

# PRIMARY FINANCIAL STATEMENTS

TARGETED OUTREACH ACTIVITIES

FINANCIAL INSTITUTIONS



# DISCLAIMER

---

This paper has been prepared by the EFRAG Secretariat for discussion at a public meeting of EFRAG TEG. The paper forms part of an early stage of the development of a potential EFRAG position. Consequently, the paper does not represent the official views of EFRAG or any individual member of the EFRAG Board or EFRAG TEG. The paper is made available to enable the public to follow the discussions in the meeting. Tentative decisions are made in public and reported in the EFRAG Update. EFRAG positions, as approved by the EFRAG Board, are published as comment letters, discussion or position papers, or in any other form considered appropriate in the circumstances.

# CHANGES FROM THE PROPOSALS IN THE EXPOSURE DRAFT

---

## KEY CHANGES IN TERMS OF PRESENTATION

- **Definition of financing activities:** the IASB tentatively decided to change its approach for classifying income and expenses within the financing category and aspects of the proposals for entities with specified main business activities
- **Share of results of associates and joint ventures**
  - Dropped the proposal to distinguish integral and non-integral associates and joint ventures
  - Dropped the proposal to require the presentation of the subtotal 'operating profit and share of profit or loss of integral associates and joint ventures and the related category 'Integral associates and joint ventures'
  - The share of results of associates and joint ventures accounted for under the equity method would be required to be presented in the investing category, even if an entity invests as part of its main business activities

# CHANGES FROM THE PROPOSALS IN THE EXPOSURE DRAFT

---

## KEY CHANGES IN TERMS OF PRESENTATION

- **Cash and cash equivalents:** Income and expenses from assets that generate a return individually and largely independently of other resources held by an entity are classified in the investing category, including cash and cash equivalents.
- Still, the classification of income and expense from cash and cash equivalents would depend on an entity's main business activities. For example, for entities that invest in financial assets as a main business activity, the income and expenses from cash and cash equivalents would be classified in the operating category
- **Derivatives and hedging instruments:** income and expenses on derivatives are classified in the operating category, rather than in the investing category, under certain conditions such as the exceptions related to when it would involve grossing up gains and losses and when it would involve undue cost or effort

# CHANGES FROM THE PROPOSALS IN THE EXPOSURE DRAFT

## CORPORATES

### Statement of financial performance - 2019 Exposure Draft

Revenue	x
Changes in inventories of finished goods and WIP	x
Raw materials and consumables used	x
Employee benefits expense	x
Depreciation and amortisation expenses	x
Restructuring costs	x
<b>Operating profit</b>	<b>X</b>
Share of results of integral associates and joint ventures	x
<b>Operating profit and share of profit or loss of integral associates and JVs.</b>	<b>X</b>
Income and expenses from investments	x
Incremental expenses from investments	x
Income and expenses on derivatives and hedging instruments (specific cases)	x
Share of results of non-integral associates and joint ventures	x
<b>Profit before financing and income tax</b>	<b>X</b>
Income and expenses from cash and cash equivalents	x
Income and expenses from financing activities	x
. Interest expenses from debt issued or lease liabilities	
. Debt extinguishment and debt restructuring expenses	x
. Dividends on issued shares classified as liabilities	x
Income and expenses not from financing activities	x
. Net interest expense/income on a net defined benefit liability/asset	x
. Unwinding of the discount on a decommissioning, restoration or similar liability	x
<b>Profit before tax</b>	<b>X</b>
Income tax expense	x
<b>Profit for the year from continuing operations</b>	<b>X</b>
Loss from discontinued operations	x
<b>Profit for the year</b>	<b>X</b>

Operating

Investing

Financing

### Statement of financial performance - Redeliberations

Revenue	x
Changes in inventories of finished goods and WIP	x
Raw materials and consumables used	x
Employee benefits expense	x
Depreciation and amortisation expenses	x
Income and expenses on derivatives and hedging instruments (specific cases)	x
Restructuring costs	x
<b>Operating profit</b>	<b>X</b>
Share of results of associates and joint ventures	x
Income and expenses from investments, including cash and cash equivalents	x
<del>Incremental expenses from investments</del>	x
<b>Profit before financing and income tax</b>	<b>X</b>
<i>Income and expenses from liabilities that arise from transactions that involve only the raising of finance</i>	x
. Interest expenses from debt issued	x
. Debt extinguishment and debt restructuring expenses	x
. Dividends on issued shares classified as liabilities	x
<i>Specified income and expenses on other liabilities</i>	
. Interest expenses on lease liabilities	x
. Interest expenses and effect of changes in interest rates (in general)	x
. Net interest expense/income on a net defined benefit liability/asset	x
. Interest expenses to suppliers with extended payment period (goods&services)	x
. Unwinding of the discount on a decommissioning, restoration or similar liability	x
<i>Income and expenses on derivatives and hedging instruments (specific cases)</i>	x
<b>Profit before tax</b>	<b>X</b>
Income tax expense	x
<b>Profit for the year from continuing operations</b>	<b>X</b>
Loss from discontinued operations	x
<b>Profit for the year</b>	<b>X</b>

