

Draft Comment Letter

You can submit your comments on EFRAG's draft comment letter by using the '[Express your views](#)' page on EFRAG's website, then open the relevant news item and click on the 'Comment publication' link at the end of the news item.

Comments should be submitted by **28 September 2020**.

International Accounting Standards Board
7 Westferry Circus, Canary Wharf
London E14 4HD
United Kingdom

[XX Month 2020]

Dear Mr Hoogervorst,

Re: IASB ED/2019/7 *General Presentation and Disclosures*

On behalf of the European Financial Reporting Advisory Group (EFRAG), I am writing to comment on Exposure Draft *General Presentation and Disclosures*, issued by the IASB on 17 December 2019 (the ED).

This letter is intended to contribute to the IASB's due process and does not necessarily indicate the conclusions that would be reached by EFRAG in its capacity as advisor to the European Commission on endorsement of definitive IFRS Standards in the European Union and European Economic Area.

EFRAG welcomes that the IASB's ED is focused on improving how information is communicated in the financial statements. This project responds to a strong demand from users of financial statements and respondents to the IASB 2015 *Agenda Consultation* to undertake a project on primary financial statements. EFRAG particularly welcome the IASB's proposals to address this request in an Exposure Draft rather than in a Discussion Paper.

EFRAG also agrees with the IASB's proposal to update current requirements through the issuance of a new IFRS Standard, even if the IASB focused on information about performance in the statement of profit or loss. Such an approach has the benefit of highlighting the importance and impact of the proposed changes on the presentation of financial statements across different industries.

EFRAG highlights that the main challenge of this project is to strike the right balance between satisfying the needs of users by providing a more harmonised structure and content of the statement(s) of financial performance, while also allowing management to convey its views of the company's financial performance.

Summary of EFRAG's views on the ED

New subtotals and categories in the statement of profit or loss

In general, EFRAG welcomes the IASB's efforts to improve the structure and content of primary financial statements, as currently there is diversity in practice on the presentation of subtotals. In particular, EFRAG supports the IASB's proposals to present an operating, investing and financing category, subject to materiality considerations, as they have the potential benefit of reducing diversity in practice and improving comparability of financial statements. However, EFRAG considers that:

- it is key to have clear guidance on the notion of the ‘entity’s main business activity’, or in the course of the entity’s main business activity’ (please see EFRAG’s reply to Question 3 in Appendix 1);
- the IASB should consider, as part of the effects of these proposals, the interaction of the IASB proposals with existing regulatory frameworks on the presentation of financial statements;
- both the statement of financial performance and the statement of cash flows will have three different categories with similar labelling (operating, investing and financing) even if they are not aligned. As further described below, EFRAG would encourage a separate project on IAS 7 to improve consistency with the new content and structure of the statement of profit or loss. As long as the two statements are not aligned, EFRAG considers that it would be useful to use a different labelling in the two statements to avoid confusion;
- the ‘free’ accounting policy choice in paragraph 51(b) of the ED (for entities that provide financing to customers) may result in the loss of relevant information for users, in particular when used by non-financial institutions (e.g. manufacturer providing financing to customers); and
- it would be useful to consider whether ‘incremental expenses’ related to financing activities should also be in the financing category, by symmetry, with expenses relating to investing activities.

Integral and non-integral associates and joint ventures

EFRAG considers that providing a distinction between integral and non-integral associates and joint ventures will help users of financial statements to easily distinguish between associates and joint ventures that are closely related to the entity’s main business activities and those that are not. EFRAG’s research¹, similar to the findings of other recent studies, has shown that there is diversity in practice on the presentation of the share of profit or loss of associates and joint ventures, which was presented either before or after the subtotal ‘operating profit or loss’ by the majority of the entities analysed by EFRAG in its early stage analysis. Thus, the IASB’s proposal to split between ‘integral’ and ‘non-integral’ has the potential of enhancing comparability. However, EFRAG highlights that such presentation requirements will involve significant judgements and assumptions and they will need to be tested in practice.

EFRAG highlights that the IASB’s proposals would also apply to separate financial statements. In particular, the IASB’s proposals would apply to associates and joint ventures in the separate financial statements, which may in some cases raise questions about the applicability of the proposed definitions. EFRAG considers that there is a need for the IASB to further discuss how its proposals in general would apply to the separate financial statements, including the challenges that may arise in practice to those who prepare and use separate financial statements.

Roles of the primary financial statements and the notes, aggregation and disaggregation

EFRAG welcomes the IASB’s proposal to describe the respective roles of primary financial statements, the notes and the proposal for principles, and the general requirements on the aggregation and disaggregation, as a complement to the additional subtotals in the statement of profit or loss. EFRAG notes that having the principles and general requirements on aggregation and disaggregation of information in the financial statements, within a single place in the new standard, will improve clarity and consistency.

¹ The results of this EFRAG’s research are presented in Appendix 2 and form the basis for Early Stage Analysis (ESA).

Analysis of operating expenses

EFRAG supports the IASB's proposal to continue to require entities to present an analysis of expenses using either by-function or by-nature method, based on whichever method provides the most useful information to users of financial statements. However, EFRAG suggests that the IASB clarifies that paragraph B47 of the ED allows, or even requires, a mixed basis of presentation when an entity presents line items under paragraphs 65 and B15 of the ED.

Unusual income and expenses

EFRAG welcomes the IASB's efforts to define unusual income and expenses and to require entities to disclose such items in the notes, as such disclosure provides useful information to users of financial statements. However, EFRAG highlights that the definition of unusual items seems to be rather narrow, as it only focuses on whether expenses/income will occur in the future. Instead, EFRAG suggests the IASB considers not only items that 'will not arise for several future annual reporting periods' (as expressed in the ED) but also items that presently occur in the business, but only for a limited period of time (e.g. those identified in paragraph B15 of the ED such as restructuring costs).

Management performance measures ('MPMs')

EFRAG agrees that non-IFRS measures are often used in practice and additional guidance could bring more transparency and consistency on their use. EFRAG therefore welcomes the IASB's efforts to provide guidance on MPMs. However, EFRAG highlights a number of challenges in regard to the IASB's proposed scope and invites the IASB to consider a narrower alternative scope. EFRAG also considers that the IASB has not sufficiently articulated the link between MPMs and IFRS 8 *Operating Segments* and suggests the IASB to require an explanation of how MPMs interact with performance measures already presented under IFRS 8.

In regard to the proposed amendments to IAS 34 *Interim Financial Reporting*, EFRAG has some concerns about requiring a reconciliation of the MPMs to the most directly comparable subtotal or total specified in IFRS Standards as such reconciliations, including the tax effect and NCI effect, can be costly, particularly when preparing interim financial statements at consolidated level (e.g. tax includes income tax of different subsidiaries and not transactions).

EBITDA

EFRAG considers that it would have been useful to define EBIT and EBITDA as they are among the most used performance measures. However, as such measures have not been defined by the IASB, they should be included in the scope of the IASB's proposals regarding MPM disclosures. In addition, EFRAG suggests that the IASB clarifies the principle behind the list of measures not considered to be MPMs provided in paragraph 104 of the ED.

Statement of cash flows

EFRAG supports the IASB's proposal to require entities to use 'operating profit or loss' as the starting point for the indirect reconciliation of cash flows from operating activities in the statement of cash flows. This is because it specifies a consistent starting point for the indirect method of reporting cash flows from operating activities and reconciles the operating category in the statement of profit or loss with the operating activities in the statement of cash flows. EFRAG also supports the removal of options for the classification of interest and dividends in the statement of cash flows for non-financial entities, as it will improve consistency in presentation of similar line items and will better reflect the nature of the respective cash flows.

However, EFRAG suggests that the IASB should have a separate project on IAS 7 *Statement of Cash Flows* with the objective of having a comprehensive review of the

challenges that arise in practice (e.g. financial institutions) and improve consistency with the new content and structure of the statement of profit or loss.

Other comments: presentation of revenue and costs in different business lines

EFRAG highlights that, currently, there is diversity in practice in how entities that operate business activities in different industries present their performance (e.g. a manufacturer providing financing to customers or entities operating both banking and insurance services). Some entities present information about their different business activities in the statement of profit or loss, as part of operating profit, by adding separate rows and allocating revenues and expenses reflecting the different business activities (as in paragraph EI11 of the Illustrative Examples). On the contrary, other entities present all income and expenses related to different business activities without any business activity distinction, accompanied by more detailed information in the segment reporting section in accordance with IFRS 8.

EFRAG considers that it could be useful if the IASB could further explain how entities with different business activities should prepare their financial statements, especially when considering the example provided by the IASB in paragraph IE11 of the Illustrative Examples. The IASB should consider providing further illustration on how the split between the operating/financing and investing categories should be done in this case. In addition, the need for consistency with the requirements in IFRS 8 should be considered together with the disclosure of judgement applied to allocate revenues and costs across business activities (e.g. in case of group internal transactions between businesses), when they are presented separately on the face of the statement of profit or loss.

Other comments: proposals on other comprehensive income

EFRAG does not consider that the IASB's proposals on other comprehensive income ('OCI') are a significant improvement as they simply modify the labelling of OCI line items. EFRAG considers that it will be difficult to significantly improve the communication and understandability of OCI without addressing the distinction between profit or loss and OCI and the role of recycling.

EFRAG has also provided additional suggestions to improve presentation in the primary financial statements in *other comments* section.

EFRAG's detailed comments and responses to the questions in the ED are set out in Appendix 1 *EFRAG's responses to the questions raised in the ED*. This letter also includes Appendix 2 *Early Stage Analysis* with a preliminary impact assessment of the IASB's proposals.

If you would like to discuss our comments further, please do not hesitate to contact Filipe Camilo Alves, Robert Stojek or me.

Yours sincerely,

Jean-Paul Gauzès

President of the EFRAG Board

Contents

Draft Comment Letter	1
Summary of EFRAG’s views on the ED.....	1
Appendix 1 - EFRAG’s responses to the questions raised in the ED.....	6
Question 1 – operating profit or loss.....	6
Question 2 – the operating category.....	7
Question 3 - the operating category: income and expenses from investments made in the course of an entity’s main business activities	9
Question 4 - the operating category: an entity that provides financing to customers as a main business activity	12
Question 5 - The investing category	14
Question 6 - profit or loss before financing and income tax and the financing category	17
Question 7 - Integral and non-integral associates and joint ventures.....	19
Question 8 - Roles of the primary financial statements and the notes, aggregation and disaggregation.....	22
Question 9 - Analysis of operating expenses.....	24
Question 10 - Unusual income and expenses	27
Question 11 - Management performance measures.....	30
Question 12 – EBITDA	37
Question 13 - Statement of cash flows	39
Question 14 - other comments	42
Appendix 2 – Early Stage Analysis	46
Introduction	46
Statement of financial performance: General	47
Statement of financial performance: Level of disaggregation - number of line items..	48
Statement of financial performance: Level of disaggregation - subtotals used.....	48
Statement of financial performance: Presentation of expenses by nature and by function	51
Statement of financial performance: Single statement or two statements	52
Statement of financial performance: Unusual items.....	52
Statement of financial performance: Results of associates and joint ventures.....	53
Statement of cash flows	54

Appendix 1 - EFRAG's responses to the questions raised in the ED

Question 1 – operating profit or loss

Notes to constituents

The IASB's proposals included in the ED

- 1 *In paragraph 60(a) of the ED the IASB proposes that all entities present in the statement of profit or loss a subtotal for operating profit or loss.*
- 2 *In paragraph BC53 of the Basis for Conclusions, the IASB explains that it proposes to require entities to classify specified income and expenses into an operating category and present an operating profit or loss subtotal in the statement of profit or loss to increase comparability between entities. The IASB also highlights that this may require some entities to change how this operating profit or loss is calculated.*

Current practice on the presentation of financial statements

- 3 *From its initial research, EFRAG notices that in practice many entities (including financial institutions) present in the primary financial statements the subtotal 'operating profit or loss' or a variation of similar concept (e.g. operating earnings, operating results). However, because IFRS Standards currently do not define operating profit or loss, entities use their own definitions. As a result, EFRAG noticed that there is diversity in practice on the use of the subtotal 'operating profit or loss', including its labelling and calculation, even within the same industry (please see further details in [Appendix 2 – Early Stage Analysis](#)).*

Impact on current practice on the presentation of financial statements

- 4 *As the IASB's proposals would require entities to present on the face a subtotal that is already widely used in practice, EFRAG assesses that for many entities the IASB's proposal will not change current practice on the presentation of subtotal "operating profit or loss". However, as further explained in question 2, many entities may need to change its labelling and how this subtotal is calculated (please see further details in [Appendix 2 – Early Stage Analysis](#)).*

Question 1 – Operating profit or loss

Paragraph 60(a) of the Exposure Draft proposes that all entities present in the statement of profit or loss a subtotal for operating profit or loss.

Paragraph BC53 of the Basis for Conclusions describes the Board's reasons for this proposal.

Do you agree with the proposal? Why or why not? If not, what alternative approach would you suggest and why?

EFRAG's response

In general, EFRAG supports the IASB's efforts to improve the structure and content of primary financial statements, particularly the statement of profit or loss.

EFRAG highlights that 'operating profit or loss' is one of the most used subtotals and currently there is a lack of consistency in its use, labelling and definition. Thus, EFRAG supports the IASB's proposal to require all entities to present on the face of the statement of profit or loss the subtotal 'operating profit or loss' (with its consequent labelling), to reduce diversity in practice and improve comparability of financial statements.

Improvements to the structure and content of the statement(s) of financial performance in general

- 5 EFRAG acknowledges that the structure and content of the statement(s) of financial performance vary even among entities in the same industry and that this might reduce the ability of users of financial statements to compare the financial performance of different entities. Therefore, EFRAG supports the IASB's efforts to improve the structure and content of primary financial statements, particularly on the statement of profit or loss, as the IASB's proposed improvements also address issues that have high priority within the IASB's work plan.
- 6 Nonetheless, as further detailed in questions 3 and 4 below, EFRAG highlights that in many jurisdictions regulators and national standard setters have specific presentation requirements in addition to those required by the IFRS Standards. EFRAG suggests the IASB to closely communicate with regulators on this topic to avoid a situation where entities will need to prepare different sets of financial statements to comply with IFRS and regulators' requirements.
- 7 EFRAG also highlights that both the statement of financial performance and the statement of cash flows are not aligned and will have three different categories with similar names (operating, investing and financing). As a result, for example, the cost of an item of property, plant and equipment (e.g. depreciation expenses) would be included in the category 'operating profit or loss' while investments in long-term assets (e.g. property, plant and equipment) would be classified as investing activities in accordance with IAS 7.
- 8 Therefore, EFRAG considers that it is important at the current stage to have a clear conceptual basis for the new structure of the financial statements and clarity of the interaction between the statement of financial performance and the statement of cash flows, including the reasons why there is no alignment. EFRAG would encourage a separate project on IAS 7 to improve consistency with the new content and structure of the statement of profit or loss. EFRAG considers that, in the meantime and in case the IASB decides to not align the two statements, it would be useful to use for the categories presented a different labelling from IAS 7 to avoid confusion.

Operating profit or loss

- 9 In regard to the IASB's proposal to require all entities to present in the statement of profit or loss a subtotal for operating profit or loss, EFRAG highlights that 'operating profit or loss' is one of the most used subtotals and currently there is lack of consistency in its use, labelling and definition. The subtotal 'operating profit or loss' also plays an important role in investment and financial analysis decisions.
- 10 Thus, EFRAG supports the IASB's proposal to require all entities to present "operating profit or loss" to reduce diversity in practice and improve comparability of financial statements.

Question 2 – the operating category

Notes to constituents

The IASB's proposals included in the ED

- 11 *In paragraph 46 of the ED, the IASB proposes that operating category comprises income and expenses that:*
 - (a) *are not classified as investing or financing;*
 - (b) *are not classified as income or expenses from integral associates and joint ventures;*
 - (c) *are not classified in income taxes or discontinued operations; and*

- (d) are made in the course of an entity's main business activities, including income and expenses from the investments made in the course of an entity's main business activities and income and expenses from the financing category if entities provide financing to customers.
- 12 Therefore, operating profit or loss is defined as a residual category that would include income and expenses from an entity's main business activities (this is because of the way in which amounts excluded from operating profit or loss are defined). However, it is worth noting that:
- (a) the operating category includes unusual income and expenses (paragraph BC56 of the Basis for Conclusions);
- (b) the operating category excludes both income or expenses relating to integral and non-integral associates or joint ventures (paragraph 48 and 53 of the ED); and
- (c) the presentation of the analysis of expenses included in operating profit or loss will be based on either the nature or the function of the expenses, using whichever method provides the most useful information (paragraph 68 of the ED).

Current practice on the presentation of financial statements

- 13 As mentioned above, the subtotal "operating profit or loss" or a variation of similar concept (e.g. operating earnings, operating results) is widely used in practice, including by financial institutions.
- 14 However, EFRAG also noticed that its labelling and calculation varied between entities as, for example, some entities included results from associates and joint ventures in operating profit while others excluded them. Similarly, there is diversity in practice on the presentation of unusual/ non-recurring items and presentation of income and expenses from investment activities. Finally, it is worth noting that in many cases this subtotal was fairly similar to earnings before interest and tax (EBIT) as in many cases it only excluded finance costs and share of profit from equity accounted investments (please see further details in [Appendix 2 – Early Stage Analysis](#)).

