

## 10 years of IFRS financial statements

Listed companies have prepared their consolidated financial statements in accordance with the International Financial Reporting Standards (IFRSs) since 2005, when the Financial Supervisory Authority (FIN-FSA) also initiated its IFRS enforcement. The objectives of the IAS regulation issued by the European Union was to promote both the free flow of capital within the European internal market and the efficiency of capital markets. IFRSs fulfil investor requirements for high-quality, reliable, comparable and transparent financial reporting.

The European Commission commenced a review of the IAS regulation in the second half of 2014. FIN-FSA participated in the consultation process through ESMA<sup>1</sup>, which compiled the views of the European enforcers and prepared a reply to the Commission. The goal of the consultation process was to assess, among other things, the fulfilment of the objectives of the IAS regulation and the scope of application and eligibility criteria of the IFRSs. Another goal was to assess the costs of IFRS reporting in relation to the benefits achieved. The response to the Commission states that as a whole the IFRSs have been effective. The final consultation results will be published in spring 2015.

The governance of EFRAG<sup>2</sup> was reviewed on the basis of the Maystadt report<sup>3</sup> on the adoption of IFRSs, which was drawn up on the initiative of the Commission. EFRAG advises the European Commission on the adoption of IFRSs within the EU legislation. The goal of the Commission was, among other things, to strengthen Europe's influence as regards IFRSs. EFRAG appointed a new high level Board under its General Assembly, which is to provide final advice to the Commission on the adoption of IFRSs. The Board will also approve comment letters addressed to the IASB<sup>4</sup>. The resulting process changes will advance ESMA's assessments of the impact of IFRS regulation in terms of investor protection.

1 The European Securities and Markets Authority.

2 The European Financial Reporting Advisory Group.

3 The Maystadt report is available on the address [http://ec.europa.eu/internal\\_market/accounting/docs/governance/reform/131112\\_report\\_en.pdf](http://ec.europa.eu/internal_market/accounting/docs/governance/reform/131112_report_en.pdf).

4 The International Standards Accounting Board.

## Theme survey on financial reporting of poorly performing companies

As in previous years, the challenging financial situation affected FIN-FSA's IFRS enforcement. In the selection of companies for examination, focus was placed on risk indicators describing the financial position and on, for example, concentrated ownership. After the financial crisis, since 2008, the IFRS enforcement has increasingly focused on poorly performing companies. In 2014 FIN-FSA also carried out a survey on listed companies' financial reporting during financial and operational uncertainty.<sup>5</sup>

Certain parts of financial statements become increasingly important in times of poor corporate performance. The information on the company as a going concern should be clear, detailed and tangible. Information on judgements and assessments by management increases financial statement users' understanding of, for example, assessments of the company as a going concern and assumptions underlying the assessments. Special attention should be paid to the transparency of assumptions underlying goodwill impairment tests. Recognition of deferred tax assets arising from incurred losses also includes critical judgement and requires convincing evidence. A clear picture should be given of the financial risk. Information on the management of capital also becomes increasingly important in difficult times.

## Financial instruments, goodwill impairment testing and related party disclosures still the key areas reviewed

IFRS 13 on fair value measurement was adopted at the start of 2013, and its enforcement was one of ESMA's priorities in 2014.<sup>6</sup> FIN-FSA observed that either no information on value measurement processes and valuation techniques as referred to in IFRS 13 was disclosed in the financial statements or the information was not sufficiently detailed.

5 An article on how high-quality financial reporting supports a poorly performing company has been published in Finnish in the Market Newsletter 3/2014. FIN-FSA's Market Newsletters are available on the address <http://www.finanssivalvonta.fi/fi/Tiedotteet/Markkinat/Pages/Default.aspx>. A presentation on the same subject was made at the 2014 event for listed companies. Presentation material from the event for listed companies is available in Finnish at [http://www.finanssivalvonta.fi/fi/Listayhtiolle/IFRS/Julkaisut/Esitykset/Documents/Fivan\\_listayhtiotalaisuus\\_2014\\_kalvot.pdf](http://www.finanssivalvonta.fi/fi/Listayhtiolle/IFRS/Julkaisut/Esitykset/Documents/Fivan_listayhtiotalaisuus_2014_kalvot.pdf).

