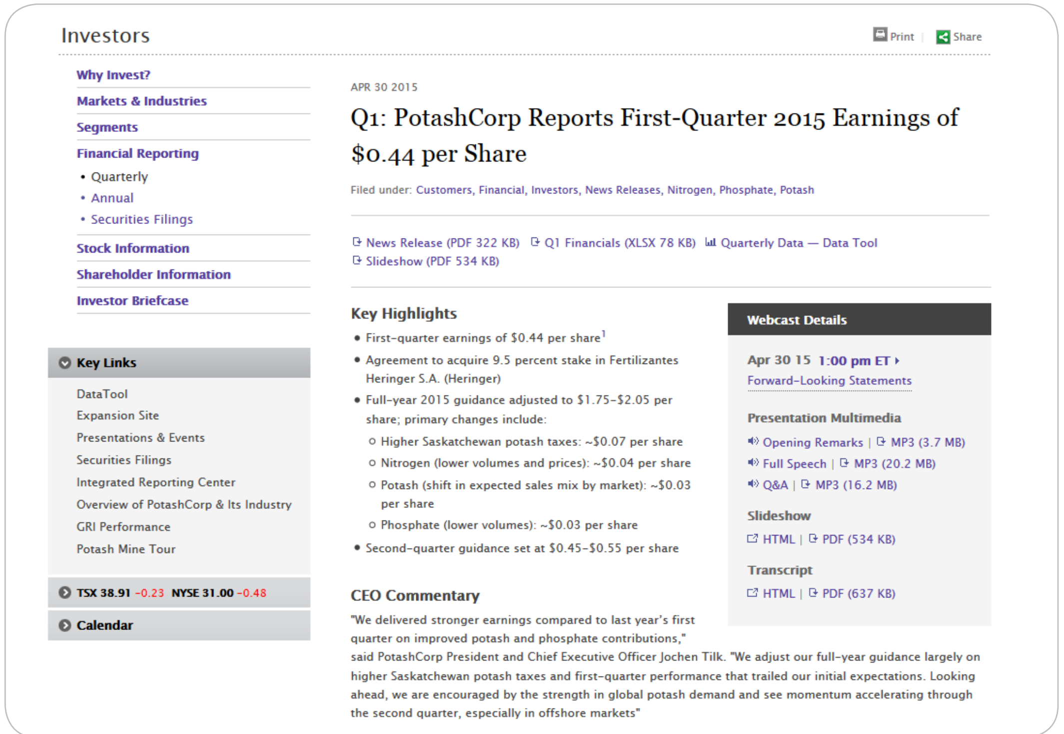
Strategy for Using Technology

In addition to complying with regulatory requirements by posting financial statements on SEDAR and providing them to investors, it is critical to consider other ways to meet an entity's disclosure objectives.

Any assessment of financial reporting strategy should include an analysis of how the entity uses technology to assist users. Although, many entities already include financial statements and supplementary information on their websites and use technology, in some form, to assist users in obtaining and understanding important financial information, the use of technology is nevertheless underutilized.

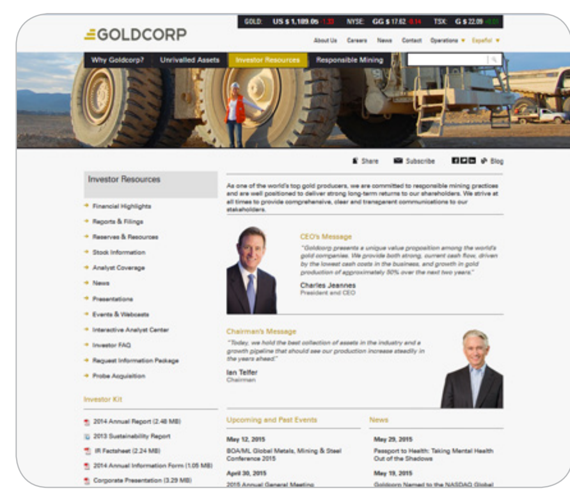
For instance, the use of enhanced document search features, filters, drop-down menus, hyperlinks (including a linked table of contents and cross referenced notes) as well as the ability to download selected portions of the financial statements can significantly enhance a user's interest and make identifying and understanding important information much easier.