Impact on current practice on the presentation of financial statements

- 15 As the IASB is proposing new guidance on the definition and labelling of a subtotal that is already widely used in practice, EFRAG assesses that the IASB's proposals are likely to significantly change its labelling and how this subtotal is used in practice (please see further details in [Appendix 2 – Early Stage Analysis](#)). Entities may react to the IASB's proposal either by eliminating the formerly used equivalent subtotal or by renaming the formerly used equivalent subtotal, in case they decide to continue to use it.

Question 2 – the operating category

Paragraph 46 of the Exposure Draft proposes that entities classify in the operating category all income and expenses not classified in the other categories, such as the investing category or the financing category.

Paragraphs BC54–BC57 of the Basis for Conclusions describe the Board’s reasons for this proposal.

Do you agree with this proposal? Why or why not? If not, what alternative approach would you suggest and why?

EFRAG’s response

EFRAG supports the IASB’s proposal to define the ‘operating category’ as described in paragraph 46 of the ED. EFRAG notes that in paragraphs 46 and B25-B31 of the ED the IASB starts by defining the operating category positively and then introduces a residual element in its definition. This residual element is further explained in paragraphs BC54 and BC55 of the Basis for Conclusions.

In this context, EFRAG highlights the importance of having clear guidance on the notion of the “entity’s main business activity” or “in the course of the entity’s main business activity”.

- 16 EFRAG supports the IASB’s proposal to define ‘operating profit or loss’ and ‘operating category’ as described in paragraph 46 of the ED. The subtotal ‘operating profit or loss’ (or a variation of a similar concept) is widely used in practice and having a common definition would have the benefit of improving comparability between entities.
- 17 In particular, EFRAG notes that in paragraphs 46 and B25-B31 of the ED, the IASB starts by defining the operating category positively (‘includes information about income and expenses from an entity’s main business activities’) and then introduces a residual element in its definition. This residual element is further explained in paragraphs BC54 and BC55 of the Basis for Conclusions. Such a definition is suitable to accommodate the needs of different business models, including those of financial institutions, and allow the use of additional subtotals within operating profit when deemed necessary (e.g. gross profit, net interest income, etc). Therefore, EFRAG considers that the outcome of the IASB’s approach to define ‘operating profit or loss’ will provide useful information to users of financial statements.
- 18 In this context, EFRAG highlights the importance of having clear guidance on the notion of the ‘entity’s main business activity’ or ‘in the course of the entity’s main business activity’ as the allocation of income and expenses to the operating category significantly relies on these notions and the use of such concepts might involve significant judgement. This is further explained in Question 3 below.

Question 3 - the operating category: income and expenses from investments made in the course of an entity’s main business activities

Notes to constituents

The IASB’s proposals included in the ED

- 19 *In paragraph 48 of the ED, the IASB proposes that an entity includes in operating profit or loss income and expenses from investments made in the course of their main business activities. The IASB considers that when an entity invests in assets that generate a return individually and largely independently of other entity resources in the course of its main business activities, the investment returns are an important indicator of operating performance.*

- 20 *In paragraph BC60 of the Basis for Conclusions, the IASB explains for some entities, such as insurers (see example IE9 of the Illustrative Examples to the ED), investing is an important activity performed in the course of their main business activities although it is arguably not their main business activity. For example, an insurer's main business activity may be underwriting, but it may invest in assets that generate returns individually and largely independently of its other resources in the course of its underwriting business activity. To ensure that income and expenses from such activities are included in the operating category, the proposals refer to investments that are made in the course of an entity's main business activities. This proposal would also capture entities for whom such activities are their main business activity.*
- 21 *The IASB's proposal only relates to returns from investments made in the course of an entity's main business activities. Entities with such investments may also have investments that are not made in the course of their main business activities. In this latter case, income or expenses arising from such investments are included in the investing category.*
- 22 *The IASB recognise that this would require entities to separate returns from investments made in the course of their main business activities and those that are not (i.e. entities would be required to make a split on the face of the statement of profit or loss). However, the IASB concluded that this would not cause significant incremental costs, as entities are likely to have this information to manage their business. In addition, users of financial statements would benefit from separate information about returns from investments that are unrelated to an entity's main business activities for all entities.*

Current practice

- 23 *From EFRAG preliminary analysis, EFRAG noticed that almost all the financial institutions analysed (banks and insurers) did not present a separate investing category in their financial statements, although some financial institutions reported the share of profit of associates and joint ventures after operating profit. In particular, the financial institutions that presented the subtotal 'operating profit or loss' included in that subtotal income and expenses from investments such as 'net investment income', 'trading results', 'dividend income', 'gains or losses on financial investments' (e.g. 'financial assets held for trading') and related impairments. (please see further details in [Appendix 2 – Early Stage Analysis](#)).*

Impact on current practice

- 24 *EFRAG assesses that in most cases the IASB's proposals are likely to affect how the financial institutions define their subtotal 'operating profit or loss'. It will also not impact the presentation of income and expenses from investments, which are already presented within operating profit or loss.*
- 25 *However, currently entities do not need to separate returns from investments made in the course of their main business activities from those that are not. Therefore, this would be a change to current practice as companies would be required to make such split under the IASB's proposals (please see further details in [Appendix 2 – Early Stage Analysis](#)).*

Question 3 – the operating category: income and expenses from investments made in the course of an entity's main business activities

Paragraph 48 of the Exposure Draft proposes that an entity classifies in the operating category income and expenses from investments made in the course of the entity's main business activities.

Paragraphs BC58–BC61 of the Basis for Conclusions describe the Board's reasons for this proposal.

Do you agree with the proposal? Why or why not? If not, what alternative approach would you suggest and why?

EFRAG's response

EFRAG agrees with the proposal as it will enhance the comparability between entities and provide relevant information to users of financial statements.

Nonetheless, EFRAG calls upon the IASB to closely communicate with regulators on the interaction of the IASB proposals with existing regulatory frameworks, particularly those that exist across Europe (e.g. on the use of additional subtotals).

- 26 EFRAG agrees with the proposal as it will enhance the comparability between entities and notes that in a majority of cases income and expenses from investments made in the course of the entity's main business activities (e.g. dividends, interest received, rental income, etc.) are already part of the operating profit in the financial sector.
- 27 In many EU jurisdictions regulators have specific presentation requirements in addition to those required by the IFRS Standards. EFRAG suggests the IASB to closely communicate with regulators on this topic to avoid entities having to prepare different financial statements to respectively comply with IFRS and regulators' requirements. The IASB should consider, as part of the effects of these proposals, the interaction of the IASB's proposals with existing regulatory frameworks on presentation of financial statements. EFRAG is seeking further information from constituents in the financial sector on how these proposals will affect them.
- 28 EFRAG also highlights the importance of having clear guidance on the notion of 'in the course of the entity's main business activity' as the allocation of income and expenses to the operating category significantly relies on these notions and use of such concepts will involve significant judgement.
- 29 For example, it may be useful to clarify that paragraph B31 of the ED ('if, applying IFRS 8 *Operating Segments*, an entity reports a segment that constitutes a single business activity, that may indicate that that business activity is a main business activity') also complements paragraph B27 of the ED.
- 30 It would also be useful to complement paragraph B27 of the ED with examples of entities that invest outside of their main business activities or even mention the company's statutes, which typically define the business to be undertaken by the company. Such guidance could help management to decide when there is a need for an entity to separate returns from investments made in the course of their main business activities from those that are not, as such a split may involve significant judgement.
- 31 EFRAG also highlights the challenges of applying these concepts to entities with multiple business activities, that include investing and financing activities, particularly when considering the perspectives of the legal entity (parent or a subsidiary) in the separate financial statements and of the group.

Question to constituents

- 32 For those in a regulated industry, would the IASB proposals in paragraph 48, for entities that invest in the course of the entity's main business activities, result in significant changes in practice that would be in conflict with regulation in your industry? Do you expect any additional challenges or significant costs?
- 33 Do you consider that separating returns from investments made in the course of an entity's main business activities from those that are not will be difficult to make in practice? Please explain.

Question 4 - the operating category: an entity that provides financing to customers as a main business activity

Notes to constituents

The IASB's proposals included in the ED

- 34 *When an entity provides financing to customers as a main business activity, the difference between the interest income from that activity and the related interest expense, which is a cost of earning that income, is an important indicator of operating performance.*
- 35 *Thus, in paragraph 51 of the ED the IASB proposes that when an entity provides financing to customers, it shall make an accounting policy choice between:*
- (a) Including in operating profit or loss only income and expenses that arise from financing activities and income and expenses from cash and cash equivalents relating to its provision of financing to customers; or*
 - (b) Including in operating profit or loss all income and expenses from financing activities and all income and expenses from cash and cash equivalents.*
- 36 *In paragraph BC69 of the Basis for Conclusions the IASB explained that presenting a subtotal of profit or loss before financing and income tax would be misleading if all of an entity's expenses from financing activities were included in that subtotal. The IASB, therefore, proposes that an entity that classifies all expenses from financing activities in the operating category shall not present a subtotal of profit or loss before financing and income tax. This applies even when such an entity presents interest income or expense on other liabilities in the financing category applying paragraph 49(c) (e.g. the unwinding of the discount on a decommissioning, restoration or similar liability).*

Current practice

- 37 *From EFRAG preliminary analysis, EFRAG noticed that the financial institutions analysed did not present a separate financing category in their financial statements. In particular, the financial institutions that presented the subtotal 'operating profit or loss' included in that subtotal income and expenses from financing activities such as interest income and expenses, fees and commissions. EFRAG also noticed that financial institutions often used subtotals similar to gross profit, such as 'net interest income' or 'net fee income' by banks and 'premiums earned' or 'net insurance benefits and claims' by insurers. Such subtotals are typically presented within operating profit or loss (please see further details in [Appendix 2 – Early Stage Analysis](#)).*

Impact on current practice

- 38 *EFRAG assesses that in most cases the IASB's proposals are likely to affect how financial institutions currently define their operating income and expenses but it will not impact the presentation of income and expenses from financing activities, which are already presented within operating profit or loss. Nonetheless, currently entities do not need to make an accounting policy for the presentation of income and expenses from financing activities, and from cash and cash equivalents, that relate to the provision of financing to customers. Therefore, this may impact current practice if some companies opt to separately present income and expenses from financing activities, and from cash and cash equivalents, that relate to the provision of financing to customers (please see further details in [Appendix 2 – Early Stage Analysis](#)).*

Question 4 – The operating category: an entity that provides financing to customers as a main business activity

Paragraph 51 of the Exposure Draft proposes that an entity that provides financing to customers as a main business activity classify in the operating category either:

- income and expenses from financing activities, and from cash and cash equivalents, that relate to the provision of financing to customers; or
- all income and expenses from financing activities and all income and expenses from cash and cash equivalents.

Paragraphs BC62–BC69 of the Basis for Conclusions describe the Board’s reasons for the proposals.

Do you agree with the proposal? Why or why not? If not, what alternative approach would you suggest and why?

EFRAG’s response

EFRAG agrees with the IASB’s proposal for entities that provide financing to customers as a main business activity, as it provides relevant information to users of financial statements.

However, EFRAG questions the IASB’s proposal to provide a the ‘free’ accounting policy choice in paragraph 51(b) to non-financial institutions (e.g. manufacturer providing financing to customers).

- 39 EFRAG agrees with the proposal as it will provide relevant information to users of financial statements and notes that in most cases income and expenses from financing activities made by an entity that provides financing to customers as a main business activity (e.g. net interest income) are already considered as part of the operating profit, particularly in the financial sector.
- 40 EFRAG acknowledges that the use of options in IFRS reduces comparability between entities, however, agrees with the IASB’s argument in paragraph BC68 of the ED. In some cases, because of the difficulty to split income or expenses between the two categories, allocation should not be required but should be permitted.
- 41 Nonetheless, EFRAG questions the IASB’s proposal to provide a the ‘free’ accounting policy choice in paragraph 51(b) of the ED to non-financial institutions (e.g. manufacturer providing financing to customers). In accordance with paragraph 51 of the ED, such type of entities would not be required to present a financing category, although in this case a financing category would provide relevant information to users of financial statements. EFRAG considers that the option in paragraph 51(b) is only relevant when providing financing to customers is the dominating business activity (when compared to other business operating segments). Finally, as already mentioned in question 3 above, in many EU jurisdictions regulators have specific presentation requirements in addition to those required by the IFRS Standards. EFRAG suggests the IASB to closely communicate with regulators on this topic.

Question to constituents:

- 42 Do you consider that it is difficult or costly to allocate income and expenses from financing activities and from cash and cash equivalents to those that do or do not relate to the provision of financing to customers? Please explain.
- 43 For those that provide financing to customers as a main business activity and are in a regulated industry, would the IASB’s proposals in paragraph 51 of the ED be in conflict with regulation in your industry? Do you expect any additional challenges or significant costs?

Question 5 - The investing category

Notes to constituents

The IASB's proposals included in the ED

- 44 *In paragraph 47 of the ED, the IASB proposes an investing category for income and expenses from specified investments and related incremental expenses. This category would include income and expenses from investments and incremental expenses related to those investments. Income and expenses from investments comprise income and expenses from assets that generate a return individually and largely independently of other resources held by the entity.*
- 45 *In paragraph BC49 of Basis for Conclusions, the IASB explains that the objective of the investing category is to identify returns from investments that are not part of the entity's main business activities. For example, equity or debt investments typically generate dividend or interest returns individually and largely independently of an entity's other assets. Separate presentation about the income or expenses arising from such assets would provide useful information to users of financial statements who often analyse returns from an entity's investments separately from the entity's main operating business.*
- 46 *In paragraph BC50 the IASB proposes that the investing category includes incremental expenses related to the investments – that is, expenses that would not have been incurred had the investment not been made.*

Current practice on the presentation of financial statements

- 47 *From EFRAG preliminary analysis, EFRAG noticed that most companies do not present on the face a separate investing category. Nonetheless, there are some entities that present a single category for financing and investing activities (please see further details in [Appendix 2 – Early Stage Analysis](#)).*

Impact on current practice on the presentation of financial statements

- 48 *EFRAG assesses that the IASB's proposals are likely to change current practice as currently companies either present a single category for financing and investing or do not present an investing category at all (please see further details in [Appendix 2 – Early Stage Analysis](#)).*

Question 5 – The investing category

Paragraphs 47–48 of the Exposure Draft propose that an entity classifies in the investing category income and expenses (including related incremental expenses) from assets that generate a return individually and largely independently of other resources held by the entity, unless they are investments made in the course of the entity's main business activities.

Paragraphs BC48–BC52 of the Basis for Conclusions describe the Board's reasons for the proposal.

Do you agree with the proposal? Why or why not? If not, what alternative approach would you suggest and why?

EFRAG's response

EFRAG supports the IASB's proposal to require the presentation of an investing category subject to materiality considerations (in accordance with paragraph 24 of the ED). Nonetheless, EFRAG considers that the IASB should better explain the interaction of paragraphs 45 and 60 (on the new requirements related to the categories and subtotals) with paragraph 24 of the ED which refers to the notion of materiality.

EFRAG notes that the IASB's approach to consider income and expenses that arise from cash and cash equivalents being related to the entity's financing allows the reflection of managements' intention in managing debt and equity financing. However, there might be considerable relevance in another possible approach where the financing category is linked to the management of liabilities that arise from financing activities (as described in IAS 7) and the investing category is linked to the management of investments in assets. EFRAG is seeking views of the constituents on this topic.

Finally, EFRAG is concerned about presenting gains and losses on derivatives in the investing category under certain conditions, particularly when referring to financial institutions. EFRAG is also seeking views on the costs of the proposal for presentation of exchange differences.

Presentation of an investing category

- 49 Even though an investing category is currently not used in practice, EFRAG acknowledges that having a separate investing category may provide useful information to users of financial statements about the returns from investments that are not part of the entity's main business activities, particularly for non-financial institutions.
- 50 EFRAG notes that the separate investing category will only be used by entities that make investments outside of their main business activities. EFRAG also highlights that these entities will have to consider paragraph 24 of the ED which states that an entity does not need to comply with a specific presentation requirement (i.e. investing category) if the information resulting from that presentation or disclosure is not material. EFRAG notes that when the investing category is material and not made in the course of the entity's main business activities, presenting an overall subtotal of operating profit (without separate presentation of the income and expenses from the investments) would not allow for a proper appreciation of the risks and diversification of the business model.
- 51 Thus, EFRAG supports the IASB's proposal to require the presentation of an investing category, subject to materiality considerations (in accordance with paragraph 24 of the ED). Nonetheless, EFRAG considers that the IASB should better explain the interaction of paragraphs 45 and 60 (on the new requirements related to the categories and subtotals) with paragraph 24 of the ED which refers to the notion of materiality.