6 Information on ESMA's priorities in 2014 is provided at [http://www.esma.europa.eu/system/files/2013-1634\\_esma\\_public\\_statement\\_-\\_european\\_common\\_enforcement\\_priorities\\_for\\_2013\\_financial\\_statements\\_1.pdf](http://www.esma.europa.eu/system/files/2013-1634_esma_public_statement_-_european_common_enforcement_priorities_for_2013_financial_statements_1.pdf).



# Report on IFRS enforcement in 2014

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Disclosure of the fair value hierarchy also needed improvement. As regards instruments to which the fair value option is applied in accordance with IAS 39, FIN-FSA noticed deficiencies in the numerical information and the disclosure of the basis for application of the fair value option. The disclosure of liquidity risk and its management still need to be developed. FIN-FSA also noticed that the maturity distribution of financial debt was not always disclosed in such manner as required in the standard.

One of FIN-FSA's enforcement themes since 2012 has been disclosures of related parties. The basis for related party disclosures is that the company correctly defines the related parties and keeps the information about them up to date. In addition, the company should have in place a process for identification of all related party transactions. According to FIN-FSA's observations, companies have not always identified all the related parties. Improvement was discernible in the financial reporting, but some deficiencies remained. For example, compensations to the management had not always been disclosed. The Accounting Board's opinion<sup>7</sup> on the note to the financial statements on pension commitments as regards the management has not always been complied with.

As in 2013, FIN-FSA continued the goodwill-related enforcement. In particular, the enforcement work focused on the basis for values of future cash flows, the determination of the discount rate and the notes to the financial statements.

The notes in IFRS financial statements and their development have been widely discussed in recent years. The notes were also one of ESMA's priorities in 2014. Companies use many standard phrases in the notes to the financial statements. This means that the notes contain boilerplate phrases from IFRS standards or model books but very little company-specific content. FIN-FSA has also noted the scarcity of information in the notes. Even information of material importance to the company may be left out of the financial statements. In particular, there have been deficiencies in the notes on financial instruments even in companies for which those instruments are material. FIN-FSA follows the discussion on notes and its enforcement pays attention to the quality of companies' notes to the financial statements.

<sup>7</sup> The Accounting Board opinion is available (in Finnish) at <http://ktm.elinar.fi/ktm/fin/kirjanpi.nsf/717602942eb71ebdc22570210049e02b/576a86887f27e772c2257bf9003e80cb?OpenDocument>.

## Many observations regarding the enforcement of standards on financial instruments

The comprehensive assessment performed by the European Central Bank (ECB) affected the volume of the IFRS enforcement, because many employees of the IFRS Enforcement Division worked in the project for half a year. In its comprehensive assessment, the ECB surveyed the banks' balance sheets, and their capital adequacy was stressed prior to the start-up of ECB banking supervision. One of the objectives was to increase the transparency, comparability and reliability of banks' financial statements.

IFRS enforcement is risk-based enforcement. Based on separately specified risk factors, the enforcement focuses on certain companies, whose financial statements and other financial reports are given a full review. Financial statements and other financial reports may also be examined partly in terms of separately selected aspects of financial reporting (thematic review). Enforcement of financial reporting requirements also includes reactive enforcement, when, based on a stock exchange announcement or complaint, the appropriateness of a company's selected single accounting methodology is examined.

The below table describes the scale of 2014 and 2013 IFRS enforcement by type of enforcement.<sup>8</sup> In 2014 the thematic enforcement focused on related party disclosures and goodwill impairment testing. The poor performance of some companies and uncertainty about their ability to continue as a going concern show as increased reactive enforcement.

Type of enforcement	Number of enforcement events in 2014	Number of enforcement events in 2013
Full review	10	14
Enforcement by theme	7	6
Reactive enforcement	10	5
<b>Sum total</b>	<b>27</b>	<b>25</b>

<sup>8</sup> The table shows the number of separate enforcement events, not the number of companies. A certain company may during the year be subjected to, for example, thematic enforcement and reactive enforcement. The number of enforcement events describes the volume of enforcement. However, the scope of individual enforcement events differs widely.

