EFRAG FR TEG - CFSS
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IFRS 18

PRESENTATION AND DISCLOSURE IN FINANCIAL STATEMENTS

ENDORSEMENT CONSIDERATIONS

2 July 2024, Brussels

EFRAG Project Team

EFRAG
Financial reporting

DISCLAIMER

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OBJECTIVE OF THE SESSION

1. To give an overview to the EFRAG Endorsement Work-plan and receive input on it
2. To inform about issues to be assessed related to the Endorsement criteria, check its completeness, and receive additional input on it

OVERVIEW

- ENDORSEMENT PROCESS (reminder)
- EFRAG WORKPLAN OVERVIEW
- IFRS ENDORSEMENT CRITERIA (reminder)
- IFRS 18 – KEY TOPICS FOR THE ENDORSEMENT PROCESS
- APPENDIX A: PRELIMINARY ASSESSMENT OF THE ENDORSEMENT CRITERIA

IFRS ENDORSEMENT PROCESS (reminder)

1

- **IASB issues** a new standard or interpretation of a standard or an amendment to an existing standard or interpretation

2

- European commission (EC) issues the **Endorsement Advice Request to EFRAG.** The endorsement advice request for the IFRS 18 was received on April 29, 2024

3

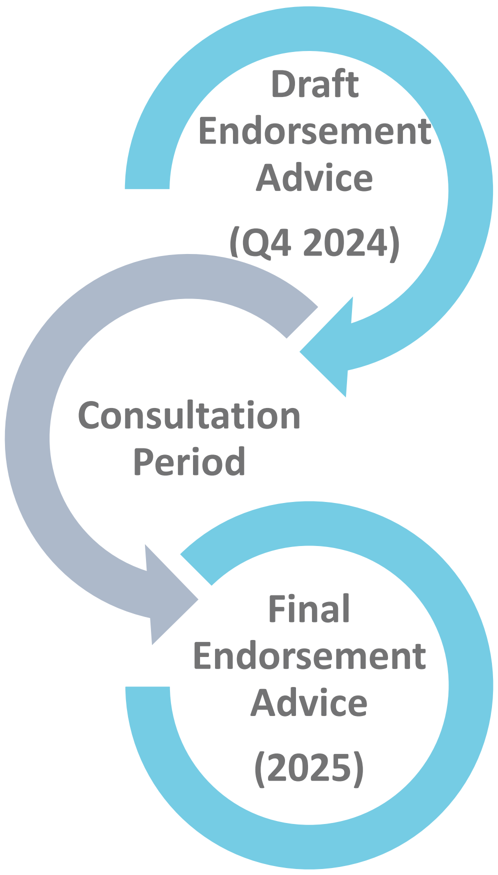
- **EFRAG provides its final endorsement advice to the EC** on endorsement after public consultation on a Draft Endorsement Advice in which the endorsement criteria are preliminary assessed

4

- If **EC decides to endorse** the new standard, it follows the necessary steps – including submission to ARC in all EU official languages, submission to the European Parliament and the Council for a 3-month scrutiny period (overall at least 6 months process) which ends with the publication in the Official Journal

EFRAG WORKPLAN OVERVIEW

1. **Preliminary identification of issues** through previous targeted outreaches, discussions with working groups, round tables and research activities
2. **Impact assessment** through the analysis of a sample of 2023 financial statements covering various industries
3. **Educational meetings** with the participation of the IASB for the EFRAG working groups, FR TEG and User Panel
4. **Educational events** with the participation of the IASB (separate dedicated events for corporates and financial institutions / insurance industry)
5. **Targeted outreaches and other activities** to assess the endorsement criteria and whether the standard is conducive to the European public good
6. **Survey**, if deemed necessary based on the outcome of the meetings with different groups and considering any specific requests from the EC



EFRAG WORKPLAN – TIMELINE APPROVED BY THE FRB

April – June 2024: gathering feedback based on the proposed steps 1-5 discussed above
July – September 2024: any additional refinement of the issues (potential surveys)
September – November 2024: preparation of the Draft Endorsement Advice
Q4 2024: Board review and approval
Q1 2025: Proposed **consultation period of 120 days** – depending on the timing of publication 150 days to avoid the busy season
Q2 2025: Review of comments and preparation of the Final Endorsement Advice
End of Q2 2025: Board review and approval

