In brief
A look at current financial reporting issues

Guidance on making materiality judgements

Issue

IFRS Practice Statement 2: Making materiality judgements

On 14 September 2017, the IASB published a Practice statement on Making materiality judgements.

The objective of the Practice statement is to provide guidance for reporting entities that are performing materiality assessments when preparing financial statements in accordance with IFRSs. The Practice statement also includes illustrative examples to help with the application of the guidance.

The Practice statement:

- uses a definition of materiality aligned with the definition in the Conceptual framework for Financial reporting;
- considers materiality judgements in relation to presentation and disclosure, and also for recognition and measurement;
- explains the application of judgement to materiality decisions based on the specific circumstances of the entity and the changes that might occur in those circumstances over time;
- requires an entity to assess whether information is material to the financial statements, even if it is already included in other publicly available information;
- clarifies that the provision of additional information required by local regulations is permitted, but the information should be presented in a way that does not obscure material information; and
- includes a four-step process, the ‘materiality process’, as a guide for materiality judgements, including identification, assessment, organisation of the information and, finally, review.

The Practice statement also addresses:

- Prior period information: considering how the materiality of items from prior periods is assessed in the current period.
- Errors: considering how errors are assessed, individually and collectively, and the effect of cumulative errors, from both a quantitative and a qualitative perspective.
- Financial covenants: explaining how materiality is assessed in relation to the impact of financial covenants, including: i) the materiality of the consequences of breaching a covenant; and ii) the likelihood that the breach would occur.

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Interim reporting: considering materiality for the period covered by the interim financial statements under analysis.

The Practice statement is not a standard, and it is not mandatory. It does not override any auditing guidance or specific local materiality guidance. Although the Practice statement is not mandatory, it is intended to be helpful to management, and it can be applied to financial statements prepared from 14 September 2017.

**Impact**

The Practice statement could provide additional information and considerations for management making a materiality assessment in the absence of local materiality guidance. However, we note that the Practice statement is not necessarily consistent with the way in which materiality is considered by some securities regulators.