Definition of an investing category

- 52 EFRAG highlights the complexity of the IASB's proposals on how to separate the investing and financing category, as such a distinction would be judgemental in nature. However, EFRAG considers that the ED proposes a convention for allocation of income and expenses to the three categories (operating, investing and financing) and such proposal has the merits of supporting comparability of the resulting information.
- 53 In relation to this convention, EFRAG highlights the challenges related to the presentation of income and expenses that arise from cash and cash equivalents (as

described in paragraph B24 of the ED) that are to be classified as part of the financing.

- 54 EFRAG notes that the IASB's approach to consider income and expenses that arise from cash and cash equivalents being part of the entity's financing (as explained by the IASB in paragraph BC39 of the Basis for Conclusions) allows to reflect management's intention in managing debt and equity financing.
- 55 However, there may be value relevance as well in another possible approach, that links the financing category to the management of an entity's liabilities that arise from financing activities (as described in IAS 7) and the investing category to the management of investments in assets. Thus, following this view, income and expenses arising from holdings of money market instruments, including those that meet the definition of cash and cash equivalents, would be in the investment category (except when an entity invests in financial assets in the course of its main business activities).
- 56 Such an approach would also have the benefit of removing the exception included in paragraph B32(a) of the ED and the exception included in the definition of income and expenses from investments ('income and expenses from assets, except for income and expenses from cash and cash equivalents, that generate a return individually and largely independently of other resources held by an entity').

Question to constituents:

- 57 Do you consider income and expenses from cash and cash equivalents (i.e. short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value) as part of the entity's financing (paragraph 54 above) or investing activities (paragraph 55 above)? Please explain.

Classification of fair value gains and losses on derivatives

- 58 EFRAG is concerned about presenting gains and losses on derivatives in the investing category under certain conditions (i.e. exceptions related to grossing up of gains and losses or the undue cost or effort), particularly when referring to financial institutions. This is because financial institutions might end up with an investing category just because of their hedging and risk management activities and it will be difficult to explain to users why some income and expenses from hedging and risk management activities have been presented as investments rather than in the operating and financial activities that they typically relate to.
- 59 In addition, EFRAG suggests the IASB to clarify whether such items would end up being presented in the operating category when considering the IASB proposal to require entities to present in the operating category, income and expenses from investments made in the course of its main business activities (as in paragraphs 47-48 of the ED).
- 60 Finally, regarding the classification of fair value gains and losses on derivatives, EFRAG considers that it would be useful to have a definition of 'risk management', to specify on how to deal with discontinuation of hedging positions and whether the results of risk mitigation will be categorised in the same way as hedge accounting.

Classification of foreign exchange differences and of fair value gains and losses on derivatives and hedging instruments

- 61 In the ED, the IASB proposes that an entity is required to classify foreign exchange differences included in profit or loss in the same sections of the statement(s) of financial performance as the income and expenses arising from the items that gave rise to the foreign exchange differences.
- 62 EFRAG is concerned that the cost of tracking the exchange differences and gains and losses on derivatives and non-derivatives (as mentioned in paragraph

BC285(b) of the Basis for Conclusions) may outweigh the benefits of classifying the items in the sections of the statement(s) of financial performance.

Question to constituents:

- 63 How costly would it be to track whether exchange differences relate to the entity's main business activities, investing activities or financing activities? Please explain.

Question 6 - profit or loss before financing and income tax and the financing category

Notes to constituents

The IASB's proposals included in the ED

- 64 *In paragraphs 60(c) and 64 the ED, the IASB proposes that all entities, except some specified entities, present a 'profit or loss before financing and income tax' subtotal.*
- 65 *In paragraph BC33 of the Basis for Conclusions the IASB notes that many users of financial statements seek to analyse an entity's performance independently of how that entity is financed. To facilitate such analysis, the IASB proposes to require an entity to classify specified income and expenses into a financing category and to present a profit or loss before financing and income tax subtotal in its statement of profit or loss.*
- 66 *In paragraphs BC34 and BC35 of the Basis for Conclusions, the IASB explains that to meet the objective of providing a useful basis for comparing an entity's performance independently of how that entity is financed, the financing category includes:*
- (a) income and expenses from financing activities (e.g. interest expenses on debt issued by the entity and lease liabilities);*
 - (b) income and expenses on cash and cash equivalents (e.g. gains or losses on disposal of cash equivalents); and*
 - (c) interest income and expenses on liabilities that do not arise from financing activities (e.g. unwinding of the discount on a decommissioning and unwinding of the discount on other long-term provisions)*
- 67 *The requirements for separate presentation of items included in the financing category enables users to adjust the amounts included in the subtotal if they hold different views about whether those items form part of an entity's financing.*
- 68 *To describe which income and expenses arise from financing activities, the IASB proposes to expand and clarify the definition of financing activities in IAS 7. Providing a clear definition of financing activities is expected to result in more transparency about classification of items included in the financing category.*
- 69 *Accordingly, the financing category includes:*
- (a) income and expenses from financing activities (see paragraph BC34);*
 - (b) income and expenses on cash and cash equivalents (see paragraphs BC35–BC38); and*
 - (c) interest income and expenses on liabilities that do not arise from financing activities (see paragraphs BC39–BC41).*

Current practice

- 70 *From EFRAG preliminary analysis, EFRAG noticed that the majority of the entities presented a financing category and a separate subtotal related to 'finance results'. Nonetheless, some of these entities included income and expenses from investments and share of profit of associates and joint ventures in the financing category. (please see further details in [Appendix 2 – Early Stage Analysis](#)).*

Impact on current practice

- 71 EFRAG assesses that the IASB proposals are likely to impact entities that currently include all income and expenses together above profit before tax and those that have a single category for financing and investments. Furthermore, those that currently present ‘finance results’ may need to change its labelling and how this subtotal is calculated (please see further details in [Appendix 2 – Early Stage Analysis](#)).

Question 6 – profit or loss before financing and income tax and the financing category

- (a) Paragraphs 60(c) and 64 of the Exposure Draft propose that all entities, except for some specified entities (see paragraph 64 of the Exposure Draft), present a profit or loss before financing and income tax subtotal in the statement of profit or loss.
- (b) Paragraph 49 of the Exposure Draft proposes which income and expenses an entity classifies in the financing category.

Paragraphs BC33–BC45 of the Basis for Conclusions describe the Board’s reasons for the proposals.

Do you agree with the proposals? Why or why not? If not, what alternative approach would you suggest and why?

EFRAG’s response

EFRAG supports the IASB’s proposal to require and define ‘Profit or loss before financing and income tax’ and the ‘financing category’. EFRAG highlights that the outcome of IASB’s proposals is, to some extent, similar to the concept of Earnings Before Interest and Tax (‘EBIT’) and that there is a strong demand from users of financial statements to define and require the presentation of a subtotal equal or similar to EBIT. However, as already mentioned above, EFRAG highlights the challenges of the IASB’s proposals to make the distinction between the investing and financing category.

EFRAG notes that in accordance with paragraph BC44 of the Basis for Conclusions, time value of money on liabilities that do not arise from financing activities can be seen either as a component of the operating category or of the financing category. EFRAG is seeking views from the constituents on this topic.

EFRAG notes that it would be useful to consider whether incremental expenses related to financing activities should also be in the financing activities in symmetry with the treatment of expenses relating to investing activities.

Presentation of a financing category

- 72 EFRAG supports the IASB’s proposal to require and define ‘Profit or loss before financing and income tax’ and the ‘financing category’.
- 73 EFRAG highlights that the outcome of the IASB’s proposals is, to some extent, similar to the concept of *Earnings Before Interest and Tax* (‘EBIT’) and that there is a strong demand from users of financial statements to define and require the presentation of a subtotal equal or similar to EBIT.

Definition of a financing category

- 74 As mentioned in Question 3, EFRAG highlights the challenges of the IASB’s proposals to make the distinction between the investing and financing category, particularly when dealing with the classification of income and expenses from cash and cash equivalents.

- 75 In addition, EFRAG notes that in accordance with paragraph BC44 of the Basis for Conclusions, time value of money on liabilities that do not arise from financing activities can be seen either as a component of the operating category or of the financing category. On the one hand, it can be argued that these income and expenses should not be classified in the financing category as they are not aligned with the overall principle of the financing category to be linked to financing activities. But on the other hand, EFRAG acknowledges that many users of financial statements consider such income and expenses to be similar to income or expenses from financing activities and would prefer such income and expenses not to be reflected within operating profit.

Question to constituents:

- 76 Do you consider income and expenses that reflect the effect of the time value of money on liabilities that do not arise from financing activities (as in paragraph B47 of the ED) as part of the entity's financing or operating activities? Please explain.

Expenses related to financing activities

- 77 In accordance with paragraph 47 of the ED, entities would classify in the investing category incremental expenses incurred to generate income and income from investments. However, the IASB is silent on incremental expenses related to the financing category.
- 78 EFRAG considers that it would be useful to have guidance on whether incremental expenses related to financing activities should also be in the financing category.

Question 7 - Integral and non-integral associates and joint ventures

Notes to constituents

The IASB's proposals included in the ED

- 79 *The IASB observed significant diversity in practice in the presentation of an entity's share of the profit or loss of associates and joint ventures accounted for using the equity method. Therefore, it considered specifying where in the statement of profit or loss an entity should present its share of the profit or loss of associates and joint ventures accounted for using the equity method.*
- 80 *The IASB's stakeholder feedback suggested that some associates and joint ventures may have important differences in characteristics:*
- (a) *the activities of some associates and joint ventures are integral to the reporting entity's main business activities. Feedback suggested this characteristic is common in joint ventures.*
 - (b) *the activities of some associates and joint ventures are not integral to the reporting entity's main business activities, that is they have little or no effect on those activities.*
- 81 *In paragraph BC80 of the Basis for Conclusions, the IASB concluded that the share of profit or loss of non-integral associates and joint ventures meets the definition of income and expenses from investments and therefore proposes to classify it in the investing category. Thus, associates and joint ventures accounted for using the equity method that are integral to the main business activities of an entity do not generate a return individually and largely independently of the other.*
- 82 *The IASB also proposes to create a separate category for income and expenses from integral associates and joint ventures and to require entities to:*
- (a) *classify income and expenses from integral associates and joint ventures in this proposed category;*

- (b) *present an operating profit or loss and income and expenses from integral associates and joint ventures subtotal; and*
- (c) *include in the above category impairment losses and reversals of impairment losses on integral associates and joint ventures; and gains or losses on disposals of integral associates and joint ventures.*

83 *In the new paragraph 20D of IFRS 12 Disclosure of Interests in Other Entities, the IASB proposes that when assessing whether an associate or joint venture is integral or non-integral to an entity's main business activities, the entity shall consider all facts and circumstances. A significant interdependency between an entity and an associate or joint venture would be an indicator of being integral to the main business activities of the entity. Examples of a significant interdependency include:*

- (a) *having integrated lines of business with the associate or joint venture;*
- (b) *sharing a name or brand with the associate or joint venture; and*
- (c) *having a supplier or customer relationship with the associate or joint venture that the entity would have difficulty replacing without significant business disruption.*

84 *To summarise, the IASB proposes to define 'integral associates and joint ventures' and 'non-integral associates and joint ventures', and to require an entity to classify its equity-accounted associates and joint ventures as either integral or non-integral to the entity's main business activities. The IASB also proposes to require an entity to provide information about integral associates and joint ventures separately from that for non-integral associates and joint ventures. An entity would be required to:*

- (a) *classify, in the integral associates and joint ventures category of the statement of profit or loss, income and expenses from integral associates and joint ventures, and present a subtotal for operating profit or loss and income and expenses from integral associates and joint ventures (paragraphs 53 and 60(b) of the ED);*
- (b) *present, as cash flows from investing activities in the statement of cash flows, cash flows from investments in integral associates and joint ventures separately from the cash flows from investments in non-integral associates and joint ventures (proposed new paragraph 38A of IAS 7);*
- (c) *present, in the statement of financial position, investments in integral associates and joint ventures separately from investments in non-integral associates and joint ventures (paragraphs 82(g)–82(h) of the ED); and*
- (d) *disclose, in the notes, information required by paragraph 20 of IFRS 12 for integral associates and joint ventures separately from non-integral associates and joint ventures (proposed new paragraph 20E of IFRS 12).*

Current practice

85 *From EFRAG preliminary analysis, EFRAG noticed that the presentation of results of associates and joint ventures varied both for corporates and financial institutions. In most cases, the results of associates and joint ventures were presented within profit before tax and were either included in or after operating profit/ EBIT. The distinction between integral and non-integral was not made as this requirement did not exist at the time of analysis (please see further details in [Appendix 2 – Early Stage Analysis](#)). The research did not show a split between integral and non-integral based on other approaches.*

Impact on current practice

86 *The EFRAG Secretariat assesses that, to comply with the IASB's proposals, all entities that present share of the profit or loss of associates and joint ventures will have to revise their current subtotals and line items, particularly those related to*

integral and non-integral, as such distinction is a new requirement (please see further details in [Appendix 2 – Early Stage Analysis](#)).

Question 7 – Integral and non-integral associates and joint ventures

- (a) The proposed new paragraphs 20A–20D of IFRS 12 would define ‘integral associates and joint ventures’ and ‘non-integral associates and joint ventures’; and require an entity to identify them.
- (b) Paragraph 60(b) of the Exposure Draft proposes to require that an entity present in the statement of profit or loss a subtotal for operating profit or loss and income and expenses from integral associates and joint ventures.
- (c) Paragraphs 53, 75(a) and 82(g)-82(h) of the Exposure Draft, the proposed new paragraph 38A of IAS 7 and the proposed new paragraph 20E of IFRS 12 would require an entity to provide information about integral associates and joint ventures separately from non-integral associates and joint ventures.

Paragraphs BC77–BC89 and BC205–BC213 of the Basis for Conclusions describe the Board’s reasons for these proposals and discuss approaches that were considered but rejected by the Board.

Do you agree with the proposals? Why or why not? If not, what alternative approach would you suggest and why?

EFRAG’s response

EFRAG considers that providing a distinction between integral and non-integral associates and joint ventures will help users of financial statements to easily distinguish between associates and joint ventures that are closely related to the entity’s main business activities and those that are not. However, EFRAG highlights that such changes to the presentation requirements would involve significant judgement and need to be tested in practice.

EFRAG notes that the IASB’s proposals would also apply to associates and joint ventures in the separate financial statements, which may in some cases raise questions about the applicability of the proposed definitions.

- 87 EFRAG welcomes the IASB’s proposal to make a distinction between integral and non-integral associates and joint ventures. EFRAG considers that providing such distinction will help users of financial statements to identify associates and joint ventures that are closely related to the entity’s main business activities.
- 88 Nonetheless, EFRAG acknowledges that such distinction involves significant judgements and assumptions. Therefore, the robustness of the definition of integral and non-integral is crucial and there is a need to test how it would work in practice.
- 89 In particular, clarify the interaction of the new two concepts ‘main business activities of an entity’ and ‘return individually and largely independently of the other assets of the entity’ as the reference to main business activities seems to indicate that integral associates and joint-ventures should be within the operating activities. In addition, the focus of the definition of integral and non-integral (i.e. the use of ‘main business activities of an entity’ and ‘return individually and largely independently of the other assets of the entity’) seems to change in different parts of the ED.
- 90 EFRAG notes that the IASB’s proposals would also apply to the separate financial statements, which may raise questions about the applicability of the proposed definitions of integral and non-integral in this context. For example, if an entity elects to account for its investments in associates and joint ventures at cost in its separate financial statements, this will raise the question of whether the classification of its investments as integral or non-integral will apply.

- 91 Similarly, for subsidiaries in the separate financial statements this will raise the question of whether the classification of its investments as integral and non-integral will apply.
- 92 EFRAG considers that there is a need for the IASB to further discuss how its proposals in general would apply to the separate financial statements, including the challenges that may arise in practice to those who prepare and use separate financial statements.

Question to constituents:

- 93 Do you consider that the IASB needs to expand the new paragraph 20D of IFRS 12, for example to include additional indicators, to reduce the level of judgement involved when making a distinction between integral and non-integral entities? Please explain.
- 94 Considering that the IASB is proposing the subtotal 'profit before financing and income tax', which includes the result of associates and joint-ventures on a net basis, do you consider that it would be useful to separately present or disclose the income tax related to associates and joint-ventures accounted for under the equity method?

Question 8 - Roles of the primary financial statements and the notes, aggregation and disaggregation

Notes to constituents

The IASB's proposals included in the ED

- 95 *In the ED, the IASB proposes descriptions of the roles of the primary financial statements and the notes in order to determine whether financial information should be included in the primary financial statements or in the notes. The proposed definitions support the objective of the financial statements which is to enable users of financial statements to assess the prospects for future cash inflows and assess management's stewardship of the entity's economic resources.*
- 96 *In paragraph 20 of the ED, the IASB defines the roles of the primary financial statements as providing structured and comparable financial information about the reporting entity which is useful for receiving a financial overview of the entity's activities, making comparisons across entities and across reporting periods for the same entity, and identifying items and areas for which users of financial statements may wish to obtain additional information in the notes.*
- 97 *Paragraph 21 of the ED defines the role of the notes as providing further information to enable users to understand the items included in the primary financial statements and supplementing the primary financial statements with other information that is necessary to meet the objective of these statements.*
- 98 *When referring to aggregation and disaggregation, the ED requires entities to present in the primary financial statements or disclose in the notes the nature and amount of each material class of assets, liabilities, income or expense, equity or cash flow. The description of those items shall faithfully represent their characteristics.*
- 99 *The ED also proposes that an entity shall classify, and aggregate, transactions and other events based on their shared characteristics. If the items do not have common characteristics, they shall not be aggregated. Additionally, the principle of aggregation and disaggregation of financial information shall not obscure relevant information or reduce the understandability of the information presented or disclosed. An entity may aggregate immaterial items that do not share characteristics and shall describe them in a way that faithfully represents those dissimilar items by:*

- (a) aggregate immaterial items with other items that share similar characteristics; or
- (b) aggregate immaterial items with other items that do not share similar characteristics, but which may be described in a way that faithfully represents the dissimilar items.