EFRAG WORKPLAN OVERVIEW

PRELIMIARY IDENTIFICATION OF ISSUES – PREVIOUS AND CURRENT DISCUSSIONS

- Comment letters
- Round tables
- Targeted outreaches
- Discussions with EFRAG FR TEG
- Discussions with EFRAG FRB
- Discussions with EFRAG working groups

EFRAG:
SUMMARY OF THE ISSUES AND RECOMMENDATIONS
and various discussions with IASB

IASB:
Changes to the IFRS 18 proposed requirements to mitigate raised issues and accommodate various stakeholders

EFRAG:
Research activities (articles and commentaries issued in advance of the publication), review of the draft version of IFRS 18

EFRAG:
Identification of the remaining topics

EFRAG WORKPLAN OVERVIEW

3. EDUCATIONAL MEETINGS

Educational meetings for all EFRAG's working groups with the participation of the IASB PFS (IFRS 18 team) and a Board Member.

Educational meetings structured as follows:

- General presentation of IFRS 18 focusing on the points relevant for each group;
- Discussion of the topics previously raised by the working groups and how the topics were addressed in the final version of IFRS 18;
- Identification of any other topics relevant for the endorsement criteria.

30 April 2024 – FIWG

14 May 2024 – FR TEG & UP

16 MAY 2024 – RRAWG

28 May 2024 – IAWG

EFRAG WORKPLAN OVERVIEW

EDUCATIONAL EVENTS

EFRAG organised joint events with the IASB, BusinessEurope, EACB, EBF, ESBG and Insurance Europe, two educational sessions for corporate and financial institution stakeholders.

The events were structured as follows:

- Presentation of main requirements of IFRS 18 / tailored for Corporates and FI;
- Application of detailed requirements identified as hot topics in previous EFRAG discussions and through questions raised upfront;
- Participants with speaking rights (companies that previously participated in the round tables and targeted outreaches) will be able to address their questions directly to the IASB;
- Other viewers will be able to raise the questions through Q&A.

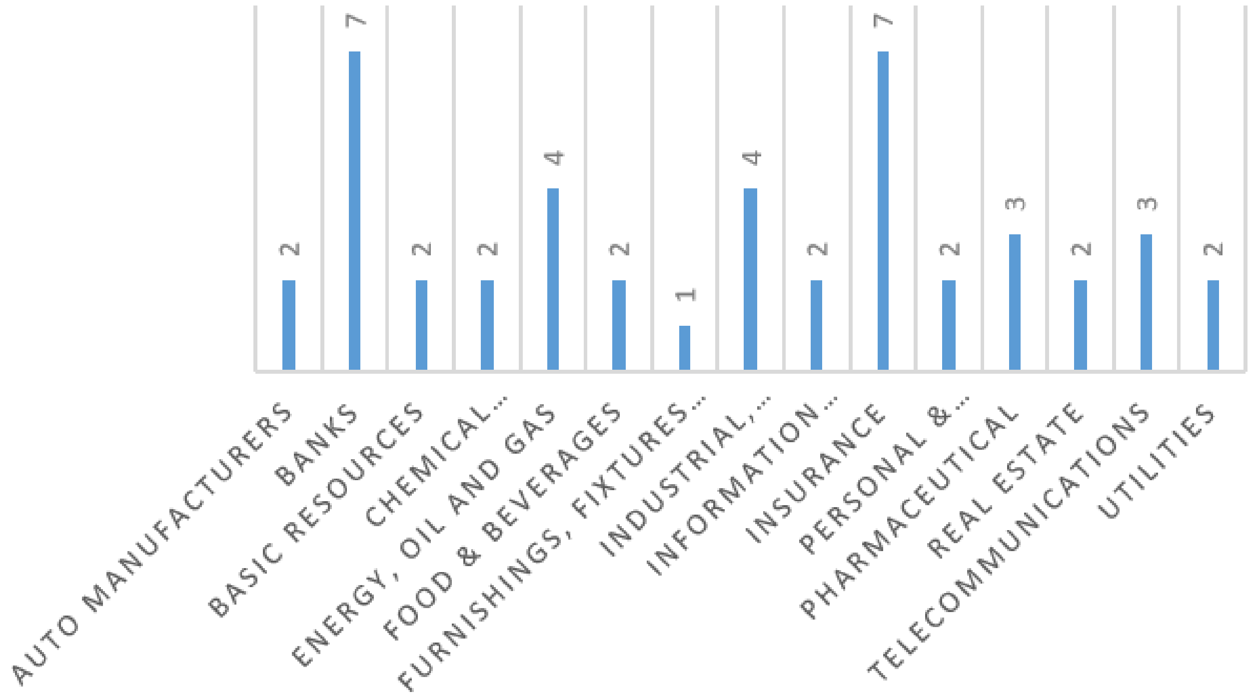
The recordings of the events are available here:

