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Enforcement of compliance with information requirements for securities issuers in 2019

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Purpose of the report

This report provides information on the enforcement of information requirements for securities issuers in connection with their participation in trading in the capital market.

The report is prepared for users of regulated information, issuers and auditors to contribute to the proper and consistent application of the relevant reporting requirements. High-quality transparent information is a crucial factor that drives the investors' decision-making process. Improper performance of information disclosure obligations of issuers results, in turn, in a lack of universal and equal access to complete and accurate information, which is of key importance to proper operation of market forces. The lack of transparency of information undermines investor confidence in the market and the securities traded therein.

1 Introduction

The tasks of the Public Companies Department (DSP) of the Polish Financial Supervision Authority (PL: Urząd Komisji Nadzoru Finansowego, UKNF) include supervising the compliance by supervised entities with requirements relating to their participation in trading in the capital market, to the extent specified in the legislation – in accordance with Article 7(1) point 2 of the Act on capital market supervision.¹

The supervision exercised by the DSP in the area of information requirements covers financial reporting (in particular compliance with IFRSs²), management or directors' reports and non-financial information. The DSP also supervises inside information of all issuers whose securities are admitted to trading on an organised market (on a regulated market and in an alternative trading system – ATS³).

The information published by issuers is assessed for compliance with the applicable requirements and appropriate measures are taken to address the breaches of those requirements.

Parts two to five of this report provide information on supervisory actions undertaken in 2019 in relation to specific areas of supervision, i.e. financial reporting, timeliness and completeness of annual reports, non-financial information and inside information.

Part six discusses particularly relevant issues in the field of financial reporting that have arisen during the reviews conducted in 2019 and are so important that issuers should pay attention to them when preparing financial statements for subsequent reporting periods.

2 Review of financial statements and supervisory actions

Enforcement of compliance of issuers' financial reporting with appropriate reporting regulations uses selection of issuers based on a combination of a

risk-based approach, random sampling and/or rotation. Not all financial statements of each issuer are subject to review.

Selecting financial statements for review and type of review

In 2019, the selection for the purpose of assessment of compliance with the applicable financial reporting regulations included, in particular, financial statements of issuers:

¹ Act of 29 July 2005 on capital market supervision (consolidated text: Journal of Laws 2019, item 1871, as amended).

² International Accounting Standards, International Financial Reporting Standards and related interpretations published as European Commission Regulations.

³ The scope of supervision of issuers operating in an ATS is indicated in Chapter 5.

- to whom recommendations had been addressed;
- for whom an auditor had drawn up an audit report containing a modified opinion or a review report containing a modified conclusion;
- with a significant level of debt arising from the issuance of bonds and liabilities to assets ratio, and an adverse value of the current liquidity ratio;
- who carry out the first public offering of shares, in connection with the administrative procedure for approval of the prospectus;
- selected randomly.

Table 1. Number of issuers whose financial statements were subject to periodic review in 2017–2019

Year	Number of regulated-market issuers (Warsaw Stock Exchange and Bond-Spot)* at the year-end	Number of issuers whose financial statements were subject to review**	Share in the total number of regulated-market issuers
2017	456	103	22.6%
2018	441	96	21.8%
2019	436	96	22.0%

* excluding closed-end investment funds and issuers for whom the Republic of Poland is a host state

**The number of issuers for 2018 also includes analysis of historical financial information of issuers making first public offerings (10 issuers in 2018)

Source: Own elaboration

When selecting issuers' financial statements for the periodic review in 2019, we maintained, as in previous years, a high priority of the criterion of: occurrence of qualifications in audit reports on financial statements, disclaimers of opinion or adverse opinions. Consideration was also given to the occurrence of qualifications in the auditor's half-yearly review reports, disclaimers of report or negative conclusions. Issuers with

modified opinions or review conclusions represent about a third of all reviews.

Therefore, on many occasions we have also reviewed financial statements of issuers whose ability to continue as a going concern was threatened or who have ceased to continue as a going concern. This applied mainly to the issuers who applied, or against whom another person applied, for the restructuring or bankruptcy, as well as the issuers for whom

the audit reports on financial statements or the review reports on condensed financial statements included

qualifications or disclaimer of opinion / report resulting from threats to the ability to continue as a going concern.

Table 2. Number of issuers with a modified opinion in the audit report or a modified conclusion in the review report

Reporting period	Year 2017	First half of 2018	Year 2018	First half of 2019
Qualified opinions or conclusions	19	25	20	12
Disclaimers of opinion / report	10	6	9	5
Adverse opinions or conclusions	1	1	1	0
TOTAL	30	32	30	17
Number of issuers at year-end*	456	456	441	441
Share in the number of issuers at year-end	7%	7%	7%	4%

* excluding closed-end investment funds and issuers for whom the Republic of Poland is a host state

Source: Own elaboration

Financial statements are subject to unlimited scope examination or focused examination. For issuers re-

viewed only for compliance with recommendations, a follow-up examination is carried out.

Unlimited scope examination – examination of the entire financial statements with the goal of identifying any deficiencies or mistakes.

Focused examination – examination limited to a scope concerning specific issues, the application of certain IFRSs (e.g. examination of selected items or parts of financial statements).

Follow-up examination – review of subsequent financial statements exclusively for the necessary improvements and developments, particularly when recommendations were submitted to the issuer.

