Rådet för finansiell rapportering

The Swedish Financial Reporting Board

RFR-rs 2020:04

International Accounting Standards Board
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Dear Board members,

Re: EP/2019/7 General Presentation and Disclosure

The Swedish Financial Reporting Board is responding to your invitation to comment on the Exposure Draft General Presentation and Disclosure. In summary we have the following views:

- There should be a subtotal for operating profit or loss.
- There should not be any investing category.
- Integral associates and joint ventures should be reported on an own line within operating profit or loss – non-integral associates and joint ventures should be reported on an own line outside operating profit or loss.
- Information about operating expenses should be restricted to whichever method provides the most useful information.
- There should not be a strict definition of unusual income and expenses.
- Requirements for MPMs should be limited to IFRS-statements.

There should be a subtotal for operating profit or loss

We agree that all entities should present in the statement of profit or loss a subtotal for operating profit or loss. When the objective is to complement a "bottom line" measurement of income ("profit or loss" or "net income" in a statement of profit or loss) with partial measures of income (sub-totals), "Operating profit or loss" is a good choice. The distinction between operating and financing activities is well established both in external performance assessments (including corporate valuation) and in firms' management control systems.

The experience from previous projects trying to standardise financial statements points to the difficulty in producing a robust definition based on the nature of activities in the statement of profit or loss (operating, core etc).

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From this perspective it makes sense to define the operating category as a residual. However, for this to promote useful information it is still necessary that the definitions of the other categories are appropriate.
The definitions of investing and financing are not very meaningful for firms in several industries, e.g. banks, insurance companies, property companies etc. Consequently, we agree with the classification of the operating category based on the entity's main business activities. It would not be possible to have a single standard for all industries without this provision.
However, we are concerned that you then are back to the problem of finding a robust definition based on the nature of activities – in this case the definition of a main activity. A further complication is the view that there may be more than one main activity (B26). A strict interpretation of this statement does not rule out that there might be several main activities. Altogether, this requires a robust definition of what is a main activity, that we think must be further developed.
We agree with the proposal that entities that provide financing to customers and have more than one main business activity should be able to either report in operating only income and expenses from financing activities relating to its provision to financing to customers or report in operating all income and expenses from financing activities.

There should not be any investing category

Conceptually the investing category has merit. However, for several reasons we are not convinced that a separate investment category will improve comparability across entities in practice. Restricting the specific requirements to the distinction between operating and financing there will still be challenges related to the classification. Introducing an investing category, the classification challenges will go from one (operating vs. financing) to three (adding on operating vs investing and investing vs financing). It is sometimes difficult to draw a line between investing and financing. In our opinion it does not really add value to show a gross return on assets since the actual return is a combination of assets, funding and one or several derivative contracts. The way the ED has been constructed, what will be shown in investing contra financing will be more or less random for those entities with advanced investing activities.
Furthermore, it is not clear to us to what extent the proposal that income and expenses from investments made in the course of its main business activities should be classified in the operating category will influence the relative size of the investing category. We expect that the numbers presented in the investing category will be rather small.
Finally, it is confusing when the same terms are used with different meanings. Both the statement of financial performance and the statement of cash flows will have three different categories with similar labelling but partly different definitions. We believe that the IASB should avoid using the same terms with different meanings. E.g. in the statement of cash flows the investing category also includes operating investments. As long as the two statements are not aligned, we think that it would be useful to use a different labelling to avoid confusion. Furthermore, classification of some items relating to investing and financing activities as operating in the statement of profit or loss, since they are related to a main activity, would add to the confusion. The Board should keep the term investing in its current meaning of deployment of resources in general in the statement of cash flows.

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Integral and non-integral associates and joint ventures should be treated differently

The distinction between integral and non-integral associates and joint ventures is important. Integral associates and joint ventures should be reported on an own line within operating profit or loss – non-integral associates and joint ventures should be reported on an own line outside operating profit or loss. An entity should assess whether an associate or joint venture is integral or not, given some guidelines by the standard-setter.

Information about operating expenses should be restricted to the method that provides most useful information

We support the IASB's proposal to continue to require entities to present an analysis of expenses using either by-function or by-nature, based on whichever method provides the most useful information to users of financial statements.
Furthermore, we suggest that the IASB clarifies that paragraph B47 of the ED allows, or even requires, a mixed basis of presentation when an entity presents line items under paragraphs 65 and B15 of the ED.
However, we find it inconsistent to first require an entity to apply the method that provides the most useful information and then require it to also provide information about the alternative method. There are substantial costs associated with this double reporting and while in our experience some users find it necessary to have information about expenses by nature for all entities, others do not attach them this significance. Consequently, from a cost-benefit perspective we do not think that uncertain benefits would outweigh well-established costs.

