

Applying materiality when preparing financial statements

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Gabriela Kegalj
KPMG's global IFRS presentation leader

IASB refines its definition of material and encourages companies to apply judgement

Highlights

- Preparers are encouraged to use materiality as a filter
- Refined definition and existing guidance aim to help preparers apply judgement
- IASB may issue further guidance on accounting policy disclosures

The IASB is striving to end the 'checklist' mentality by encouraging companies to use greater judgement

Materiality as a filter

Making information in financial statements more relevant and less cluttered is one of the IASB's key focus areas.

Companies make materiality judgements not only when deciding what information to disclose and how to present it, but also when making decisions about recognition and measurement.

However, management are often uncertain about how to apply the concept of materiality to disclosure, and find it easier to defer to using the disclosure requirements within IFRS as a checklist.

To help preparers of financial statements, the IASB has refined its [definition of 'material'](#) and issued [practical guidance on applying the concept of materiality](#).

Refined definition of material

This month, the IASB refined its definition of material to make it easier to understand. It is now aligned across IFRS Standards® and the Conceptual Framework.

*"Information is material if omitting, misstating or **obscuring** it **could reasonably be expected** to influence decisions that the **primary users** of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity."* **[emphasis added]**

"We welcome a more focused definition of 'material' that emphasises the role of judgement when making materiality decisions. But the reference to obscuring material information and removal of the definition of material misstatement may be challenging to operationalise."

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The amendments are effective from 1 January 2020 but may be applied earlier. However, the Board does not expect significant change – the refinements are not intended to alter the concept of materiality.

Making it easier to understand and apply

The concept of materiality needs to be clearly understood so that preparers of financial statements can apply it appropriately. The amendments provide a definition and explanatory paragraphs in one place. Some stakeholders were concerned that the previous definition might encourage entities to disclose immaterial information in their financial statements. In response, the Board promoted the concept of ‘obscuring’ to the definition, alongside the existing references to ‘omitting’ and ‘misstating’. Additionally, the Board increased the threshold of ‘could influence’ to ‘could reasonably be expected to influence’.

However, the Board has also removed the definition of material omissions or misstatements from IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

The refined definition of material complements the guidance the Board released last year, which outlines a [four-step process](#) that preparers can use to help them make materiality judgements.

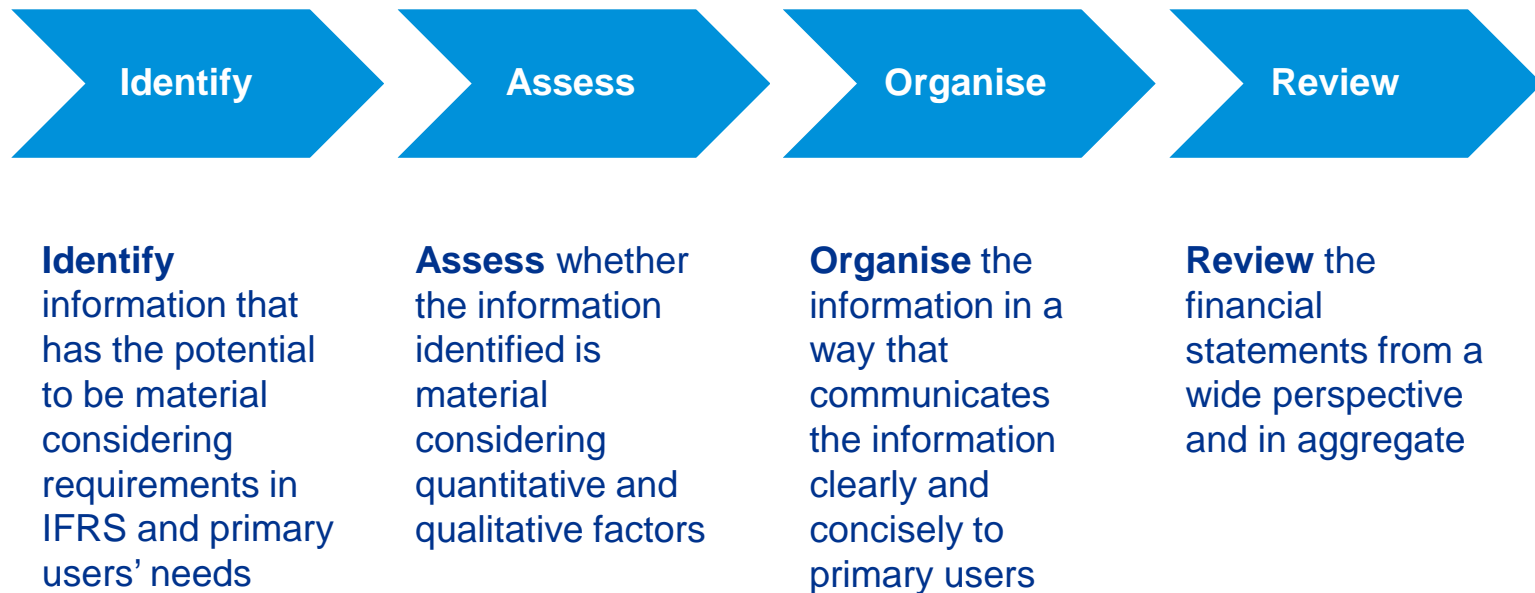
Further guidance on accounting policy disclosures

Under a separate project, [Disclosure Initiative – Accounting Policies](#), the Board is also considering issuing additional guidance and examples to help entities apply materiality judgements to accounting policy disclosures. The Board is yet to determine the timing of the exposure draft.

For more information on these developments, speak to your KPMG contact.

How do you decide what's relevant when preparing financial statements?

Making information in financial statements more relevant and less cluttered is one of the IASB's key focus areas. Its [guidance](#) includes a **four-step process** to help you make materiality judgements.



Stakeholders need information that is relevant and specific to a company's circumstances.