100 However, if the aggregated immaterial items that do not share characteristics and cannot be described in a way that faithfully represents them, the entity shall disclose in the notes information about the composition of the aggregated items by indicating that an aggregated item consists of several unrelated immaterial amounts and disclosing the nature and amount of the largest item in the aggregation.

Current practice

101 From EFRAG preliminary analysis, EFRAG noticed that the structure and content of the financial statements of both non-financial and financial entities varied significantly, including the level of disaggregation. More specifically, EFRAG noticed that for non-financial entities the level of disaggregation varied significantly, with some entities providing a low level of disaggregation. In regard to the statement of financial position, EFRAG observed cases where the line item 'other' included more than 10% of the net assets, in majority of those cases entities had disclosures about the nature of such line items. However, there were cases where entities aggregated different items in other and did not provide additional disclosures.

102 Although, financial institutions usually provided a higher level of disaggregation (many subtotals and line items), the structure of the financial statements, including disaggregation, varied significantly across entities. For example, some financial institutions separately presented 'total income' and 'total expense', while others presented income and expenses together under the same subtotal. Some financial institutions focused on identifying what operating income and expenses was, while others did not. (please see further details in [Appendix 2 – Early Stage Analysis](#)).

Impact on current practice

103 EFRAG assesses that the IASB proposals on aggregation and disaggregation are likely to affect many non-financial and financial entities which will need to revise their current presentation of line items in order to meet the new requirements for presentation and disclosure of financial statements. Many non-financial entities will need to provide a higher level of disaggregation, particularly regarding line items related to investing and financing categories. EFRAG assesses that disclosure of unusual line items in the notes to the financial statements will be a significant change in the current reporting for many non-financial entities.

104 In addition, EFRAG observes that many financial institutions will also need to revise their current reporting practice to present on the face of their financial statements line items that are not currently presented such as unwinding of discount on pension liabilities and provisions. Consequently, to comply with the new requirements both non-financial and financial entities may need to reassess whether particular line items are material to require separate presentation. (please see further details in [Appendix 2 – Early Stage Analysis](#)).

Question 8 – Roles of the primary financial statements and the notes, aggregation and disaggregation

- (a) Paragraphs 20-21 of the Exposure Draft set out the proposed description of the roles of the primary financial statements and the notes.
- (b) Paragraphs 25-28 and B5-B15 of the Exposure Draft set out proposals for principles and general requirements on the aggregation and disaggregation of information.

Paragraphs BC19–BC27 of the Basis for Conclusions describe the Board’s reasons for these proposals.

Do you agree with the proposals? Why or why not? If not, what alternative approach would you suggest and why?

EFRAG’s response

EFRAG welcomes the IASB’s efforts to improve the general requirements on disaggregation as a complement to the created additional subtotals in the statement of profit or loss. EFRAG notes that having the principles and general requirements on aggregation and disaggregation of information in the financial statements within a single place in the new standard will improve clarity and consistent application across entities.

Roles of the primary financial statements and the notes

- 105 EFRAG welcomes the IASB proposal of providing additional guidance on the respective roles of the primary financial statements and notes. EFRAG considers that defining the roles can help define the boundaries between the notes and the primary financial statements. In EFRAG’s view, the term ‘primary financial statements’ is generally well understood and EFRAG has not heard of major concerns raised by constituents.
- 106 However, EFRAG recalls that in its comment letter on Discussion Paper DP/2017/1 *Disclosure Initiative - Principles of Disclosure*, EFRAG expressed concern that the proposed role of the primary financial statements focuses too much on the elements (assets, liabilities, equity, income, expenses). More specifically, EFRAG has concerns that the description noted in paragraph 20(a) of the ED may be too narrow. Instead, EFRAG considers that the defined role of the primary financial statements should focus on the overall position, performance, cash flows and stewardship of the entity, rather than the individual line items.

Aggregation and disaggregation

- 107 EFRAG welcomes the IASB’s efforts to improve disaggregation as a complement to the additional subtotals, particularly when dealing with groups of line items that have dissimilar characteristics and if the disaggregation leads to the disclosure of material information.
- 108 EFRAG considers that having the principles and general requirements on aggregation and disaggregation of information in the financial statements in a single place within the new standard (paragraphs 25-28 and paragraphs B5-B15 of the ED) will bring clarity and improve consistent application, especially when dealing with large residual balances and ‘other’ balances both in the statement of financial position and statement(s) of financial performance.
- 109 EFRAG also supports the IASB’s decision not to introduce a quantitative threshold for the disaggregation of a group of items. EFRAG is of the view that a principle-based rather than a rule-based guidance should be developed to address the over-aggregation of line items.

Question 9 - Analysis of operating expenses

Notes to constituents

The IASB’s proposals included in the ED

- 110 *In paragraph 68 of the ED, the IASB proposes that an entity present in the statement of profit or loss an analysis of expenses included in operating profit or loss based on either the nature or the function of the expenses, using whichever method provides the most useful information.*

- 111 *As in practice the entities sometimes use the mixture of the both methods, the IASB decided to require an entity to use the single method that would provide the most useful information to the users of its financial statements. To help entities assess which method is most useful in their circumstances, in paragraph B45 of the ED the IASB provides a set of factors that an entity will have to consider.*
- 112 *In response to feedback from users of financial statements that analysing expenses using the function of expense method can lead to a loss of useful information, in paragraph 72 of the ED, the IASB proposes that an entity presenting an analysis of operating expenses using the function of expense method would also be required to disclose in a single note an analysis of its total operating expenses using the nature of expense method.*

Current practice

- 113 *From EFRAG preliminary analysis, EFRAG noticed that a small majority of corporates used presentation by-function, followed by the presentation by-nature and only some of them used the mixed presentation of expenses. The results were different among financial institutions with the majority using a by nature presentation with one or more-line items presented by function, such as administrative expenses (please see further details in [Appendix 2 – Early Stage Analysis](#)).*

Impact on current practice

- 114 *EFRAG assesses that the IASB proposals are likely to impact financial institutions and only a limited number of corporates, particularly those that use a presentation by function with one or more line items presented by nature, such as unusual items (please see further details in [Appendix 2 – Early Stage Analysis](#)).*

Question 9 – Analysis of operating expenses

Paragraphs 68 and B45 of the Exposure Draft propose requirements and application guidance to help an entity to decide whether to present its operating expenses using the nature of expense method or the function of expense method of analysis. Paragraph 72 of the Exposure Draft proposes requiring an entity that provides an analysis of its operating expenses by function in the statement of profit or loss to provide an analysis using the nature of expense method in the notes.

Paragraphs BC109–BC114 of the Basis for Conclusions describe the Board’s reasons for the proposals.

Do you agree with the proposals? Why or why not? If not, what alternative approach would you suggest and why?

EFRAG’s response

EFRAG is sympathetic towards the IASB’s proposal to continue requiring entities to present an analysis of expenses using either by-function or by-nature method, based on whichever method provides the most useful information to the users of financial statements.

However, EFRAG suggests the IASB clarifies that paragraph B47 of the ED allows or even requires a mixed basis of presentation when an entity is required to present line items under paragraphs 65 and B15 of the ED. EFRAG suggests the IASB to include the reference to paragraph B15 directly in paragraph B47 of the ED for clarity purposes.

Analysis of expenses classified in the operating category

- 115 EFRAG welcomes the IASB’s proposal to continue requiring entities to present an analysis of expenses either by-function or by-nature, based on whichever approach provides the most useful information to the users of financial statements.

- 116 In paragraph B46 of the ED the IASB explains that an entity shall not provide an analysis of expenses classified in the operating category using a mixture of the nature and the function of expense methods. However, in paragraph B47 the IASB seems to contradict this principle by requiring minimum line items to be presented on the face regardless of this choice (e.g. use of the line item ‘cost of sales’ in by-nature presentation or use of ‘impairment of trade receivables’ in by-function presentation as stipulated in paragraph IE6 of the Illustrative Examples). EFRAG considers that it would be useful if the IASB explained its primary objective for the presentation of expenses by nature or by function, including the role of a mixed basis of presentation and the disclosures of expenses by nature in that objective.
- 117 In addition, EFRAG understands that a mixed presentation may still be allowed, or even required, as in accordance with paragraphs 65, B15 and B47 of the ED, an entity might be allowed or required to present additional line items by nature. In paragraph B47 of the ED, the IASB already highlights that an entity shall present in the statement of profit or loss the line items required by paragraph 65 (i.e. minimum line items to be presented in the statement(s) of financial performance) regardless of the method of analysis of expenses used. Nonetheless, in this paragraph the IASB does not specifically mention paragraph B15 of the ED which may also give rise to the separate presentation in the statement(s) of financial performance of line items of income and expense by nature.
- 118 Therefore, EFRAG suggests the IASB to include the reference to paragraph B15 directly in paragraph B47 of the ED for clarity purposes.

Disclosures

- 119 EFRAG agrees with the IASB’s proposal to require entities that present an analysis of expenses by function of expense on the face of the financial statements also to provide in the notes an analysis of its total operating expenses using the nature of expense method.
- 120 EFRAG acknowledges that paragraph 104 of IAS 1 already requires entities that classify expenses by function to disclose additional information on the nature of expenses. EFRAG acknowledges that such disclosures are not always provided in practice. Thus, EFRAG welcomes the IASB’s proposed improvements in paragraph 72 of the ED, and related application guidance in paragraph B48 of the ED, which make the requirement for disclosures clearer and directly related to the operating profit or loss category.

Question to constituents:

- 121 Do you consider that it is useful to have disclosures by nature in single note when an entity presents its expenses within operating profit or loss by function (i.e. when an entity assesses that presentation by function provides the most useful information)? Do you anticipate that such information will be costly to provide? Please explain.
- 122 Do you consider that it is useful to have in the statement of profit or loss:
- (a) a strict presentation either by nature or by function (no mix);
 - (b) a general presentation by nature or by function together with limited additional requirements as suggested in the ED by the IASB; or
 - (c) a mix presentation basis (no restrictions). Please specify why.

Application guidance

- 123 EFRAG considers that the list of factors proposed by the IASB in paragraph B45 could be helpful for entities to determine whether a by-function or by-nature method provides the most useful information to users.

Question 10 - Unusual income and expenses

Notes to constituents

The IASB's proposals included in the ED

- 124 *In paragraphs 100-102 of the ED, the IASB proposes to require all entities to disclose information regarding unusual income and expenses, defined as having limited predictive value i.e. when it is reasonable to expect that income or expenses that are similar in type and amount will not arise for several future annual reporting periods.*
- 125 *The IASB proposes the following information to be disclosed:*
- (a) amount of each unusual income or expense;*
 - (b) narrative description of a transaction or event that gave rise to that item and why income or expenses that are similar in type and amount are not expected to arise for several future annual financial reporting periods;*
 - (c) the line items in the statement of financial performance in which each item of unusual income or expense is included; and*
 - (d) an analysis of the included expenses using the nature of expense method, when an entity presents an analysis of expenses in the statement of profit or loss using the function of expense method.*
- 126 *The IASB clarifies that income and expenses from remeasurement are not unusual income and expenses and that classifying as unusual bases on expectations about the future rather than past occurrences.*
- 127 *It should be noted that the IASB's proposal for unusual income and expenses is different from the requirement for presentation of extraordinary items that was removed from IAS 8 in 2003. In paragraph BC 128 of Basis for Conclusion, the IASB explains that extraordinary items were defined as clearly distinct from the ordinary activities of an entity and were presented in their own category after tax, separately from profit or loss from ordinary activities whereas unusual income and expenses, are classified within particular categories in the statement of profit or loss together with usual income and expenses, according to their nature, function or other characteristics.*

Extraordinary items

- 128 *EFRAG notes that the explanation from paragraph 87 of IAS 1 was removed in the ED. Consequently, the proposed guidance does not refer to extraordinary items nor explains whether the presentation of items of income and expense as 'extraordinary items' in the statement of profit or loss or in the notes will continue to be forbidden. EFRAG also notes that paragraph BC128 of Basis for Conclusions provides the explanations regarding the extraordinary category but does not provide explanations on the extraordinary line items as in paragraph 87 of IAS 1.*

Current practice regarding unusual items in statement of financial performance

- 129 *In its preliminary analysis, EFRAG noticed that entities, generally, do not include an explicit reference to unusual or extraordinary line items on the face of the statement of financial performance. However, the entities that make such explicit reference, disclose the total amounts in separate note. Moreover, various terms are used to refer to unusual items. The nature of the line items presented as unusual included restructuring costs, non-recurring net finance income (cost), impairment of assets, reversal of impairment on financial assets, and litigations related expenses. Please see further details in [Appendix 2 – Early Stage Analysis](#) – part on unusual items.*

Impact of the proposals on current practice

- 130 EFRAG assesses that the IASB's proposals to define unusual income and expenses are likely to require entities to reconsider the line items presented on the face as extraordinary, non-recurring, unusual, etc. Moreover, entities may need to revise the current subtotals in the statement of financial performance whether they fit into the new proposed structure. Please see further details [Appendix 2 – Early Stage Analysis](#) – part on unusual items.

Question 10 - Unusual income and expenses

- (a) Paragraph 100 of the Exposure Draft introduces a definition of 'unusual income and expenses'.
- (b) Paragraph 101 of the Exposure Draft proposes to require all entities to disclose unusual income and expenses in a single note.
- (c) Paragraphs B67–B75 of the Exposure Draft propose application guidance to help an entity to identify its unusual income and expenses.
- (d) Paragraphs 101(a)–101(d) of the Exposure Draft propose what information should be disclosed relating to unusual income and expenses.

Paragraphs BC122–BC144 of the Basis for Conclusions describe the Board's reasons for the proposals and discuss approaches that were considered but rejected by the Board.

Do you agree with the proposals? Why or why not? If not, what alternative approach would you suggest and why?

EFRAG's response

EFRAG welcomes the IASB's efforts to define unusual income and expenses and to require entities to disclose such items. In EFRAG's opinion, the proposals would result in useful information provided to users and will reduce the diversity in practice of providing financial information about unusual income and expenses.

However, EFRAG highlights that the definition of unusual items seems to be rather narrow, as it only focuses on whether expenses/income will occur in the future. Instead, EFRAG suggests the IASB to consider not only items that will not arise for several future annual reporting periods (as expressed in the ED) but also items that occur presently in the business, but only for a limited period of time (e.g. those identified in paragraph B15 of the ED such as restructuring costs). Thus, EFRAG would suggest that entities are required to provide disclosures on the items identified in paragraph B15 of the new Standard.

EFRAG notes that the translation of term 'unusual' may raise issues in some jurisdictions.

Finally, EFRAG considers that it would be useful to clarify whether entities can present unusual items on the face of the financial statements by specifically referring to 'unusual line items' and 'unusual subtotals' within the categories defined by the IASB or with the use of columns.

Unusual items

- 131 Currently, entities often disclose unusual or similarly described expenses and income in order to exclude them from information about underlying or normalised earnings. However, users of financial statements express concerns that the way entities provide this information varies significantly. It is often not clear how or why items have been identified as unusual.
- 132 EFRAG therefore acknowledges that information about unusual items is relevant for users of financial statements and that currently there is diversity in practice on how

entities provide such information. EFRAG notes the findings of ESMA Report *On the use of Alternative Performance Measures and on the compliance with ESMA APM Guidelines* (ESMA32-334-150) (ESMA APM Report). In its report, ESMA points to the most common adjustments to the APMs items are restructuring and impairment costs. EFRAG notes, however, that the ESMA APM Report only covers entities that are required to apply ESMA APM Guidelines².

