This paper has been prepared by the EFRAG Secretariat for discussion at a public meeting of EFRAG TEG. The paper forms part of an early stage of the development of a potential EFRAG position. Consequently, the paper does not represent the official views of EFRAG or any individual member of the EFRAG Board or EFRAG TEG. The paper is made available to enable the public to follow the discussions in the meeting. Tentative decisions are made in public and reported in the EFRAG Update. EFRAG positions, as approved by the EFRAG Board, are published as comment letters, discussion or position papers, or in any other form considered appropriate in the circumstances.

Primary Financial Statements Overview of comments received in the outreach events and field-testing

Objective

1 The objective of the session is to provide EFRAG TEG members with an overview of the feedback received in the EFRAG outreach activities and field-testing.

2 The document was presented to EFRAG TEG in the EFRAG TEG meeting on 24 September 2020. As an appendix to this agenda paper we have included the first reactions of the EFRAG TEG (so only the Appendix is new).

Overview of the comments received

3 In general, stakeholders in the outreach events welcomed the IASB's ED and the IASB's efforts to improve how information is communicated in the financial statements.

4 Stakeholders also noted that the main challenge of this project is to strike the right balance between:

(a) providing more comparability and allowing management to convey its views of the company's financial performance. For example, 'comparability should be mainly considered for peers within the same industry and not across different industries as having the same subtotals across different industries may improve comparability but will reduce the relevance of financial statements'. Comparability would bring benefits for the users of financial statements; and

(b) the costs for preparers (e.g. update the IT systems for the allocation of income and expenses to the new categories and disclosures by nature when presenting by function) and benefits for users from having more disaggregation and disclosures.

5 Some stakeholders, representative of SMEs, questioned about the interaction of the IASB proposals with the existing structure established in the accounting directive, which is subsequently integrated into national law.

New subtotals and categories in the statement of profit or loss

6 In general, stakeholders welcomed the IASB's efforts to improve the structure and content of primary financial statements. Many welcomed having more granular information on the face of the financial statements, particularly users of financial statements.

<u>*Operating category*</u>

7 In general, stakeholders supported the IASB's efforts to define and require the subtotal 'operating profit or loss' as it is one of the most used subtotals and currently there is a lack of consistency in its use, labelling and definition ('good anchor point').

8 Most users of financial statements also welcomed the fact that associates and joint ventures did not impact the operating profit subtotal. By contrast, a number of preparers considered that some or all their associates and joint ventures should be presented within the subtotal operating profit or loss as they were integral to their operations and viewed by management as such.

9 Nonetheless, when discussing the definition of operating profit or loss, stakeholders provided different views:

(a) mixed views on having a definition of 'operating profit or loss' that contains a positive and a residual element. Some considered that the residual element was fundamental, others called for the IASB to focus more on the positive definition of operating profit or loss to avoid it being a dumping ground (e.g. focus on core profit);

(b) it is key to have clear guidance on the notion of the 'entity's main business activity', or in the course of the entity's main business activity' (in line with EFRAG's DCL), particularly when an entity has multiple business activities. One stakeholder opined that EFRAG provides suggestions to the IASB how to avoid the use of the 'main business activity' criterion;[1]

(c) some stakeholders suggested to include by-products to the normal (main) production as being part of the activities that would be categorised in operating;

(d) The IASB should consider, as part of the effects of these proposals, the interaction of the IASB proposals with existing regulatory frameworks on the presentation of financial statements (in line with EFRAG's DCL);

(e) questioned the 'free' accounting policy choice in paragraph 51 of the ED:

  (i) for financial institutions, any distinction between 'providing financing to customers' and 'pure financing' is artificial and judgemental. Thus, stakeholders questioned the usefulness of the option in paragraph 51(a) for financial institutions (not mentioned in EFRAG DCL) as it would impair comparability; and

  (ii) For corporates, the accounting option in paragraph 51(b) may result in the loss of relevant information for users (e.g. manufacturer providing financing to customers) and impair comparability (in line with EFRAG's DCL).