As illustrated below, the website of Potash Corporation of Saskatchewan Inc. allows easy navigation between related documents and other materials. For example, it supplements a quarterly earnings release with links to the full financial report, to recordings, slideshows and transcripts of the related webcast, and to other data tools. At the same time, a broader menu offers links to materials addressing other financial periods and to other relevant information. Many other formats are possible, of course.



Source: www.potashcorp.com

To view another example of a good use of technology, visit www.goldcorp.com. In 2014, Goldcorp Inc. was recognized by CPA Canada for producing high-quality electronic disclosure at the CPA Canada Awards of Excellence in Corporate Reporting. The judges applauded the company for posting a video from its annual general meeting on YouTube and commended the company's blog for helping users better understand company activity. Goldcorp's website also received high marks for its easy navigation and general usability.



Source: www.goldcorp.com

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Step 2 — Focus on Materiality

Materiality plays a significant role in the preparation of financial statements. However, this concept is not always applied effectively, resulting in the inclusion of immaterial information in the financial statements. For example, it is often perceived that many companies, regulators and auditors use a "checklist mentality" towards financial reporting, creating the urge to provide each and every disclosure mentioned in IFRS.

Materiality plays a significant role in the preparation of financial statements. However, this concept is not always applied effectively, resulting in the inclusion of immaterial information in the financial statements.

Information is material if omitting it or misstating it could influence economic decisions made by users relying on financial information disclosed in the financial statements. In other words, materiality is entity-specific and is a function of the nature or magnitude of the items to which the information relates in the context of an individual entity's financial statements.

When determining whether an item is material, both qualitative and quantitative factors should be considered.

As discussed in Step 1, an assessment of what might influence the economic decisions of users is part of this process. Management also considers the input of auditors and others (e.g., lawyers etc.) on what is material in a particular situation.

As part of its effort to address concerns about disclosure overload, the International Accounting Standards Board (IASB) clarified in 2014 that:[1]

- Important information should *not* be obscured by aggregating information or by providing immaterial information.
- Materiality considerations apply to *all* parts of the financial statements, including the notes.
- Even when a standard requires a specific disclosure, materiality considerations *do* apply and therefore it may not be necessary, in certain circumstances, to make a specific disclosure.

The above points are articulated well by the Chairman of the IASB, Hans Hoogervorst, in a speech entitled "Breaking the Boilerplate."[2] The following are some quotations from the speech:

1 In December 2014, the IASB completed the first step in its Disclosure Initiative with the publication of *Disclosure Initiative (Amendments to IAS 1)*. The narrow-focus amendments to IAS 1 *Presentation of Financial Statements* clarify, rather than significantly change, existing IAS 1 requirements.

2 Refer to the June 27, 2013 **speech "Breaking the Boilerplate" by Hans Hoogervorst**.

- “the materiality principle does not only mean that material items should be included, but also that it can be better to exclude nonmaterial disclosures. Too much detail can make the material information more difficult to understand—so companies should proactively reduce the clutter! In other words, less is often more.”
- “a materiality assessment applies to the whole of the financial statements, including the notes. Many think that items that do not make it onto the face of primary financial statements as a line item need to be disclosed in the notes, just to be sure. We will have to make clear that this is not the case. If an item is not material, it does not need to be disclosed anywhere at all in the financial statements.”
- “if a Standard is relevant to the financial statements of an entity, it does not automatically follow that every disclosure requirement in that Standard will provide material information. Instead, each disclosure will have to be judged individually for materiality.”

The following table discusses some examples of how to apply the notion of materiality more rigorously.

