



EFRAG
35 Square de Meeûs
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Att.: Ms. Françoise Flores

Dear Françoise,

EFRAG'S COMMENTS ON THE EXPOSURE DRAFT CONCEPTUAL FRAMEWORK FOR FINANCIAL REPORTING ISSUED BY THE IASB

We are pleased by the opportunity to express our views on the Exposure Draft in the public consultation for your comment letter to the IASB on their proposed new framework for financial reporting.

Maersk's views on the new Conceptual Framework differ to some extent from the views of EFRAG and therefore Maersk chose to submit its own comment letter to the IASB Discussion Paper in January 2014. We have noticed that only few of Maersk's views are reflected in the Exposure Draft and therefore we have decided not to repeat ourselves in a second comment letter to the IASB. Instead, this time we will seek to explain to EFRAG our concerns for the development of the new Conceptual Framework, which is found critical in relation to the ongoing and future development of IFRSs.

We are not only concerned about the objective of the Conceptual Framework as considered by the IASB, to which you will find more comments below. We are also concerned that alternative paths towards more useful information to users in financial reports are not sufficiently analysed and discussed. We also find that the increased use of control is creeping in without being properly substantiated. Maersk has brought this to IASB's attention in our comment letters to recent projects, and lately we have realised how this change impacts the recognition of revenue from some of our services. Although it is not a critical change to Maersk, we have not understood why revenue is not already represented faithfully in accordance with the principles in IAS 18.

The Conceptual Framework Discussion Paper was in many respects an attempt to analyse and discuss alternative paths, even if it was somewhat tied in to the traditional concepts. Nevertheless, it was welcomed that we were given the opportunity to suggest new ways that may not previously been explored.

We are fully aware that the views and suggestions of Maersk would turn financial reporting into another direction than where the IASB is currently heading. In our view the IASB is moving away from the concepts and accounting language that are generally understood by the management and the business units in Maersk. It is an ongoing challenge to explain the thoughts of IASB and the background for most of the changes.

Although at this point in time we have resigned from changing the views of the IASB, we do hope this letter can inspire EFRAG to new ideas in case an EFRS should ever emerge.

General comments

The Exposure Draft (ED) was unfortunately disappointing reading, not only because few of Maersk's suggestions were taken into consideration, but also because the ED essentially is a defence for the decisions made in recent IFRS projects. In addition, the ED seems to offer a range of options between which the IASB can choose in its development of Standards. We agree with EFRAG that the ED will not prevent endless discussions on fundamental questions in this process. We prefer a re-opening of discussions on the Conceptual Framework in a particular matter, if needed, rather than individual Standards deviating from the framework.

We are not against flexibility in the choice of accounting policies, on the contrary, but we think the flexibility should rather be offered to the preparers of financial reports. When the objectives and qualitative characteristics of financial information is clearly described, and the basic concepts for recognising, measuring and presenting determined, then the Standards should only elaborate on definitions and principles for the individual components in the financial statements. Many IFRSs already today require preparers to make significant judgements in the application of the accounting principles. The only hindrance for preparers is that the principles and the application guidance are becoming more and more complicated. Hence, we believe most preparers would prefer to make the judgements on the basis of more simplified and conceptual principles.

One of the things we find is inappropriate in a Conceptual Framework is the extensive slackness in the language. Terms like 'may', 'in some cases', 'normally' are in our view not suitable for a framework, unless it is explained more clearly in which cases something shall apply and when deviations to the normal are defensible. We do not find it sufficient either to state the advantages and disadvantages of different measurement methods. The Conceptual Framework should rather determine what is sought achieved by the use of historic cost and fair values. If what is sought differs depending on the business model, then let this be the driver for the choice of measurement method.

Stewardship

In paragraph 11 in your comment letter you state: "To meet the objective of providing information for the assessment of stewardship, financial statements should report on past transactions and events and the information should focus on having confirmatory value".

We fully agree to this statement and think that elevating the significance of confirmatory value to users should lead to a preclusion of current cost as an appropriate measurement basis, for example.

