PRIMARY FINANCIAL STATEMENTS

SUMMARY REPORT

ROUNDTABLE WITH CORPORATES

24 October 2022

This report has been prepared for the convenience of European constituents by the EFRAG Secretariat and has not been subject to review by either the EFRAG FR Board or the EFRAG FR Technical Expert Group. The views expressed in this presentation are those of the presenter, except where indicated otherwise.

Introduction

In order to receive input from preparers and to stimulate the discussion on the key tentative changes to the IASB® proposals included in the Exposure Draft ED/2019/7 *General Presentation and Disclosures* (as a result of the IASB's redeliberation), ("the Exposure Draft" or "the ED"), EFRAG and the IASB arranged a joint outreach roundtable with corporate companies on 24 October 2022. This report has been prepared for the convenience of European constituents to summarise the event and will be further considered by the organisations involved in their respective due processes on the proposals.

The purpose of the targeted outreach activity is to assess whether the selected tentative decisions made by the IASB will function as intended and achieve the intended balance of costs and benefits.

The information obtained in the outreach will also:

- help the IASB in completing its due process and will be used to support the IASB's decisions on any of the proposals before issuing an IFRS Accounting Standard; and
- support EFRAG's potential endorsement advice activities once the IFRS Accounting Standard is published.

Jens Berger, EFRAG FR TEG Vice-Chair, welcomed participants and provided an overview of the agenda.

Bertrand Perrin, IASB Board member, presented the status of the project and the purpose of the targeted outreach. Furthermore, he stated that the feedback collected during the outreach activities would be a key component of the IASB's process when finalising the proposals and deciding on the next step of this project. He clarified that the IASB's discussions on the results of the outreach activities would be held in the first half of 2023.

Ioana Kiss, EFRAG Technical manager, presented EFRAG's planned outreach activities, which include:

- Two roundtables with corporate companies (e.g., Energy, Industrials, Healthcare, Technology, Telecoms, Utilities, etc), including those that conduct investing or financing activities as part of their main business activities (e.g., manufacturers providing financing to customers);
- One roundtable with financial institutions (e.g., banks and insurance companies), conglomerates and investment property companies;
- One roundtable with users and preparers, in the form of a webinar, with the objective of discussing whether the IASB has achieved the intended balance of costs and benefits; and
- Discussions with the EFRAG Working Groups including the EFRAG User Panel and ad hoc meetings with representatives of users and preparers.

The preparers involved in the roundtable on 24 October 2022 were asked to provide their feedback on the IASB's selected tentative decisions as detailed below.

The following companies participated in this roundtable:

- Nestlé
- Norsk Hydro
- Rompetrol
- Vonovia

Roundtable discussion

For each topic identified below:

- **Bertrand Perrin** and **Nick Barlow**, IASB Technical Staff, introduced the main parts of the IASB's tentative decisions to be discussed and responded to participants questions (Appendix 1 – IASB Outreach information (September 2022)).
- **Filipe Camilo Alves**, EFRAG Senior Technical manager, and **Ioana Kiss**, outlined the preliminary feedback arising from the EFRAG's outreach activities to date (Appendix 2 – Slides with key messages received in advance of the meeting_24 October).

TOPIC 1: Subtotals and categories in the statement of profit or loss

The IASB Staff presented a comparison of the structure of the statement of profit or loss as proposed in the ED with the new structure resulting from the IASB's redeliberations until September 2022, outlined the main new required subtotals and described the content of the operating, investing and financing categories.

Questions for participants:

(a) Is the revised proposal for classifying income and expenses within the financing category clearer and easier to apply than the proposal in the ED?

(b) Are you aware of any issues that may arise from the expected change in outcome from the ED for lease liabilities and amounts payable for goods and services received?

(c) Does the revised proposal for classifying income and expenses in the financing category result in a change from the proposals in the ED for the classification of any income and expenses from liabilities other than lease liabilities and amounts payable for goods and services received?

(d) Are you aware of any entities that provide financing to customers as a main business activity that do not also invest in financial assets as a main business activity that would be impacted by the possible change to the ED?