Accounting Policies		
	Identify Only Relevant Significant Accounting Policies	• Disclose only significant accounting policies relevant to understanding the financial statements. • Do not disclose accounting policies irrelevant to current or comparative period activities, even if they might become relevant in the future. • For example, if the entity, in the current and comparative period, did not have joint arrangements, the inclusion of an accounting policy on such arrangements is not relevant. Similarly, if an entity’s financial assets, in the current and comparative period, are all classified as loans and receivables, then there is little value in describing the recognition and measurement policies for other categories of financial assets that existed in the past or might exist in the future.
	Avoid Boilerplate Disclosure	• The most useful disclosures are tailored, entity-specific, and go beyond repetition of the requirements in the standards. • A user of financial statements should be able to understand how the policy is applied in the entity’s circumstances. • IAS 1 notes that disclosing accounting policies selected from alternatives allowed in IFRS is especially useful to users. Often, however, an entity’s accounting policy disclosures only confirm that it applies the basic requirements of the relevant standards. In such cases, a boilerplate description of how the standard works provides little value to users (such information is readily available from a variety of sources). Entities might discuss with their auditors and advisors how such content could be reduced to an acceptable amount.

Section	Topic	Guidance
Accounting Policies	**Discuss Applicable Future Changes**	• When an entity has not adopted a new standard or interpretation that has been issued but not yet in effect, IFRS require the entity to disclose known or reasonably estimable information about the possible impact that application will have on the financial statements. • If the impact of the new standard or interpretation is not material or its scope is not relevant to the entity, discussion of such pronouncements may unnecessarily add to the volume of disclosures.
Judgments and Estimates	**Tailor Disclosures about Significant Judgments and Estimates**	• IFRS require disclosure of management's judgments and estimates made in the process of applying the entity's accounting policies that have the *most significant effect* on the amounts recognized in the financial statements. Such disclosure enables users to better understand how the accounting policies are applied and to make comparisons among entities. • Discussion of significant judgments and estimates should be limited to those having a material impact on the financial statements and tailored to entity-specific facts and circumstances. • Canadian securities regulators have commented on several occasions that disclosures of significant judgments and estimates are often made in boilerplate statements and/or for matters that are not significant or do not involve sufficient uncertainty. These disclosures often reiterate significant accounting policies without actually describing (in a tailored, entity-specific context) the specific judgment or the assumptions underlying the estimates. • The objective of disclosing sources of estimation uncertainty is to focus users' attention on assets or liabilities that carry a significant risk of being adjusted within the next financial year (i.e., because of the inherent uncertainty of making assumptions about the future). For example, although the process of valuing equity-settled stock options issued to employees usually involves significant estimation by its nature, this does not generally result in assets or liabilities with a significant risk of being adjusted. Consequently, the role of estimates in this area can sometimes be adequately conveyed in the summary of accounting policies or other note disclosures and does not automatically need to be further highlighted as a source of estimation uncertainty. • Only the judgments that have the most significant effect on the amounts recognized in the financial statements need to be emphasized. For example, when using price times quantity (i.e., P × Q) to measure the value of a single common share traded in an active market, the relevance of judgment and estimates is often limited because the price per unit is observable and the quantity of units is confirmable. Even though the fair value may fluctuate and result in adjustments to the financial statements in the future, the adjustments are not the result of significant management judgment or estimation uncertainty.[3]

3 In 2014, the IASB published for public comment an Exposure Draft detailing proposals concerning the measurement of investments in subsidiaries, joint ventures and associates at fair value when those investments are quoted in an active market. These proposals consider the unit of account and whether the fair value of such investments should reflect the measurement of the investment as a whole or of the individual financial instruments included within that investment. In such circumstances, determining the appropriate unit of account requires judgment and will depend on specific facts and circumstances. Readers should monitor the development of these proposals.