- Corporates
- Financial Institutions, Insurance Companies and Conglomerates

EFRAG WORKPLAN OVERVIEW

IMPACT ASSESSMENT

Impact assessment based on the analysis of the 2023 financial statements of 45 European listed entities covering a wide range of industries, countries and sizes (market capitalisation).



QUESTION TO THE FR TEG and CFSS

1. Do you have any comments on the EFRAGs Endorsement Plan?
2. What comment period do you consider being sufficient?

IFRS ENDORSEMENT CRITERIA and KEY TOPICS FOR THE ENDORSEMENT PROCESS

IFRS ENDORSEMENT CRITERIA (reminder)

IFRS 18 was published in April 2024 and will be effective for annual reporting periods beginning on or after 1 January 2027, with earlier application being permitted, subject to the adoption in the EU.

Regulation (EC) No 1606/2002 (IAS Regulation) establishes the criteria for the IFRS Accounting Standards to be adopted in the EU.

Technical endorsement criteria

- Relevance
- Reliability including prudence
- Comparability
- Understandability
- True and Fair view

European public good criteria

- Potential effect on EU economy (financial stability, competitiveness)
- Potential effects on stakeholders
- Costs and benefits analysis

Other criteria

- No other criteria were requested by the EC

IFRS ENDORSEMENT CRITERIA (reminder)

- **Relevance** – information is relevant when it influences the economic decisions of users by helping them evaluate past, present or future events or by confirming or correcting their past evaluations. Information is also relevant when it assists in evaluating the stewardship of management.

- **Reliability** – information has the quality of reliability when it is free from material error and bias and can be depended upon by users to represent faithfully what it either purports to represent, or could reasonably be expected to represent, and is complete within the bounds of materiality and cost. There are a number of aspects to the notion of reliability: freedom from material error and bias, faithful representation, and completeness.

- **Comparability** - the notion of comparability requires that like items and events are accounted for in a consistent way through time and by different entities, and that unlike items and events should be accounted for differently.

IFRS ENDORSEMENT CRITERIA (reminder)

- **Understandability** - the notion of understandability requires that the financial information provided should be readily understandable by users with a reasonable knowledge of business and economic activity and accounting, and the willingness to study the information with reasonable diligence. Further, in assessing whether the information resulting from the application of a Standard is understandable, EFRAG considers whether that information will be unduly complex.

- **True and Fair view** – a Standard will not impede information from meeting the true and fair view principle when, on a stand-alone basis and in conjunction with other IFRS Standards, it:
  a) does not lead to unavoidable distortions or significant omissions in the representation of that entity's assets, liabilities, financial position and profit or loss; and
  b) includes all disclosures that are necessary to provide a complete and reliable depiction of an entity's assets, liabilities, financial position and profit or loss.

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IFRS 18 - KEY TOPICS FOR THE ENDORSEMENT PROCESS

CLASSIFICATION OF INCOME AND EXPENSES ARISING FOR EQUITY-ACCOUNTED INVESTMENTS IN THE INVESTING CATEGORY

PREPARERS FROM INSURANCE INDUSTRY:

Results related to the insurance contracts should be within operating category to avoid mismatch with contracts-related expenses. Some classification will be influenced by accounting policy choice and not differences in business models.

Application of IAS 28 upon transition will not be possible in some circumstances based on the IAS 28 scope.

USERS:

Disagreeing with providing industry-specific exception. For the insurance industry acknowledged importance of distinction between investments that are at the service of insurance liabilities and the others.

ENDORSEMENT CONSIDERATIONS:

- Compromise through the introduction of a specified subtotal "operating profit or loss and income and expenses from investments accounted for using the equity method", which is not MPM.
- Possibility to reconsider the application of IAS 28 upon transition.
- Possibility to present additional metrics within MPM section of the financial statement (subject to MPM requirements).