In general, participants welcomed the revised structure and content of the statement of profit or loss.

However, participants raised a number of questions and called for additional application guidance or illustrative examples on the classification of specific items. For example, participants raised questions on the classification of:

- "transaction costs directly related to the issue of debt" (when considering the presentation of "debt extinguishment and debt restructuring expenses" which were presented in the financing category in the illustrative example);
- Income and expenses from foreign exchange differences that arise from intragroup transactions, including borrowings (e.g., cash pooling) and declared dividends;
- gains or losses arising from disposals of businesses, including the recycling of foreign currency differences accumulated in the cumulative translation adjustment reserve resulting from consolidation techniques; and
- gains or losses that arise from subsequent measurement changes of fair value puts on non-controlling interest.

One participant said that communications with users tend to be based on non-GAAP measures but they would like these communications to be based on information in the primary financial statements. In such cases, Management Performance Measures ("MPM") should only be necessary to a limited extent.

Some participants considered that for some of the items identified above (e.g., gains or losses arising from disposals of businesses), the presentation in the operating category did not seem to be appropriate as these items were not related to the entity's main business activities. In addition, one participant detailed that an entity should have the possibility to present items such as gains or losses arising from disposals of businesses in a separate line item in order to avoid arbitrary allocation to the other functions.

In addition, one participant considered that for an entity that uses a net-debt concept, presentation of income and expenses from cash and cash equivalents in the financing category would be more appropriate.

In response to the participants questions, the **IASB Staff** clarified that:

- on foreign currency exchange differences, the IASB had tentatively decided to require an entity to classify foreign exchange differences included in the statement of profit or loss in the same category of the statement of profit or loss as the income and expenses from the items that gave rise to the foreign exchange differences (for example, foreign currency exchange differences on intercompany loans would be classified in the same category as the balance that gives rise to the foreign exchange difference), except when doing so would involve undue cost or effort (which would lead to a classification in operating profit);
- the IASB had tentatively confirmed to not develop a direct definition of operating profit. It has instead been defined as a default category. Thus, it is not limited to income and expenses from an entity's main business activities. As a result, some of the items mentioned above would be presented within operating profit as they do not meet the definitions of the other categories;
- in determining whether to provide application guidance on a specific topic, the IASB would consider factors, such as whether the topic is pervasive; and
- the decision to remove income/expenses from cash and cash equivalents from the financing category was party in response to feedback from investors who view financing from a gross debt perspective.

Filipe Alves highlighted the importance, especially for users, of having, within the financing category, a clear distinction between "income and expenses from liabilities that arise from transactions that involve only the raising of finance" and those related to "specified income and expenses on other liabilities", either in two separate line items/subtotals in the statement of profit or loss or in the disclosures.

Jens Berger noted that additional line items should be presented in the statement of profit or loss when they are relevant for users. Nevertheless, the process to assess whether the entity needs to add line items has been quite difficult in the past. Therefore, if there are some specific items that are relevant for some stakeholders, these should be included in the mandatory line items.

The **IASB Staff** explained that the requirement to present specified line items and additional line items is mainly driven by whether those line items will provide an understandable overview of the entity's income and expenses and the materiality of the disaggregated information.

TOPIC 2: Subtotals - Accounting for associates and joint ventures accounted for using the equity method

The IASB tentatively decided to require entities to present income and expenses from all associates and joint ventures accounted for using the equity method in the investing category of the statement of profit or loss.

The IASB also tentatively decided that income and expenses from associates and joint ventures not accounted using the equity method should be presented in the investing category unless investing in financial assets is a main business activity of the entity. In such cases, income and expenses from associates and joint ventures not accounted for using the equity method should be presented in the operating category.

One participant acknowledged that the IASB's tentative decisions would be easy to implement and would not require management judgment. Nonetheless, this participant noted that associates and joint ventures may contribute to an entity's main business activities and in such cases, they are typically included in operating profit. Thus, the IASB's tentative decisions would represent a change to current practice.