Table 3. Number of issuers whose financial statements were subject to the periodic review in 2019, broken down by type of examination

Type of examination	Number of issuers
Unlimited scope examination	10
Focused examination	84
Follow-up examination	2
Total	96

Source: Own elaboration

In 2019, the focused examination covered mainly the topics highlighted in ESMA's *European common enforcement priorities for 2018 annual financial reports* and compliance with the requirements on disclosures about going concern and disclosures about liquidity risk.

The topics covered by the European common enforcement priorities for 2018 financial statements⁴ included:

- issues related to the application of IFRS 15 *Revenue from Contracts with Customers*;
- issues related to the application of IFRS 9 *Financial Instruments*; and
- disclosure of the expected impact of implementation of IFRS 16 *Leases*.

The following figure shows selected areas of non-compliance resulting from the review of issuers' financial statements carried out in 2019.

⁴https://www.knf.gov.pl/o_nas/wspolpraca_miedzynarodowa/unia/ESNF/aktualnosci?articleId=63613&p_id=18

Figure 1. Selected areas of non-compliance identified during the review of financial statements in 2019.

IFRS 9	• No disclosure or unclear accounting policies • Doubts about the provision matrix • Failure to take into account the small chances of obtaining economic benefits • Failure to take into account a change in the timing of payments • Failure to take into account a change resulting in derecognition from the balance sheet
IFRS 15	• No disclosure or unclear accounting policies • Unclear method of analysing and evaluating individual contracts • Doubts as to whether the issuer is an agent or a principal • Lack of transparency in the presentation of assets/liabilities on the balance sheet • No disclosures concerning the categories of revenue
Going concern, liquidity risk	• Unjustified statement of 'no threat to the ability to continue as a going concern' • No disclosures on threats to the ability to continue as a going concern • Vague disclosures on liquidity risk management • Insufficient information in the maturity analysis for financial liabilities • Lack of information on the breach of the terms of financing
Consolidation, business combination, joint control, subordinate entities	• No consolidation of the actual subsidiary • Unjustified consolidation of another entity • Doubts about the existence of joint control over another entity • Unclear rules for measurement of an investment in an associate • No disclosures on merger
Taxes	• Unjustified recognition of assets arising from disputes with tax administration • Questionable recognition of deferred tax assets • No disclosure of evidence to support the recognition of deferred tax assets
Impairment of assets	• Use of an incorrect beta measure • Adoption of a high growth rate for post-forecast period cash flows • Doubts about the consistency of assumptions for the impairment test • Failure to do the testing for impairment of cash-generating units (CGU) with goodwill after a business combination • Failure to take into account the indications for impairment • Incomplete disclosures on impairment tests
Fair value	• Disregarding the debtor's position in the valuation of their debt instruments • Treating the adjusted purchase price as fair value

Source: Own elaboration based on the review

As regards the practical application of IFRSs, it is also useful to take note of the ⁵packages of decisions on the enforcement of financial information,

Enforcement actions

After a review of financial statements, if there are any concerns or doubts about their correctness, the issuer or audit firm is asked to provide further clarification, pursuant to Article 68(1) and (2) of the Act on public offering.⁷

Pursuant to Article 68(5) of the Act on public offering, the Board of the Polish Financial Supervision Authority (PL: Komisja Nadzoru Finansowego, KNF Board) issues recommendations for an

made by the European national enforcers⁶ and published on the ESMA's website.

issuer to put an end to any breach of information requirements. The purpose of a recommendation is to allow the issuer to eliminate non-compliance as soon as possible by amending the relevant financial statements, and to ensure that the users of financial statements have access to fair and complete information. The implementation of recommendations is monitored.

Communication with the issuer and recommendations

In 2019, a **demand to provide explanations** on financial reporting was addressed to 67 issuers.

3 Review of non-financial disclosures and enforcement actions

Under Article 49b of the Accounting Act⁸, entities, including issuers of securities admitted to trading on a regulated market, must include in their management or directors' report, as a separate part, a non-financial statement, or prepare a separate non-financial report.

In 2019, the enforcement of non-financial information involved analysis

of compliance of all non-financial reports of issuers under Article 49b of the Accounting Act, which means that the reports were reviewed for the presence of the following information to the extent necessary to evaluate the issuers' business:

- a short description of the entity's business model;

Non-financial reporting: legal framework

⁵<https://www.esma.europa.eu/>

⁶<https://www.esma.europa.eu/press-news/esma-news/esma-publishes-23rd-extract-eecs-database>

⁷ Act of 29 July 2005 on public offering, conditions governing the introduction of

financial instruments to organised trading, and public companies (Journal of Laws 2019, item 623, as amended).

⁸ Accounting Act of 29 September 1994 (consolidated text: Journal of Laws 2019, item 351).

- the non-financial key performance indicators relevant to the entity's business;
- a description of the policies applied by the entity in relation to environmental, social and employee matters, respect of human rights, anti-corruption and bribery matters, as well as a description of the results of those policies;
- a description of due diligence processes, if the entity applies them within the framework of the above-mentioned policies;
- a description of material risks in the entity's business that may adversely affect non-financial matters, and a description of how those risks are managed.

Non-financial reporting

The disclosure requirements for non-financial information for 2018 applied to **158 issuers**, including:

- 10 issuers reports at entity-level only,
- 60 issuers reports at group-level only,
- 88 issuers in relation to both entity-level and group-level reports.

A total of **178 non-financial disclosures** for 2018 were made public by issuers, including:

- 79 statements,
- 99 reports.

Nine issuers benefited from the exemption from the obligation to make non-financial statements/reports pursuant to Article 49b(11) of the Accounting Act, as a non-financial statement/report containing information concerning the relevant issuer had been published by the next most senior parent.