\*The EFRAG Secretariat has included a high level of disaggregation just to illustrate the classification of some items. However, the **materiality principle and the role of disclosures** have to be considered (i.e. disaggregation may appear in the disclosures)

# CHANGES FROM THE PROPOSALS IN THE EXPOSURE DRAFT

## BANKS (OPTION ALL IN OP)

### Statement of financial performance - 2019 ED

Interest income	x
Interest expense	x
<b>Net interest income</b>	<b>x</b>
Fee and commission income	x
Fee and commission expense	x
<b>Net fee and commission income</b>	<b>x</b>
Net trading income	x
Net investment income, including cash and cash equivalents	x
Credit impairment losses	x
Employee benefits expense	x
Depreciation and amortisation expenses	x
<b>Operating profit</b>	<b>X</b>
Share of results of integral associates and joint ventures	x
<b>Operating profit and share of profit or loss of integral associates and joint ventures</b>	<b>X</b>
Share of results of non-integral associates and joint ventures	x
Income and expenses not from financing activities	x
. Net interest expense/income on a net defined benefit liability/asset	x
. Unwinding of the discount on a decommissioning, restoration or similar liability	x
<b>Profit before tax</b>	<b>X</b>
Income tax expense	x
<b>Profit for the year</b>	<b>X</b>

**Operating**  
(includes investing and financing activities that are part the entity's main business activities)

Investing & financing activities that are not part of main business activities

### Statement of financial performance - - Redeliberations

Interest income	x
Interest expense	x
<b>Net interest income</b>	<b>x</b>
Fee and commission income	x
Fee and commission expense	x
<b>Net fee and commission income</b>	<b>x</b>
Net trading income	x
Net investment income, including cash and cash equivalents	x
Credit impairment losses	x
Employee benefits expense	x
Depreciation and amortisation expenses	x
<b>Operating profit</b>	<b>X</b>
Share of profit or loss of associates and joint ventures	x
<b>Specified income and expenses on other liabilities</b>	<b>x</b>
. Net interest expense/income on a net defined benefit liability/asset	x
. Unwinding of the discount on a decommissioning, restoration or similar liability	x
. <b>Interest expenses on lease liabilities</b>	<b>x</b>
<b>Profit before tax</b>	<b>X</b>
Income tax expense	x
<b>Profit for the year</b>	<b>X</b>

\***Cash and cash equivalents** presented in the financing or operating category if an entity finances customers as a main business activity

\***Cash and cash equivalents** presented in the investing or operating category if an entity invests as main business activity

# CHANGES FROM THE PROPOSALS IN THE EXPOSURE DRAFT

## INSURANCE

### Statement of financial performance - 2019 ED

Insurance revenue	X
Insurance service expenses	X
<b>Insurance service results</b>	<b>X</b>
Interest revenue calculated using the effective interest method	X
Dividends and fair value changes on financial assets	X
Incremental expenses from investments	X
Other investment revenue	X
Credit impairment losses	X
Insurance finance expenses	X
<b>Net financial result</b>	<b>X</b>
Other expenses	X
<b>Operating profit</b>	<b>X</b>
Share of results of integral associates and joint ventures	X
<b>Operating profit and share of profit or loss of integral associates and joint ventures</b>	<b>X</b>
Share of results of non-integral associates and joint ventures	X
<b>Profit before financing and income tax</b>	<b>X</b>
Income and expenses not from financing activities	X
. Net interest expense/income on a net defined benefit liability/asset	X
. Unwinding of the discount on a decommissioning, restoration or similar liability	X
<b>Profit before tax</b>	<b>X</b>
Income tax expense	X
<b>Profit for the year</b>	<b>X</b>

\*Cash and cash equivalents presented in the financing or operating category if an entity finances customers as a main business activity

Operating  
(includes investing activities that are part of the entity's main business activities)