In defining the primary users of financial information, we are concerned about widening the group of users, for which financial reports shall primarily be prepared. This is because we foresee an increase in the scope of IFRS regulation. Without committing ourselves in this letter to an opinion on integrated reporting, we favour the idea that IFRSs are focused on the needs of existing and potential investors, lenders and other creditors for financial information to assist decisions on whether to provide funds to an entity. This includes information about how efficiently and effectively the entity's management has discharged its responsibilities to use the entity's resources. Undoubtedly, those providing funds to an entity have other information needs than financial information; however, we cannot think of a reason why these should be regulated by IFRS. Other users in need of financial information can benefit from the IFRS regulation without changing the group of users at which IFRSs are targeted.

Relevance and faithful representation

In general, we believe the term faithful representation is understandable and do not have a particular preference for reverting to the term 'reliability'.

We support your comments regarding prudence and measurement uncertainty. There is only one aspect we think is not covered, and that is if prudence should also be exercised in the Conceptual Framework. As you point out in paragraph 36, faithful representation cannot be limited to strict compliance with a computation process and disclosures. We do not think the ED is sufficiently prudent in its definition of fair value in chapter 6, when not putting more weight on the fact that fair value often is not an accurate figure. According to the ED "fair value is the price that **would** be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date". It would be more prudent to state that fair value is the price that **may** be received or paid in a transaction at the measurement date. Using the term "would" instead of "may" mirrors the idea that an estimate can be neutral all together. In our view, a logical consequence of re-introducing prudence in chapter 2 would be to amend the definition of fair value in chapter 6.

The role of financial statements

Although the IASB does not ask about views on this section of chapter 3, we urge EFRAG to consider commenting on the fact that the cash flow statement does not play a role in the ED. We believe that the cash flow statement is as equally important to users as the income statement. In fact, we do not believe that the financial position plays an equivalent role in the user's assessment of the prospects for future net cash inflows, acknowledging that some items in the financial position, in combination with unrecognised commitments, do play a role.



As we understand it, financial performance in the ED refers to the income statement. In our view, this is too narrow. It is more likely that financial performance by users is assessed both in terms of profits or losses on an accrual basis and in terms of cash flow generation. When the objective of financial reporting is to provide useful information for users to project future cash flows, it should be easy to conclude that the cash flow statement plays a confirmatory role, and possibly also a predictive role. In the end, an entity survives or dies on its ability to generate net cash inflows.

Therefore, we suggest another term than financial performance is used when referring to the income statement only.

For this section we also have a small comment to paragraph 3.6 in the ED. It states that not all assets and liabilities are necessarily recognised. We suggest adding that not all income is necessarily recognised, when unrealised gains of recognised assets or liabilities are not recognised due to the chosen measurement basis or prudence.

The reporting entity

We agree, there is no urgent need to justify the choice of control as the basis for consolidation from a conceptual perspective.

Definition of elements

To some extent we agree with the definitions of elements in chapter 4. What we disagree with is the link between the definition of elements and the financial statements. By linking the definitions of elements to the financial statements, the ED without any justification determines that control is a recognition criterion.

In addition, we see no reason to separate executory contracts that are equally unperformed from the definitions of elements. Right to receive goods or services and obligations to perform work are the same regardless of whether cash has been transferred and those rights and obligations cannot be excluded from the resources and claims, if the financial information shall be complete. It is correct, that rights and obligations in equally unperformed contracts are interdependent as it is stated in paragraph 4.41 in the ED, but we do not agree that they cannot be separated and therefore constitute a single right or obligation. Parties in executory contracts have agreed to exchange economic resources, but there is a difference between cash and a commodity, for example. They have different liquidity and the risk inherent in cash is different than risk inherent in a commodity. What to recognise in the financial position and how is another question.

We do not oppose defining some of the elements in relation to the financial statements. Income and expenses, for example, could be defined as the increases/decreases in **recognised** assets/liabilities that result in increase/decrease in equity other than those relating to distributions to holders of equity claims.