The non-financial statements/reports for 2018 were prepared in accordance with the following standards:

- GRI (Global Reporting Initiative) – 60 issuers,
- SIN (Non-financial Information Standard) - 23 issuers,
- own standards – other issuers.

Non-financial reporting: enforcement actions

In 2019, as part of the enforcement of non-financial information, 8 issuers received **recommendations** to make public annual reports containing non-financial statements/reports as specified in Article 49b of the Accounting Act.

The recommendations concerned:

- the description of material risks in the entities' business,
- the description of non-financial key performance indicators relevant to the entity's business,
- insufficient range of micro-data.

4 Analysis of timeliness of publication and completeness of the issuers' periodic reports, and enforcement actions

As of 31 December 2019, the requirement to publish periodic reports pursuant to Article 56(1) point 3 of the Act on public offering applied to **436 issuers** of securities admitted to trading on a regulated market, other than investment funds.

In addition, as of 31 December 2019, **338 issuers** that were parents of groups were required to publish consolidated periodic reports.

In total, in 2019, more than **2 thousand periodic reports** were published by issuers.

In the case of 23 issuers there were problems with the timely fulfilment of periodic reporting requirements. Enforcement actions were undertaken in relation to those entities.

449 issuers of securities admitted to trading on a regulated market other than investment funds were subject to the requirement to publish the reports for 2018.

Monitoring the timeliness and completeness of periodic reports

The enforcement actions undertaken in 2019 with regard to the timely publication of the issuers' periodic reports included:

- 14 cases where a competent department of the UKNF was asked to request the Warsaw Stock Exchange **to suspend trading** pursuant to Article 20 of the Act on trading in financial instruments⁹, in connection with a failure to publish periodic reports in a timely manner or a failure to include in the annual and half-yearly reports, as appropriate, the auditor's report on the audit or review of financial statements, including:
 - lack of the report for 2018,

⁹ Act of 29 July 2005 on trading in financial instruments (consolidated text: Journal of Laws 2018, item 2286, as amended).

- lack of the auditor's report on the audit of financial statements for 2018,
- lack of report for the first quarter of 2019,
- lack of report for the first half of 2019,
- lack of the auditor's report on the review of financial statements for the first half of 2019.

As part of the monitoring of completeness of periodic reports, special attention was paid to the compliance by issuers with the new provisions of the Regulation on current and periodic information¹⁰ in relation to the inclusion of additional elements specified in § 70(1) points (7) and (8) and § 70(6)(I) concerning:

- the management report and the statements of the supervisory

board on the selection of the audit firm to audit the annual financial statements, and compliance with the rules governing the appointment, composition and operation of the audit committee,

- inclusion, in the issuer's management or directors' report, of information about the audit committee.

Most irregularities identified were the ones listed above.

The enforcement actions undertaken in 2019 with regard to the completeness of the issuers' periodic reports included:

- addressing **recommendations** to 61 issuers pursuant to Article 68(5) of the Act on public offering, to submit, supplement or correct periodic reports. Those included recommendations:
 - to supplement the management report drawn up on the basis of a statement of the supervisory board on the selection of the audit firm to audit the annual financial statements in accordance with the rules,

¹⁰ Regulation of the Minister of Finance of 29 March 2018 on current and periodic information provided by issuers of securities and on conditions under which information required by legal regulations of a third country may be recognised as equivalent (Journal of Laws 2018, item 757).

- to supplement the report with a statement of the supervisory board that the rules on the appointment, composition and operation of the audit committee are complied with, or that the requirements laid down in the applicable rules for entrusting the function of audit committee to the supervisory board have been fulfilled, and that the audit committee or the supervisory board was performing the tasks of the audit committee provided for in the applicable rules,
 - to supplement the information contained in the corporate governance statement in relation to the audit committee by identifying persons who fulfil the statutory criteria of independence, persons who have the skills and knowledge in the field of accounting and/or audit of financial statements, with an indication of how such skills and knowledge have been acquired, and persons who have the skills and knowledge relating to the industry in which the issuer operates, with an indication of how they have been acquired,
 - to supplement the report with the supervisory board's assessment, with reasons, of the issuer's management or directors' report and financial statements for their compliance with the books, documents and facts,
 - to supplement the management or directors' report with the names of suppliers and/or customers where the share of one customer or supplier has reached at least 10% of the total sales revenue,
 - to supplement the management or directors' report, where the issuer issued securities during the period covered by the report, with information on when, for what purposes and in what amount the proceeds from the issue were earmarked,
 - to supplement the management or directors' report with details of past-due liabilities and short-term contingent liabilities and information on whether the issuer has the funds to settle them and, if not, when and how the company has acquired or is planning to acquire cash and what barriers it has encountered and what actions it has taken or is planning to take,
- sending to 82 issuers a **request for clarification** in connection with doubts as to the correctness of the annual reports for 2018 as specified in the 1st indent.

5 Review of issuers' inside information and enforcement actions

As of 31 December 2019, the requirement to publish inside information applied to **911 issuers**, including 517 on a regulated market (national and foreign issuers of shares, issuers of covered bonds, local government units and issuers of investment certificates and issuers of bonds) and 395 in an alternative trading system (issuers of shares and bonds). As regards the is-

suers whose securities were introduced to an alternative trading system, the enforcement of inside information, in accordance with the Act on public offering, is carried out by the trading system organiser. To that end, the KNF Board cooperates with the Warsaw Stock Exchange and intervenes when an alternative trading system organiser has difficulty in obtaining explanations from issuers.