Investing

Financing

### Statement of financial performance - Redeliberations

Insurance revenue	X
Insurance service expenses	X
<b>Insurance service results</b>	<b>X</b>
Interest revenue calculated using the effective interest method	X
Dividends and fair value changes on financial assets	X
<del>Incremental expenses from investments</del>	X
Other investment revenue, including cash and cash equivalents	X
Credit impairment losses	X
Insurance finance expenses	X
<b>Net financial result</b>	<b>X</b>
Other expenses	X
<b>Operating profit</b>	<b>X</b>
Share of profit or loss of associates and joint ventures	X
<b>Profit before financing and income tax</b>	<b>X</b>
<del>Specified income and expenses on other liabilities</del>	<del>X</del>
. Net interest expense/income on a net defined benefit liability/asset	X
. Unwinding of the discount on a decommissioning, restoration or similar liability	X
<del>. Interest expenses on lease liabilities</del>	<del>X</del>
<b>Profit before tax</b>	<b>X</b>
Income tax expense	X
<b>Profit for the year</b>	<b>X</b>

\*Cash and cash equivalents presented in the investing or operating category if an entity invests as main business activity

# CHANGES FROM THE PROPOSALS IN THE EXPOSURE DRAFT

---

## KEY CHANGES IN TERMS DISCLOSURES

- **Management performance measures** – the IASB tentatively decided to:
  - Add a rebuttable presumption that a subtotal of income and expenses included in public communications outside financial statements represents management’s view of an aspect of the entity’s financial performance applying the definition and
  - Simplify the method of calculating the tax effect for reconciling items
- **Disclosure of operating expenses by nature** – see the following slide
- **Unusual income and expenses** - The IASB tentatively decided that it will not proceed with any specific requirements for unusual income and expenses as part of this project



# DISCLOSURES OF OPERATING EXPENSES BY NATURE

---

## DISCLOSURE OF OPERATING EXPENSES BY NATURE

<b>Depreciation</b>
Cost of sales
Selling expenses
General and administrative expenses
Research and development expenses
<b>Amortisation</b>
Selling expenses
<b>Employee benefits</b>
Cost of sales
Selling expenses
General and administrative expenses
Research and development expenses

The ED proposed requiring an entity that provides an analysis of its operating expenses using the function of expense method in the statement of profit or loss to disclose in a single note an analysis of total operating expenses using the nature of expense method

The feedback received was mixed and the proposed approach was seen as being costly to apply. To achieve a more balanced outcome between costs for preparers and benefits for users, the IASB tentatively decided:

- to require an entity to disclose the amounts of depreciation, amortisation and employee benefits included in each line item in the statement of profit or loss; and
- to explore a general requirement that would require an entity to disclose, for all operating expenses disclosed in the notes, the amounts included in each line item in the statement of profit or loss



## ADDITIONAL QUESTIONS

---

# ADDITIONAL QUESTIONS ON FINANCING CATEGORY

---

## HYBRID CONTRACTS WITH HOST LIABILITIES AND EMBEDDED DERIVATIVES

- The IASB tentatively to require an entity to classify income and expenses related to:
  - separated host liabilities to be classified in the same way as income and expenses on other liabilities;
  - separated embedded derivatives to be classified in the same way as income and expenses on stand-alone derivatives;
  - contracts that are not separated to be classified in the same way as income and expenses on other liabilities
- The IASB tentatively decided to develop disclosure requirements for situations in which an entity designates an entire hybrid contract as at fair value through profit or loss with the objective giving users information about when the use of the fair value option changes the classification of income and expenses
- For liabilities that arise from transactions that do not involve only the raising of finance; that are hybrid contracts in the scope of IFRS 9 measured at amortised cost; and include an embedded derivative (the economic characteristics risks of which are closely related to the economic characteristics and risks of the host contract), the IASB decided to explore an approach that would classify all income and expenses in the financing category of the statement of profit or loss

# ADDITIONAL QUESTIONS ON FINANCING CATEGORY

---

## EXAMPLE OF HYBRID CONTRACTS WITH HOST LIABILITIES AND EMBEDDED DERIVATIVES

- **Loan with repayments linked to a commodity price** - an entity is exposed to risk relating to a commodity price through its operating activities and uses a derivative embedded in the loan to manage that risk. Applying the IASB's tentative decision,
  - the loan would be treated as a liability that is solely financing with all income and expenses classified in the financing activity;
  - the gains and losses on the separated derivative used for risk management would be classified in the operating category

## QUESTIONS

- *Are the IASB's tentative decisions on hybrid contracts with host liabilities and embedded derivatives clear and easy to apply?*
- *Do participants identify any potential implementation and application concerns?*

