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Primary Financial Statements Cover Note

Objective

- 1 The objective of the session is to:
 - (a) provide an update to EFRAG FRB members on the IASB's latest tentative decisions; and
 - (b) obtain input from EFRAG FRB members:
 - (i) on factors that the IASB should consider in determining the transition period and effective date of the forthcoming IFRS Accounting Standard *General Presentation and Disclosures*;
 - (ii) to understand the expected benefits and costs for stakeholders in your region of the forthcoming IFRS Accounting Standard to help the IASB develop the Effects Analysis that will be published together with the IFRS Accounting Standard.

Background

- 2 In December 2019, the IASB published the [Exposure Draft *General Presentation and Disclosures*](#) focused on improving how information is communicated in the financial statements, with a focus on information about performance in the statement of profit or loss. The IASB's comment period ended in September 2020. EFRAG sent its [comment letter](#) to the IASB on 2 November 2020.
- 3 In early 2021, the IASB discussed the feedback received and has since made numerous tentative decisions on key aspects of the proposals in response to the feedback received. Some of these tentative decisions would result in changes from the proposals in the ED.
- 4 In September 2022, the IASB launched an outreach on a targeted selection of its tentative decisions through roundtable discussions on topics. In addition, EFRAG sought feedback on additional topics where the IASB's tentative decisions would change the proposals in the ED.
- 5 Also in September 2022, EFRAG FR TEG and EFRAG CFSS members discussed the targeted outreach activities planned by EFRAG and the IASB on a selection of tentative decisions that represented a change to the initial proposals included in the IASB's exposure draft on this project.

- 6 From October to November 2022 EFRAG organised, jointly with the IASB and in coordination with the national standard setters, a series of roundtables. The summary reports of the roundtables on 24 October, 2 November, 4 November and 15 November have been published on EFRAG Website.
- 7 Finally, the EFRAG Secretariat prepared a [summary report](#) with recommendations that reflects all the feedback received during the roundtables, working groups meetings and other ad-hoc meetings.

Summary report and recommendations

- 8 In December 2022, EFRAG published a [summary report](#) that informs about the topics addressed during the targeted outreach by the IASB and those in addition by EFRAG and the feedback received on it. The report, that was submitted to the IASB together with a letter, includes EFRAG's recommendations based on the feedback received.
- 9 In general, participants in the roundtable discussions welcomed the IASB's efforts to improve the structure and content of primary financial statements, particularly users of financial statements, as it would improve comparability and relevance. Participants also welcomed the roundtables organised by EFRAG and the IASB's efforts to address the comments received by the IASB on its ED, particularly on difficult topics such as disclosures by nature when presenting by function and the proposed disclosures on unusual income and expenses.
- 10 However, some preparers noted that the IASB's proposals would still lead to considerable implementation costs for them in specific areas, such as the proposed disclosures by nature when presenting by function. Participants in the roundtables also raised a number of questions and expressed concerns on the IASB's tentative decisions.
- 11 Some of these questions and concerns had already been raised in the IASB's consultation on the 2019 ED. Nonetheless, most of the concerns and questions were related to the implementation of the revised proposals. The key concerns expressed by participants were:
 - (a) **Operating category:** there were questions on the classification of specific items and concerns on having an operating category defined as a residual category, which would be wide and reflect ancillary activities and unusual items (similar feedback was received in the 2019 ED consultation). For conglomerates, determining the entity's main business activities at the reporting-entity level will be complex and costly;
 - (b) **Financing category:** the wording used by the IASB to define the financing category was not always well understood and there was a call for additional application guidance. Many financial institutions also expressed concerns on the IASB's revised proposal on the classification of income and expenses from lease liabilities, which could no longer be reclassified into the operating category under paragraph 51 of the ED;
 - (c) **Cash and cash equivalents:** both users and preparers highlighted that it would be more appropriate for corporates to present income and expenses from cash and cash equivalents in the financing category, particularly for those that use a net-debt concept. Financial institutions and conglomerates

were also concerned about not having the possibility of classifying income and expenses from cash and cash equivalents within operating profit under paragraph 51 of the ED;