IFRS 18 - KEY TOPICS FOR THE ENDORSEMENT PROCESS

ANALYSIS OF EXPENSES BY NATURE WHEN PRESENTING BY FUNCTION

PREPARERS: concerns about the costs for providing such a disclosure.

IASB PROPOSED COST MITIGATING SOLUTION: limit to 5 categories & the amounts disclosed are not required to be expense amounts (i.e., it could include the amount capitalised)

USERS: supportive of the requirement to disclose by nature when presenting by function. Concerns about IASB's proposed solution which will not allow the reconciliation to the P&L

ENDORSEMENT CONSIDERATIONS:

- Cost mitigating solution with positive impact on the cost/benefit criteria.
- Improved comparability of the information (transparency), however understandability might be impaired by the presentation of total cost amount (not only expense amounts).
- Additional cost foreseen by the Insurance Industry who just changed its IT systems to align with IFRS 17.

IFRS 18 - KEY TOPICS FOR THE ENDORSEMENT PROCESS

CONCEPT OF "USEFUL STRUCTURED SUMMARY"

Concept introduced during balloting process, seemed to go beyond the IASB tentative decisions by introducing exceptions to the general disaggregation requirements (e.g., risk to overriding structural requirement, materiality assessment...)

USERS and PREPARERS: to further investigate potential impacts on the structure of the financial statements and related costs and benefits

ENDORSEMENT CONSIDERATIONS :

- Allowing additional flexibility to the companies to present relevant structure of the P&L.
- This extra flexibility may reduce overall comparability, notwithstanding defined subtotals

IFRS 18 - KEY TOPICS FOR THE ENDORSEMENT PROCESS

MPMS:
SCOPING AND REBUTTABLE PRESUMPTION

- Highly regulated entities raised concerns on the effective applicability of the rebuttable presumption for all the significant measures communicated for regulatory purposes;
- Used with or without prominence is a highly judgemental concept. Additional clarifications included only in the Basis for Conclusions cannot be enforced;
- Practical challenges in determining which is the most directly comparable subtotal or total for the reconciliation (ex. “net debt cost”);
- All of the above resulting in additional cost and complexity, which may reduce understandability

MPMS:
TAX EFFECT AND EFFECT ON NON-CONTROLLING INTEREST FOR EACH RECONCILING ITEM

- May result in a complex presentation, particularly if an entity also presents by segment, impacting understandability;
- Simplified approach was introduced for the calculation of the tax effects, as cost mitigating measure, however not for the effect of NCI;
- Preparers question the relevance /usefulness of the information.

IFRS 18 - KEY TOPICS FOR THE ENDORSEMENT PROCESS

DEFINITION OF THE FINANCING CATEGORY, specifically for the financial institutions. Classification of income and expenses from liabilities into the financing category, when the underlying liabilities are not of the financial nature

Examples raised are interest expense on leases and pension liabilities

Classification of income and expenses from the HYBRID CONTRACTS, specifically for the financial institutions and insurance industry

Classification of income and expenses from the DERIVATIVE INSTRUMENTS in the default operating category and related potential volatility of these instruments

Additional guidance was provided by the IASB along with the illustrative examples and flowcharts. **These issues are deemed addressed**.

TRANSITION REQUIREMENTS, specifically to the restatement of the comparative periods. The concern related to the cost of the restatement for the entities who are required to provide more than one comparative periods.

=>> no transition relief provided

IFRS 18 - KEY TOPICS RAISED BY EFRAG FR TEG AND USER PANEL
Conglomerates

For conglomerates, determining the entity's main business activities AT THE REPORTING-ENTITY LEVEL will be complex and costly

Further clarification regarding the notion of 'an entity's main business activities', especially when considering different levels of reporting entities in a group context and the RELATIONSHIP WITH THE SEGMENT REPORTING INFORMATION UNDER IFRS 8

[IFRS 18.B30] An entity may have more than one main business activity. For example, an entity that manufactures a product and also provides financing to customers may determine that both its manufacturing activity and customer-finance activity are main business activities. To classify income and expenses into the categories of operating, investing and financing as required by this Standard, an entity need only determine whether either of, or both, investing in assets and providing financing to customers are main business activities.