- 133 Therefore, EFRAG welcomes the proposals to introduce a definition of unusual income and expenses, guidance to help entities identify unusual income and expenses, and to require entities to disclose such items in the notes to financial statements, in a single place.
- 134 However, EFRAG highlights that the scope of the IASB's definition seems to be rather narrow, as it only focuses on whether expenses/income will occur in the future. Instead, EFRAG suggests the IASB to consider not only items that will not occur in the future (as expressed in the ED) but also items that are occurring presently in the business, but only for a limited period of time (e.g. those identified in paragraph B15 of the ED such as restructuring costs). Such information would be useful to users of financial statements to forecast future cash flows and identify any disrupts in the earnings trend.
- 135 Furthermore, there may be a tendency for preparers to continue to focus on unusual expenses rather than unusual income. Thus, EFRAG considers that the explanations in paragraph BC130 on neutrality in relation to equivalent reporting for unusual income and expense are relevant and could be reflected in the final standard. In this regard, EFRAG would welcome a strong principle from the IASB to define unusual items.
- 136 Apart from the above comments on the scope, EFRAG highlights that the classification of unusual income and expenses, based on future expectations rather than on past occurrences, may create implementation issues. For example, a discontinued item of income or expenses (as defined in IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*), with a historical pattern, may likely fall into the definition of unusual income and expenses. In other words, the criteria of unusual income and expenses are likely to capture discontinued operations, operations of a disposed subsidiary, disposed joint operations, or other items of income and expenses related to a ceased or disposed operations.
- 137 EFRAG notes that the translation of term 'unusual' may raise issues in some jurisdictions as it carries more meanings than intended by the IASB, including activities potentially not allowed by the by-laws.
- 138 Finally, to complement the IASB's proposal on unusual expenses and income, EFRAG would suggest that entities are required to provide disclosures on the items identified in paragraph B15 of the new Standard, as these are the most common adjustments to performance measures, often commonly understood as unusual.
- 139 We acknowledge that in the IASB's Snapshot, the IASB explains that applying its proposals, unusual items would not be presented in a separate category in the statement of profit or loss. Instead, unusual items would be presented together with 'usual' income and expenses in their respective categories in the statement(s) of financial performance, according to their nature, function or other characteristics.
- 140 However, EFRAG considers that it would be useful to clarify whether entities can present unusual items on the face of the financial statements by specifically referring to 'unusual line items' (e.g. unusual litigation) and 'unusual subtotals' (e.g. operating

² ESMA APM Guidelines became applicable in all EEA countries except Croatia, Denmark and Iceland in July 2016.

profit before unusual items) within the categories defined by the IASB or with the use of columns (as in paragraph 110 of the ED for MPMs).

Question 11 - Management performance measures

Notes to constituents

The IASB's proposals included in the ED

141 *In paragraphs 103 – 110 of the ED, the IASB proposes to define management performance measures (MPMs) and to require entities to disclose them in a note. MPMs are subtotals of income and expenses that:*

- (a) *are used in public communications outside financial statements;*
- (b) *complement totals or subtotals specified by IFRS Standards; and*
- (c) *communicate to users of financial statements management's view of an aspect of an entity's financial performance.*

142 *Furthermore, MPMs should faithfully represent aspects of entity's financial performance and be described in a clear and understandable manner (i.e. should not mislead users).*

143 *The disclosed information would cover:*

- (a) *management's statement that MPMs provide management's view of an aspect of the entity's financial performance and are not necessarily comparable with measures sharing similar descriptions provided by other entities, and explanation why an MPM communicates management's view of performance, how it's calculated, and how it provides useful information;*
- (b) *a reconciliation between an MPM and the most directly comparable subtotal or total included in paragraph below, including the income tax effect and the effect on non-controlling interests for each reconciliation item.*

144 *However, the IASB decided to exclude the following totals or subtotals from the scope of the disclosure requirements:*

- (a) *all income and expenses subtotals and totals required by the new Standards;*
- (b) *gross profit or loss (i.e. revenue less cost of sales) and similar subtotals;*
- (c) *operating profit or loss before depreciation and amortisation;*
- (d) *profit or loss from continuing operations; and*
- (e) *profit or loss before income tax.*

145 *Finally, the ED proposes to amend IAS 33 Earnings per Share, and explicitly permit entities to disclose adjusted EPS ratios only when the nominators of such adjusted EPS ratio would be based on allowed total or subtotal in the statement of financial performance, or a disclosed MPM.*

APMs and MPMs

146 *EFRAG points to the following differences between Alternative Performance Measures, as defined in ESMA Guidelines on Alternative Performance Measures (ESMA/2015/1415) (ESMA APM Guidelines), and MPMs. It needs to be stressed that the scope of ESMA APM Guidelines does not coincide nor cover the scope of the IASB's proposals regarding MPMs, which may raise confusion.*

147 *The term APM, as defined by ESMA, is much broader than the term MPM as defined in the IASB's proposals. APMs include financial measures of historical or future financial performance, financial position, or cash flows, other than a financial measure defined or specified in the applicable financial reporting framework. Some APM examples include operating earnings, cash earnings, earnings before onetime*

charges, earnings before interest, taxes, depreciation and amortisation (EBITDA), net debt, autonomous growth or similar terms denoting adjustments to line items of statements of comprehensive income, statements of financial position or statements of cash flow. MPMs, however, only include subtotals of income and expenses.

148 In accordance with ESMA's definition, the following examples are not APMs:

- (a) measures defined or specified by the applicable financial reporting framework e.g. revenue, profit or loss or earnings per share;
- (b) physical or non-financial measures e.g. number of employees, number of subscribers, sales per square meter;
- (c) social and environmental measures e.g. greenhouse gases emissions, breakdown of workforce by type of contract or by geographic location;
- (d) information on major shareholdings, acquisition or disposal of own shares and total number of voting rights;
- (e) information to explain the compliance with the terms of an agreement or legislative requirement such as lending covenants or the basis of calculating the director or executive remuneration.

149 On the other hand, the application scope of ESMA APM Guidelines is narrower because the guidelines only apply to the information published in prospectuses, supplements to prospectuses, and regulated information which is understood as management reports disclosed to the market in accordance with the Transparency Directive, and disclosures issued under the requirements of article 17 of the Market Abuse Regulation, for example ad-hoc disclosures including financial earnings results; whereas the scope of IASB's proposals regarding MPMs apply to all public communication.

150 EFRAG notes that the ESMA guidelines on APMs do not apply to the financial statements³. Similarly, ESMA APM Guidelines do not apply to prudential measures including measures defined in the Capital Requirements Regulation and Directive – CRR/CRD IV.

Current practice

151 EFRAG has not conducted an analysis on the use of non-IFRS defined measures by preparers. Therefore, EFRAG's analysis is informed by the recent [ESMA APM Report](#). EFRAG notes, however, that the ESMA APM Report only captures the practice of entities that are required to apply ESMA APM Guidance⁴.

152 EFRAG needs to emphasise that the ESMA APM Report clarifies that not all the definitions of APMs are disclosed and it is not always clear whether an APM is an adjusted measure or not, and when it is, what are the adjustments. ESMA therefore only considers the adjustments disclosed or included in the definitions.

153 Based on the sample analysed, ESMA concluded that issuers on average disclose more APMs in management reports, followed by ad-hoc disclosures, and primary financial statements.

Use of APMs in primary financial statements

154 Only 7% of issuers in the sample do not include any APMs in the statement of profit or loss (see paragraph 75 of ESMA APM Report). While the use of APMs in the

³ By derogation to the scope described in paragraph 3 of ESMA Guidelines - for details, please refer to paragraph 4 of ESMA Guidelines on APMs and Question 2 of ESMA's Questions and Answers on Alternative Performance Measures Guidelines ESMA32-51-370

⁴ ESMA APM Guidelines became applicable in all EEA countries except Croatia, Denmark and Iceland in July 2016.

primary financial statements is significantly lower than in management reports or ad-hoc disclosures, issuers still include a significant number of APMs in their primary financial statements. Issuers in the sample disclosed an average of three APMs per issuer inside the primary financial statements, out of which a vast majority may satisfy the definition of an MPM (see paragraph 156, below).

- 155 *Although the large majority of the APMs used are not adjusted, 17% of issuers which reported APMs, disclose adjusted APMs in the statement of profit or loss.*

Most common used APMs in primary Financial Statements

- 156 *The most common non-adjusted APMs disclosed by issuers belonging to the nonfinancial sector are EBIT or Operating Results (83%), followed by Gross Profit (53%) and Financial Results (25%) - see paragraph 77 of ESMA APM Report. Issuers in the financial sector frequently disclose Net Interest Income (58%), Operating Results (37%) and Net Commissions (32%) in the statement of profit or loss.*

- 157 *EFRAG notes that the most common used APMs related to income and expenses, mentioned above, may satisfy the criteria of paragraph 103 of the ED. However, some are also listed in paragraph 104 of the ED and, consequently, would not qualify as MPMs and would not require to be disclosed in accordance with the ED.*

Most common adjustments to APMs presented in Primary Financial Statements

- 158 *In relation to adjusted APMs, the most common APMs presented on the face of the statement of performance are Adjusted EBIT or Operating results (16%), Adjusted Net Profit (7%) and Adjusted EPS (7%) – see paragraph 78 of ESMA APM Report. No significant differences are found when comparing adjusted APMs included as subtotals in the financial and non-financial sector.*

- 159 *Adjustments made to IFRS measures differ significantly from one issuer to another, even within the same sector of activity. However, what seems to be consistent among issuers is that most adjustments relate to costs or expenses (such as restructuring, impairment or litigation costs) rather than income. Hence, the adjusted APMs often portray a more positive picture of an issuer's performance than the disclosed IFRS measures, subtotals included inside financial statements or non-adjusted APMs.*

- 160 *EFRAG notes that the adjusted APMs, mentioned above, may satisfy the criteria of paragraph 103 of the ED. Consequently, as these are adjusted profit or loss measures, they may qualify as MPMs and may require to be disclosed in accordance with the ED.*

Use of APM in management commentary and ad-hoc disclosures

- 161 *The report reveals that all issuers in the sample use APMs in their communications to the market.*

- 162 *In the report, out of the 229 observations (123 management reports and 106 ad-hoc disclosures), a total of 3,210 APMs were collected, representing 385 different types of APMs.*

- 163 *The reason there are 123 management reports and 106 ad-hoc disclosures in the sample is that not all issuers in the sample published annual earnings results in accordance with Article 17 of the Market Abuse Regulation.*

- 164 *On average, issuers disclose around 14 APMs in ad-hoc disclosures and management reports. In this respect, it is important to highlight that issuers disclose more APMs in management reports than in ad-hoc disclosures (16 APMs versus 12 APMs on average). The difference in number of APMs between management reports and ad-hoc disclosures can be explained by the fact that ad-hoc disclosures are usually short documents containing the main highlights of the performance of an issuer. On the other hand, management reports are usually long documents of*

more than 100 pages that include a detailed description of the performance and the main events related to an issuer during a specific reporting period.

- 165 EFRAG notes that out of 17 (seventeen) APMs used in management commentaries of entities from non-financial sectors, listed as most common in ESMA APM Report, six relate to cashflows or entity's financial position, and a further six are performance measures but are either ratios or are not based on IFRS measures of costs or income. The remaining five APMs correspond to the APMs presented in the statements of profit or loss. The findings for adjusted APMs used in non-financial sectors are similar.
- 166 For financial institutions, out of 15 (fifteen) APMs listed as most common, nine either relate to financial position or are ratios. Out of the remaining six most common APMs, five correspond to the APMs presented in the statements of profit or loss.
- 167 Regarding the adjusted ratios listed as most common for financial institutions, out of 13 (thirteen) APMs, six correspond to the measures presented in statements of profit or loss, and other are ratios, or correspond to other primary financial statements.

Impact on current practice

- 168 EFRAG's analysis was informed by the ESMA APM Report. EFRAG notes, however, that ESMA APM Report only covers the APMs reporting practice of companies that apply the ESMA APM Guidance⁵.
- 169 As already mentioned in paragraph 152 above, the report clarifies that the preparers (issuers) do not provide all the definitions of APMs and, therefore, APMs could only be identified using their labels. Moreover, since the definitions were not provided, it was not clear whether an APM was an adjusted figure, and what the adjustments made were.
- 170 Therefore, EFRAG assesses that the IASB's proposals may have a significant impact on comparability and clarity of the information provided in the financial statements.
- 171 However, we note that the scope of IASB's proposals regarding MPMs does not include performance measures presented in the financial statements when such measures are not used in public communication. Such measures are also not covered by ESMA APM Guidelines as they are not disclosed outside the financial statements⁶.
- 172 Moreover, given the reported high number of APMs presented in public information (e.g. management commentaries and ad-hoc disclosures), EFRAG assesses that the IASB's proposals, would on one hand provide more clarity to the disclosed performance measures and would require this information to be audited. On the other hand, it would bring a significant number of non-IFRS measure disclosures into the IFRS financial statements or alternatively reduce the numbers of APMs due to the burden of disclosing them in financial reports.

Question 11 – Management performance measures

- (a) Paragraph 103 of the Exposure Draft proposes a definition of 'management performance measures'.

⁵ ESMA APM Guidelines became applicable in all EEA countries except Croatia, Denmark and Iceland (which are still in the process of applying) in July 2016.

⁶ for details, please refer to paragraph 4 of ESMA APM Guidelines and Question 2 of ESMA's Questions and Answers on Alternative Performance Measures Guidelines ESMA32-51-370

- (b) Paragraph 106 of the Exposure Draft proposes requiring an entity to disclose in a single note information about its management performance measures.
- (c) Paragraphs 106(a)–106(d) of the Exposure Draft propose what information an entity would be required to disclose about its management performance measures.

Paragraphs BC145–BC180 of the Basis for Conclusions describe the Board’s reasons for the proposals and discuss approaches that were considered but rejected by the Board.

Do you agree that information about management performance measures as defined by the Board should be included in the financial statements? Why or why not?

Do you agree with the proposed disclosure requirements for management performance measures? Why or why not? If not, what alternative disclosures would you suggest and why?

EFRAG’s response

EFRAG agrees that non-IFRS measures are often used in practice and additional guidance could bring more transparency and consistency in their use. EFRAG therefore welcomes the IASB’s efforts to provide guidance on MPMs.

However, EFRAG notes that the scope is limited to subtotals of income and expenses (thus it will not solve all the existing issues related non-IFRS measures) and highlights a number of challenges in regard to the IASB’s proposed scope. EFRAG is also seeking views from constituents on possible alternative approaches to define a narrower scope.

Finally, EFRAG considers that the IASB has not sufficiently articulated the link between MPMs and IFRS 8 and suggests the IASB to require an explanation of how MPMs interact with performance measures already presented under IFRS 8.

Information about management performance measures

173 EFRAG agrees that non-IFRS measures like MPMs or APMs are often used in practice and additional guidance could bring more transparency and consistency in their use. EFRAG recalls that many users consider non-IFRS measures useful for assessing a company’s business and performance and that users have called for more transparency and consistency in their use. That would include clear labelling as MPM, disclosing calculation formulas, providing comparative figures and reconciliations with IFRS defined subtotals, etc.

174 EFRAG therefore welcomes the IASB’s efforts to provide guidance and require additional disclosures on the use of MPMs, particularly when they are presented within the financial statements.

Scope of the IASB’s proposals on management performance measures

175 EFRAG acknowledges the importance of the issues related to presenting non-IFRS performance measures in public communication, such as management reports, ad-hoc disclosures and prospectuses.

176 EFRAG is also sympathetic towards the arguments provided in paragraph BC151 of the Basis for conclusions where the IASB explains that including MPMs in the financial statements would make them subject to the same requirements regardless of the entity’s jurisdiction; would improve the discipline with which they are prepared; and improve their transparency as such an approach would have the benefit of bringing into the financial statements some MPMs that would be audited.

177 Nonetheless, EFRAG notes the following issues arising from the IASB’s proposal:

- (a) the scope of MPMs is limited to subtotals of income and expenses and that such scope will not solve all the existing issues on non-IFRS measures as many of them are related to ratios, indicators of financial position or of cash flows and other measures such as organic growth;
 - (b) raises questions on whether the IASB should require the disclosure of subtotals which are actually presented outside of the financial statements;
 - (c) the IASB would need to clearly define 'public communications' and its scope (e.g. whether it would refer to entity's public communications over the year and which public communications would be in the scope). EFRAG notes that the scope of the IASB's proposals seems to be wide in terms of public communication which may create many issues (e.g. scanning all the possible communications);
 - (d) requires entities to present subtotals in the financial statements that are not aligned with the entity's accounting policies. Such a requirement would raise issues for auditors, give more prominence to non-IFRS defined subtotals or even elevate such subtotals to IFRS-defined terms;
 - (e) raises questions on whether metrics required by regulators would be considered as MPMs and, therefore, required to be reconciled to the most comparable subtotal indicated by IFRS Standards;
 - (f) raises questions on whether changes in the use of MPMs or their calculation would constitute a change in an accounting policy and, consequently, whether entities may only change when it results in the financial statements providing reliable and more relevant information (MPMs often change over time);
 - (g) raises practical challenges related to the disclosures on the effect of tax and non-controlling of each line item included in reconciliation, particularly when considering that the IASB is not requiring the presentation of adjusted earnings per share;
 - (h) raises audit issues, for instance, MPMs presented in a management commentary would be obligatory audited whereas the management commentary itself, would not;
 - (i) the current scope of application of the IASB's proposal would create a third category of measures, which are not IFRS-measures nor APMs, and has the potential to attribute undue prominence to non-GAAP measures; and
 - (j) raises questions why there are no disclosure requirements for entities that use MPMs within the financial statements but not outside the financial statements.
- 178 Additionally, EFRAG considers that the guidance in paragraph 104 of the ED exempting some of performance measures from the requirement to provide reconciliation in the notes (e.g. gross profit), seems to be made on rules-based rather than on a principle-based approach.
- 179 Moreover, EFRAG also suggests the IASB to consider introducing the same disclosure requirements for other non-GAAP performance measures presented within financial statements, that may not satisfy the proposed criteria of MPMs (e.g. adjusted revenues and ratios). The IASB would though need to appropriately amend paragraph 103 of the ED and to remove paragraph 103(a).