(f) mentioned the effect of the definition of "main business activities" on the classification of associates and joint ventures as integral;

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[1] Currently the draft comment letter notes [summarised] "EFRAG also highlights the importance of having clear guidance on the notion of 'in the course of the entity's main business activity' as the allocation of income and expenses to the operating category significantly relies on these notions and use of such concepts will involve significant judgement. [Examples are provided…] EFRAG also highlights the challenges of applying these concepts to entities with multiple business activities, that include investing and financing activities, particularly when considering the perspectives of the legal entity (parent or a subsidiary) in the separate financial statements and of the group."

(g) Some considered it useful to clarify the relation to the definition of operating segments under IFRS 8 *Operating Segments*;

10 One stakeholder (representative of a financial conglomerate) noted the interaction between the operating and investing category and the presentation requirements in IFRS 17 *Insurance Contracts*. For example, it would impact the classification of the interest margin, the new line items related to the insurance result and the absolute amount of expenses included in the statement of profit or loss. To continue to use the subtotal 'gross margin' which was required by regulators and provided useful information to users, this stakeholder explained that they would need to split and reclassify a significant part of their expenses, among other complex adjustments, whose allocation is required by IFRS 17.

11 One stakeholder noted to have a ringfenced activity that collects cash and cash equivalent ranging from current account to deposits and invests cash in public debt. They cannot provide financing to customers. The investment is in public debt so income and expenses should be in operating but in accordance with the ED it is not possible.

<u>Investing category</u>

12 In general, stakeholders acknowledged the objective of the IASB's proposal to introduce an investing category (i.e. to identify returns from investments that are not part of the entity's main business activities).

13 Nonetheless, stakeholders referred to a number of implementation challenges:

(a) More guidance would be needed on the definition particularly on:

(i) the concept of 'in the course of the entity's main business activity'. Identifying returns from investments that are not part of the entity's main business activities is difficult for the entities that invest in the course of their main business activities (in line with EFRAG DCL);

(ii) incremental expenses incurred generating income and expenses from investments (not specifically mentioned in EFRAG DCL);

(iii) more examples of investments that are not part of the entity's main business activities (not specifically mentioned in EFRAG DCL);

(iv) questions were raised on how the new requirements on the investing category would interact with the notion of materiality referred in paragraph 24 of the ED (in line with EFRAG DCL) when considering that often the investments that are not part of the entity's main business activities are not material; and

(v) questions whether the investing and financing categories could be optional or merged.

(b) concerns about presenting gains and losses on derivatives in the investing category under certain conditions (i.e. exceptions related to grossing up of gains and losses or the undue cost or effort), particularly when referring to financial institutions (in line with EFRAG DCL).

<u>Financing category</u>

14 On the financing category, stakeholders generally understood and agreed with a subtotal focused on income and expenses on liabilities arising from financing activities.

15 Nonetheless, there were more questions on the classification of 'income and expenses from cash and cash equivalents' and 'interest income and expenses on

other liabilities' (e.g. the unwinding of discounts on pension liabilities and provisions):

(a) When referring to the questions on the presentation of cash and cash equivalents stakeholders provided mixed views:

(i) some considered that it should be included in the investing category because an entity had invested in asset by management decision;

(ii) some considered that it should be presented in the financing category, nonetheless, acknowledged that the IASB's proposal would put tension on the definition of 'cash and cash equivalents' and suggested that the IASB focus on 'financial assets that are managed for short term liquidity';

(iii) some noted that the classification of cash and cash equivalents may depend on its use. For example, if it is cash and cash equivalents allocated to working capital (cash and cash equivalents used for operating needs), then any related income and expenses should be within operating profit. If it is large cash balances in excess of their operating needs, then income and expenses should be within financing category (i.e. linked to net debt);

(iv) some (analysts) supported the allocation of the income from cash and cash equivalents to financing category as it was treated in the same way as pension deficit for the analytical purposes;

(v) some considered that the distinction between treasury investments and other type of investments could be challenging and artificial. Alternatively, the financing category could be linked to the management of liabilities that arise from financing activities and the investing category to the management of investments in assets (in line with one of the two views considered in EFRAG DCL); and

(vi) some preparers referred to materiality. Income and expenses from cash and cash equivalents may be immaterial amounts. Therefore, an accounting policy choice might be appropriate.

(b) When referring to the questions on the presentation of unwinding of discount, stakeholders provided mixed views:

(i) some considered that it should be included in operating category, particularly when related to operating liabilities,

(ii) some referred to the financing category as it reflected the cost to provide finance, and

(iii) some considered that it would be useful to have guidance on time value of money related to assets.