+ Illustrative Example II-4

QUESTION TO THE FR TEG and CFSS

1. Do you have identified any additional items relevant for the assessment of the endorsement criteria?
2. Do you have any educational sessions in your jurisdictions from which you could gain feedback relevant for the assessment of the endorsement process. If so could you please inform us about any additional issues detected?
3. EFRAG FRB and EFRAG FR TEG (and its WG) did not identify any blocking factors for the endorsement process. What are the most important areas to be covered in the endorsement advice from your point of view?
4. Do you have any comments on the assessment attached in the appendix?

APPENDIX A: PRELIMINARY ASSESSMENT OF THE ENDORSEMENT CRITERIA

ENDORSEMENT CRITERIA ANALYSIS
Example

CLASSIFICATION OF INCOME AND EXPENSES ARISING FOR EQUITY-ACCOUNTED INVESTMENTS IN THE INVESTING CATEGORY

Technical endorsement criteria

- Relevance

  Preparers: reduced relevance for the Insurance sector and for several entities in the Banking sector or some corporates. These investments are considered to be part of the operating result. Operating result is incomplete.

  Users: strongly against sector-specific standard, understanding the issue raised by the Insurance and Banking sector, however prefer to have an operating result free of tax and financing impacts – which means to present the results of these investments outside of the operating category to not mix a net and a gross result. This would allow to calculate margins and follow developments easily.

  IASB: Consultation on integral and non-integral investments was not a success. Mitigation: Specified subtotal that does not require MPM reconciliation. User request not to mix net and gross results was followed.

- Reliability

  Preparers: Incomplete operating result as classification is driven by measurement method rather than the business model.

  Users: Any result from investments that should be considered being part of the operating result can be explained in the notes or management commentary as such.

- Comparability

  Preparers: similar investments would be classified differently based on the measurement method, reducing comparability.

  Users: improved comparability within the sector as well as across the sectors by having defined sub-totals and not mixing pre-tax results with post-tax results (results of the investments are post-tax). Additional information can be provided to distinct investments in such being related to the operating business.

ENDORSEMENT CRITERIA ANALYSIS
Example

CLASSIFICATION OF INCOME AND EXPENSES ARISING FOR EQUITY-ACCOUNTED INVESTMENTS IN THE INVESTING CATEGORY

Technical endorsement criteria

- Understandability
  - Preparers: Especially from the insurance sector, complain that it would not be understandable to present a negative operating result as the insurance cost are part of the operating result while the income from the investment for it is presented within investing.
  - Operating result currently includes as of today some of the investments depending on the business model.
  - Users: Improved structure of the profit and loss statement and disaggregation requirements help to understand the presentation.
- True and Fair view – preparers and users didn’t raise any issues
- Cost / Benefit considerations
  - Preparers: presenting relevant operating result will require presenting it as MPM, inducing additional costs for resulting disclosure requirements. Option provided by IASB to re-assess the application of IAS 28 upon transition will induce additional cost.
  - Users: benefits of having defined sub-total computed in the same way within and across industries outweigh the associated costs.

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ENDORSEMENT CRITERIA ANALYSIS
Categories and subtotals

Users (U) and Preparers (P) views		Relevance	Reliability	Comparability	Understand ability	Cost/Benefit balance
Classification of income and expenses arising from equity-accounted investments	P	Reduced for Insurance sectors, issues for the Banking sector and some corporates	Reduced as classification driven by measurement method vs business model	Reduced especially for banks and Insurance sectors – similar investments classified based on measurement method	Reduced Especially for banks and Insurance sectors	Additional cost associated with mitigating options (re-assessment of IAS 28, MpMs)
	U	No impact overall, against sector-specific requirements	To be further investigated	Improved within the sector and cross-sectors	No impact overall, against sector-specific requirements	Benefits of having defined homogeneous sub-total within and across industries
Assessment of the entity's main business activities (conglomerates)	P	Mixed views (assessment at the reporting entity level may differ from a subsidiary), conglomerates see challenges	No impact	Reduced as the assessment is judgmental	Mixed views (articulation with IFRS 8 Segment reporting may be complex), when different levels report	Additional cost related to the assessment of the main business activity at each reporting entity level
	U	To be further investigated	No impact	Reduced as the assessment is judgmental	Improved when applying the concept of useful structured summary	To be further investigated