Alternative approach for the IASB to consider

Alternative 1: MPMs in the financial statements and guidance in the MCPS

- 180 EFRAG considers that the existing issues about comparability and understandability of performance measures used in financial communications arise primarily in communications outside the financial statements. EFRAG notes that, since 2016, European issuers that are subject to Transparency Directive, Market Abuse

Regulation or the Prospectus Directive, are generally required to apply ESMA APM Guidelines when publishing regulated information as defined by the Transparency Directive. Such guidance is aimed at providing adequate discipline and preventing that undue prominence is given to non-GAAP measures.

- 181 EFRAG considers that the ESMA APM guidelines, when applied consistently by issuers, improve the comparability, reliability and comprehensibility of financial information, thereby contributing to investor protection.
- 182 EFRAG suggests the IASB to review the scope of its proposals on MPMs and to limit its use to MPMs that are voluntarily presented within the financial statements and have an explanation of how such MPMs interact with those already presented under IFRS 8.
- 183 Finally, for the MPMs presented outside the financial statements (e.g. in the management commentary), EFRAG understands that not all jurisdictions have guidance on the use of APMs outside the financial statements. To address this issue, EFRAG suggests the IASB to consider introducing the proposed MPM disclosure guidance in the IFRS Practice Statement 1 *Management Commentary*.

Alternative 2: MPMs in the communications released jointly with the annual or interim report, including earning releases

- 184 An additional alternative approach would be to define public communication as the communication released jointly with the annual report or interim report of the company, including earning releases.

Questions to constituents

- 185 What is your assessment of the overall costs and benefits of the IASB's proposal on the calculation of the income tax effect and the effect on non-controlling interests for each item disclosed in the reconciliation as required by paragraph 106(b)?
- 186 What is your assessment on number of MPMs that will need to be disclosed by entities under the IASB's proposals? Please indicate which MPMs you have identified.
- 187 What is your assessment on the relevance of the MPMs identified (is it too much? too little? which additional ones?)
- 188 Do you agree with the scope of the IASB's proposals? If not, which alternative (Alternative 1 or Alternative 2 above) would you prefer so that financial statements remain relevant?
- 189 Do you agree with EFRAG's suggestion to apply the MPM requirements also to the non-GAAP performance measures, presented within financial statements, that may not satisfy the proposed criteria of MPMs (e.g. adjusted revenues and ratios)?
- 190 The ED is introducing more structure in the presentation requirements, including a requirement to present on the face of the income statement a new subtotal named "operating profit or loss", which will become an IFRS defined measure. Entities that currently use a performing measure labelled "operating profit or loss" on the face or in the notes will be forced to either (i) change the label for their performing measure and continue to use both the old measure and the new IFRS defined "operating profit", or to (ii) discontinue the pre-existing performance measure, replacing its use with the new IFRS defined "operating profit or loss".

In the context described above, do you believe that the IASB's proposals on the structure and content of the statement of profit or loss will lead to an increased number of MPMs?

Illustrative Examples

- 191 EFRAG welcomes the IASB's efforts to provide illustrative examples on disclosing MPMs. However, EFRAG notes that the example, provided in *Illustrative Examples*, is not clear. According to the ED, such disclosures should clearly state what are the adjustments used to reconcile an MPM with the most directly comparable subtotal or total specified by IFRS Standards, and what is the effect of each the reconciling adjustments on income tax and non-controlling interest. While the presentation of the adjustments used to reconcile the MPM is clear, the presentation of effect of the adjustments on income tax and non-controlling interest is not. In EFRAG's opinion, such a disclosure should clearly label all the reconciling adjustments and their effects on income tax and non-controlling interest using the clear labels. In the example, however, the income tax and non-controlling interest effects are mixed with the reconciliation of other MPMs and, furthermore, with the disclosure on unusual items.
- 192 EFRAG, therefore, suggests the IASB to reconsider the structure of the example and the way it provides information on MPMs and unusual items.

Question 12 – EBITDA

Notes to constituents

The IASB's proposals included in the ED

- 193 *In paragraphs BC172–BC173 of Basis for Conclusion, the IASB explains why it decided not to define earnings before interest, tax, depreciation and amortisation (EBITDA). The IASB considered, but rejected, describing operating profit or loss before depreciation and amortisation as EBITDA and explained that this would imply operating profit or loss to be the same as earnings before interest and tax.*
- 194 *However, the IASB proposes to exempt from the disclosure requirements for MPMs a subtotal calculated as operating profit or loss before depreciation and amortisation.*
- 195 *Consequently, if an entity discloses in the notes a measure calculated as operating profit or loss before depreciation and amortisation, that measure would not be considered an MPM and the disclosures would not be required.*
- 196 *That means, if an entity presents EBITDA in the financial statements, it would be considered as an MPM and it would need to provide the disclosures in the notes required for MPMs, including the reconciliation.*

Current practice regarding EBITDA

- 197 *In its preliminary analysis, EFRAG noticed that non-financial entities use EBITDA as one of the subtotals in the statements of financial performance. Please see further details in [Appendix 2 – Early Stage Analysis](#) – part on the level of disaggregation: subtotals used.*

Question 12 – EBITDA

Paragraphs BC172–BC173 of the Basis for Conclusions explain why the Board has not proposed requirements relating to EBITDA.

Do you agree? Why or why not? If not, what alternative approach would you suggest and why?

EFrag's response

In EFRAG's opinion, defining EBIT and EBITDA would be useful for users of financial statements and would reduce diversity in practice. As they have not been defined by the IASB, they should be included in the scope of the IASB's proposals regarding MPM disclosures.

Furthermore, EFRAG suggests the IASB to clarify the principle behind the list of measures not considered to be MPMs provided in paragraph 104 of the ED.

Definition of EBIT, EBITDA and other similar measures

- 198 EFRAG acknowledges the reasons provided by the IASB not to define EBIT, EBITDA or similar measures. However, EFRAG highlights that there is a strong demand from users of financial statements for the IASB to define or even require the presentation of EBITDA (earnings before interest, tax, depreciation and amortisation), one of the most common performance measures used by users of financial statements.
- 199 Nonetheless, considering that EBIT and EBITDA have not been defined by the IASB, EFRAG considers that they should be under the scope of the IASB's proposals on MPMs, when presented within the financial statements.

Subtotals specified by IFRS Standards that are not management performance measures

- 200 EFRAG acknowledges that the IASB recognised some subtotals, currently not specified by IFRS Standards, as commonly used in the financial statements and well understood by users of financial statements. In the IASB's opinion such subtotals include gross profit or loss (i.e. revenue less cost of sales) and similar subtotals, operating profit or loss before depreciation and amortisation, profit or loss from continuing operations, and profit or loss before income tax.
- 201 The IASB proposes, therefore, to specify a list a such subtotals, that would not be considered MPMs, would not require reconciliation, and would be a starting point for reconciliation of MPMs.
- 202 EFRAG agrees that providing a reconciliation for such measures would not provide additional information because their purposes and relationship to totals or subtotals specified by IFRS Standards are well understood and would usually be apparent from their presentation in the statement of profit or loss.
- 203 However, the drafting of paragraph 104 of the ED, which specifies those subtotals, is not clear. The description of the measures, included in the list, may be misleading and the reasons to include or exclude measures from the list are unclear, indicating that the list is rules-based. Further proof of that is that users of financial statements⁷ challenged the IASB's proposal to exempt from the MPM's disclosure requirements the subtotal 'operating profit or loss before depreciation and amortisation' as EBITDA typically excludes impairments from assets that are amortised or depreciated.
- 204 As mentioned in paragraph 169 above, since the list in paragraph 104 of ED seems to be made on a rules-based rather than on a principle-based approach, EFRAG suggests the IASB to clarify its wording by providing a principle that would assist preparers when assessing whether or not a measure satisfies the condition to be considered as an MPM.

⁷ EFRAG User Panel members

Question 13 - Statement of cash flows

Notes to constituents

The IASB's proposals included in the ED on the new starting point

205 *The ED proposes to amend the requirements in paragraph 18(b) of IAS 7 to require a consistent starting point for the indirect reconciliation of cash flows from operating activities. Currently, paragraph 20 of IAS 7 requires the use of 'profit or loss' subtotal to determining the net cash flows from operating activities under the indirect method. However, the practice shows that entities interpret the paragraph differently and use various starting points such as 'profit attributable to shareholders', 'profit from continuing operations', 'profit before tax' or 'operating profit'. This creates diversity in practice and reduces comparability across entities' statements of financial performance.*

The IASB's proposals included in the ED on investing activities

206 *The ED proposes to amend to the definition of 'investing activities' in paragraph 6 of IAS 7 to stipulate that investing activities also include the receipt of interest and dividends. This amendment aims at removing the classification options for interest and dividends that currently exists in the statement of cash flows.*

207 *Paragraph BC51 of the Basis for Conclusions explains that the investing category in the statement of profit or loss is different from investing activities as defined in IAS 7. The investing category in the statement of profit or loss only includes the returns from financial assets (e.g. equity or debt investments) that generate dividend or interest returns individually and largely independently of an entity's other assets. Yet, the investment activities in IAS 7 include investments made in long-term assets that will generate future returns, which is a wider concept as it includes 'investments in financial assets' and 'investments in operating assets' (such as property, plant and equipment) which are used in the course of the entity's main business activities (income and expenses related to investments in operating assets, such as depreciation, are classified in the operating category of the statement of profit or loss rather than in the investing category).*

The IASB's proposals included in the ED on financing activities

208 *The ED clarifies the description of 'financing activities' in paragraph 6 of IAS 7 by indicating that 'financing activities involve the receipt or use of a resource from a provider of finance with the expectation that:*

- (a) the resource will be returned to the provider of finance; and*
- (b) the provider of finance will be appropriately compensated through the payment of a finance charge that is dependent on both the amount of the credit and its duration.'*

209 *Paragraph BC35 of the Basis for Conclusions details that the financing category in the statement of profit or loss includes: income and expenses on liabilities arising from financing activities; income and expenses from cash and cash equivalents and interest income and expenses on non-financial liabilities such as net defined benefit liabilities and decommissioning liabilities. Consequently, the financing category in the statement of profit or loss has a broader scope than the financing activities as defined in IAS 7.*

The IASB's proposals included in the ED on the classification of interest and dividends

210 *Based on the revised definitions in paragraph 6 of IAS 7 and the proposals in paragraphs 33A and 34A-34D, the ED specifies that for non-financial entities:*

- (a) interest paid, including interest capitalised as part of the cost of an asset applying IAS 23 Borrowing Costs, and dividends paid should be classified as cash flows from financing activities; and*

(b) cash receipts from interest and dividends as cash flows from investing activities.

211 For financial entities, the ED proposes to classify dividends received, interest paid, and interest received all in a single category of the statement of cash flows (that is, either as operating, investing or financing activities). When deciding on the classification, the entity shall refer to the classification of income or expenses related to such cash flows in the statement of profit or loss. When the entity classifies related income or expenses in more than one category of the statement of profit or loss, the entity shall make an accounting policy choice to classify the cash flows in one of the corresponding categories of the statement of cash flows.

Current practice

212 From EFRAG preliminary analysis, EFRAG noticed that there is diversity in practice on the starting point to determine the net cash flows from operating activities. The majority of non-financial entities used 'profit after tax' subtotal as a starting point to determine the net cash flows from operating activities. The remaining non-financial entities used as a starting point 'profit before tax' or operating profit. With respect to financial institutions, the majority of them used 'profit before tax' or 'profit or loss' as a starting point for their presentation of cash flows.

213 The presentation of interest received, and dividends received, in the statement of cash flows varied with majority of non-financial entities presenting those items in operating activities and the remaining entities - in investing activities. Nearly half of the entities presented interest paid in operating activities and dividends paid in financing activities.

214 Many financial institutions presented interest paid and interest received within operating activities. However, such classification was not always clearly presented on the face of the statement of cash flows or the interest paid was classified as financing. Dividends paid were typically classified as financing activities and dividends received from equity instruments as operating activities. (please see further details in [Appendix 2 – Early Stage Analysis](#) – part regarding cash flow statements).

Impact on current practice

215 EFRAG assesses that the IASB's proposals on the statement of cash flows are likely to significantly change the current practice when using the indirect reconciliation of cash flows from operating activities. Thus, most non-financial and financial entities will have to revise their statement of cash flows to start with operating profit subtotal.

216 EFRAG further assesses that non-financial entities will have to revise the presentation of interest received, interest paid, and dividends received in the statement of cash flows. No significant impact is expected for the presentation of dividends paid which are presented within the financing activities section.

217 With regards to financial entities, the presentation of interest paid and received, and dividends received will impact the statement of cash flows depending on how these entities will classify related income and expenses in the statement of profit or loss. It is likely that many financial entities will present most, or all, of their interest income, interest expenses and/ or dividend income in the operating section of the statement of profit or loss. EFRAG assesses that in such cases there would not be a significant change in practice. (please see further details in [Appendix 2 – Early Stage Analysis](#) – part regarding cash flow statements).

Question 13 – Statement of cash flows

- (a) The proposed amendment to paragraph 18(b) of IAS 7 would require operating profit or loss to be the starting point for the indirect method of reporting operating cash flows from operating activities.
- (b) The proposed new paragraphs 33A and 34A–34D of IAS 7 would specify the classification of interest and dividend cash flows.

Paragraphs BC185–BC208 of the Basis for Conclusions describe the Board's reasons for the proposals and discusses approaches that were considered but rejected by the Board.

Do you agree with the proposals? Why or why not? If not, what alternative approach would you suggest and why?

EFRAG's response

EFRAG supports the IASB's proposal to require entities to use the 'operating profit or loss' as the starting point for the indirect reconciliation of cash flows from operating activities in the statement of cash flows, as it specifies a consistent starting point for the indirect method of reporting cash flows from operating activities. It also reconciles the operating category in the statement of profit or loss with the operating activities in the statement of cash flows.

EFRAG supports the removal of options for the classification of interest and dividends in the statement of cash flows for non-financial entities. This will improve consistency in presentation of similar line items and will better reflect the nature of the respective cash flows. EFRAG observes that some of those line items will be classified into different categories in the statement of cash flows and the statement of profit or loss.

However, EFRAG suggests the IASB to have a separate project on IAS 7 with the objective of having a comprehensive review of the challenges that arise in practice (e.g. financial institutions) and improve consistency with the new content and structure of the statement of profit or loss.

Finally, EFRAG would welcome guidance on the presentation of arrangements where an intermediate is used to pay trade receivables (i.e. supply-chain financing arrangements or reverse factoring).

Starting point for the indirect method of reporting operating cash flows

- 218 EFRAG supports the IASB's proposal to require entities to use the same starting point for the reconciliation of operating cash flows in the statement of cash flows using the indirect method as currently there is diversity in practice.
- 219 EFRAG also supports the IASB's proposal to use the operating profit or loss subtotal as the starting point for reconciliation. EFRAG considers that there are pros and cons for using either profit after tax or operating profit or loss. However, considering that the definition of the operating category in the statement of profit or loss is not aligned with the definition of operating activities in the statement of cash flows, such reconciliation becomes even more relevant as it will provide a link between the two statements. In addition, EFRAG assesses that it will reduce the number of necessary adjustments to the line items that have an investing or financing nature.

Classification of interest and dividend cash flows

- 220 EFRAG supports the removal of options in IAS 7 *Statement of Cash Flows* for the classification of interest and dividends and the introduction of additional guidance for the definition of financing activities. EFRAG expects that this will bring more

consistency in presentation of similar line items and will better reflect the true nature of the respective cash flows.

Other improvements to the statement of cash flows

- 221 EFRAG welcomes the IASB's efforts to make targeted improvements to IAS 7, however we consider that there is a need for a separate project on IAS 7 with the objective of having a comprehensive review of the challenges that arise in practice, particularly in regard to some financial institutions (e.g. banks and life insurers) where the statement of cash flows is not considered useful. Therefore, EFRAG suggests the IASB to:
- (a) make further research work on having a statement of cash flows that is structured differently for financial institutions to ensure that it provides relevant information to users and mentioned EFRAG's Discussion Paper issued in 2015 *The Statement of Cash Flows: issues for Financial Institutions* ([here](#));
 - (b) consider the issues raised in the UK FRC discussion paper *Improving the Statement of Cash Flows* ([here](#)); and
 - (c) improve consistency and eliminate current presentation inconsistencies between the statement of financial performance and the statement of cash flows in this separate project on IAS 7 (e.g. interest revenue from cash and cash equivalents is classified in the financing category in the statement of profit or loss, whereas all interest received is classified as cash flows from investing activities in the statement of cash flows as explained in paragraph BC197 of the Basis for Conclusions).