Enforcement of inside information

In 2019, as part of the enforcement of issuers' inside information, 55 recommendations were made to stop infringements of information disclosure obligations, including:

- a failure to make public information on the submission of an application for the opening of restructuring or insolvency proceedings, a failure to provide information on the court decisions made in the course of restructuring and insolvency proceedings,
- a failure to identify the opening of negotiations as inside information, a vague designation of the subject-matter of the negotiations and the counterparty,
- a failure to identify the parties to contracts concluded by issuers, the financial terms, the subject-matter of contracts, specific contractual stipulations, information on the links with the counterparty,
- a failure to identify the information on termination of a contract as inside information, a failure to indicate the effects of termination,
- processes distributed over time (including processes related to the purchase or sale of assets, acquisition of other entities), in particular due to the failure to properly identify subsequent inside information, update information on the results of subsequent stages,
- a failure to identify the information on deterioration in the financial position as inside information, inaccurate indication of the circumstances and reasons of such deterioration.

The purpose of the enforcement actions taken in that respect was to ensure that inside information was made public by issuers in a manner which al-

lows investors to access such information quickly and make a full, proper and timely assessment of such information.

6 Selected areas of financial reporting that require attention

Following the 2019 review, this report presents issues that require attention while drawing up financial statements for the financial year 2019 and subsequent reporting periods. This will include requirements covered by ESMA's most recent common enforcement priorities.

In addition to topics directly related to the application of the relevant accounting standards, a new particular issue is the European Single Electronic Format (ESEF).

European common enforcement priorities for 2019 annual financial reports

- specific issues related to the application of **IFRS 16 Leases**;
- follow-up of specific issues related to the application of **IFRS 9 Financial Instruments** for credit institutions and **IFRS 15 Revenue from Contracts with Customers** for corporate issuers; and
- specific issues related to the application of **IAS 12 Income Taxes** (including application of **IFRIC 23 Uncertainty over Income Tax Treatments**).

European common enforcement priorities

6.1 Impact of COVID-19

The ongoing COVID-19 pandemic affects also the business activities of issuers. They should therefore draw attention to the need to accurately reflect, in the financial statements, the impact of the pandemic on the financial position, performance and cash flows of the entity concerned.

The events and transactions occurring before the end of the reporting period should be included directly under the headings of the main parts of financial

statements. Special attention should be paid to the items for which recognition or measurement depends on estimates, including forecasts. The pandemic may reduce the certainty about future events and consequently about the correctness of estimates. Regardless of the entity's obligation to recognise and measure individual items to the best of its knowledge, the financial statements should also include disclosures on any significant

judgement and estimation uncertainty (see paragraphs **122–134 of IAS 1 Presentation of Financial Statements**).

From the point of view of users of financial statements, information on the events after the reporting period may also be very useful. The requirements in that respect apply to both annual financial statements (paragraphs **21–22 of IAS 10 Events after the Reporting Period**) and interim financial statements (paragraph **6A(h) of IAS 34 Interim Financial Reporting**).

It is appropriate to follow communications from supervisory authorities, including the European institutions: [ESMA](#), [EBA](#) and [EIOPA](#), relating to financial reporting. Particular attention should be paid to positions on the application of IFRS 9 *Financial Instruments* by creditors.¹¹ The positions focus on the classification and measurement of financial assets measured at amortised cost in connection with the implementation of special relief

measures for debtors, provided for in both the generally applicable law and the law applied on the initiative of credit institutions. It has been stressed that each case should be examined individually, any automatic use of standard interpretations should be avoided and, consequently, that the previous approach is not advisable in the following areas:

- identification of a significant increase in credit risk (SICR);
- forecasting cash flows for the purpose of determining expected credit losses;
- considering the public guarantees provided by public authorities in determining expected credit losses;
- identifying items for which a forbearance measure was granted.

It should be stressed that, as with the application of other standards, issuers should disclose all significant judgements and estimation uncertainty related to the implementation of the IFRS 9 requirements.

6.2 Application of IFRS 9

IFRS 9, although it had the greatest impact on financial statements of financial institutions, is significant for all issuers applying IFRSs. Attention should be paid to, *inter alia*, disclosures related to the application of IFRS 9, in particular the disclosures on the aspects of ECL¹² estimation which are

subject to significant judgement and may be individualised for each entity. The IFRS 9 requirements on the estimation and recognition of credit losses are closely related to the disclosure requirements laid down in the provisions of another standard, i.e.

¹¹ [ESMA's Public statement of 25 March 2020: Accounting implications of the COVID-19 outbreak on the calculation of expected credit losses in accordance with IFRS 9 \(ESMA32-63-951\)](#).

[EBA's Statement of 25 March 2020 on the application of the](#)

[prudential framework regarding Default, Forbearance and IFRS9 in light of COVID-19 measures](#).

¹¹ cont. [EBA's Guidelines of 2 April 2020 on legislative and non-legislative moratoria on loan repayments applied in the light of the COVID-19 crisis](#)

¹² Expected credit loss.

IFRS 7 *Financial Instruments: Disclosures*. Having regard to the quality of subsequent financial statements drawn up by issuers, it should be stressed that information related to credit risk, required under IFRS 7, may be relevant to the understanding of financial statements.

It is common for issuers outside the financial institutions sector to apply practical ECL solutions which very often take the form of a provision matrix for the entity's receivables.