Other Disclosures		
	Refine Disclosures about Financial Instruments	• Perhaps because of the perceived additional sensitivity or complexity attached to financial instruments, entities are often less comfortable in applying materiality assessments to the information they provide. The result is unnecessarily long financial instrument note disclosures. • Disclosures related to financial instruments should be limited to those that are relevant and should be tailored accordingly. For example, if an entity's financial instruments are all measured at amortized cost and are all short-term in nature (e.g., current accounts receivable), there is limited value in providing a detailed description of the fair value measurement hierarchy and how it relates to the entity's financial instruments.
	Assess Other Disclosures	• Even if an item in the financial statements is material, it does not necessarily follow that *every* disclosure requirement in the related standard is material. For example, disclosures about share-based payments often extend over several pages. For some entities it might be appropriate, based on their entity-specific facts and circumstances, to disclose only the material aspects. For instance, depending on the facts and circumstances, an entity might conclude that disclosures relating to stock options outstanding at the end of the reporting period are material, but that some disclosures relating to activity during the period are not.

Illustrative Financial Statements
Preparers should exercise caution when referencing illustrative financial statements.

Illustrative financial statements are typically created by auditing firms and others to capture a wide range of transactions and events. Preparers need to assess carefully the sample disclosures found in such statements and understand that the disclosures are often intended to be generic and not tailored to an individual entity's facts and circumstances.

Failure to assess relevance and materiality may result in copying irrelevant or immaterial information, thus unnecessarily adding to the volume of disclosures, obscuring important information and not being helpful to users of the financial statements.

Step 3—Refine Content, Formatting and Presentation

Use Plain Language

Documents written in plain language are easier to read and understand. Plain language is concise, clear, direct, and tailored to the circumstances.

Preparers should avoid jargon and technical terms and, whenever possible, use plain language to increase understanding for a wide range of readers.

ITV PLC, a U.K. company, inserts "Keeping it simple" text boxes throughout its financial statements to help readers engage with their formal disclosures. The example below demonstrates how a technical topic, such as derivative financial instruments, can be discussed in an understandable manner.

4.3 Derivative financial instruments

Keeping it simple . . .

A derivative is a type of financial instrument typically used to manage risk. A derivative's value changes over time in response to underlying variables such as exchange rates or interest rates and is entered into for a fixed period. A hedge is where a derivative is used to manage an underlying exposure.

The Group is exposed to changes in interest rates on its net borrowings and to changes in foreign exchange rates on its foreign currency transactions and net assets. In accordance with Board approved policies, which are included in note 4.5, the Group uses derivatives to hedge these underlying exposures.

Derivative financial instruments are initially included in the balance sheet at their fair value, either as assets or liabilities, and are subsequently remeasured at fair value or 'marked to market' at each reporting date. Movements in instruments measured at fair value are recorded in the income statement in net financing costs.

An interest rate swap is an instrument to exchange a fixed rate of interest for a floating rate, or vice versa, or one type of floating rate for another. A cross-currency interest rate swap exchanges a fixed or floating interest rate in one currency for a floating or fixed interest rate in another currency.

Analysis of the derivatives used by the Group to hedge its exposure and the various methods used to calculate their respective fair values are detailed in this section.

Source: **www.itvplc.com**

Simplify disclosures by using:

- short sentences
- no duplication
- simple language (i.e., limit the use of accounting and economic jargon)
- defined terms consistently
- full terms (i.e., avoid acronyms)
- active instead of passive voice (e.g., "we agreed" is better than "an agreement was reached")
- good grammar

Refine Format and Presentation

Most financial statement preparers follow a set order when presenting the notes. They first provide a summary of significant accounting policies, and then add the other notes in an order that more or less reflects the sequence in which the items appear on the face of the financial statements.

Although IAS 1 *Presentation of Financial Statements* currently observes that the notes are "normally" presented in such an order, it does not mandate it, noting that it "may be necessary or desirable to vary the order of specific items within the notes". In other words, preparers have the flexibility to decide the order of their note disclosures and are not limited to the particular order listed in IAS 1.

Preparers have the flexibility to decide the order of their note disclosures and are not limited to the particular order listed in IAS 1.

Regardless of the order, an entity needs to retain a systematic and consistent structure for its note disclosures (except where changes in circumstance demand a change to the sequencing).