Reverse factoring

- 222 Currently, in IFRS, there is no specific reference to reverse factoring, however, there are accounting standards requirements that are relevant in determining the appropriate accounting policies (IFRS 9, IAS 1, IAS 7). Applying these standards requires significant judgement, particularly, as reverse factoring arrangements can differ significantly.
- 223 Therefore, EFRAG would welcome specific reference whether this type of liabilities should be presented as trade payables or as a financial debt/borrowing (from bank) in the statement of financial position. Similarly, EFRAG would welcome guidance on whether payments related to reverse factoring is best presented as an operational cash flow or a financing cash flow in the statement of cash flows.
- 224 Furthermore, better disclosure requirements are necessary in situations such as reverse factoring where an intermediate is used to pay trade receivables (supply-chain financing arrangements).
- 225 In those arrangements, the classification of such transactions as trade creditors is included in working capital changes and forms part of the operating cash flows instead of representing a financing liability in the financing cash flows. This reduces the transparency of information by smoothing operating cash flows and understating borrowings.

Question 14 - other comments

Notes to constituents – Summary of proposals in the ED on other comments

Other comprehensive income

- 226 *As explained in paragraph BC14 of the ED, the IASB decided not to reconsider when income or expenses should be reported in OCI or when such items should be reclassified to the statement of profit or loss. The IASB argued that this topic has already been considered as part of its Conceptual Framework for Financial Reporting.*

- 227 However, the ED includes proposals designed to improve the communication of information about income and expenses included in OCI. More specifically:
- (a) the labelling “items of OCI that may be reclassified (recycled) to profit or loss in subsequent periods” would be replaced by “Income and expenses to be included in profit or loss in the future when specific conditions are met”; and
 - (b) the labelling “items of OCI that are permanently reported outside profit or loss and will not be reclassified” would be replaced by “Remeasurements permanently reported outside profit or loss”.

IASB proposed amendments to other standards

- 228 In the ED, the IASB proposes a number of amendments to other standards, including IAS 33 Earnings per Share; IAS 34 Interim Financial Reporting; IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors, IFRS 7 Financial Instruments: Disclosures and IFRS 12 Disclosure of Interests in Other Entities.
- 229 The ED proposes amendments to IAS 8 and IFRS 7 to move the requirements currently set out in IAS 1 that would be better located in those Standards.
- 230 In regard to IFRS 12, the IASB proposes requirements relating to the definition of integral and non-integral associates and joint ventures and separate disclosures about integral and non-integral associates and joint ventures.
- 231 In regard to IAS 33, the IASB proposes amending IAS 33 to restrict the numerator used to calculate adjusted earnings per share to subtotals presented in IFRS Standards or an MPM that is attributable to holders of equity claims of the parent.
- 232 Finally, the IASB proposes amending IAS 34 to require disclosure of information about MPMs in the notes to an entity’s condensed interim financial statements. In addition, The IASB proposes that the presentation of headings and subtotals in condensed financial statements in condensed interim financial report(s) starts in the first year an entity applies draft IFRS (e.g. if the effective date would be on 1 January of 202x, an entity would be required to present the heading and subtotals in condensed financial statements in condensed interim financial report(s) by 30 June of 202x).

Question 14 – Other comments

Do you have any other comments on the proposals in the Exposure Draft, including the analysis of the effects (paragraphs BC232–BC312 of the Basis for Conclusions, including Appendix) and Illustrative Examples accompanying the Exposure Draft?

IASB proposals on the presentation of other comprehensive income

- 233 EFRAG acknowledges that the use of OCI and recycling has already been comprehensively discussed as part of the IASB’s project on the *Conceptual Framework for Financial Reporting*. However, EFRAG notes that OCI and recycling are still often not well understood by investors and, consequently, not used by them.
- 234 In addition, some respondents to the 2015 IASB’s Agenda Consultation stated that the Primary Financial Statements project would provide the IASB with an opportunity to analyse aspects of performance reporting that in their view, the Conceptual Framework project has failed to address or has not addressed satisfactorily (for example the definition of financial performance or profit or loss, the distinction between profit or loss and OCI).
- 235 Therefore, EFRAG regrets that the IASB has not discussed this topic further to clarify which items of income and expense should be presented in profit or loss and which in OCI, as well as on the role of recycling.
- 236 In addition, EFRAG does not consider the IASB’s proposals significantly improving the current requirements as they simply modify the labelling of OCI line items.

EFRAG considers that it will be difficult to significantly improve the communication and understandability of OCI without addressing the distinction between profit or loss and OCI and the role of recycling.

- 237 Finally, EFRAG highlights that relevant information about OCI is also provided in the statement of financial position (e.g. separate components of equity), thus any future discussions on OCI should also consider the statement of financial position and its interaction with the statement of financial performance.

Interaction of the IASB's proposals on statement of profit or loss and the statement presenting comprehensive income

- 238 EFRAG highlights that the IASB's ED is silent with regards to the use of new categories within the other comprehensive income even though there are transactions and events where the income and expenses have to be allocated to both the statement of profit or loss and other comprehensive income (e.g. hedging activities).
- 239 For presentation purposes, an entity is required to allocate the income and expenses to the different categories in the statement of profit or loss, however the IASB's ED it is silent on whether the statement presenting comprehensive income should provide any information in regard to which category of the statement of profit or loss items of OCI may be recycled in the future.

IASB's proposed amendments to other standards

- 240 In regard to the proposed amendments to IAS 34, EFRAG has some concerns about requiring a reconciliation of the MPM to the most directly comparable subtotal or total specified in IFRS Standards, including the effect of tax and non-controlling interests (NCI) separately for each of the differences between the MPM and the IFRS measure at interim financial statements.
- 241 This is because, MPM reconciliations, including tax effect and NCI effect can be costly, particularly when preparing interim financial statements at consolidated level (e.g. tax includes income tax of different subsidiaries and not transactions).
- 242 As mentioned above, EFRAG would prefer that the IASB would limit the scope of its requirements to MPMs. EFRAG considers that a narrower scope would reduce significantly the costs mentioned in paragraph above.

Other primary financial statements

- 243 EFRAG welcomes the IASB's efforts to improve how information is communicated in the financial statements, with a focus on information about performance in the statement of profit or loss.
- 244 EFRAG considers that there is still room to improve primary financial statements. In particular, EFRAG considers that the IASB should consider in the future potential improvements to the statement of changes in equity, statement of cash flows and statement of financial position.

Statement of financial position

- 245 EFRAG assesses that the IASB should consider requiring, through minimum line items or subtotals, disaggregation of equity on the face of the statement of financial position to clearly identify and differentiate different subclasses of equity (e.g. ordinary shares and financial instruments that could be settled by issuing ordinary shares – implementation guidance).
- 246 In addition, EFRAG considers that it would also be useful to have a definition of debt, a key metric for users of financial statements, and related disclosures.

The statement of changes in equity

- 247 EFRAG considers there is a need to improve the statement of changes in equity to increase comparability and understandability for users of the financial statements, particularly on information related to separate components of equity related to other comprehensive income, information about other classes of equity instruments/shares and equity-like instruments and extended information about capital management. EFRAG considers that the IASB should look for improvements to/ the statement of changes in equity, particularly when considering that the IASB is not likely to address this issue within the Financial Instruments with Characteristics of Equity project (FICE) project.

Other comments: presentation of revenue and costs in different business lines

- 248 EFRAG highlights that currently there is diversity in practice on how entities that operate business activities in different industries present their performance (e.g. a manufacturer providing financing to customers or entities operating both banking and insurance services). Some present information related to the different business activities in the statement of profit or loss as part of operating profit, by adding separate rows and allocating revenues and expenses (as in paragraph IE11 of Illustrative Examples). On the contrary, others present all income and expenses related to different business activities without any business distinction, accompanied by a more detailed information in the segment reporting provided in accordance with IFRS 8.
- 249 EFRAG considers that it could be useful if the IASB could further explain how entities with different business activities related to different industries should prepare their financial statements, especially when considering the example provided by the IASB in paragraph IE11 of the Illustrative Examples. The IASB should consider whether there is a need to provide further illustration on how the split between the operating/financing and investing categories in this case. In addition, the need for consistency with the requirements in IFRS 8 should be considered together with the disclosure of judgement applied to allocate revenues and costs across business activities (e.g. in case of group internal transactions between businesses), when they are presented separately on the face of the statement of profit or loss.

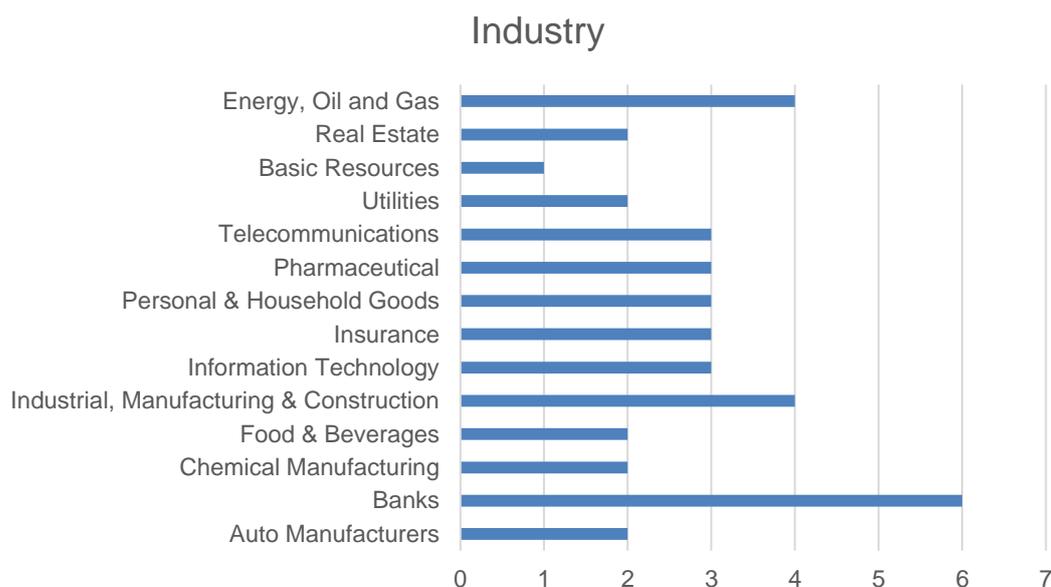
Question to Constituents

- 250 Do you agree that the IASB should consider providing more guidance for the presentation of revenues and costs when they are allocated to different business activities on the face of the statement of profit or loss, including consistency with IFRS 8 and disclosure on judgement applied in the allocation process?

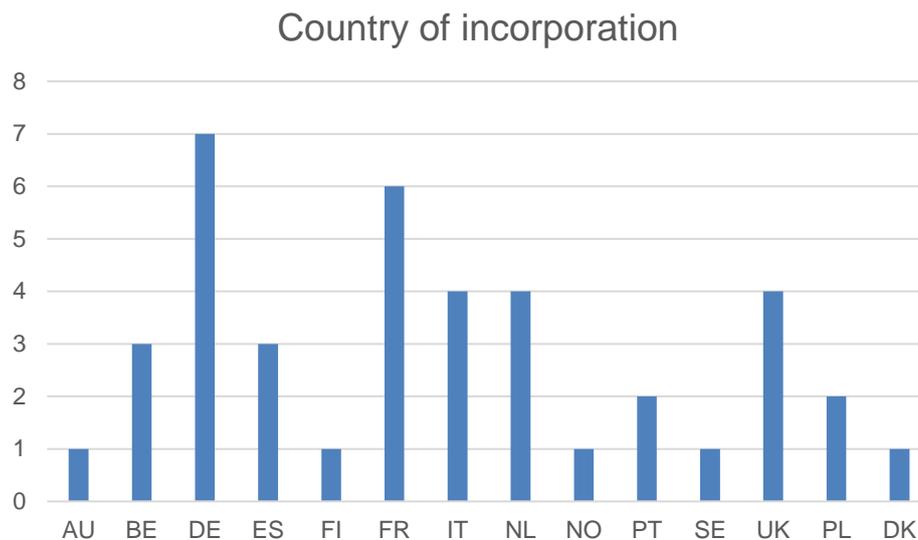
Appendix 2 – Early Stage Analysis

Introduction

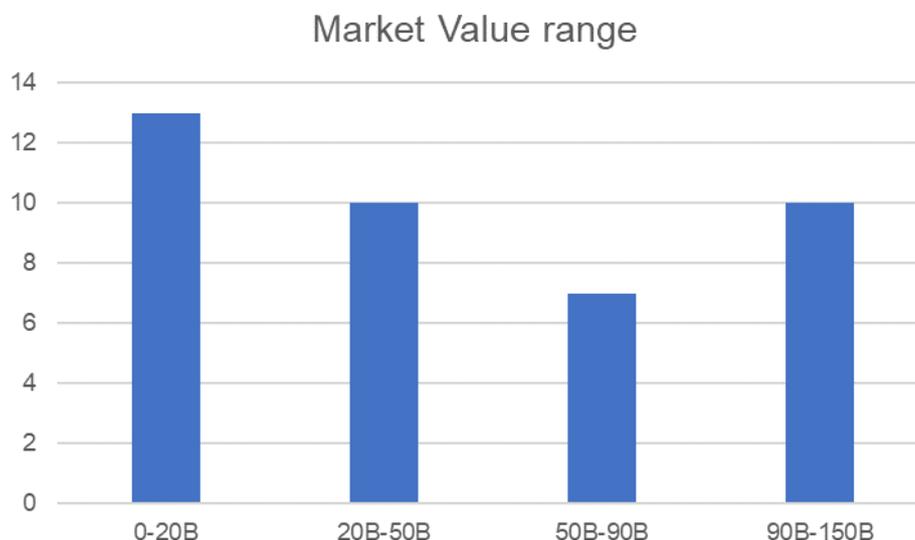
- 251 The EFRAG Secretariat analysed the financial statements of 40 European listed entities included in the S&P Europe 350 Index and STOXX 600 in order to understand current practices on presentation and how the IASB's tentative decisions will impact current practices on presentation.
- 252 We note that the sample of 40 listed entities is not statistically representative for the European listed entities. For this sample, the EFRAG Secretariat specifically selected a sample that would cover a wide range of industries, countries and sizes (market capitalisation).
- 253 The findings of the research are generally consistent with the findings of the IASB Staff, summarised in the Basis for Conclusion of the ED, and other relevant reports including a recently published ESMA report *On the use of Alternative Performance Measures and on the compliance with ESMA's APM Guidelines* (ESMA32-334-150). Nevertheless, the EFRAG Secretariat used the finding of the ESMA report in the part regarding management performance measures.
- 254 The EFRAG Secretariat analysed entities from 14 different industries. We selected a larger number of financial institutions to better understand the impact of the IASB's proposals focused on entities with financing and investing activities.



- 255 The EFRAG Secretariat also analysed entities incorporated in 14 different European countries.



- 256 Finally, the EFRAG Secretariat selected entities with different sizes in terms of market capitalisation to avoid focusing only on the biggest European listed entities.



Statement of financial performance: General

Non-financial institutions

- 257 In general, the structure and content of the financial statements of the non-financial entities analysed varied significantly. For example, some entities separately presented information about operating, financing and investing activities, while others were simply presenting all the above activities without subtotals in the statement of financial performance and therefore as part of profit before tax.

- 258 Considering the IASB's tentative decisions on the structure and content of financial statements, the EFRAG Secretariat assesses that in general the IASB's proposals would lead to a significant change to current practices on presentation of financial statements.

Financial institutions

- 259 In general, although financial institutions usually provide a higher level of disaggregation (many subtotals and line items), the structure of the financial statements varies significantly. For example, some financial institutions separately present 'total income' and 'total expense', while others present income and

expenses together under the same subtotal. Some focus on identifying what is operational income and expenses, while others do not.

- 260 Considering the IASB's tentative decisions on the structure and content of financial statements, the EFRAG Secretariat assesses that in general the IASB's proposals would lead to a significant change to current practice on presentation of financial statements. Detailed explanations can be found below.

Statement of financial performance: Level of disaggregation - number of line items

Non-financial institutions

- 261 The EFRAG Secretariat noted that for non-financial entities the level of disaggregation varied significantly from 8 to 24 line-items. We also observed that for financial institutions the level of disaggregation tends to be higher. We observed that on average non-financial entities presented 14 line-items which were distributed in the following way:

- (a) Up to 10 line-items: 13%
- (b) From 11 to 15 lines-items: 65%
- (c) More than 15 line-items: 23%

- 262 The IASB has tentatively decided to require new additional subtotals based on new categories⁸ in the statement of profit or loss. Therefore, to comply with such requirements, many entities will need to provide a higher level of disaggregation, particularly in regard to line items related to the investing and financing categories.

Financial institutions

- 263 Financial institutions tend to provide a higher level of disaggregation than non-financial entities. For example, we observed that financial institutions presented on average 22-line items while non-financial entities presented on average 14 lines items. Further, the number of line items were distributed as follows:

- (a) Up to 10-line items: 0%
- (b) From 11 to 15 line-items: 11%
- (c) More than 15 line-items: 89%

- 264 The IASB has tentatively decided to require new additional subtotals based on new categories in the statement of profit or loss. Therefore, to comply with such requirements, the EFRAG Secretariat assesses that many financial institutions will need to revise their current line items (e.g. revise presentation of line items such as unwinding of discount on pension liabilities and provisions).