It should be noted that financial assets for which no impairment losses are recognised represent an exception, in particular in the case of trade receivables and receivables on loans granted. It is expected that the carrying amount of those assets will not be the same as the nominal value of the financial instrument. The possibility to apply a practical solution (e.g. the provision matrix) is without prejudice to the basic requirements on the ECL model (see paragraph B5.5.35 of IFRS 9).

6.3 Credit risk and liquidity risk

When presenting information on each type of risk arising from financial instruments, reference should be made to concrete entity-specific and group-specific information on the level of exposures to each risk and how they arise, as well as appropriate changes as compared to the previous period (**paragraphs 33 and 34 of IFRS 7 *Financial Instruments: Disclosures***).

Both quantitative and qualitative disclosures are important, as stated in

The method of determining the provision matrix should be clear. The method of identifying the group of defaulted assets (receivables) should be comprehensible and verifiable. The review should cover the assets that have remained past due for a long period of time (12 months, 18 months, 24 months), especially if their carrying amount is significant.

Paragraph 5.4.4 of IFRS 9 stipulates that assets should be reduced in their entirety if the entity has no reasonable expectations of recovering such assets. Such a write-off can relate to an asset in its entirety and result in its derecognition.

It is important to stress that the preparation of subsequent financial statements should involve a careful analysis of the estimation and recognition of expected credit losses and that it is necessary to ensure adequate and clear disclosures in that respect.

paragraph 32A of IFRS 7. According to **paragraph 34(a) of IFRS 7**, quantitative data on the degree of risk exposure at the end of the reporting period are based on information provided internally to the entity's key management personnel, e.g. the management board or CEO.

The following are the elements of disclosures that require special attention in the preparation of the financial statements.

IFRS 9 outside financial institutions

Credit risk

The following failures to provide disclosures about credit risk should be addressed:

- how the issuer defined default for various financial instruments and the reasons for choosing those definitions, in the light of **paragraphs 35F(b) and B8A of IFRS 7**. Information on the definitions of default adopted by the issuer is intended to help users of financial statements to understand how the entity has applied the expected credit loss requirements of IFRS 9. It is therefore also important to clarify what factors are taken into account when assessing the reversal of a significant increase in credit risk, taking into account **paragraph B8A(c) of IFRS 7**.
- presentation of financial assets that are more than 30 days past due for which the issuer rebutted the presumption that the credit risk has increased significantly since initial recognition (**paragraph 35F(a)(ii) of IFRS 7**), including justification of the approach taken,
- indication whether the entity uses practical expedients related to significant increase in credit risk,
- indication of the amount of exposure of non-performing loans (NPLs) at the end of the reporting period and a reference of that amount to the reported amount of assets in Stage 3,

Liquidity risk

The primary disclosure requirement in the area of **liquidity risk** is to provide a maturity analysis for financial liabilities, which should also cover trade

- the presentation of assets by type (e.g. class, product type) where there was a significant increase in the probability of default over the lifetime of an asset, including presentation of indicators taken into account in the assessment process.

The inclusion of the above information in financial statements is necessary to understand the impact of credit risk on the amount, time distribution and uncertainty of future cash flows.

The entities which draw up financial statements should therefore pay particular attention to quantitative and qualitative information which enables the users of financial statements to assess the amounts reported in the financial statements that result from expected credit losses, including changes in the amount of expected credit losses and the reasons for such changes.

Undoubtedly, an important disclosure that allows the assessment of the exposure and concentration of credit risk is the presentation of the gross carrying amount of financial components (including contract assets) broken down by credit risk rating grades, and the presentation of exposure to credit risk on loan commitments and financial guarantee contract (see **paragraph 35M of IFRS 7**).

payables (**paragraph 39 of IFRS 7**). The analysis consists in presenting the maturities of (past due and non-past due) financial liabilities in detailed time

Credit risk (IFRS 7)

Liquidity risk (IFRS 7)

bands as indicated in paragraph **B11 of IFRS 7** (also for comparative data). Important information from the point of view of users of financial statements is the disclosure of how the settlement of liabilities will be distributed over the next 12 months. The presentation of intervals of less than 12 months definitely facilitates the analysis of such information, as it is often crucial for assessing the situation of the issuer and its prospects to match inflows and outflows of cash in the short term. On the other hand, the presentation of excessive maturity bands of short-term liabilities (or merely a breakdown into long-term and short-term liabilities) does not reflect the degree of concentration of payments over time and in many cases makes it impossible to analyse the liquidity risk involved.

It is necessary to pay attention to disclosures regarding liquidity risk management, in particular the concrete and specific activities that are relevant to the assessment of the issuer's ability to meet its liabilities. Special attention is required in relation to the means and instruments the issuer can use to respond to a reduction in liquidity (**paragraph 39(c) of IFRS 7**). Unfortunately, financial statements often contain only vague information on

that subject and do not contain any specific information in the liquidity risk note and do not refer to other parts of the financial statements containing useful information.

When fulfilling the above-mentioned requirements of IFRS 7, one should take into account the disclosures about liquidity risk specified in Appendix B (**paragraphs B10A, B11A–F**), which forms an integral part of IFRS 7. There is no doubt that the assessment of the extent of the risk makes it possible to explain how the aggregated quantitative data disclosed on the basis of information provided internally to key managers have been established. In addition, where there are different possible maturities of a liability, the maturity analysis should disclose that liability as at the earliest date within which it may be due.

Disclosures about risks relating to financial instruments, including liquidity and credit risks, are of particular importance when there are uncertainties regarding the continuity of the operations of the issuer and its group. For the issuers that are undergoing a restructuring process, it is essential to disclose the maturity analysis for the financial liabilities resulting from an approved arrangement with creditors.