There should not be a strict definition of unusual income and expenses

We welcome the IASB's attempt to improve the information about unusual items. Such disclosures provide useful information to users of financial statements.
We agree that unusual items should not be reported on a separate line, but included in other items, and the appropriate information disclosed in a single note. Due to the difficulty in finding a definition of unusual items the starting point should be to report them in the same way as all other items.
However, we believe that the proposed definition does not to capture what is intended. The definition seems to focus on items close to those covered by IFRS 5, instead of focussing on items that are unusual for the present business. The historical record is a robust starting point for an assessment of what is usual and unusual respectively.
The difficulty to find an unambiguous definition of items affecting comparability (unusual items, extraordinary items, non-recurring items etc.) is well established from many previous standard-setting projects. This is an indication that an interaction between preparers and users might be the best way forward towards a proper balance between promoting comparability and providing entity-specific information.
Therefore, we propose that the IASB should avoid a strict definition and instead focus on describing the purpose of the disclosure requirements and promote consistency in the disclosures made by an individual entity. A strict definition might force entities to search for unusual items according to a definition that they might not consider relevant.

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Requirements of management performance measures should be limited to IFRS-statements

We support the IASBs attempt to give guidance regarding MPMs. However, we believe that the IASB should limit its standard setting to MPMs given within the financial statements covered by the IASB standard. There are three basic reasons for that : (1) Risk of being in conflict with local law (2) Too wide-reaching requirements outside of the IFRS financial statement may restrict the information given to users of information produced by the entities due to the burden of showing reconciliations of that information within the financial statements (3) Create an impossible situation for the auditors of the financial statements when the IASB refers to any information published outside of the financial statements.

We agree with the decision not to include EBITDA as a mandatory sub-total. There are many different variations of this measure in practice. It would be better if firms were allowed to define their own management performance in this respect.

Statement of cash flows

We agree with having operating profit as the starting point for the cash flow statement. This is consistent with the prominent role of that sub-total in the statement of profit or loss. As mentioned in our comment on the investing category above, the use of main activity to define operating items in the statement of profit or loss is not synchronised with the classification in the cash flow statement. Regarding the classification of interest paid/received and dividends paid/received the same criticism applies for dividends received as mentioned above in our comments on the investing category.

A description of the roles of primary financial statements and the notes

We welcome the IASB's proposal to describe the respective roles of primary financial statements and the notes as well as the proposal for principles and general requirements on the aggregation and disaggregation, as a complement to the additional subtotals in the statement of profit or loss.

Practical guidelines have the potential to guide preparers and thus improve clarity and consistency. However, the principles to aggregate and disaggregate are quite abstract. It is proposed that items that share a common characteristic should be aggregated, while items that do not have that should be treated separately. We think that the contribution to useful information from these principles is limited.

We also question general requirements such as the one in B4, that to meet the objective of financial statements, an entity supplements the primary financial statements with information about the nature and extent of unrecognised assets, liabilities, equity, income and expenses.

Such general requirements are hard to enforce and it is difficult for a preparer to be reasonably sure that all requirements have been satisfied, and that the entity is not exposed to future challenges of compliance.

Other comments

The issues in this exposure draft are fundamental relating to assessments of the performance of an entity and its management. The basic question is to what extent a standard-setter should prescribe specific requirements for this and to what extent the management of an entity, in interaction with its peers and users of the information,

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should be able to present their statement of profit or loss in a way that in their view best represents the outcome of the business.
The aim of the specific requirements is to promote comparability across firms. In BC7 it is remarked that the lack of specific requirements has led to diversity in the presentation and calculation of subtotals, even among entities in the same industry. In our opinion, a variation is to be expected across industries, but also within an industry a certain variation could be expected, since firms have different business models. Furthermore, particularly listed firms often operate in more than one industry. There is a risk that too specific requirements only will produce statements in the same format, without increasing the comparability across firms in terms of what is the ultimate purpose of the comparison, to compare firms' capacity to generate earnings. On the contrary, a loss of entity-specific information might reduce the usefulness for assessing the capacity to generate earnings with the firm's business model.
From our national experience we do not really see any big problems from a system where many issues e.g. related to unusual items and MPM are handled in an interaction between users and preparers within an industry, while we see many of the specific requirements proposed as quite problematic. A more restricted approach to specific requirements might have the additional advantage that it could be handled through a revised IAS 1 rather than producing a completely new standard.
We appreciate that IASB has conducted more than 50 meetings with users, which constitute the basis for the requirements to streamline the statement of profit or loss. Our experience is that there is substantial diversity across user groups (credit and equity analysts, sell and buy side analysts) and also in working methods within a group. We realize that the use of big databases requires uniformity. However, that comes at a cost. The information will be less entity specific. It is the task of investors and analysts who chose to use big databases to organize the data from the statements of profit or loss for their own purposes.

In the assessment of the expected costs of implementation and application (BC 240-245) it is implied that the costs to make changes in presentation are lower compared to changes in recognition and measurement. We don't agree. An entity that reports according to IFRS must, subject to the materiality constraint, follow all the standards' requirements. Since they are linked to the business model and control of a firm the indirect costs of changing are high.

If you have any questions concerning our comments, please address our Executive member Carina Edlund by e-mail to: Carina.Edlund@radetforfinansiellrapportering.se.

Stockholm, 28 September 2020

Yours sincerely

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Chairman

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