<u>New categories in general</u>

16 Many stakeholders (particularly preparers) raised questions on the classification of very specific line items such as:

(a) foreign exchange differences (e.g. foreign exchange differences on intercompany loans), fair value gains and losses on derivatives and hedging instruments between the operating, financing and investing categories;

(b) interest from extended payment terms to customers (operating category) and interest on trade payables (financing category), in particular whether there should be symmetry in their treatment;

(c) contingent consideration from business combinations;

(d) goodwill impairment losses; and

(e) income and expenses from non-current assets held for sale.

17 During the field test preparers pointed out that the classification to categories of foreign exchange differences, fair value gains and losses on derivatives and hedging instruments would require system changes.

18 Consolidation issues were discussed. Will the categorizations of items of income and expense change at the different consolidation levels?

19 A number of stakeholders, particularly users of financial statements:

(a) highlighted the importance of the subtotal EBITDA, which is widely used by investors, analysts and databases;

(b) considered that the reference to the use of 'operating profit before amortisation and depreciation' was a step forward as it was similar to EBITDA;

(c) it was not clear if EBITDA or EBIT were an MPM (e.g. if EBITDA is equal to 'operating profit before amortisation and depreciation' whether it would still be an MPM). If it was an MPM, then it had to be clearly identified and disclosed; and

(d) suggested that the IASB considers including the subtotal 'operating profit before amortisation, depreciation and impairment' in paragraph 104 of the ED.

20 Although the allocation of exchange differences and hedging was not a significant issue for most banks as their income and expenses will be mainly within operating profit, many corporates raised concerns on the level of cost and judgement related to the allocation of income and expenses for hedging instruments and exchange differences (e.g. it would require changes to the IT systems on a worldwide basis).

Integral and non-integral associates and joint ventures

21 This was one of the most debated topics where stakeholders provided many comments and expressed some concerns.

22 When discussing this issue with users of financial statements, they provided mixed views:

(a) a majority of users supported the IASB proposals to separate income from associates and joint ventures from the operating results, but did not find useful the split of integral and non-integral as proposed by the IASB. Users found it artificial and bringing no added value for their analysis;

(b) some users supported the IASB proposals as they would provide useful information of what was operational and contributed to the core business. This is aligned with EFRAG DCL (however questions about the level of judgement and the effective functioning in practice were raised in EFRAG DCL);

(c) some users considered that the distinction between integral and non-integral provided useful information but suggested that such information could be provided in the disclosures;

(d) some users acknowledged that separating integral and non-integral associates and joint ventures could provide useful information; however, the distinction was going to be very subjective or even subject to management abuse, putting into question its relevance in the end. In its DCL, EFRAG also mentioned that the split will involve significant judgements and assumptions and it will need to be tested in practice; and

(e) some users simply did not agree with the distinction as it was going to be a very subjective decision and would raise many questions such as the company's long-term commitment to its investment and presenting post-tax results together with pre-tax information.

23 Many users also questioned the need for a separate subtotal on integral associates and joint ventures as it provided too much prominence to associates and joint ventures), particularly from users (not mentioned in EFRAG DCL).

24 Users also questioned the presentation of the subtotal net of income tax as part of an aggregated subtotal which was gross of tax.

25 When discussing with preparers, comments were mainly focused on implementation concerns:

(a) it would be useful to expand paragraph 20D of IFRS 12 to ease implementation (in line with EFRAG DCL), reduce the level of judgement and ensure comparability. This is because the proposed presentation requirements would, in some cases, require significant judgements (in line with EFRAG DCL) and be subject to abuse. In addition, the definition of integral associate and joint venture seems to be narrow as in some cases associates and joint ventures may be, in accordance with paragraph 20D of IFRS 12, classified as non-integral while management considers them as integral (not mentioned in EFRAG DCL). For example, in certain markets only minority positions are allowed (joint ventures with a minority stake or associates), not permitting a company to exercise control. Due to business reasons, the level of operational integration may be low but nevertheless the management may see these entities as being part of their main business activities. In addition, the brand name of the joint venture partner who has the majority of the shares is adopted and/or for regulatory purposes a company needs to be set up so that it has its own finances (i.e. no financial integration). In these cases, stakeholders would still view these joint-ventures as integral, but the current indicators would not allow such classification. A frequent suggestion was that the IASB addresses a wider range of investment situations (e.g. cycle of investment) and adds an indicator focused on whether investments are or not related to the same sector of the entity's main business activities. While the general feedback was to avoid a prescriptive approach to the definition in order to keep the new concept as principles based, illustrative examples would be of help;