6.4 Application of IFRS 15

IFRS 15 introduces certain changes in the recognition of revenue and related disclosures. The application of the new standard in relation to changes in presentation and disclosures may be significant, even if the quantitative effect itself is negligible. The standard must apply to parties

carrying out very diverse activities around the world, so the regulation uses general terms that can potentially cover any type of business. At the level of a single entity applying IFRS 15, there is a need to make the provisions of IFRS 15 more specific, so

Disclosure of accounting policies

that they fit the type of business concerned. Therefore, when preparing their financial statements, issuers should make every effort to ensure that the accounting policies are presented at a level of detail that will allow investors to understand the accounting principles concerning revenue and their impact on financial statements. This means that the financial statements should contain a description of the individualised and specific accounting policies used by the issuer, as opposed to extensive parts taken from IFRS 15 or template descriptions.

The description of accounting policies should refer to, *inter alia*:

- identification of performance obligations (see **paragraph 119 of IFRS 15**),
- determination of the transaction price and allocation of the transaction price to the performance obligations (see **paragraph 126 of IFRS 15**),
- the methods for measuring the degree of fulfilment of the performance obligation, including a description of the issuer-specific reasons for recognising revenue, i.e. a description of cases in which such revenue is recognised either over

time or at a point in time (see **paragraphs 124–125 of IFRS 15**).

- recognition of contract assets and contract liabilities from contracts with customers (see **paragraph 117 of IFRS 15**),
- updated estimates of transaction prices (see **paragraph 118 of IFRS 15**).

In addition, it should be stressed that with regard to revenue, paragraph 114 of IFRS 15 requires disclosure of how the categories of revenue from contracts with customers adopted by the issuer depict how the nature, amount, timing and uncertainty of revenue and cash flows are affected by economic factors.

It should be noted that in some cases the above-mentioned disclosure elements may be irrelevant to the issuer concerned. However, if, in the implementation or application of IFRS 15, a given aspect requires a deeper analysis by the management, this may be a prerequisite for considering that it would be appropriate to provide the relevant information and comment on a personalised accounting policy. Therefore, for such disclosures to be useful, they should be presented in the context of the contracts, terms and conditions and situations that are typical of the issuer.

6.5 Implementation of IFRS 16

Specific issues related to the application of IFRS 16 *Leases* in the 2019 financial statements for lessees.

IFRS 16 is effective for annual reporting periods beginning on or after 1 January 2019, with earlier application permitted but only if the entity also implemented IFRS 15 by the effective

date of that standard. The monitoring and assessment activities in relation to 2019 annual financial reports of is-

suers, in line with ESMA's enforcement priorities¹³, will include i.a. the implementation of IFRS 16.

Lease term

ESMA expects issuers to provide information on the judgements made by the management in determining the lease term (**paragraphs 18–21 and B34–41 of IFRS 16**). ESMA stresses that determination of the lease term is one of the aspects that require the use of judgement, notably when the lease contract does not contain specific clauses regarding the termination, cancellation or renewal of the lease. ESMA points out the IFRS Interpretations Committee's agenda decision of 26 November 2019 (*IFRS IC Agenda Decision*)¹⁴ on lease terms and the

economic life of leasehold improvements recommends that issuers that may be affected by the Agenda Decision to continuously monitor the future discussions within the IFRS IC and to provide appropriate information on the accounting policies. ESMA encourages issuers to disclose sufficient information on the judgements made in determining the lease term that is necessary to achieve the objective of **paragraph 51 of IFRS 16** and for compliance with the requirements set out in **paragraphs 122 and 125 of IAS 1 Presentation of Financial Statements**.

IFRIC Agenda Decisions vs. lease term

Discount rate

An issuer that is a lessee should measure the lease liability, discounting the lease payments using the interest rate implicit in the lease. If the interest rate implicit in the lease cannot be readily determined, the lessee should use its incremental borrowing rate, which should be determined as a specific

rate for the relevant lease, considering the underlying asset and the terms and conditions of the lease. ESMA highlights the IFRS IC discussion on the issue¹⁵ and reminds issuers to consider the objective set out in IFRS16 when determining the incremental borrowing rate.

Presentation and disclosures

ESMA notes that issuers that are lessees should disclose in the financial statements information that is useful to the users of the financial statements. The disclosures should enable users to assess the effect that leases have on the statements of financial

position, the statement of comprehensive income and the statement of cash flows (**paragraphs 51–52 of IFRS 16**).

One of the disclosure requirements in the first year of application of the new

¹³ ESMA Public Statement on European common enforcement priorities for 2019 annual financial reports (ESMA32-63-791) https://www.knf.gov.pl/o_nas/wspolpraca_miedzynarodowa/unia/ESNF/aktualnosci?articleId=67515&p_id=18

¹⁴ <https://www.ifrs.org/news-and-events/updates/ifric-updates/november-2019/#3>

¹⁵ <https://www.ifrs.org/news-and-events/updates/ifric-updates/september-2019/#7>

standard is an appropriate explanation of the nature and impact of any changes in accounting policies as well as the quantification of the impact on each item of the financial statements (**paragraph 28 of IAS 8 and paragraphs C12–C13 of IFRS 16**) and changes in presentation (**paragraphs 47–50 of IFRS 16**). In addition, the issuers are required to provide information on significant judgements and assumptions made when applying IFRS 16 (**paragraphs 122–126 of IAS 1**). These judgements may include, in particular, determining the lease liability (e.g. lease term, discount rate used) as well as assessing whether a contract meets the definition of a lease under IFRS 16.