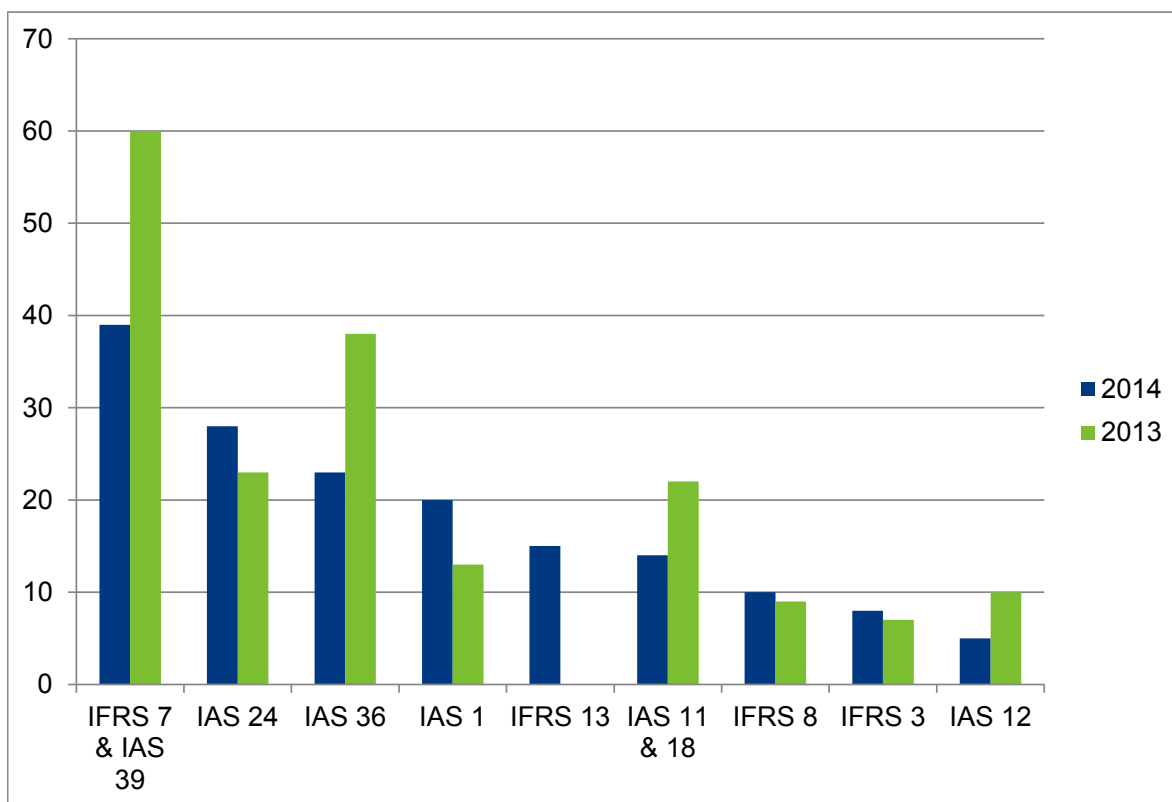


# Report on IFRS enforcement in 2014

The chart below shows the priorities of IFRS enforcement by standard in 2014 and 2013.

In 2014 there were fewer enforcement observations than in the previous year. A large part of the enforcement observations focused on the application of the standards on financial instruments (IFRS 7 and IAS 39). The increased enforcement of IAS 1 on presentation of financial statements relates to the issue of a going concern. Observations as regards IFRS 13 on fair value measurement were evenly focused on both non-financial and financial assets. The number of observations was large, because numerous deficiencies were observed in the application of the new standard. A typical number of observations concerned IFRS 3 on business combinations and IFRS 8 on operating segments.

**Chart 1. Enforcement priorities by standard in 2014 and 2013 (number of observations)**



## More corrections to financial statement information were required

Half of the enforcement observations required correction in the next financial statements, compared to 41% in 2013. A requirement of correction always indicates that FIN-FSA considers the observed deficiency to be serious.