Within these parameters, preparers should consider how variations in presentation might assist users. The most obvious deficiency of the conventional ordering (described above) is that the complete information on a particular matter might be distributed among different parts of the financial statements. For example, an entity might address intangible assets in the summary of significant accounting policies, in its disclosure on significant judgments and estimates and then again in an "intangible assets" note. Such fragmentation might be addressed by organizing the notes by topic so that all the information on a particular matter can be found in one place.

To improve the format and presentation of financials statements:

- Include a table of contents.
- Use headers and sub-headers.
- Group related disclosures together (e.g., on a financial statement line item or other logical basis) or sequence them in order of importance.
- Use bullet points.
- Use tables and charts.
- Use legible typeface.
- Use cross-references.

In its 2013 annual financial statements, Potash Corporation of Saskatchewan Inc. provides some examples of how this might be done.

ADDITIONAL ACCOUNTING POLICIES, ESTIMATES AND JUDGMENTS

To facilitate a better understanding of the company's consolidated financial statements, significant accounting policies, estimates and judgments (with the exception of those identified in this Note 2) are disclosed throughout the following notes, with the related financial disclosures by major caption:

Note	Topic	Accounting Policies	Acco a	
3	Receivables	X		
4	Inventories	X		
5	Property, plant and equipment	X	X	123
6	Investments	X	X	126
7	Other assets		X	128
8	Intangible assets	X	X	129
11	Derivative instruments	X	X	131
12	Long-term debt	X		133
13	Pension and other post-retirement benefits	X	X	134
14	Provisions for asset retirement, environmental and other obligations	X	X	140
16	Revenue recognition	X	X	144
17	Cost of goods sold	X		147
17	Selling and administrative expenses	X		147
21	Income taxes	X	X	148
23	Share-based compensation	X	X	152
24	Fair value of financial instruments	X		155
26	Commitments	X	X	161
27	Contingencies	X	X	162
28	Guarantees	X		165
29	Related party transactions	X		

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NOTE 8 INTANGIBLE ASSETS

ACCOUNTING POLICIES

An intangible asset is defined as being identifiable, able to bring future economic benefits to the company and controlled by it. An asset meets the identifiability criterion when it is separable or arises from contractual rights.

Intangible assets are recorded initially at cost and relate primarily to production and technology rights, contractual customer relationships, computer software and goodwill. Internally generated intangible assets relate to computer software and other developed projects. An intangible asset is recognized when it is probable that the expected future economic benefits attributable to the asset will flow to the company and the cost of the asset can be measured reliably.

Costs associated with maintaining computer software programs are recognized as an expense as incurred. Development costs are recognized as intangible assets when the following criteria are met:

- It is technically feasible to complete the asset so it will be available for use;
- Management intends to complete the asset and use or sell it;
- The asset can be used or sold;
- It can be demonstrated how the asset will generate probable future economic benefits;
- Adequate technical, financial and other resources to complete the development and to use or sell the asset are available; and
- The expenditure attributable to the asset during its development can be reliably measured.

Directly attributable costs that are capitalized as part of the asset include applicable employee costs. Development costs previously recognized as an expense are not recognized as an asset in a subsequent period.

Amortization expense is recognized in net consistent with the function of the intangi reviewed, and adjusted if appropriate, at t

Changes in the expected useful life or the future economic benefits embodied in the the amortization period or method, as app in accounting estimates.

All business combinations are accounted f Identifiable intangible assets are recogniz Goodwill is carried at cost, is no longer ar the cost of an acquisition over the fair valu identifiable assets of the acquired subsidia the date of acquisition. Separately recogni accumulated amortization and impairmen disposal of an entity include the carrying a the entity sold.

ACCOUNTING ESTIMATES AND JUDGMENTS

Judgment is necessary to determine whether expenditures made by the company on non-tangible items represent intangible assets eligible for capitalization. Finite-lived intangible assets are accounted for at cost and are amortized on a straight-line basis over their estimated useful lives.

Goodwill is allocated to CGUs or groups of CGUs for the purpose of impairment testing based on the level at which it is monitored by management, and not at a level higher than an operating segment. The allocation is made to those CGUs or groups of CGUs that are expected to benefit from the business combination in which the goodwill arose.

