

Proposals for better communication in financial statements

Intro to the public consultation on Primary Financial Statements

8th September 2020
CFA Society India

The views expressed in this presentation are those of the presenter, not necessarily those of the International Accounting Standards Board or the IFRS Foundation.

Welcome!

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Housekeeping

The views expressed are those of the presenters, not necessarily those of the International Accounting Standard Board (Board) or the IFRS Foundation.

The Exposure Draft is available for download on the Primary Financial Statements project webpage at www.ifrs.org/projects/work-plan/primary-financial-statements.

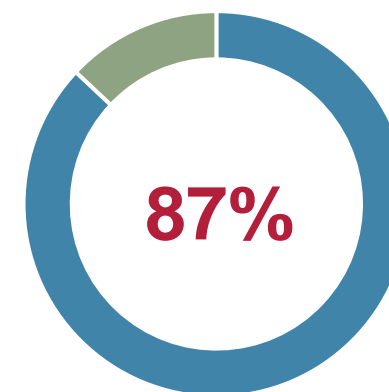
Adoption of IFRS® Standards

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 = IFRS Standards required

144 of 166 jurisdictions
require IFRS Standards
for all or most publicly
accountable companies



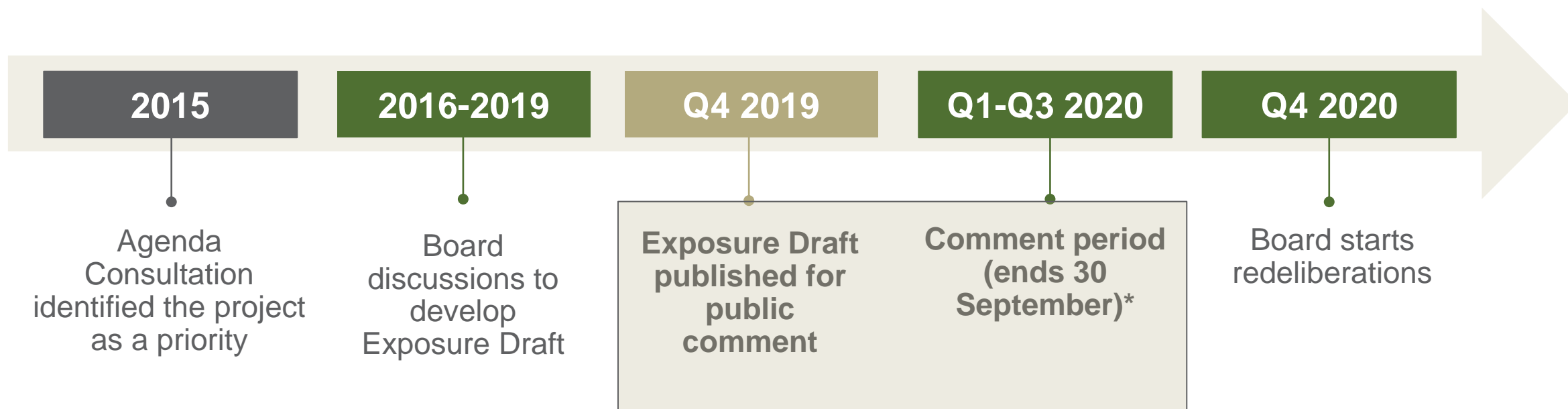
Primary Financial Statements project

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objective

To improve how information is communicated in the financial statements, with a focus on information included in the statement of profit or loss



*Extended from 30 June due to covid-19 pandemic.

Project responds to investor needs

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What investors say

Board's main proposals



Subtotals in the statement of profit or loss need to be comparable between different companies.

1

Require companies to present additional **defined subtotals** in the statement of profit or loss.



Companies should provide more granular information and information grouped in a way that provides better inputs for our analysis.

2

Strengthen requirements for **disaggregating information**.



Performance measures defined by management can provide useful information, but should be used in a more transparent and disciplined way.

3

Require companies to disclose information about **management performance measures** in the notes.