# ADDITIONAL QUESTION ON DERIVATIVES

## CLASSIFICATION OF DERIVATIVES: DEFAULT CATEGORY

		Gains or losses on:	
		Derivatives	Non-derivative financial instruments
Used for risk management	Hedging instruments	Classify in the category affected by the risk the entity manages, except when it would involve grossing up gains or losses—then classify in the investing category.	
	Not designated in hedging relationships	Apply the classification requirements for hedging instruments except if such classification would involve undue cost or effort—then classify in the investing category.	Apply requirements for classification in paragraphs 45–55 of the Exposure Draft.
Not used for risk management		Classify in the investing category, except when used in the course of a main business activity—then classify in the operating category.	Not relevant for this paper

		Gains or losses on:	
		Derivatives	Non-derivative financial instruments
<u>Underlined text is a change from proposals in the Exposure Draft</u>			
		Classify in the category affected by the risk the entity manages, except when it would involve grossing up gains or losses—then classify in the <u>operating</u> category	
		Classify as above except if such classification involves undue cost or effort—then classify in the <u>operating</u> category	Apply requirements for classification in paragraphs 45–55 of the Exposure Draft.
		<u>Classify in the operating category, unless the derivative relates to financing activities and is not used in the course of the entity's main business activities. In this case, classify in the financing category.</u>	Not applicable to this paper

### QUESTION

- Do participants identify any potential implementation and application concerns the classification of fair value gains or losses on derivatives and hedging instruments?

# ADDITIONAL QUESTIONS ON MANAGEMENT PERFORMANCE MEASURES

---

## SCOPE OF MANAGEMENT PERFORMANCE MEASURES

- The IASB tentatively decided to include in the scope of the MPM requirements the numerator or denominator of a ratio, if that numerator or denominator meets the definition of an MPM.
- For example, if an entity uses 'adjusted earnings per share', then the 'adjusted earnings' (the numerator) will have to be included in a single note in the financial statements accompanied by disclosures
- The IASB tentatively decided **not to** further explore expanding the scope of MPMs to include measures based on line items presented in the statement(s) of financial performance, cash flows and financial position. The IASB also did not expand the scope of MPMs to include ratios.
- Often the subtotals used in a ratio are also used on their own as performance measures and are therefore in the scope. However, they may be excluded from the scope when they are included solely in a ratio (e.g., 'adjusted earnings' used in adjusted earnings per share)

# ADDITIONAL QUESTIONS ON MANAGEMENT PERFORMANCE MEASURES

---

## QUESTIONS

- *Do you think that the proposed requirement to include the numerator or denominator of a ratio in the scope of MPMs will result in:*
  - *useful information for users (as ratios are often calculated differently);*
  - *significant costs for preparers?*
- *Do you consider useful to have only the numerator or denominator as an MPM?*
  - *For example, is it useful that for an adjusted ROE, ROA and ROTE, only the 'adjusted net income' will have to be included in a single note in the financial statements accompanied by disclosures?*

# ADDITIONAL QUESTIONS ON SUBSIDIARIES, ASSOCIATES AND JVs

---

## PRESENTATION OF INCOME AND EXPENSES FROM SUBSIDIARIES, ASSOCIATES AND JVs

### Consolidated Financial Statements

- The income and expenses from associates and joint ventures not accounted for using the equity method would be presented in the investing category unless investing is a main business activity of the entity. If investing is a main business activity of the entity, then such income and expenses are presented in the operating category (already in the ED).
- The share of results of associates and joint ventures accounted for under the equity method would be required to be presented in the investing category, even if an entity invests as part of its main business activities (IASB tentative decision).

### Separate Financial Statements

- the share of profit or loss of all equity accounted investments would be classified in the investing category
- the income and expenses of equity investments not accounted for using the equity method (i.e. cost or in accordance with IFRS 9) would be presented in the investing category unless investing is a main business activity of the entity



# ADDITIONAL QUESTIONS ON SUBSIDIARIES, ASSOCIATES AND JVs

---

## QUESTIONS

- **Consolidated financial Statements:** *Do you think that the proposed requirement to include all equity accounted investments in the investing category will result in useful information for users?*
- **Separate financial statements:** *Do you think that the proposed requirements for the presentation of subsidiaries, associates and joint ventures will result in useful information for users?*



EFRAG is co-funded by the European Union and EEA and EFTA countries. The contents of EFRAG's work and the views and positions expressed are however the sole responsibility of EFRAG and do not necessarily reflect those of the European Union or the Directorate-General for Financial Stability, Financial Services and Capital Markets Union (DG FISMA). Neither the European Union nor DG FISMA can be held responsible for them.



THANK YOU



EFRAG  
Aisbl - ivzw  
35 Square de Meeüs  
B-1000 Brussel  
Tel. +32 (0)2 210 44 00  
[www.efrag.org](http://www.efrag.org)