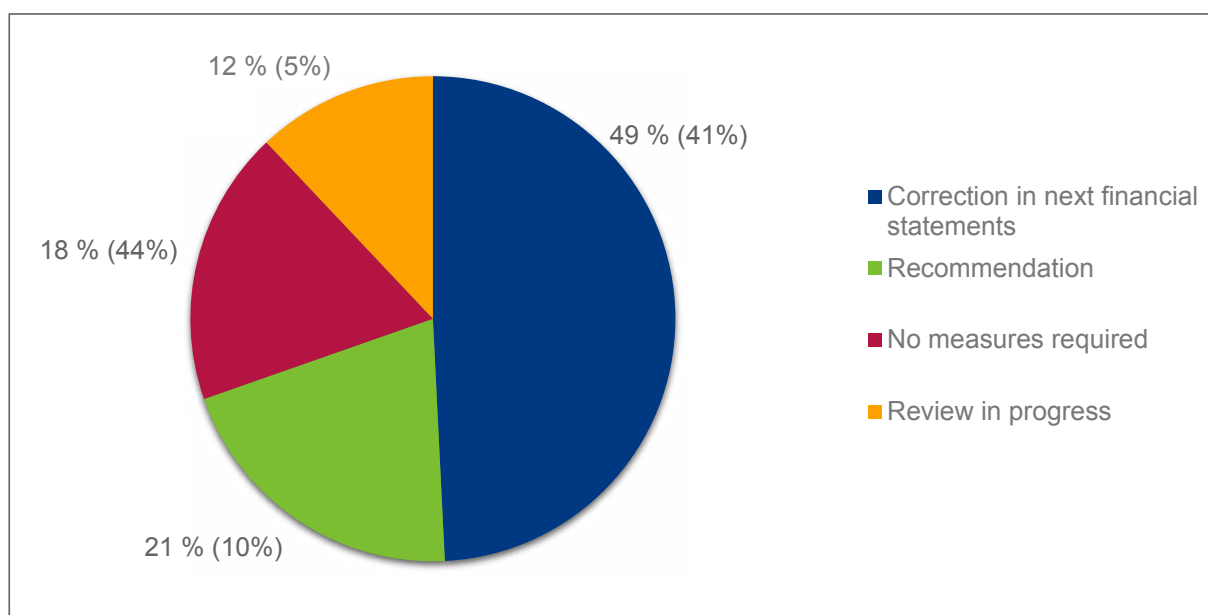
Errors concerning earlier periods must be corrected retrospectively in accordance with IAS 8. FIN-FSA often requires corrections in the next financial statements, but does not require adjustments for comparative purposes. The reason for this is that FIN-FSA does not systematically assess the materiality of the observations on the basis of IAS 8, because this assessment is difficult for an outsider without first discussing the matter widely with the company. Consequently FIN-FSA presupposes that the company itself assesses the materiality of the observation and carries out the corrections accordingly. FIN-FSA considers clear standard incompatibilities, related to a material balance sheet item or a note that is material due to its character, as material deficiencies that should be corrected. FIN-FSA highlights the seriousness of its requirements in its enforcement letters.

In 2014 the observations not only covered information to be disclosed in the financial statements but also to a significant extent valuation and recognition issues. The most serious observations on valuation and recognition concerned goodwill, related party determination and financial instruments. Of the enforcement observations, shown in the chart, representing deficiencies that FIN-FSA required to be corrected in the next financial statements, nearly 20% were related to materially deficient financial statements according to FIN-FSA.

In every fifth enforcement observation, FIN-FSA recommended improvements of the next financial statements. More recommendations were given in 2014 than in 2013. In 2014 the recommendations were particularly related to IAS 24 on related party disclosures and IAS 1 on presentation of financial statements, whereas in 2013 the recommendations mainly concerned IAS 36 on impairment of assets and IFRS 7 on disclosures of financial instruments.

In about one fifth of the enforcement observations, FIN-FSA required no measures. In 2013 there were more of such observations.

**Chart 2. Distribution of measures required of companies based on individual enforcement observations in 2014 and 2013**



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## FIN-FSA committed to harmonised enforcement methods

Towards the end of 2014 FIN-FSA began to apply ESMA's revised guidelines on examination procedures for enforcement of financial statements.<sup>9</sup> The purpose of the guidelines is to put in place consistent and efficient supervisory practices so as to underpin investors' confidence in financial markets through more detailed guidelines. The new provisions do not essentially change the current IFRS enforcement, but they establish permanent practices in certain areas and thus increase enforcement efficiency. Enforcers must increasingly bring significant new financial reporting issues, fulfilling certain criteria, into the European discussion before the enforcement decision is made. The selection of companies should be risk-based in combination with a sampling and/or rotation approach, as compared to the previous, only risk-based selection. European IFRS enforcers also jointly decide on priorities for the following year. The obligation to comply with common enforcement priorities is now included in the guidelines.