- Related disclosures are grouped together on a topical basis.
- The significant accounting policy, related accounting estimates and judgments as well as any supporting numerical reconciliations and/or details are presented together.
- Headers and bullet points are used to organize information.

SUPPORTING INFORMATION

Goodwill is the only intangible asset with an indefinite useful life recognized by the company. All other intangible assets have finite useful lives. Following is a reconciliation of intangible assets:

	Goodwill [1]	Other	Total
Carrying amount – December 31, 2012	$ 97	$ 29	$ 126
Additions	–	14	14
Amortization	–	(3)	(3)
Carrying amount – December 31, 2013	$ 97	$ 40	$ 137
Balance at December 31, 2013 comprised of:			
Cost	$ 104	$ 82	$ 186
Accumulated amortization	(7)	(42)	(49)
Carrying amount	$ 97	$ 40	$ 137
Carrying amount – December 31, 2011	$ 97	$ 18	$ 115
Additions	–	13	13
Amortization	–	(2)	(2)
Carrying amount – December 31, 2012	$ 97	$ 29	$ 126
Balance at December 31, 2012 comprised of:			
Cost	$ 104	$ 68	$ 172
Accumulated amortization	(7)	(39)	(46)
Carrying amount	$ 97	$ 29	$ 126

[1] The company's aggregate carrying amount of goodwill was $97 (2012 – $97), representing 1.0 percent of shareholders' equity at December 31, 2013 (2012 – 1.0 percent). Substantially all of the company's recorded goodwill relates to the nitrogen segment.

Source: **www.potashcorp.com**

Cross Reference

A cross-reference directs a reader to another area of the report for additional information. Cross-references are sometimes used to link points of information:

- within the financial statements, between the financial statements and the notes, and among the notes themselves
- between the financial statements and some other statement or report, such as the MD&A

Cross-referencing can help reduce the volume of disclosure and the duplication of information within the financial statements.

Some IFRS allow an entity to include required information in a report accompanying the financial statements (such as the MD&A) provided the financial statements contain a cross-reference to that other report and that report is available to users on the same terms and at the same time as the financial statements.

For example, the following standards allow some form of cross-referencing under specific circumstances:

- IFRS 1 *First-time Adoption of International Financial Reporting Standards* (e.g., IFRS 1.32)
- IFRS 7 *Financial Instrument: Disclosures* (e.g., IFRS 7.21B, IFRS 7.B6)
- IAS 19 *Employee Benefits* (e.g., IFRS 19.150)
- IAS 34 *Interim Financial Reporting* (e.g., IAS 34.16A)

To be effective, cross-references must be specific and understandable.

An example of cross-referencing can be seen in note 31 of Royal Bank of Canada's 2014 annual financial statements. In the note on financial instrument risk management, the company cross-references to its MD&A.

Note 31 Nature and extent of risks arising from financial instruments

We are exposed to credit, market and liquidity and funding risks as a result of holding financial instruments. Our risk measurement and objectives, policies and methodologies for managing these risks are disclosed in the shaded text along with those tables specifically marked with an asterisk (*) on pages 52 to 77 of the Management's Discussion and Analysis. These shaded text and tables are an integral part of these Consolidated Financial Statements.

Source: www.rbc.com

The use of cross-referencing needs to be discussed with the entity's auditor because it will be important to clearly define the scope of the auditor's report as well as the material being audited.

Step 4—Apply a Truly Condensed Approach to Interim Reporting

IAS 34 *Interim Financial Reporting* applies when an entity prepares interim financial statements. Under IAS 34, interim financial statements may be either complete or condensed. In general, condensed interim financial statements include (at a minimum) a set of condensed financial statements, selected explanatory notes (as specifically required by IAS 34) and any additional notes required to ensure the interim financial statements are not misleading.

Although the primary focus of Steps 1-3 is on annual financial statements, the same points generally apply to interim financial statements as well.