The **IASB Staff** highlighted that the IASB had tentatively decided to add "operating profit or loss and income and expenses from investments accounted for using the equity method" to the list of specified subtotals in paragraph 104 of the ED. Therefore, if management considers it useful to separately present associates and joint ventures within an additional subtotal (below the operating profit), this subtotal would not be considered as a management performance measure.

Another participant welcomed the IASB's tentative decisions on the presentation of associates and joint ventures and highlighted that entities would have the opportunity to show additional subtotals in the statement of profit or loss, when considered relevant, which could help management to explain how they manage their business (either as an IFRS specified subtotal or MPM).

TOPIC 3: Subtotals – Presentation of operating expenses

The IASB tentatively decided to require operating expenses to be presented in the statement of profit or loss either by nature or by function (and to allow mixed presentation) and to include application guidance which supports entities deciding which method provides more useful information.

Questions for participants:

(a) Do you think these tentative decisions of presentation of operating expenses will result in useful information for users? Are they clear and easy to apply?

(b) Do you identify any potential implementation and application difficulties or concerns?

One participant welcomed the IASB tentative decision that entities could still present an analysis of operating expenses using the method by nature or by function, depending on which provides the most appropriate information, depending on the industry. This participant also noted that a mixed presentation was not very helpful.

Another participant agreed with the IASB's tentative decision to withdraw the prohibition for a mixed presentation. Nevertheless, this participant highlighted the risk that providing a rigid description of the function of expense method could reduce the usefulness of the information (e.g., presenting the total Research and Development costs ("R&D"), including the restructuring costs, would inflate the R&D expense presented in the income statement and potentially providing deceptive information about the real cost of resources allocated to the R&D activities of an entity in a given period) and lead to arbitrary allocation of expenses that, based on their nature, are not clearly allocated to the lines that are presented by function (e.g., gain/loss on business disposals, impairment of fixed assets related to natural disasters, social unrest/riots or wars).

The **IASB Staff** acknowledged the concerns but highlighted the importance of also allocating all directly attributable income and expenses to the lines that are presented by function (e.g., research & development).

TOPIC 4: Disclosures of operating expenses by nature

The IASB tentatively decided to require an entity which presents operating expenses by function to disclose the amounts of depreciation, amortisation and employee benefits included in each line item in the statement of profit or loss.

Questions for participants:

(a) Does the IASB's tentative decision provide a better balance of costs and benefits than the proposal in the ED?

(b) Do you think the list of line items in the proposal should also include impairments and write-downs of inventories?

(c) Do you think requiring an entity to disclose, for all other operating expenses disclosed in the notes, the amounts included in each line item in the statement of profit or loss would provide a similar balance between costs and benefits as the revised proposal?

One participant explained that, from experience, when an entity decides to report operating expenses by function, it is also able to report the total operating expenses by nature. When consolidating by function, the IT system has defined rules to flag whether an item is inter-company or not and can eliminate intercompany items. In this participant view, this was complicated and challenging, but doable. This participant did not see any significant practical and technical implementation issues when the underlying IT system has been set up to capture the information. Nonetheless, this participant would prefer disclosing, in a single note, an analysis of total operating expenses using the nature of expense method without allocating them to each line item in the statement of profit or loss (as proposed in the ED). The IASB's tentative decision to disclose the amounts of depreciation, amortisation and employee benefits included in each line of the income statement would be costly and complex to implement, particularly for groups that have different IT systems locally or small and medium entities with limited IT system's capability.

Similarly, another participant emphasised the risk of undue cost and efforts to disclose the amounts of depreciation, amortisation and employee benefits included in each line of the income statement presented by function. Such disclosures would require changes to IT systems and internal processes of information, including internal controls. This participant would prefer to simply provide the total amount of amortisation, depreciation and employee costs (without allocation to individual line items). In his view, this could be extended to some or even all other costs by nature that are presented in the operating category (as proposed in the ED).

Finally, participants considered that users would like to have more information about the composition of line items presented by function. One participant added that the description (without quantification) of the main elements making up each line item in cost by function presentation would be more appropriate and could help to address users' concerns.