*The Exposure Draft also contains other proposals, including targeted improvements to the statement of cash flows.

CFA Institute reports on Non-GAAP financial measures

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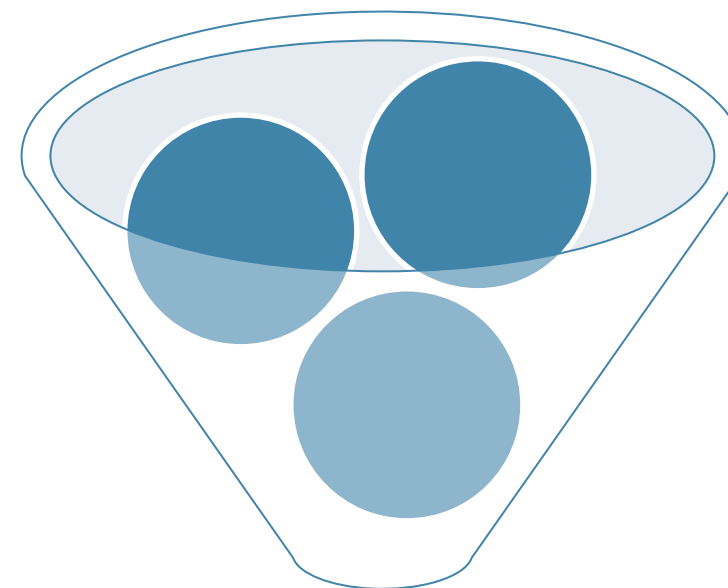
**INVESTOR USES,
EXPECTATIONS,
AND CONCERNS
ON NON-GAAP
FINANCIAL
MEASURES**



**BRIDGING THE GAP:
ENSURING EFFECTIVE
NON-GAAP AND
PERFORMANCE
REPORTING**



CFA Institute suggestions to improve
quality of reporting on performance
measures



Some of which, relate
to the Project
proposals

1 Subtotals in the statement of profit or loss

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Revenue	347,000
Other income	3,800
Changes in inventories of finished goods and work in progress	3,000
Raw materials used	(146,000)
Employee benefits	(107,000)
Depreciation	(37,000)
Amortisation	(12,500)
Professional fees and other expenses	(10,030)
Operating profit	41,270
Share of profit or loss of integral associates and joint ventures	(600)
Operating profit and income and expenses from integral associates and joint ventures	40,670
Share of profit or loss of non-integral associates and joint ventures	3,380
Dividend income	3,550
Profit before financing and income tax	47,600
Expenses from financing activities	(3,800)
Unwinding of discount on pension liabilities and provisions	(3,000)
Profit before tax	40,800
Income tax	(7,200)
Profit for the year	33,600

Operating

Integral associates
and joint ventures

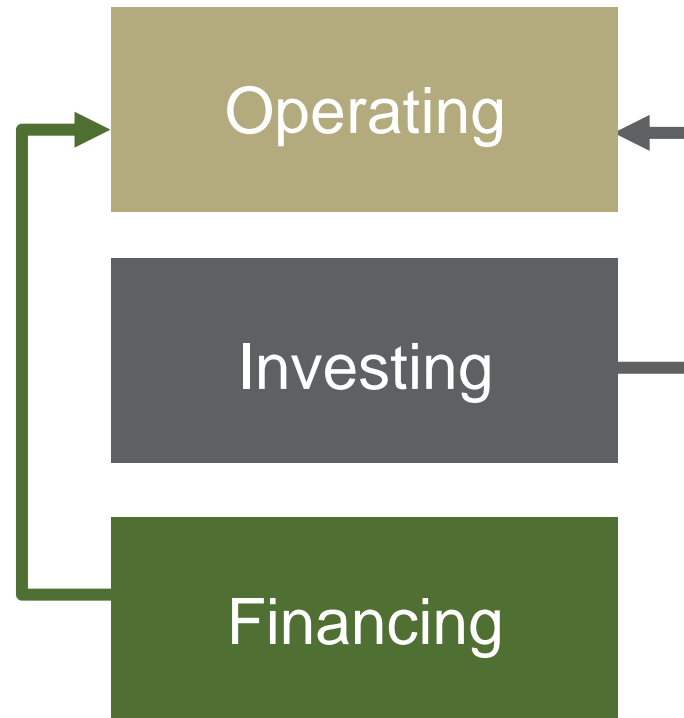
Investing

Financing

1 Application to financial entities

Income and expenses from financing activities and cash and cash equivalents included in operating profit