IAS 34 permits less information to be reported on the grounds that the interim financial statements are providing an update to annual financial statements. For example, IAS 34 allows the omission of many of the notes necessary for the annual financial statements. Instead, the notes in the condensed interim financial statements include primarily an explanation of the events and changes significant to an understanding of the changes in the entity's financial position and performance since the end of the last annual reporting period.

IAS 34 presumes the reader of interim financial statements will also have the latest annual financial statements available. Therefore, the notes in the interim condensed financial statements need not repeat information already available in the most recent annual financial statements. It is *not* necessary, for example, to provide a summary of significant accounting policies in condensed interim financial statements (assuming those policies are unchanged); it is sufficient to say that the accounting policies followed are described in the most recent annual financial statements. If, however, those policies or methods have been changed, a description of the nature and effect of the change should be included in the interim report.

IAS 34 presumes the reader of interim financial statements will also have the latest annual financial statements available. Therefore, it is unnecessary that the notes in the interim condensed financial statements repeat information already available in the most recent annual financial statements.

Despite the absence of any requirement to do so, many entities provide significantly *more* information in their interim financial statements than required by IAS 34. In some cases, this may be justified based on an entity's knowledge of its users' requirements and expectations; in other cases, however, gratuitous interim disclosure may be harmful because it could obscure significant changes that have occurred since the end of the last annual reporting period.

In 2014, CPA Canada and the Canadian Investor Relations Institute (CIRI) published *Interim Reporting Strategies* which notes that the optimum approach to interim reporting may differ from one entity to the next. For example, for a long-standing and relatively stable industrial entity, subject to largely predictable operating cycles and with well-defined relationships with its investors, the emphasis may be on updating rather than on repetition, on highlighting matters that may have differed from investors' expectations, and on reporting against established key performance indicators. In contrast, an entity in the development stage, and still working on establishing credibility and relationships with investors, might think there is greater value in reporting in detail each period on specific areas crucial to its success, even if this entails some repetition of previous reporting.

To view a good example of condensed interim reporting visit **www.potashcorp.com**. In 2014, Potash Corporation of Saskatchewan Inc. was honoured at the 2014 CPA Canada Awards of Excellence in Corporate Reporting. The judges applauded the company's "succinct third-quarter interim financial statements, which provided only updated or new information."

CPA Canada and the Canadian Investor Relations Institute (CIRI) have published a report on interim reporting strategies. The report takes the view that choices involved in interim reporting should be considered a strategic matter designed to maximize the credibility of interim communications and stakeholder confidence in those communications.

Interim Reporting Strategies

www.cpacanada.ca

Step 5—Keep Looking Ahead

Principles of Disclosure

At the time of this publication (April 2015), the IASB is undertaking a broad-based Disclosure Initiative to explore how disclosures under IFRS can be improved. The initiative includes a Principles of Disclosure discussion paper to identify and develop a set of principles for disclosure in IFRS that could form the basis of a standards-level project. The focus is on reviewing the general requirements in IAS 1 *Presentation of Financial Statements*, IAS 7 *Statement of Cash Flows* and IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* and considering how they might be revised. To monitor developments on the IASB Disclosure Initiative visit **www.IFRS.org** or click **here**.

Standards-Level Review of Disclosure

Subsequently, the IASB intends to review the disclosure requirements in existing standards to identify and assess conflicts, duplication and overlap. The review will consider the principles being developed in the Principles of Disclosure project as well as the IASB *Conceptual Framework for Financial Reporting*.

Materiality

The IASB also has a current research project on materiality. In this project, the IASB is considering how materiality is being applied in practice. The IASB is intending to provide guidance on the application of materiality, which is expected to take the form of a Practice Statement. The IASB is also intending to insert a paragraph into IAS 1 that clarifies the key characteristics of materiality.

Amendments to IAS 1

In December 2014, the IASB issued amendments to IAS 1 which, among other things:

- Clarify the materiality requirements in IAS 1 and emphasize the potentially detrimental effect of overwhelming useful information with immaterial information.
- Clarify that specific line items in the statement(s) of profit or loss and other comprehensive income and the statement of financial position can be disaggregated.
- Add requirements for how an entity should present subtotals in the statement(s) of profit or loss and other comprehensive income and the statement of financial position.