The lessees are also required to provide disclosures specified in **paragraphs 53–60 of IFRS 16**, including *inter alia*:

- depreciation charges for the lease assets (right-of-use assets) by class,

Impairment of right-of-use assets

At the end of each reporting period, a right-of-use asset is subject to an assessment whether there is an indication that the asset may be impaired and if such an indication is found, the entity tests the asset for impairment (**paragraph 33 of IFRS 16**). Therefore, it may be necessary to adapt the impairment test to take into consideration the specificities of lease accounting when calculating the cash-flows for the purpose of determining the recoverable amount. In this respect, in

an interest expense on the lease liabilities, expense relating to short-term leases and leases of low-value assets, expense relating to variable lease payments (not included in the measurement of lease liabilities), income from subleasing lease assets, total cash flow from leases, components added to lease assets, gains and losses on sale and lease-back transactions, the carrying amount of the lease assets at the end of the reporting period (**paragraphs 53–54 of IFRS 16**),

- entity-specific qualitative and quantitative information on the nature and main characteristics of leases, future outflows not included in the measurement of lease liabilities, sale and leaseback (**paragraphs 59 and B48–B52 of IFRS 16**),
- maturity analysis of the lease liabilities, separately from the analysis of other financial liabilities (**paragraph 58 of IFRS 16**).

addition to the disclosures required in **paragraph 134 of IAS 36**, ESMA encourages issuers to provide information on how the methodologies, inputs and assumptions used for carrying out their impairment tests have changed, for instance in determining the carrying amount and the value in use of the CGU that includes the right-of-use asset as well as the treatment of lease liabilities in the impairment test.

Transitional provisions

In relation to the transition disclosures, issuers should disclose the transition method they have chosen (**paragraph C5 of IFRS 16**), the practical expedients applied (**paragraph C10 of IFRS 16**), and the recognition exemption in IFRS 16 (**paragraph 5 of IFRS 16**).

ESMA reminds issuers that the right-of-use asset recognised by a lessee at the date of initial application for leases previously classified as operating leases under IAS 17 may differ from the lease liability under the modified retrospective method (for example, when any prepaid or accrued

lease payments exist before the date of initial application) (**paragraph C8(b)(ii) of IFRS 16**).

If the modified retrospective approach has been applied, ESMA reminds issuers that they are required to explain any difference between the operating lease commitments disclosed when applying IAS 17 and the lease liabilities recognised under IFRS 16 and to provide information on the weighted average incremental borrowing rate applied to leasing liabilities at the date of first application (**paragraph C12 of IFRS 16**).

Alternative performance measures

As a result of the implementation of IFRS 16, some issuers have modified or included new alternative performance measures (APMs) in their communication documents (e.g. *ad hoc* disclosures, prospectuses or management reports). ESMA points out that in accordance with the ESMA Guidelines on APMs (ESMA/2015/1057, Annex

IV, 30 June 2015), the issuers' reports should include information on APMs. Special disclosures on APMs should be provided by the issuers who have applied the modified retrospective approach and for whom the financial data for the current reporting period and previous years will not be comparable.

6.6 Control and consolidation

One of the most important issues of financial reporting that often require in-depth analysis is to determine whether an entity controls another entity and whether that another entity should be consolidated. The respective rules are contained in IFRS 10 Consolidated *Financial Statements*.

The provisions of IFRS 10 require an assessment in terms of control over an entity and determination of the status of the parent irrespective of the nature of the investor's involvement in

the entity (see **paragraph 5 of IFRS 10**). In turn, exercising control over another entity requires the parent to draw up consolidated financial statements (**paragraph 4 of IFRS 10**).

It should be stressed that in assessing whether the issuer controls the investee, it is necessary consider all relevant facts and circumstances.

The economic environment in which entities (issuers) operate is not uniform and therefore, in practice, a variety of solutions is used in the relations

between the cooperating entities. Businesses operate in different organisational structures, have different business models and complicated co-operation rules, and often have formal or informal personal links between them. The IFRS itself indicates that sometimes the assessment of power is obvious and is based on rights and so the power can be assessed by taking into account the voting rights. In other cases, however, the assessment is more complex and will require more than one factor to be considered, for example when the power results from one or more contractual arrangements (**paragraph 11 of IFRS 10**). This issue needs to be emphasised, given that in practice there are often cases where the assessment of the existence of power and control requires a deeper analysis than an assessment of the voting rights held. Some issues need to be considered in the process of assessing the existence of control over other entities, especially in non-obvious cases where there is a need for a broader approach to the assessment of control.

As part of the assessment of power, IFRS 10 points to the appropriateness of the analysis for the existence of 'more than a passive interest in the investee', as stated in **paragraph B19 of IFRS 10**. This applies, for example, where strong and multi-faceted long-term business relations or personal links exist or have existed between the issuer and other entities. Even the informal links existing in the past may constitute a prerequisite for analysing them in terms of the possibility of exercising power over another entity if the impact of such links is relevant to the current situation. An example is

the situation in which the key management personnel of a given entity are current or previous employees of the issuer (see **paragraph B19(a) of IFRS 10**).