ENDORSEMENT CRITERIA ANALYSIS
Categories and subtotals

Users (U) and Preparers (P) views		Relevance	Reliability	Comparability	Understand ability	Cost/Benefit balance
Classification of interest expenses on leases in the financing category	P	Reduced as often considered part of operating results of an entity	No impact		Reduced as often considered part of operating results of an entity	Additional cost for Insurance Industry (IT systems aligned on IFRS 17 requirements)
	U	To be further investigated	No impact	Improved cross-sectors	To be further investigated	To be further investigated
Classification of interest expenses on employee benefit plans in the financing category	P	Reduced for Insurance sector*	No impact		Reduced for Insurance sector*	Additional cost for Insurance Industry (IT systems aligned on IFRS 17 requirements)
	U	To be further investigated	No impact	Improved cross-sectors	To be further investigated	To be further investigated

* Preparers from insurance industry raised concern that the interest expenses on employee benefit plans classified directly attributable to an insurance contract in the financing category may not align with the requirements of IFRS 17 to include insurance service expenses within the operating results.

ENDORSEMENT CRITERIA ANALYSIS
Management-defined Performance Measures

Users (U) and Preparers (P) views		Relevance	Reliability	Comparability	Understand ability	Cost/Benefit balance
Scoping and rebuttable presumption	**P**	Mixed views, performance metrics were disclosed previously and are not expected to change as such	Improved, information will be audited	Improved, additional information will be provided allowing comparability	Mixed views, used with or without prominence is highly judgmental, only P&L related metrics are in scope,	Increased cost all industries. Additional cost for Financial and Insurance sector to rebut the presumption for metrics required by regulation and not considered MPMs by entity
	U	Improved, additional information will be provided, in a single note	Improved, information will be audited	Improved, additional information will be provided allowing comparability	Improved, additional information will be provided	Benefit for the users (all metrics in a single note, details of the calculation)
Reconciliation, including NCI and Income Tax effect	**P**	Mixed views, information was not requested by users in the past	Mixed views for tax: even if the information is audited, the information content is questionable due to the simplification for taxes; Overall -Improved, information will be audited		Mixed views, complex presentation may reduce understandability, most directly comparable subtotal posing practical challenges	Increased cost for all industries. Cost relief provided for tax effects but not NCI
	U	Improved, additional information will be provided, in a single note	Improved, information will be audited	Improved, additional information will be provided allowing comparability	Improved, additional information will be provided allowing comparability	Benefit for the users (reconciliation and effects on NCI and tax provide additional information)

ENDORSEMENT CRITERIA ANALYSIS
Grouping of information

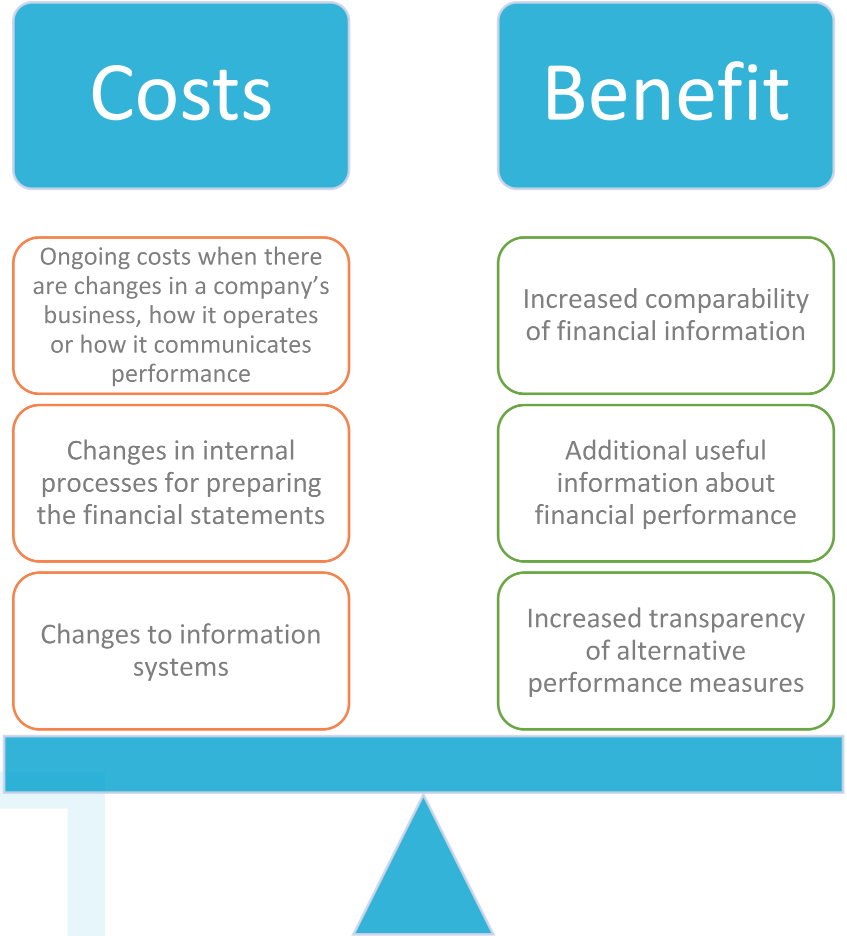
Users (U) and Preparers (P) views		Relevance	Reliability	Comparability	Understand ability	Cost/Benefit balance
Analysis of expenses by nature when presenting by function	**P**	Questionable – presentation by function is well established internationally – why additional information Reduced for Insurance industry*	Reduced due to the estimation involved			Increased cost all industries for those presenting by function or having mixed presentation. Additional cost for Financial and Insurance sector*
	U	Improved – very helpful for projections	To be further investigated	Improved	Overall improved, but total cost amount can be presented, not limited to expense-only amount (and therefore not reconciling to P&L)	Improved, transparency of the information is enhanced
Concept of "useful structured summary"	**P**	Improved, additional subtotals are allowed to meet the objectives of the financial statements	Question was raised whether it allows to condense information	Overall improved, however the structure (notwithstanding defined subtotals) can vary		
	U	Improved	To be further investigated	To be further investigated	To be further investigated	To be further investigated