As for equity, technically it represents the residual interest in the **recognised** assets of the entity after deducting all its **recognised** liabilities. However, is equity not the most important term to define? A common understanding of what earnings are and when these should be reflected in the financial statements, in our opinion, would provide the best guidance in what to recognise, when, how and at which value. The business model should be taken into consideration in this respect, but other factors may also play a role.

Our proposal to define earnings is not an attempt to argue for a pure matching approach when recognising income and expenses on an accrual basis. We agree that no asset or liability should be recognised that does not meet the definition of an asset or liability. The definition of earnings is relevant to determine, for example, the extent to which unrealised gains should be recognised or when an entity should commence recognising profits when executing on a sales contract. We do not find it sufficiently justified why an equity investment classified as available-for-sale (IAS 39) in all cases should be measured at fair value and not at cost. Similarly, we do not understand why recognising revenue on transfer of control rather than on the basis of work performed is more relevant or more faithfully represented in terms of reporting earnings.

There are a few other points we would like to make to the contents of chapter 4:

- If an economic resource is a right that has the potential to produce economic benefits, how does goodwill fit into this definition?
- In the equity section (paragraphs 4.43-47) it is unclear to us whether this is a description of equity in unconsolidated financial statements or consolidated financial statements:
 - Is information about restrictions on particular components of equity (legally, regulatory or other) not only relevant in unconsolidated financial statements?
 - What is useful information from dividing equity into more than one class of equity in unconsolidated financial statements vs. consolidated financial statements?
 - It may also be worth mentioning in this connection that equity in consolidated financial statements (and equity in unconsolidated financial statements, when the parent applies the equity method for measuring investments in subsidiaries, joint ventures and associates) includes the share of equity in joint ventures and associates, where the parent does not control the distribution of dividends.

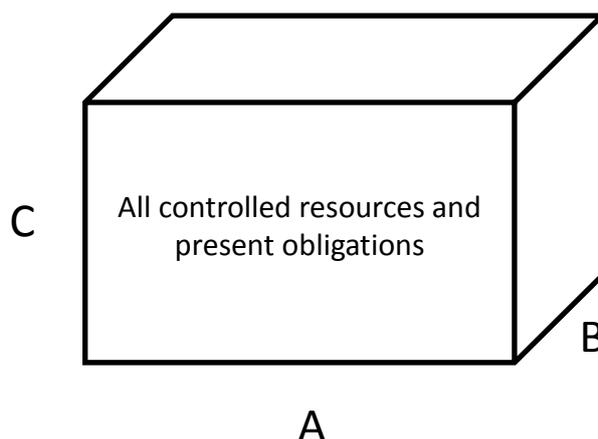
Recognition

In the questions on recognition Maersk has its greatest concerns for the development, where control has become the prevailing concept in almost all areas since the issue of IFRS 10 'Consolidation'. Generally, we are not objecting to the use of control for consolidation purposes, and the way it is explained in IFRS 10 is understandable and practically applicable. However, the benefits of transferring the concept to what shall be recognised in the financial position are questionable. From what we read in EFRAG's comment letter, and experience from the

discussions in other projects, this development is raising many critical questions, where from our perspective one seems to be absent: Have the right concept been chosen? We think not.

To begin with, the first section in chapter 5 in the ED on the recognition process seems to be general knowledge and we cannot see how it contributes to the following discussion on recognition and derecognition criteria.

It would be more useful to take as a starting point a three dimensional view on an entity's controlled resources and present obligations:



The A dimension is the resources and present obligations recognised in the financial position. Essentially, this position is a representation of prepaid costs (intangibles, tangibles, prepayments for goods and services), items held for sale or investment (inventories, equities etc.), loans and receivables, debt and payables, prepayments from customers, reservations for uncertain obligations and cash. The net position represents the undistributed earnings and contributions from owners. In our view, this dimension should only include assets owned, or virtually owned, by the entity.