Particular consideration should be given to situations in which the entity, as part of close business relationships with other entities:

- is able to direct the manufacturing processes so as to achieve economies of scale, cost savings using the assets and processes of other entities;
- exchange expertise and know-how with cooperating entities (see **paragraph B57 of IFRS 10**);
- has a decisive influence on the funding of those cooperating entities (setting deadlines for their debts, guaranteeing their obligations) (**paragraph B19(b)(i) and (ii) of IFRS 10**);
- there is a strong specialisation of production,
- the manufacturing processes of the entity and a given counterparty are complementary, and the operational efficiency and profitability of the issuer depends on the results of the cooperation (**paragraph B57(c) of IFRS 10**).

A comprehensive approach is needed to analyse the facts and circumstances that may indicate the exercise of power over another entity. The said **paragraph B19** indicates other elements which suggest that the issuer's interest in an entity may be more than passive and, in combination with other rights, may indicate that the entity has power.

Actual control

Particular attention should also be paid to the fact that according to **paragraph 12 of IFRS 10**, an issuer may have power even if its rights to direct the relevant activities of another entity on a day-to-day basis have not yet been exercised, it is only sufficient for the issuer to have that possibility. Thus, in the assessment process, the issuer should take into account the facts and circumstances showing that the issuer has the practical ability to direct the relevant activities, not merely confined to voting rights or contractual arrangements (see **paragraph B18 of IFRS 10**).

Another important issue in the assessment of control is whether an investor with decision-making rights determines whether it is a principal or an agent (see **paragraph 18 of IFRS 10**). In this respect, when assessing control over the investee, the issuer should consider the nature of its relationship with other parties (**paragraph B4 of IFRS 10**) and determine, *inter alia*,

whether those other parties are acting on its behalf, i.e. they are 'de facto agents', which requires an assessment of the situation, considering not only the nature of the relationship but also how those parties interact with each other and the issuer (see **paragraph B73 of IFRS 10**).

Furthermore, if the facts and circumstances indicate that there has been a change in one or more elements of the three elements of control (see also **paragraphs B80–B85**), it is necessary to carry out a reassessment as to the control of the entity concerned (see **paragraph 8 of IFRS 10**). Control may be lost due to contractual arrangements, as a result of which the issuer cannot continue to benefit from the entity in which it invests. It should therefore be noted that the assessment of control should be carried out on an ongoing basis, considering the changes in the circumstances and facts that may be relevant in this respect.

Analysing the relations and links between entities and evaluation in terms of controlling another entity is often a complex process, due to the diversity of solutions that are used in economic realities. These are only some of the provisions which, in the opinion of the persons drawing up this report, contain important issues to be taken into account, but each entity should carry out its own analysis tailored to the economic circumstances in which it operates.

Individual assessment of control

6.7 European Single Electronic Format (ESEF)

In accordance with the provisions of the Transparency Directive¹⁶ and regulatory technical standards on the specification of a single electronic reporting format (RTS on ESEF)¹⁷, issuers whose securities are admitted to trading on a regulated market in the European Union will be required to prepare their financial reports in a European single reporting format (ESEF) for financial years beginning on or after 1 January 2020. According to the RTS on ESEF, issuers will prepare their annual reports and consolidated annual reports in XHTML format. Reports prepared in that format can be opened and viewed using a standard web browser. In addition, in the case of consolidated annual reports, the RTS on ESEF require that the core parts of consolidated financial statements¹⁸ be marked up (tagged) in accordance with the ESEF taxonomy, based on IFRS Taxonomy and using the XBRL markup language. The XBRL tags are to be embedded in the XHTML documents using Inline XBRL (iXBRL) specification. Furthermore, according to the RTS on ESEF, starting from 1 January 2022, notes to consolidated financial statements must also

be marked up using the 'block tagging' standard, which means that entire sections of notes will be tagged by a single taxonomy element.

The new RTS on ESEF requires each issuer, in particular, to perform an in-depth analysis for the presence, in ESEF taxonomy, of the tags needed to identify individual items in the main parts of consolidated financial statements. Such analysis is intended to prevent unnecessary formation of taxonomy extensions. It should also be noted that taxonomy extension elements must be created in accordance with the principles set out in the RTS on ESEF and the ESEF Reporting Manual¹⁹ available on the ESMA and KNF website.

The UKNF has started work to adapt the existing ESPI system to the adoption, validation and publicity of ESEF reports. The adaptation of ESPI to the ESEF requirements marks the beginning of a new reporting platform for the exchange of user-friendly information based on modern information technologies.

¹⁶ Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC.

¹⁷ Commission Delegated Regulation (EU) 2018/815 of 17 December 2018 supplementing Directive 2004/109/EC of the European Parliament and of the Council with regard to regulatory technical standards on the specification of a single electronic reporting format.

¹⁸ A statement of financial position (balance sheet), a statement of profit or loss and other comprehensive income (income statement, profit and loss account), a statement of cash flows, a statement of changes in equity.

¹⁹https://www.esma.europa.eu/sites/default/files/library/esma32-60-254_esef_reporting_manual.pdf
https://www.knf.gov.pl/knf/pl/komponenty/img/Esef_reporting_manual_68573.pdf

7 Summary

The purpose of publication of issuers' information is to provide stakeholders with information that is useful in making investment decisions. Regulated information should provide an appropriate level of detail, which will help to fully understand the impact of a given topic on the issuer's activities. It is particularly useful to take into account information that is entity-specific.

It should be remembered that:

- including many pieces of irrelevant information reduces the understandability of the report,
- the fair and comprehensible reporting may require disclosure of additional information which is not explicitly required by specific provisions,
- boilerplate language should be avoided,
- facts and circumstances that require a particular analysis and evaluation by the management may constitute material information expected by users of regulated information of the issuer.