## International cooperation a necessary basis for national IFRS enforcement

FIN-FSA is active in ESMA, one task of which is to coordinate the European IFRS enforcement. ESMA's permanent Corporate Reporting Standards Committee (CRSC) governs all work related to financial reporting, auditing, disclosure of periodic information and storage of regulated information. A Consultative Working Group is also meeting in connection with CRSC. The working group is composed of representatives of the market participants, and its task is to hear the views and ideas of different participants. The Finnish representatives in the group were Ms **Marjaana Alho** from Stora Enso (Vice President) and Ms **Tuija Soanjärvi**, Professional Board Member.

The IFRS Project Group is an ESMA working group that prepares ESMA's comments on new IFRS standards and interpretations and changes therein for the IASB and IFRS IC. In its comments it considers both investor information and standard enforceability. In 2014 the working group sub-

mitted five comment letters to the IASB and six to EFRAG. In 2014 the working group also extensively participated in the preparation of ESMA's draft guidelines on performance measures.

In the EECS meetings<sup>10</sup> national enforcers handle issues related to listed companies' IFRS financial statements, both prior to and after enforcement decisions. In 2013, nine EECS meetings were held and FIN-FSA participated in all of them. ESMA's new enforcement guidelines also require that FIN-FSA participates in the meetings. ESMA manages a data base in which the enforcement decisions of the European IFRS enforcers are collected. ESMA regularly publishes part of the national enforcement decisions and decisions adopted by the EECS. By November 2014 a total of 180 enforcement decisions had been published. The aim of the publication of decisions is to promote a consistent application of IFRS standards and transparency of enforcement in Europe. FIN-FSA prepares summaries of the published decisions in the Market Newsletters.<sup>11</sup>

In May 2014 ESMA published a report on IFRS 3 on business combinations. ESMA examined the consolidated financial statements of 56 listed European companies. Enforcers in different countries, including FIN-FSA, have run into similar problems in their enforcement of the standard. In general, the notes on business combinations were sufficiently comprehensive and clear, but there were still sub-areas that needed improvement. Qualitative descriptions disclosed by companies on factors influencing goodwill were deficient and the descriptions were often of a general nature, without sufficient detail. Furthermore, nearly one quarter of the companies had not identified intangible assets other than goodwill in connection with a business acquisition.<sup>12</sup>

<sup>9</sup> The enforcement guidelines are available at <http://www.esma.europa.eu/system/files/2014-esma-1293fi.pdf>.

<sup>10</sup> European Enforcers' Coordination Sessions.

<sup>11</sup> Summaries of the enforcement decisions are available at <http://www.finanssivalvonta.fi/fi/Listayhtiolle/IFRS/Julkaisut/EECS/Pages/Default.aspx>.

<sup>12</sup> The report is available at [http://www.esma.europa.eu/system/files/2014-643\\_esma\\_report\\_on\\_the\\_ifrs\\_3.pdf](http://www.esma.europa.eu/system/files/2014-643_esma_report_on_the_ifrs_3.pdf).



## Significant national legislation – reform of the supervision of auditors

Reform of the European legislation on supervision of auditors also widely affects the corresponding supervision in Finland. It has been recommended that the supervision of auditors in Finland should be integrated into the public sector to make it possible to comply with new obligations contained in the EU regulation. According to a national bill, the supervision of financial market participants would be organised so that FIN-FSA in certain situations also could supervise the legal compliance of an auditor's procedures. In addition, adequate coordination between the supervision of auditors and FIN-FSA would become legally regulated. In its statement to the Ministry of Employment and the Economy, FIN-FSA has supported changes in the supervision.<sup>13</sup> FIN-FSA considers that the supervision of auditors in the financial sector is not on an adequate level in Finland. FIN-FSA is also a member of the working group for changes in the auditing legislation, set up in December. FIN-FSA is represented by Ms **Ingalill Aspholm**.

Presently FIN-FSA participates in the supervision of auditors through its membership in the Auditing Board of the Central Chamber of Commerce. For the time being, Ms **Tiina Visakorpi** is a member of the Auditing Board and Ms Ingalill Aspholm a deputy member. FIN-FSA enforces IFRS compliance as regards financial statements and the Auditing Board supervises auditors' auditing of financial statements.

Through its membership in the Accounting Board, FIN-FSA promotes good accounting practice in accordance with the national accounting legislation. Ms Virpi Haaramo is a member of the Accounting Board and Ms Reija Anttila a deputy member. In addition, Ms Virpi Haaramo is a member of the working group for accounting legislation reform. The working group prepared a *memo on reliefs for small companies, in light of the 2013 financial statements directive*, which it circulated for comments in October 2014.