The B dimension is the resources and present obligations from contracts that are unperformed (or partially unperformed by both parties to the contract, i.e. the so called executory contracts. These include contracts for the sale and purchase of goods and services, capital commitments, operating lease commitments, etc. The net position does not represent earnings, but committed future net cash flows (many of which are already disclosed as required in individual IFRSs). Future interest payments could also be included in this dimension. Such information could provide useful information if presented in a collective statement in the notes.

The C dimension is other controlled resources and present obligations, not include in A or B, which has a potential of being realised under certain circumstances. These include the value of brands, inventions or designs, research or exploration findings and un-extracted natural

resources, as well as unrealised gains (losses) of recognised assets (e.g. increase in fair value of property carried at cost) or liabilities (e.g. increase in fair value of debt carried at amortised cost). Risks from contingent obligations not recognised in the financial position due to an assessment of likelihood, also belong to this dimension. Most of the items in the C dimension are difficult to measure and information about them would in many cases be provided in a narrative form if found relevant to disclose, since the values could be debated indefinitely.

Presenting resources and present obligations in dimensions like this will allow users to achieve a more comprehensive picture of the reporting entity. In addition, the dimensions of the 'box' will be different for entities with different business models, even if the entities are comparable in terms of the amount of resources available to them. It will be possible for users to compare and understand the differences in the chosen business models.

Furthermore, another advantage of the dimensional model is that it does not separate commitments from operating lease and services. In many contracts these are difficult to separate and the reasons for disclosing one commitment to the other are not sufficiently justified.

Other comments to chapter 5:

- **Measurement uncertainty:** we are uneasy with a principle of not recognising a present obligation that is subject to a high degree of measurement uncertainty. If the existence of a present obligation is certain and an outflow of significant economic resources is probable, we find an amount in any case shall be reserved in the financial position. Surely, it must be in the interest of lenders and creditors that retained earnings in equity are not available for distribution, when the entity is exposed to significant cash outflows from an uncertain matter.
- **Low probability of cash outflows:** we do not favour the principle of recognising items of low probability and doubt that an estimate reflecting the low probability provides useful information. We believe the most useful information, and the less costly to produce, is to recognise only outflows that are probable and estimate those using the 'most likely amount'.

Derecognition

We find it noteworthy that the criteria for derecognition is said to normally occur on the loss of control of an asset, when control is not at all mentioned as a criteria for recognition. Using the term 'normally' does not help the inconsistency in the text.

Although it is somewhat difficult to comprehend the purpose of the proposed principles for derecognition, we fear that they may lead the IASB to introducing a lessor model in the future similar to the one proposed for type A leases in the exposure draft from 2013. We found this model was highly inappropriate for entities like Maersk that holds its assets primarily to generate revenue from sale of services.

Measurement

In general, we find that fair value should only be used as measurement basis for assets that are readily realisable. In many cases we do not find fair value an appropriate measure for non-current assets that may not be easily realised.

In addition, we find it pointless to include in a measure of earnings unrealised gains or losses for non-current assets, which the management has no current intentions to realise, depending on the business model obviously.

We see that EFRAG has some of the same thoughts; however we do not support the idea of using different measurement bases for the financial position and profit and loss statement with the difference in the OCI. We are afraid such a construction will be difficult to understand and that it entails the risk of making the OCI even more incomprehensible to management and many users. When it comes to the lists of advantages and disadvantages of historic cost versus current value, we think some obvious facts are left out. Examples include:

<i>Measurement basis</i>	<i>Advantages</i>	<i>Disadvantages</i>
Historic cost	The deferral of gains until realised is a prudent approach, when an asset is not readily realisable, or the management has no current intentions to dispose an asset	
	If the view is that fair value increases the comparability between entities, the opposite can be said for historic cost: it reveals the differences	
Current value		Recognising unrealised gains can be considered less prudent
		Results in fluctuations in earnings not driven by the management's actions in the period
		May not be relevant if the management has no current intentions to dispose an asset
		It may be highly uncertain that an estimated fair value represents the price an entity would actually receive in a transaction, as eventually the price is the result of negotiations, where many factors are unpredictable

The ED does not mention in paragraph 6.23 that supply and demand in the market is a key factor or that eventually the willingness or determination of the seller and buyer to enter into a transaction plays an important role, as do their respective negotiation power. The fact that the ED does not mention these factors illustrates an unfortunate perception that fair value can be calculated in a model.