- 265 In addition, the EFRAG Secretariat has not seen line items related to the unwinding of the discount of some liabilities being separately presented on the face of the financial statements. Therefore, financial institutions may need to reassess whether such line items are material to require separate presentation.

Statement of financial performance: Level of disaggregation - subtotals used

Non-financial institutions

- 266 The EFRAG Secretariat noted that most of the entities (60%) had at least 4 subtotals:

⁸ Operating profit, operating profit or loss and share of profit or loss of integral associates and joint ventures, profit or loss before financing and income tax, investing category, financing category and income and expenses related to these two categories.

- (a) Gross profit;
- (b) Operating profit;
- (c) Profit before tax (required by IAS 1); and
- (d) Profit for the year (required by IAS 1).

267 We also noted that 54% of the entities also used (part) subtotals within other subtotals. For example, some entities presented 'total operating costs', 'total operating income' and then 'total operating profit'.

268 The entities analysed use various subtotals on the face of the statement of financial performance including:

- (a) **Gross profit:** all the entities that presented their analysis of expenses by function presented this subtotal.
- (b) **Operating profit:** this subtotal was used by the majority (65%) of entities. The subtotal operating profit typically excluded line items related to share of profit from equity accounted investments, exceptional items, finance costs, investment costs and income taxes. However, the composition of the operating profit varied between entities as, for example, some entities included results from associates and joint ventures in operating profit while others excluded them, and similarly with income and expenses from investment activities. Finally, in many cases this subtotal was similar to earnings before interest and tax (EBIT) as it only excluded finance costs and share of profit from equity accounted investments, however, was labelled as operating profit.
- (c) **Profit before interest and tax or EBIT:** Only 19% of the entities made explicit reference to EBIT. This subtotal excluded items such as 'net financial expenses', 'unwinding of discount of provisions', 'share of profit from equity accounted investments' and 'income taxes'. Their calculation also varied between entities as for example some entities included results from associates and joint ventures in EBIT while others excluded them. Finally, as referred above, in many cases "operating profit" was a term similar to 'EBIT'.
- (d) **Finance results:** Many entities (45%) presented a separate subtotal related to 'finance results'. However, there is no definition within IFRS Standards of what should be included in finance costs. Financing activities are currently defined only in IAS 7 as activities that result in changes in the size and composition of the contributed equity and borrowings of the entity.
- (e) **Profit before tax:** all entities used this subtotal as required by IAS 1.
- (f) **Profit for the year:** all entities used this subtotal as required by IAS 1.

269 Other less-common subtotals presented include the following:

- (a) Gross operating profit;
- (b) Total revenues and total costs;
- (c) Total operating cost and total operating income;
- (d) Profit on sales;
- (e) Income (expenses) from investments;
- (f) Income from property management; and
- (g) EBITDA.

270 The EFRAG Secretariat assesses that the IASB's proposals on new subtotals based on new categories will significantly impact current practices on the presentation of the following subtotals:

- (a) **Operating profit:** currently there is no definition of operating profit in IFRS Standards, and therefore it is a subtotal defined by management. The IASB tentatively decided to provide guidance on the calculation of operating profit, which means that entities will have to revise one of their most common performance measures.
- (b) **EBIT:** currently there is no definition of EBIT in IFRS Standards, and therefore it is a subtotal defined by management. The IASB tentatively decided to provide guidance on the calculation of 'profit before finance and tax', thus some entities will have to revise their calculation of the subtotal 'EBIT'.
- (c) **Finance results:** currently there is no definition within IFRS Standards of what should be included in finance costs. The IASB tentatively decided to define a financing category, thus entities will have to revise their presentation of the subtotal 'finance results'.
- (d) **Investing category:** from the sample analysed, only one entity presented a separate category for investment activities. Therefore, most entities analysed will need to revise their structure to separately present income and expenses from investments.
- (e) **Financing category:** from the sample analysed, 71% of the entities presented a financing category. Some of these entities included the share of profit of associates and joint ventures in this category. There were also some entities that presented a single category for financing and investing. Therefore, the introduction of a financing category will impact many entities that currently include all income and expenses together above profit before tax and those that have a single category for financing and investing.
- (f) **Use of different subtotals:** entities will have to reconsider whether they will be able to continue to use some of their subtotals (e.g. EBITDA).

Financial institutions

271 Financial institutions tend to use more subtotals than non-financial entities (on average, financial institutions used 8 subtotals while non-financial entities used 5 subtotals). Financial institutions presented many different subtotals such as:

- (a) **operating income, operating expenses and/or operating profit:** the majority of the financial institutions (56%) used a subtotal related to operating profit. These subtotals normally included interest income, fee and commission income, trading income, dividend income, gains or losses on financial assets and liabilities, personnel and other administrative or operating expenses. In many cases, this subtotal excluded line items such as 'share of profit in associates and joint ventures', impairment charges (e.g. loans), 'goodwill', 'net gain on non-current assets' and 'net less on held for sale group entity';
- (b) **subtotals similar to gross profit** (i.e. represent the difference between a type of revenue and directly related expenses incurred in generating that revenue):
 - (i) net interest income (typically used by banks);
 - (ii) net fee income (typically used by banks);
 - (iii) premiums earned (typically used by insurance entities); and
 - (iv) net insurance benefits and claims (typically used by insurance entities)
- (c) **total income and total expenses:** the majority of the financial institutions (67%) used subtotals that were an aggregation of mostly income (with some negative components) or mostly expenses, such as 'total income' or 'total expenses'.

- (d) **profit before tax:** All financial institutions used this subtotal as required by IAS 1.
 - (e) **profit or loss:** All financial institutions used this subtotal as required by IAS 1. Some financial institutions used different terms such as 'net income' or 'net result' to present their profit for the period.
- 272 Financial institutions used many other subtotals on the face of the statement of financial performance, including subtotals within subtotals (e.g. subtotals related to impairments or subtotals that excluded non-recurring items).
- 273 None of the financial institutions made explicit reference to 'profit before interest and tax' or 'EBIT'. In addition, none of the financial institutions presented a separate subtotal or category named 'finance result' or 'investment result'.
- 274 The IASB has tentatively decided to require new additional subtotals based on new categories. Therefore, to comply with such requirements, the EFRAG Secretariat assesses that many financial institutions will need to revise their current presentation and the resulting subtotals to understand whether they will comply with the new required structure (e.g. those that present the information by separately presenting 'total income' and 'total expenses').
- 275 In particular, currently there is no definition of operating profit, therefore it is a subtotal defined by management. The IASB tentatively decided to provide guidance on the calculation of operating profit, therefore financial institutions will have to revise one of their most common performance measures.

Statement of financial performance: Presentation of expenses by nature and by function

Non-financial institutions

- 276 Our research revealed the following:
- (a) The most common classification used by entities (45%) was to present their analysis of expenses classified by function. Of the remaining entities, 35% used a classification of expenses by nature and 13% classified both by nature and function. For 6% of the entities it was difficult to conclude.
 - (b) We noted a trend within some industries:
 - (i) *Auto manufacturers:* Preference for presentation by function;
 - (ii) *Industrial, Manufacturing and construction:* preference for presentation by function;
 - (iii) *Information technology:* preference for presentation by function;
 - (iv) *Pharmaceutical:* preference for presentation by function;
 - (v) *Telecommunication Services:* preference for presentation by nature; and
 - (vi) *Utilities:* preference for presentation by nature.
 - (c) Entities that presented both by nature and function used line items such as 'distribution expenses' and 'administrative expenses' together with items such as restructuring, provisions, amortisation, depreciation and impairments.
- 277 The EFRAG Secretariat assesses that the IASB's proposals to require an entity to present an analysis of expenses included in operating profit or loss using a classification based on either their nature or function (no mix) would impact a limited number of entities that use a combined approach by mixing the nature and function presentation. In addition, all entities will have to reassess whether their presentation provides the most useful information to users of financial statements in accordance with the guidance proposed by the IASB.

Financial institutions

- 278 Some financial institutions (44%) presented their analysis of expenses using the classification based on their nature while the remaining financial institutions (56%) used a classification based on a combined approach by mixing the nature (e.g. depreciation and amortisation expense) and function presentation (e.g. administrative expenses).
- 279 The EFRAG Secretariat assesses that the IASB's proposals to require an entity to present an analysis of expenses included in operating profit or loss using a classification based on either their nature or function (no mix) will affect many financial institutions that use a combined approach by mixing the nature and function presentation as they typically mention 'general and administrative expenses', 'other administrative expenses' and 'acquisition and administrative expenses'.

Statement of financial performance: Single statement or two statements

- 280 The majority of the entities in the sample used two statements to present their performance, thereby contributing to comparability across countries and industries. However, we note that outreach activities have suggested that investors often do not use or understand the other comprehensive income part of the statement of financial performance.
- 281 All the financial institutions in the sample used two statements to present their performance, thereby contributing to comparability.

Statement of financial performance: Unusual items

Non-financial institutions

- 282 The majority of entities (61%) did not include an explicit reference to unusual line items on the face of the statement of financial performance.
- 283 For the entities that made explicit reference to unusual items on the face of the statement of financial performance, we noted that:
- (a) They disclosed the total amount in a separate note;
 - (b) different terms were used to refer to unusual line items – two entities used the term 'extraordinary contributions'. Other entities referred to them as 'non-underlying items', 'items affecting comparability' or 'special items';
 - (c) five entities included these amounts in operating profit, three entities excluded them from operating profit; two entities presented unusual items after profit before taxes. One entity had the effect of non-recurring items in each relevant subtotal;
 - (d) the nature of the line items presented as unusual included:
 - (i) restructuring costs;
 - (ii) non-recurring net finance income(cost);
 - (iii) impairment of assets;
 - (iv) reversal of impairment on financial assets; and
 - (v) litigations related expenses.
- 284 The EFRAG Secretariat assesses that the IASB's proposals and definition of unusual income and expenses will require entities to reconsider the line items presented on the face non-recurring or unusual, etc. Additionally, entities will have to reconsider whether the subtotals that exclude line items such as restructuring costs, litigation expenses, or impairments (e.g. profit before income tax and extraordinary items) will fit within the new structure proposed by the IASB.

Financial institutions

- 285 Financial Institutions did not include an explicit reference to the term non-recurring, exceptional, non-core items or extraordinary on the face of the statement of financial performance.
- 286 However, line items and subtotals that could be considered as non-recurring were presented separately. For example:
- (a) Subtotals such as 'net operating income before change in expected credit losses and other credit impairment charges'; and
 - (b) Expense line items such as impairments, net gain on non-current assets, goodwill, net loss on the sale of a group and cost of risk that were presented separately between subtotals.
- 287 The IASB has tentatively decided to require new additional subtotals based on new categories. Therefore, to comply with such requirements, the EFRAG Secretariat assesses that many financial institutions will need to revise their current subtotals and line items, particularly those related to non-recurring items. For example, financial institutions that are currently excluding non-recurring items (e.g. impairments) from their operating profit would have to revise their presentation.

Statement of financial performance: Results of associates and joint ventures

Non-financial institutions

- 288 The presentation of the share of results from associates and joint ventures varied. In most cases (84%), the share of results from associates and joint ventures was presented within profit before tax. In such cases, 19% of those entities included them in operating profit/ EBIT and 52% after operating profit /EBIT. However, entities which did not have an operating category in their statement of financial performance included the share of profit(loss) from associates and joint ventures between the gross profit and profit before income taxes.
- 289 Only one entity in our sample of 31 non-financial entities presented a statement of financial performance with clearly separate operating, financing and investing categories. This entity included the share of profit (loss) from equity-accounted investments in the investing category.
- 290 There were 8 entities that presented a separate line item for the results of equity-accounted investments between two other subtotals, however, no particular subtotal was created to show the results in performance before and after this had been considered.
- 291 The EFRAG Secretariat assesses that the IASB's proposals on integral and non-integral will significantly affect all entities that currently present a share of profit or loss from associates and joint ventures as currently none of the entities analysed made a distinction between integral and non-integral.

Financial institutions

- 292 The presentation of the share of profit or loss from associates and joint ventures varied. However, the presentation of results of associates and joint ventures was often shown after operating profit or at the bottom close to the subtotal profit before tax.
- 293 The IASB has tentatively decided to separately present integral and non-integral associates and joint ventures. Therefore, to comply with such requirements, the EFRAG Secretariat assesses that all financial institutions that present share of profit of associates and joint ventures will need to revise their current subtotals and line items, particularly those related to integral and non-integral, a distinction that currently is not being made.

294 An example is included below to illustrate the new presentation requirements:

	Interest income	X
	Interest expense	X
	Net interest income	X
	Fee and commission income	X
	Fee and commission expense	X
	Net fee and commission income	X
	Net trading income	X
	Net investment income	X
	Credit impairment losses	X
	Employee benefits expense	X
	Depreciation and amortisation expenses	X
	Operating profit	X
	Share of results of integral associates and joint ventures	X
	Operating profit and share of profit or loss of integral associates and joint ventures	X
	Share of results of non-integral associates and joint ventures	X
	Unwinding of discount on pension liabilities and provisions	X
	Profit before tax	X
	Income tax expense	X
	Profit for the year	X

Statement of cash flows

Non-financial institutions

295 When analysing the statement of cash flows, we noted that:

- the **starting point** for reporting cash flows from operating activities when the indirect method is used varied. The majority of the entities (65%) used 'profit after tax'. The remaining entities used 'profit before tax' or operating profit;
- the presentation of **interest received**, and **dividends received** in the statement of cash flows varied. The majority of the entities (65%) presented interest received from debt investments, dividends received from equity investments and dividends received from joint ventures or associates in operating activities, while the others used investing activities;
- nearly half of the entities (48%) presented interest paid as in the operating category of the statement of cash flows; and
- all entities presented **dividends paid** within the financing activities.

296 In regard to how the IASB's proposals will change current practice, the EFRAG Secretariat assesses that the IASB's proposals will impact some but not all sections of the statement of cash flows.

- starting point for determining the net cash flows from operating activities:** the IASB's tentative decision to start with the subtotal operating profit is a significant change to current practice. Thus, a majority of the entities will have to revise their statement of cash flows to start with operating profit when using the indirect method;
- dividends paid:** the IASB's tentative decision to classify all dividends paid within financing activities will not change current practice as all entities analysed presented dividends paid within the financing activities section;

- (c) **Interest paid:** the IASB's tentative decision to classify all interest paid within financing activities will affect many non-financial entities (48%) that currently classify interest paid within operating section;
- (d) **Interest received:** the IASB's tentative decision to classify all interest received within the investing category will significantly change current practice as the half of non-financial entities (48%) classified interest received as operating rather than investing; and
- (e) **dividends received:** the IASB's tentative decision to classify all dividends received within the investing category will affect many non-financial entities (32%) that current classify dividends received within operating section.

Financial institutions

- 297 All of the financial institutions analysed used the indirect method in their statement of cash flows. However, they had different starting points for their presentation of cash flows. The majority of the financial institutions used either 'profit before tax' (44%) or 'profit or loss' (44%) as a starting point. Only 11% started with 'operating profit'.
- 298 Concerning the classification of interest, many financial institutions presented **interest paid** and **interest received** within 'operating activities'. However, such classification was not always clearly presented on the face of the statement of cash flows when financial institutions used the indirect method. In some cases, this information is separately presented in a subtotal within the operating cash flows section or at the bottom. There were also cases where interest paid was classified as financing. For example, interest paid related to intra-group borrowings or net cash impact of interest margin relating to hedging derivatives on financing debt.
- 299 In regard to **dividends paid**, when presented they were typically classified as financing activities.
- 300 In regard to **dividends received** from equity instruments, when presented they were typically classified as operating activities. However, there was one case where cash flows from dividends received from equity instruments were classified as investing activities. one financial institution classified dividends received from associates and joint ventures in operating activities.
- 301 Finally, most of the references to associates and joint ventures were related to acquisition and disposals of associates and joint ventures, which were classified as investing activities.
- 302 In regard to how the IASB's proposals will change current practice, the EFRAG Secretariat assesses that:
- (a) **starting point for determining the net cash flows from operating activities:** the IASB's tentative decision to start with the subtotal operating profit is a significant change to current practice. Thus, most financial institutions will need to revise their statement of cash flows to start with operating profit;
 - (b) **dividends paid**, the IASB's tentative decision to classify all dividends paid within financing activities will not change current practice as all financial institutions analysed presented dividends paid within the financing activities section; and
 - (c) **Interest paid, interest received and dividends received:** the impact on the statement of cash flows will depend on how financial institutions will classify related income/expenses in P&L. Applying the proposals for classification in the statement(s) of financial performance for financial entities, it is likely that many financial entities will present most, or all, of their interest income, interest expenses and/or dividend income in the operating profit section of the

statement(s) of financial performance. The EFRAG Secretariat assesses that in such cases, there would not be a significant change in practice. The financial institutions that have classified interest paid as financing (e.g. interest paid related to intra-group borrowings or net cash impact of interest margin relating to hedging derivatives on financing debt) or interest received as investing, will have to revise their classifications in the statement of financial performance as the classification in the statement of cash flows will depend on classification of related income/expenses in the statement of financial performance.