## Events for listed companies support predictable supervision

In early December 2014, FIN-FSA arranged two events on the subject of listed companies' financial reporting for a total audience of about 160 participants. The purpose of the events was to inform listed companies and auditors on the observations made in connection with IFRS enforcement in 2014. Information on the IFRS enforcement process and the priorities for next year's IFRS enforcement is also useful to the companies. An additional purpose of the events for listed companies is to gather together interested parties represented in the financial reporting.

In addition to the enforcement observations, the 2014 theme of the events for listed companies was financial reporting of poorly performing companies, business combinations and new consolidation standards. A review of the 10-year history of IFRS enforcement was also presented at the events, as were the European enforcement and regulation systems and ESMA's new enforcement guidelines. The participants also got the latest news on issuers' disclosure obligation.<sup>14</sup>

A combined total of six articles and news releases on IFRS enforcement were published in the 2014 Markets Newsletters. Appendix 2 to this report contains a summary of all the publications and news releases published in 2014. The IFRS information on the FIN-FSA website is available at <http://www.finanssivalvonta.fi/fi/Listayhtiolle/IFRS/Pages/Default.aspx>.

## For further information, please contact

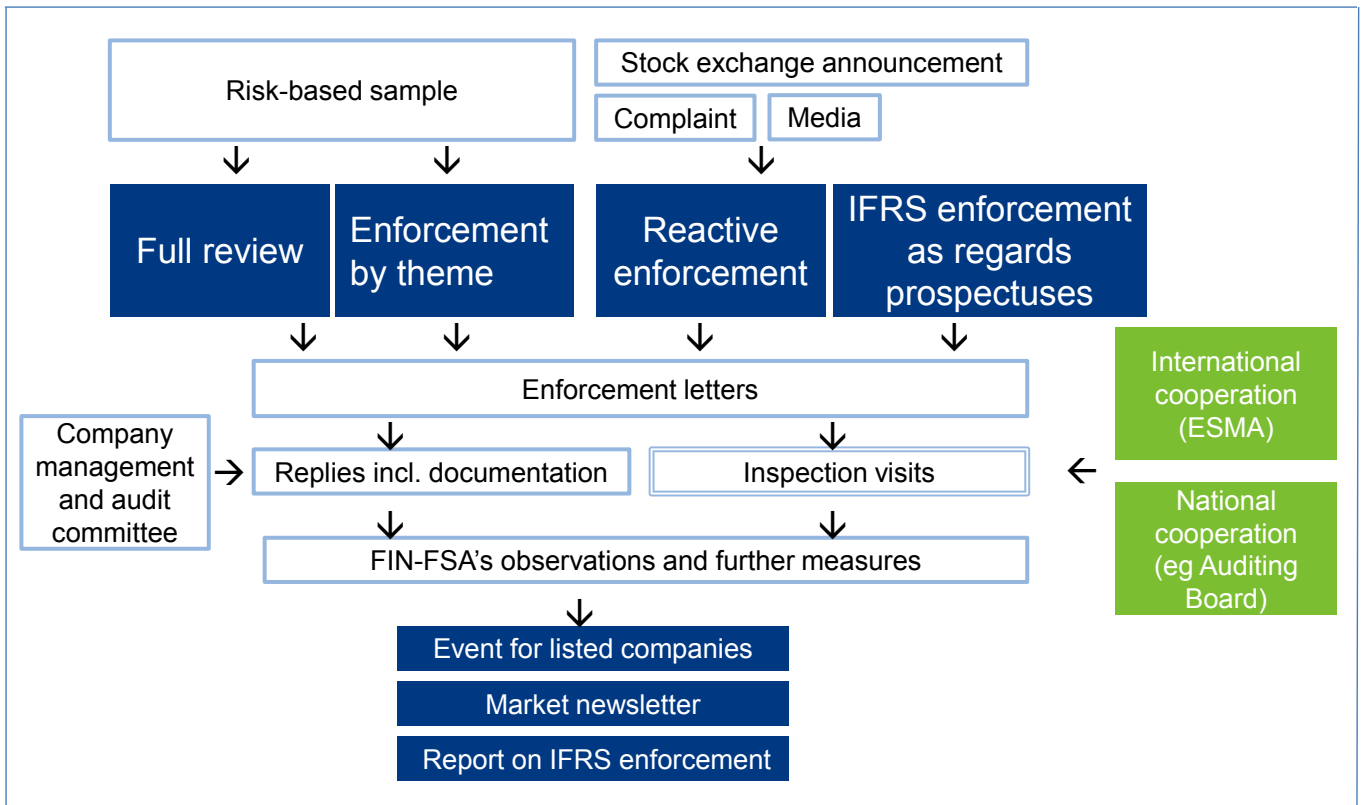
Tiina Visakorpi, Head of Division, tel. +358 10 831 5383.