- Only applicable to entities providing financing to customers as a main business activity
- Examples may include banks and entities that provide financing to customers to purchase the entity's products.
- Accounting policy choice whether to move *all* such income and expenses or *only* those related to providing financing to customers



Income and expenses from investments made in the course of main business activities included in operating profit

- Examples may include insurers, investment entities and investment property companies.
- Does not apply to income and expenses from associates and joint ventures accounted for using the equity method.

1 Example—investment and retail bank

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Interest revenue calculated using the effective interest method	356,000
Interest expense	(281,000)
Net interest income	75,000
Fee and commission income	76,800
Fee and commission expenses	(45,300)
Net fee and commission income	31,500
Net trading income	9,100
Net investment income	11,600
Credit impairment losses	(17,300)
Employee benefits	(55,100)
[other line items not shown in this illustration]	(11,800)
Operating profit	43,000
Share of profit or loss of integral associates and joint ventures	(2,400)
Operating profit and income and expenses from integral associates and joint ventures	40,600
Share of profit or loss of non-integral associates and joint ventures	4,200
Profit before tax	44,800
Income tax expense	(11,200)
Profit for the year	33,600

all expenses from financing activities are classified in the operating category rather than the financing category

income (expenses) from investments made in the course of main business activities are classified in the operating category, rather than the investing category

no 'profit before financing and income tax' subtotal

2 Disaggregation

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Roles of the primary financial statements and the notes

- Roles of the primary financial statements and the notes clearly described
- Use the description to determine whether information should be included in the primary financial statements or in the notes

Principles for aggregation and disaggregation

- Principles for aggregation and disaggregation of information
- Three-step guidance to apply the principles
- Requirements for grouping dissimilar immaterial items (avoiding 'other')

Required line items

- New required line items, including goodwill and separate line items for integral and non-integral associates and joint ventures

Analysis of operating expenses

- Use method for analysis of operating expenses (by nature or by function) that provides the **most useful information** (not a free choice)
- Disclose analysis of **total** operating expenses by **nature** in the notes if analysis by function is presented in the statement of profit or loss

2 Example – operating expenses by nature of inputs

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Changes in inventories of finished goods and work in progress	3,000
Raw material used	(146,000)
Employee benefits	(107,000)
Depreciation	(27,000)
Amortisation	(5,500)
Impairment of property, plant and equipment	(5,000)
Impairment losses on trade receivables	(4,500)
Property taxes	(5,200)
Litigation expenses	(1,900)
Gains (losses) on derivatives	(5,500)
Other miscellaneous expenses	(4,930)
Operating expenses total	(309,530)

2 Unusual income and expenses

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Definition



Income and expenses with **limited predictive value**.

Income and expenses have limited predictive value when it is reasonable to expect that income or expenses that are similar in type and amount will not arise for several future annual reporting periods.

Income and expenses from the recurring remeasurement of items measured at a current value would not normally be classified as unusual.