Presentation

Unfortunately we cannot support EFRAG's view on profit and loss and OCI.

We find the problems lie with the traditional way of structuring the profit and loss statement. Instead of rethinking how to present profit and loss completely, the OCI was introduced years ago leading to having a group of items resulting from remeasurements which tend to be ignored (for good or worse) when financial performance is reviewed in management commentaries or in analysts' reports. We do not believe a rethinking of the OCI will eliminate this problem, on the contrary.

As already noted we find that some of the fair value remeasurements in the OCI may not even be relevant to recognise (e.g. fair value adjustments of non-current assets). If, for some reasons it is found relevant to measure such assets at fair value, why not presenting the fair value adjustment in the profit and loss statement?

For cash flow hedges, the question is why unrealised gains and losses are not balanced in the financial position as accrued costs/income? When cash flow hedges are considered as 'unmatched items' where the future recognition of the matching item is certain or probable, there seems to be no reason to reflect them in earnings, in whichever format these are presented.

The actuarial gains and losses of defined benefit plans may concern payments to be made in a distant future and may be highly uncertain. Nevertheless, the controlling, or acceptance, of risks associated with defined benefit plans differs from entity to entity and might as well be included in the profit and loss statement, if properly structured.

Lastly, translation adjustments of foreign operations: we have still not understood why these should be included in a performance statement. After all, the adjustments arise from translating from functional currency to presentation currency. If the presentation currency is changed, the cumulated translation reserve in equity changes and still on disposal of a foreign operation the cumulated adjustment shall be transferred to profit and loss. What does this component of the gain or loss from the disposal represent? In our view, these translation adjustments are technical adjustments and should be presented as adjustments within the equity, when equity at beginning of the period is reconciled to equity at the end of the period.



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If concluding that earnings in the period should only be presented in one statement, how could it then be structured? We support the idea that the business model should play a role, when classifying items in the profit and loss statement (if being the name of only earnings statement). It should be possible, though, to define some major groups of subtotals. Maersk has proposed a model to the IASB in the comment letter to the discussion paper for the Conceptual Framework last year. Please see the enclosed.

The undersigned is at your disposal if you want to discuss further some of the views and comments presented in this letter.

Yours sincerely

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Encl.: Maersk's proposal of a new structure for a single 'Profit or Loss Statement'

**Maersk's proposal of a new structure for a single 'Profit or Loss Statement':**

Type of return	Example of line items
Operating activities	Revenue
	Expenses
	Other ordinary income/costs
	Operating profit before amortisation/depreciation
Strategic investments	Amortisation/depreciation costs
	Tax of the above
	Operating profit, net of tax
	Profit or loss from associates and joint ventures, net of tax
Single transactions	Return from other non-current equity investments, net of tax
	Profit or loss from strategic investments, net of tax
	Gain or loss from sale of assets, businesses or activities
	Costs or income associated with the purchase of business or activities
Remeasurements	Major restructuring or integration projects (if relevant)
	Tax of the above
	Single transactions, gain/loss net of tax
	Impairment of assets and reversals
Financial items	Remeasurement of defined benefit obligations
	Tax of the above
	Gain/loss from remeasurements, net of tax
	Interest income and expenses
Discontinued operations	Exchange rate gains/losses
	Fair value adjustments of derivatives not designated as hedges (inclusive ineffective hedges)
	Return from non-strategic investments (securities, etc.)
	Tax of the above
All	Financial items, net of tax
	Discontinued operations, net of tax
	Profit or loss for the period