* Insurance industry argument that IFRS 17 requirements do not leave a choice to present by nature as majority of the P&L line items are defined by IFRS 17 (i.e. insurance service cost etc.)

ENDORSEMENT CRITERIA ANALYSIS
Other changes & transition

Users (U) and Preparers (P) views		Relevance	Reliability	Comparability	Understand ability	Cost/Benefit balance
Restatement of any comparative period	**P**	Improved in regard to the quality of information provided and considering impacts on the audit opinion		Improved	Improved in regard to the quality of information provided, homogeneous information for all periods presented	Increased cost for any additional comparative period presented
	U			Improved comparability with previous periods	Improved as provides homogeneous information for all periods presented under IFRS 18	Improved benefits by having comparative periods restated
FV option under IAS 28.18 – different interpretation of IAS 28.18 and increased volatililty in the P&L	**P**	Mixed views, diversity in practice noted, limited applicability of FV option for Financial and Insurance sector		Mixed views, diversity in practice, measurement driven and not business model driven		Increased costs associated with the re-assessment of applicability of IAS 28 or fair value measurement
	U	To be further investigated		To be further investigated	To be further investigated	To be further investigated
Limited changes to cash flow statement	**P**			Improved, reducing diversity in practice	Mixed views, risk of misleading related to the same labelling of categories	May induce costs related to changes necessary in the IT systems
	U	To be further investigated		Improved, reducing diversity in practice	Mixed views, risk of misleading related to the same labelling of categories	Improved - starting point and presentation

PRELIMINARY COST-BENEFIT ANALYSIS OF IFRS 18 REQUIREMENTS



COST MITIGATIONS IN IFRS 18

- **Reliefs for undue cost** or effort for classification in the statement of profit or loss of:
  - gains or losses on derivatives not designated as hedging instruments applying IFRS 9 Financial Instruments; and
  - foreign exchange differences.
- **Accounting policy choice** for companies that provide financing to customers as a main business activity
- **Equity-accounted investments**
  - introduction of a specified subtotal "operating profit or loss and all income and expenses from investments accounted for using the equity method", which is not MPM
  - Option to change measurement method at transition by applying IAS 28.18.
- **Disclosure of operating expenses by nature**
  - Limiting the requirement to disclose specified expenses by nature to five
  - Amounts disclosed for nature expenses may be the cost incurred for the period
- MPMs – Scoping → **Rebuttable presumption** in the definition of MPMs
- MPMs – reconciliation → **Simplified approach** to calculating income tax effects for each reconciling item disclosed in MPM reconciliations

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