Disclosures

Amount &
narrative
description

Amount disaggregated by:

- line items presented in statement of profit or loss; and
- line items disclosed in analysis of operating expenses by nature, if the entity analyses expenses by function in the statement of profit or loss

③ Management performance measures (MPMs)

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Disclosure in the notes of subtotals of income and expenses that:

Are used in public communications
outside financial statements

Complement totals or subtotals specified by IFRS Standards

Communicate **management's view** of an aspect of an entity's financial performance

Accompanied by disclosures in a **single note** to **enhance transparency**

3 Example of MPM reconciliation in the notes

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Adjusted operating profit (MPM)	52,870	Tax	NCI
Restructuring in Country X	(5,400)	900	(1,020)
Revenue adjustment	(6,200)	1,550	-
Operating profit (IFRS-specified)	41,270		



Most directly comparable subtotal/total specified by IFRS Standards—can be:

- any of the three subtotals proposed in this project;
- profit before tax, profit from continuing operations or measures similar to gross profit; or
- operating profit before depreciation and amortisation



Simplified approach to calculating the tax effect

3 Not all performance measures are MPMs

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Performance measures

Non-financial performance measures

For example:

- Number of subscribers
- Customer satisfaction score
- Store surface

Financial performance measures

(Sub)totals of income and expenses

IFRS-specified

For example:

- Profit or loss
- Operating profit
- Operating profit before depreciation and amortisation

MPMs

For example:

- Adjusted profit or loss
- Adjusted operating profit
- Adjusted EBITDA

Other measures that are not subtotals of income/expenses

For example:

- Free cash flow
- Return on equity
- Net debt
- Same-store sales

3 Improvements compared to current situation

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Location	Management performance measures and related disclosures would be in a single location* in the notes to the financial statements, rather than scattered across public communications or on the face.
Audit	Including MPMs in financial statements is expected to bring such measures into the scope of audit.
Content of disclosures	The proposed disclosure requirements are similar to existing regulatory guidance. However, the disclosure of tax & NCI effects is likely to be new.
Consistency across countries	Management performance measures would be subject to the same requirements regardless of the entity's jurisdiction.

*Measures that do not meet the definition of an MPM (see previous slide) would not be affected by the proposals.

The Board is proposing not to define EBITDA

- The Board could not identify a single underpinning concept.
- Not used in some industries.
- Calculation is diverse in practice.

The Board is proposing to define ‘operating profit before depreciation and amortisation’

- Would be allowed—but not required—to be reported.
- If used, no MPM disclosures would be required for this measure.
- The Board has not labelled it ‘EBITDA’ because its content does not match what the acronym ‘EBITDA’ stands for.

Proposals for statement of cash flows – illustration

(indirect method)

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Operating profit	X
Adjustments for:	
Depreciation	X
[...]	
Income taxes paid	(X)
Net cash from operating activities	X
Acquisition of integral joint venture X	(X)
Acquisition of non-integral associate Y	(X)
Dividends received from integral associate A	X
Dividends received from non-integral associate B	X
Purchase of property, plant and equipment	(X)
[...]	
Net cash used in investing activities	(X)
Dividends paid	(X)
[...]	
Net cash used in financing activities	(X)
Net increase in cash and cash equivalents	X


Consistent starting point
for indirect method for
operating cash flows

Separate presentation of
cash flows from integral
and non-integral
associates and joint
ventures within investing
cash flows

Elimination of
classification options for
interest and dividends

Structure of the Exposure Draft

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New IFRS Standard 	Proposed new presentation and disclosure requirements	+	Related requirements brought forward from IAS 1 with limited wording changes
Amendments to other Standards	<ul style="list-style-type: none">• IAS 7—statement of cash flows• IFRS 12—associates and JVs• IAS 33—earnings per share• IAS 34—interim reporting		Other requirements of IAS 1 —moved to IAS 8 and IFRS 7

➔ **Withdraw IAS 1** 

Get involved in this consultation

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Contact our investor engagement team to schedule an outreach meeting:

- E-mail: investors@ifrs.org

More resources for CFA India members here

- Website: www.ifrs.org/investor-centre
- Twitter: [@IFRSinvestors](https://twitter.com/IFRSinvestors)



Check out the [Snapshot](#) for more information about the proposals



Access the Consultation documents:

- [Exposure Draft](#)
- [Basis for Conclusions](#)
- [Illustrative Examples](#) and a comparison of proposals with requirements of IAS 1

individual
views
expressions
feedback
questions
comments
expressions of individual views
questions or comments
feedback
questions
and viewpoints
and comments