- Clarify that entities have flexibility with respect to the order in which they present the notes, but also emphasize that an entity should consider understandability and comparability when deciding that order.
- Remove potentially unhelpful guidance in IAS 1 for identifying a significant accounting policy.

The amendments to IAS 1 can be applied immediately, and become mandatory for annual periods beginning on or after January 1, 2016. These amendments should simplify financial statements and entities are encouraged to consider them now.

Look Ahead

This publication reflects information available at the time of issuance (April 2015) and may, in some respects, be superseded by subsequent changes to standards or other initiatives. This confirms the point emphasized throughout this document, that the optimum approach to disclosure may change over time for any number of reasons, both external and internal. Also, the needs and interests of investors may evolve over time (e.g., because of changes in the shareholder base or as an entity becomes subject to greater coverage by analysts).

It follows that the board and management should regularly review the effectiveness of an entity's financial reporting practices, including how those practices align with developments in standard setting and regulation. Changes should be made whenever required and be balanced against stakeholders' interests in comparability and consistency of financial reporting. Whenever an entity's major objectives or strategies change, there should be consideration of the potential effects on disclosure policies and processes.

Appendix A — What Questions Should I Ask?

20 Questions Preparers Should Ask Themselves about Simplifying Financial Statements

Strategy, Policy and Process

1. Have we developed a well-articulated policy framework for disclosure that meets the needs of our users?
2. Have we established a qualified disclosure committee to oversee the financial statement simplification process?
3. Have we developed a rigorous understanding of materiality, considering both quantitative and qualitative aspects, based on a well-supported understanding of what information most influences the economic decisions of users of our financial statements?
4. Have we discussed with our auditors our plans to simplify our financial statements and any decisions already made?
5. Have we established a process for regular reporting to the audit committee (or similar body) and for obtaining their feedback?
6. Do we have procedures to revisit all these matters at least annually and when circumstances change?
7. Have we appropriately documented our plans for simplifying our financial statements and considered (where appropriate) the possible effects on internal controls over financial reporting?

Content and Format

8. Do we use plain language in our financial statements, minimizing the use of boilerplate and generic explanations?
9. Do we provide sufficient cross-referencing to help a user locate information with minimum effort?
10. Should our current presentation be amended to, for example, organize disclosures in a different sequence?
11. Have we eliminated all accounting policies and disclosures that are no longer relevant to our current financial statements?
12. Do our disclosures of significant judgments and estimates focus on only the judgments that will have the most significant effect on the amounts recognized and on estimates affecting assets or liabilities that carry a significant risk of being adjusted within the next fiscal year?
13. Have we reviewed our notes for immaterial disclosures?
14. Have we assessed whether our interim financial statements are sufficiently condensed, having taken into consideration IAS 34 as well as the needs of our users?
15. Have we reviewed the financial reporting section of our website to ensure it is as accessible and user friendly as possible?
16. Have we considered how we might better use our technology to improve the accessibility and usefulness of the information we provide?
17. Have we considered the financial statements of other entities for best practices and useful ideas?
18. Have we reviewed the status of the IASB Disclosure Initiative and how it might affect us?
19. In our efforts to simplify our financial statements, have we addressed areas where disclosure should be increased?
20. Are we satisfied that our financial statements comply with all applicable requirements of IFRS and securities law?

FIVE STEPS TO SIMPLIFYING FINANCIAL STATEMENTS—TODAY

This publication sets out a principled five-step approach to simplifying financial statements by reducing disclosure overload and streamlining disclosure while achieving both more effective communication and full compliance with the intent of disclosure requirements.

These steps can be taken *now* by management, with reference to the standards and requirements currently in place. They provide an opportunity to add immediate value to an entity's financial statements, without requiring significant investments of money, time or resources.

This publication focuses on actions that can be taken quickly and add immediate value to an entity's financial statements.

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