EFRAG TEG-CFSS meeting
22 March 2022
Paper 11-02
EFRAG Secretariat: PFS team

PRIMARY FINANCIAL STATEMENTS

EFRAG TEG-CFSS MEETING

22 March 2022

European Financial Reporting Advisory Group

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OVERVIEW

UPDATE ON THE PROJECT

ANALYSIS OF OPERATING EXPENSES

UPDATE ON THE PROJECT

PROJECT STATUS AND REDELIBERATIONS TO DATE

EFRAG SECRETARIAT ANALYSIS

- **Investing category**: The IASB has tentatively decided to add further application guidance to ensure consistent application. However, at this stage the IASB has not provided additional guidance on incremental expenses.
- **Financing category, including classification of hybrid contracts:** the IASB tentatively decided to change its approach on the classification of items in the financing category and to add new detailed guidance (e.g., hybrid contracts). This may be considered a significant change to the ED, which respondents have not had yet the opportunity to comment. Considering this, the EFRAG Secretariat recommends the use of consultative groups and targeted consultation to support the IASB’s decision to finalise its proposals.
- **Equity-accounted associates and joint ventures**: The IASB’s tentative decision does not seem to be fully aligned with EFRAG Comment letter as EFRAG agreed with the distinction between integral and non-integral associates and joint ventures (but called for more application guidance), highlighted that equity accounted investments may need to be reported in the operating category in particular circumstances, and asked for clarifications on how the IASB's proposals would apply to subsidiaries, associates and joint ventures in the separate financial statements.

PROJECT STATUS AND REDELIBERATIONS TO DATE

EFRAG SECRETARIAT ANALYSIS

- **Presentation of operating expenses by nature or by function:** The IASB's tentative decisions are fairly aligned with EFRAG comment letter (e.g. provide more application guidance on the function of expense). The tentative decision to withdraw the strict prohibition of a mixed presentation also reduces the pressure on the distinction between presentation by-function and by-nature. However, the EFRAG Secretariat considers that the IASB should clarify when and to which extent entities may use mixed presentation, particularly when considering minimum line items, financial conglomerates and use of 'unusual items' on the face (e.g. restructurings).

- **Minimum line items**: the IASB has not yet considered requiring, through minimum line items or subtotals, disaggregation of equity on the face of the statement of financial position.

- **Unusual items**: Although the IASB has not concluded its discussions and has decided to develop application guidance on unusual items (as requested by EFRAG), the IASB has not clarified or addressed, at this stage, many of EFRAG's requests (e.g. whether the whole amount should be recognised as unusual or only the incremental part of it when the amount varies significantly from previous periods). The definition of unusual items continues to seem to be narrow, as it focuses on whether expenses/income will occur in the future.

PROJECT STATUS AND REDELIBERATIONS TO DATE

EFRAG SECRETARIAT ANALYSIS

- **MPMs – Definition -** The IASB has addressed some of the concerns related to narrowing the definition of public communication. However, the EFRAG secretariat expresses concerns about establishing a rebuttable presumption that a subtotal of income and expenses included in public communications outside financial statements represents management's view of the entity's financial performance and to provide application guidance on how to assess whether the entity has reasonable and supportable information to support the rebuttal. This would increase the complexity and number of disclosures related to this topic. Instead, the EFRAG Secretariat would prefer an improved definition of MPMs, which clearly states which measures are in the scope (i.e. those developed by management and not defined or specified by IFRS) and which measures are typically out of the scope (e.g. performance measures developed and required by regulators).
- **MPMs - Disclosures**: the IASB tentative decision to require an entity to disclose, for each reconciling item, the amount(s) related to each line item(s) in the statement(s) of financial performance, is a significant change to the ED which has not been tested and respondents have not had the opportunity to comment. The ED itself was less prescriptive and the illustrative example provided by the IASB in its ED was just a way of providing the information (not a specific format that was required in the main standard).

PROJECT STATUS AND REDELIBERATIONS TO DATE

EFRAG SECRETARIAT ANALYSIS

- **EBITDA:** the IASB has considered that issue of excluding impairments from assets that are amortised or depreciated. However, the IASB has not yet clarified whether EBITDA and other similar measures should be included in the scope of the IASB's proposals regarding MPM disclosures if they do not represent operating profit or loss before depreciation, amortisation, and specified impairments'.
- The EFRAG Secretariat agrees with the IASB's approach for redeliberation's until now, however highlights the importance of ensuring that both its decision on presentation and disclosures are relevant for entities with specified main business activities (e.g. financial institutions). Therefore, the IASB should proceed with its discussions on the different topics (for all corporate entities) and ensure at the end of the discussions that the proposals are adequate for entities with specified main business activities (e.g. financial institutions).

ANALYSIS OF EXPENSES

ANALYSIS OF EXPENSES – PROFIT OR LOSS STATEMENT

EFRAG SECRETARIAT ANALYSIS

From EFRAG's outreach activities and comment letters, the EFRAG Secretariat acknowledges

- that many entities currently using a 'function of expense' method fail to disclose additional information on the nature of expenses and if such information is presented, it may be scattered across several notes.
- many users consider that information on the nature of expenses is useful in predicting future cash flows and that only a few natural items are specifically required in paragraph 104 of IAS 1 (ie depreciation, amortisation and employee benefits expense).
- many preparers disagree with the requirement to disclose additional information on the nature of expenses when classifying expenses by function because they are unable to provide this information with their current accounting systems.
- both users and preparers were likely to accept a more balanced outcome (e.g. providing a partial presentation by nature of some fundamental operational expenses).

ANALYSIS OF EXPENSES – DISCLOSURES

The EFRAG Secretariat considers that the IASB could take some steps to improve current requirements, including:

- give more prominence to the existing requirements in paragraph 104 of IAS 1;
- make clear that disclosures required in paragraph 104 of IAS 1 should be presented in a single note;
- relate these disclosures to the operating profit or loss category (as proposed in the ED);
- extend the list of natural items that are specifically currently required in paragraph 104 of IAS 1. For example, refer to the natural items already required by IAS 1 (e.g., ‘costs of restructuring’) and other IFRS Standards (e.g., ‘impairment losses’ as required by IAS 36), subject to materiality. In addition, confirm with users which natural items are fundamental for them;
- mention in the application guidance that a disclosure in a ‘partial matrix’ form could be a useful way of presenting the information and include such format as an illustrative example (as a way of presenting the information but not as a requirement, similar to the approach taken in IFRS 15 for the disaggregation of revenue);
- after identifying the “expanded list of natural items”, the IASB Staff could consider whether a requirement, rather than example, for a partial matrix would meet the cost-benefit threshold.

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THANK YOU

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