- (d) **Hybrid contracts:** the IASB's tentative decisions were considered unclear and there was a call for the IASB to provide the underlying rationale and more application guidance on its tentative decisions;
 - (e) **Derivatives:** corporate companies expressed concerns that the default category for the classification of derivatives and hedging instruments was now the operating category;
 - (f) **Associates and joint ventures:** there were mixed views on the presentation of income and expenses from associates and joint ventures (similar feedback was received in the 2019 ED consultation) and many questions were raised on the use of additional subtotals related to associates and joint ventures (e.g., interaction of such subtotals with the IASB's proposals on specified subtotals and MPMs);
 - (g) **Associates and joint ventures for insurance companies:** the insurance industry highlighted that the issue of associates and joint ventures is important and requested presenting investments in associates and joint ventures that are linked to insurance contracts within the operating profit. Else, there would be a mismatch as the operating category would only include expenses related to insurance contract liabilities and no associated investment results from the assets held to service those liabilities;
 - (h) **Analysis of expenses:** users and preparers often expressed different views on the proposed disclosures. Users and a few preparers were more supportive of the IASB's approach included in the 2019 ED, while other preparers preferred the IASB's revised disclosures. However, targeted outreach participants (including users) acknowledged that the IASB's tentative decision was a compromise, even if it will costly for preparers;
 - (i) **Management performance measures:** there were questions on the extent to which additional subtotals would be considered as MPMs. Highly regulated entities, such as banks, raised questions on the effective applicability of the rebuttable presumption for all the significant measures communicated for regulatory purposes. Finally, there were mixed views on the simplified approach to calculating the tax effect; and
 - (j) **Unusual items:** although many preparers welcomed the IASB's tentative decision to withdraw its proposals on unusual income and expenses, the majority of users and regulators were disappointed with the IASB's decision. These considered that any high-level application guidance would be useful to mitigate diversity in practice.
- 12 Finally, several participants highlighted the importance of completing the project as soon as possible as it was considered an improvement over IAS 1 *Presentation of Financial Statements* and, overall, very useful. In this respect, these participants were willing to reach a compromise in order to facilitate a timely publication of a future standard.

- 13 Considering the feedback received and EFRAG's position in its letter to the IASB on the 2019 ED, EFRAG considered that it would be useful to:
- (a) **Operating category:** retain the existing approach but consider the comments provided by EFRAG in its comment letter on the IASB's 2019 ED and support it with an explanation of the reasoning behind the chosen approach and its resulting impact on the use of MPMs in the Basis for Conclusions;
 - (b) **Financing category:** improve the definition of the financing category by providing application guidance to better explain the wording used by the IASB in its definition and illustrate how its definition would apply to certain transactions;
 - (c) **Cash and cash equivalents:** classify income and expenses from cash and cash equivalents in the financing category as it would provide relevant information to users, particularly when corporates use a net-debt concept. In addition, for financial institutions and conglomerates, it would be useful to retain the possibility of classifying income and expenses from cash and cash equivalents in the operating category under paragraph 51 of the ED;
 - (d) **Hybrid contracts:** have additional clarifications and application guidance (e.g., illustrative examples and/or flowchart to help implementation) to help preparers understand the mechanics of the IASB's tentative decisions, including determining when hybrid instruments should be classified in the operating category;
 - (e) **Derivatives:** clarify the IASB's proposals related to situations that would involve grossing up gains and losses and consider alternative solutions, including revisiting the default presentation in the operating category, to mitigate the issue of corporates related to bringing the impact of derivatives into the operating category, which could bring significant volatility to this category;
 - (f) **Associates and joint ventures:** have more information and transparency on the nature of the investments in associates and joint ventures in the disclosures (e.g., investees that are also in the value chain of the group and as such closely linked to their operations) and have clarifications on the interaction of having additional line items and subtotals (in accordance with paragraph 66 of the ED) with the IASB's proposals on specified subtotals and MPMs, including when the reconciliation disclosure requirements would apply;
 - (g) **Associates and joint ventures for insurance companies:** present results from investments in associates and joint ventures that are linked to insurance contracts (e.g., that are backing up insurance liabilities) in the operating category. Otherwise, there would be a mismatch as the operating category would only include expenses related to insurance contract liabilities and no associated investment results from the assets held to service those liabilities;
 - (h) **Analysis of expenses:** retain the IASB's revised approach on requiring companies to disclose an analysis of their operating expenses by nature when presenting by function but would suggest adding impairments to the list of minimum items to be disclosed. In addition, EFRAG is not in favour of an approach for 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. Finally, the analysis of the costs and benefits of the proposed disclosures should be carefully explained in the IASB's effects analysis;