<sup>13</sup> FIN-FSA's statement is available at [http://www.finanssivalvonta.fi/fi/Saantely/Lausunnot/Documents/Fivan\\_lausunto\\_20140910.pdf](http://www.finanssivalvonta.fi/fi/Saantely/Lausunnot/Documents/Fivan_lausunto_20140910.pdf).

<sup>14</sup> The presentation material used at the events for listed companies is available on FIN-FSA's website at <http://www.finanssivalvonta.fi/FI/LISTAYHTIOLLE/IFRS/JULKKAISUT/Pages/Default.aspx>.

# Report on IFRS enforcement in 2014

## Process of the IFRS enforcement



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## The Financial Reporting Division's news items in 2014

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### Presentations

- Events for listed companies December 2014 - Presentation material (in Finnish)

### News releases

- Report on IFRS enforcement 2013: Extensive enforcement of compliance with standards on financial instruments (News release 27 February 2014, 3/2014)

### Market newsletters and other articles

- ESMA published new enforcement decisions (Market newsletter 4/2014, in Finnish)
- A correction to the focus of IFRS enforcement in 2015 (Market newsletter 4/2014, in Finnish)
- High quality financial statement information supports the company in its weak financial condition (Market newsletter 3/2014, in Finnish)
- ESMA reviewed the application of accounting requirements for business combinations in IFRS financial statements (Market newsletter 3/2014, in Finnish)
- The proposed auditor's report will enhance the transparency of the audit (Market newsletter 2/2014, in Finnish)
- ESMA published new enforcement decisions (Market newsletter 2/2014, in Finnish)

### IFRS-reports

- Report on IFRS enforcement 2013

### Extracts from the EECS database of decisions

- List of decisions published in the Extracts from the EECS's Database of Enforcement (18.11.2014)
- ESMA publishes 16th Extract from the EECS's database of enforcement (18.11.2014)
- List of decisions published in the Extracts from the EECS's Database of Enforcement (9.4.2014)
- ESMA publishes 15th Extract from the EECS's database of enforcement (9.4.2014)

### News releases by the European Securities and Markets Authority (ESMA)

- ESMA publishes official translations of the ESMA Guidelines for enforcement of financial information (28.10.2014); ESMA:n ohjeet tilinpäätöstietojen valvonnasta
- ESMA publishes its European common enforcement priorities for 2014 financial statements (28.10.2014)
- IFRS Foundation and ESMA sign joint Statement of Protocols (15.7.2014)
- ESMA publishes accounting enforcement guidelines (10.7.2014)
- ESMA publishes the report on the review on the application of accounting requirements for business combinations in IFRS financial statements (16.6.2014)
- ESMA publishes the Report on Activities of IFRS Enforcers in Europe in 2013 (23.5.2014)

### FIN-FSA opinions

- 5 December 2014 FIN-FSA's opinion to the Parliamentary Finance Committee on the Government Bill proposing a new Auditing Act and Act on auditing of public sector entities and public finances as well as some related acts (in Finnish)
- 10 September 2014 FIN-FSA's opinion to the Ministry of Employment and the Economy on a draft Government Bill proposing a new Auditing Act and related legislation as well as draft decrees related to the bill (in Finnish)
- 30 June 2014 FIN-FSA's opinion to the Ministry of Employment and the Economy on a draft Government Bill proposing amendments of the Auditing Act (in Finnish)
- 3 June 2014 FIN-FSA's opinion to the Parliamentary Finance Committee: Government letter to the Parliament on the Communication of the European Commission on long-term financing of the European economy (in Finnish)

Publications and press releases: <http://www.finanssivalvonta.fi/fi/Listayhtiolle/IFRS/Julkaisut/Pages/Default.aspx>.