Filipe Alves stated that based on recent discussions with users, some of them had mentioned that some entities currently disclosed all or almost all the operating expenses by nature in the notes and users had expressed concerns that the IASB's partial disclosure approach could lead to a loss of information as entities would stop providing information for all or almost all the operating expenses by nature.

The **IASB Staff** explained that the IASB's tentative decision aims to give to investors useful and reliable information on the composition of functions presented in the statement of profit or loss while providing a relief to entities from providing disclosures of total operating expenses by nature, which could require an excessive effort for those entities not having already set up their IT systems for this purpose.

TOPIC 5: Disclosures - Management Performance Measures

> *The IASB tentatively decided to add a rebuttable presumption that a subtotal of income or expenses included in public communications outside the financial statements represents management's view of an entity's financial performance and to simplify the method of calculating the tax effect for reconciling items.*
>
> *Questions for participants:*
>
> *(a) Do you think that establishing such rebuttable presumption will achieve the intended objectives?*
>
> *(b) Does the revised method to calculate the tax effect of individual reconciling items provide a better balance of costs and benefits than the proposal in the ED?*

Scope of the management performance measures requirements

One participant considered that the definition of an MPM should be extended to include measures related to the statement of financial position, statement of cash flows and ratios (e.g. Debt/Equity and Debt/EBITDA). This would permit management to reconcile the different perspectives, the one on the management report and the one on the primary financial statements. Such measures would also have the benefit of being audited.

Bertrand Perrin highlighted that this project was mainly focused on the statement of profit or loss and, therefore, management defined measures related to the statement of financial position and statement of cash flows were currently out of the scope. However, this matter may be further discussed within a future project focused on the statement of cash flows.

Rebuttable presumption

One participant agreed with the IASB's tentative decision to establish such a rebuttable presumption in order to align financial statements to management's communication to stakeholders.

Reconciliations and simplified method of calculating the tax effect for reconciling items

Participants expressed concerns on the IASB's proposal to require disclosures on the tax effect for each item disclosed in the reconciliation, even with the simplified approach proposed by the IASB, both in terms of practical issues and usefulness of the information. In particular, participants:

- noted that for global groups, which operate in different countries with different tax regimes, the tax effect of a reconciling item may be very complex and may not result in meaningful information, especially when a transaction is reflected in other comprehensive income or when subsidiaries contribute differently to consolidated tax calculation base (for example with profit or tax loss). This complexity could also impact the auditability of such information; and
- considered that the revised simplified method could reduce the reliability and the usefulness of the information.

One participant noted that the IASB seemed to be going in the right direction, even if some judgment would still be required on the tax effect for each reconciling item.

Finally, one participant noted that users would prefer linking the reconciliations to the operating segments as per IFRS 8 *Segment Information* rather than to each reconciling line item in the statement of profit or loss. Consequently, this participant questioned whether it was worth requiring entities to disclose, for each reconciling item, amount(s) related to each line item in the statement(s) of financial performance.

The **IASB Staff** explained that the simplified approach to the calculation of the tax effect on each reconciling item aims at making such calculations more mechanical and reducing the judgment required. This should balance costs for preparers and benefits for users.

TOPIC 6: Unusual items

> *The IASB tentatively decided that it will not proceed with any specific requirements for unusual income and expenses as part of this project.*

One participant acknowledged the IASB's decision to not proceed with any specific requirements for unusual income and expenses as part of this project as there is lack of consensus on a common definition of unusual income and expenses.

TOPIC 7: Additional EFRAG's question

> *The IASB tentatively decided to classify in the operating category, rather than in the investing category, income and expenses on derivatives under certain conditions such as grossing up gains and losses or undue cost or effort.*

There were no significant comments on this topic.

Concluding remarks

Jens Berger thanked participants for their participation in the roundtable discussion of the IASB's tentative decisions to change the Exposure Draft ED/2019/7 *General Presentation and Disclosures* (ED) and for the time devoted to the preparation of the meeting. He also informed participants that the EFRAG Secretariat would prepare a summary report, which will include the main feedback received from each outreach session, and a cumulative summary report, which will summarise the feedback received from all the outreach activities, by the end of December 2022.