- (i) **Management performance measures:** have additional application guidance on the extent to which additional subtotals (e.g., subtotals of subtotals and subtotals merely reflecting reclassification of line items) would be permitted and whether they would be considered as MPMs or specified subtotals. EFRAG also expresses some concerns on establishing a rebuttable presumption on MPMs for highly regulated entities as this could increase complexity and may unintendedly enlarge the scope of MPMs. EFRAG is concerned that the IASB's 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 may significantly increase the costs for some preparers; and
 - (j) **Unusual items:** have a definition of unusual items (a workable definition that could be improved in the future with practice) or at least information on how an entity defines its unusual items (if the entity identifies such items in the financial statements). It would also be useful to provide clarity on the possibility of showing separately in the statement of profit or loss items that an entity views as non-recurring or unusual items (e.g., a subtotal within the IASB's required subtotals).
- 14 Finally, EFRAG highlighted that this project responded to a strong demand from users of financial statements to have improvements on how information is communicated in the financial statements.
- 15 In its January 2023 meeting the IASB discussed the feedback received from the targeted outreach including the one from EFRAG. Based on the feedback the IASB decided to add four topics to its workplan. The additional topics on the redeliberation plan are:
- (a) whether it should reconfirm its decision on classification of income and expense from associates and joint ventures accounted for using the equity method;
 - (b) whether it should develop application guidance for classifying income and expense from off-balance-sheet items;
 - (c) whether it should develop guidance for including interest expense on lease liabilities in operating profit if subleasing is a main business activity; and
 - (d) whether it should develop further application guidance for the proposed rebuttable presumption in the definition of management performance measures.
- 16 In addition, the IASB also redeliberated the proposals in its ED relating to:
- (a) the general requirements on disaggregation;
 - (b) other comprehensive income; and
 - (c) the statement of cash flows - interest received and classification for entities with specified main business activities.

- 17 Agenda paper 10-02 – Update on the IASB tentative decisions includes an overview to the developments.

EFRAG TEG-CFSS discussions

- 18 On 15 March 2023, EFRAG FR TEG and EFRAG CFSS members received an update on the IASB’s latest tentative decisions on the project. In addition, the members discussed the factors that the IASB should consider in determining the transition period and effective date of the forthcoming IFRS Accounting Standard. Finally, EFRAG FR TEG and EFRAG CFSS discussed the expected benefits and costs for stakeholders in their jurisdictions.
- 19 Members generally welcomed the IASB’s adjustments to its redeliberation plan to address the feedback received in the outreaches, including discussions on the presentation of income and expenses that arise from associates and joint ventures. Nonetheless, members highlighted the importance of having an open and transparent process on topics that will be addressed in the drafting process, particularly improvements to the financing category and management performance measures.
- 20 On the transition period and effective date, some members considered that a 24-month transition period may not be long, particularly when considering the IASB’s proposal for entities to present the new subtotals in the condensed financial statements in interim financial reports, (including comparatives), the impacts that it will have on digital reporting and the information used internally by management. In addition, the IASB’s forthcoming discussions on disclosures by nature when presenting by function were considered fundamental.
- 21 Finally, members generally agreed with the IASB’s cost-benefit analysis but highlighted the importance of updating the impact analysis at the end of the IASB’s redeliberations.

Questions for EFRAG FRB members

- 22 Do EFRAG FRB members have any comments on the IASB’s tentative decisions on its redeliberation plan (i.e. topics added and topics that will not be included in the redeliberation plan), considering EFRAG’s Summary Report and Recommendations?
- 23 For entities in your jurisdiction, **what new information will they need to gather** to apply the requirements in the new IFRS Accounting Standard?
- 24 Are there any entities in your jurisdiction that are **planning to apply early** the new IFRS Accounting Standard?
- 25 How much time between finalisation and effective date is needed, assuming no relief from providing comparative information?
- 26 Do you have any comments on the **expected costs and benefits to preparers and users** in your jurisdiction?

Next steps

- 27 The EFRAG Secretariat will continue to monitor the IASB’s discussions.

Agenda Papers

- 28 In addition to this cover note, agenda papers for this session are:
- (a) Agenda paper 10-02 – Update on the IASB tentative decisions;
 - (b) Agenda paper 10-03 – Expected costs and benefits and effective date.