(b) importance of having clear guidance on the notion of the 'entity's main business activities' (in line with EFRAG DCL);

(c) there is a need for the IASB to further discuss how its proposals would apply to the separate financial statements (in line with EFRAG DCL); a question was raised why this distinction was not considered for subsidiaries too;

(d) questions on the IASB's proposals from a cost-benefit perspective ("is it worth to make the distinction?");

(e) questions on how the IASB proposals should be applied when considering immaterial associates and joint ventures;

(f) questions on whether this information could only be disclosures (same as suggested by users above);

(g) there is room to improve the equity method (e.g. separate presentation of income tax or full allocation of the results from associates and joint ventures to the new categories) but agreed that this should be addressed in a different project;

(h) a different approach for financial institutions may be required as associates and joint ventures are either not material or part of the operating profit or loss, particularly for insurance industry;

(i) the classification of an associate or join venture as non-integral may affect the business organisation and raise internal issues and the investee, including its employees, may be concerned about the classification as non-integral (e.g. may be seem as a first step for disinvestment);

(j) the interaction between the ED and long-term interest notion in accordance with IAS 28 *Investments in Associates and Joint Ventures* should be clarified (e.g. would the income from the long-term interest be aggregated into the results from the integral associate on the face?);

(k) the interaction between the ED and IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* to be clarified, as well as for instruments that follow under the FVCOI option in accordance with IFRS 9 *Financial Instruments*; and

(l) questions on whether the notion integral/non-integral should be assessed from the point of view of the investor or investee;

Analysis of operating expenses

26 When discussing which method provides the most useful information, EFRAG received mixed views on this topic:

(a) some preferred analysis of expenses by nature (mainly users), as such information can be better used for forecasting future cash flows and was the only way to have a consistent set of information with the cash flow statement;

(b) some preferred a by function presentation (with more disaggregation) together with disclosures by nature, including in the interim financial statements (mainly users);

(c) some considered that a mixed approach provided more flexibility to management to explain the entity's performance (mainly preparers). A mixed approach basis was working well in some industries and considered that a change in current requirements would require a significant change of the IT systems;

(d) some agreed with the IASB's proposals to not allow a mix presentation basis (mainly users);

(e) some were happy with the approach in the ED and IAS 1 *Presentation of Financial Statements* (to have an option); and

(f) in some cases, entities should be allowed or seem to be required to follow a mixed approach, particularly for conglomerates that reflected different business activities on the face of the financial statements (insurance and banking). The IASB should clarify if the disclosure requirements by nature would also apply under such circumstances.

27 In general, stakeholders requested more guidance on description by nature and by function (e.g. restructuring, administrative expenses, goodwill impairment). Stakeholders also highlighted the importance of having a common practice within an industry for comparability purposes; in this regard implementation costs were mentioned and that the implementation changes on presentation should not be repeated shortly after the implementation of this new upcoming standard.

28 When discussing more practical issues, no significant concerns came from those that currently present their operating expenses by nature. Those that presented their analysis of expenses by function:

(a) called for more guidance on the presentation by function (e.g. no clear definition of items such as 'cost of sales' and 'administrative expenses') and on the use of the line item 'other expenses';

(b) judgments to allocate some income and expenses by nature to the by function line items (e.g. restructuring expenses and goodwill impairment losses);

(c) referred to the high costs (IT systems auditing) related to the disclosures of total operating expenses by nature when presenting by function on the face and questioned their added value to users;

(d) called for clarifications on the link between paragraphs B46 and B15 of the ED (already in EFRAG DCL);

(e) mainly those applying a mixed presentation and some users considered that a mixed approach provided more flexibility to management to explain the entity's performance;

(f) whether the guidance on the analysis of expenses should also apply to other categories of the statement of profit or loss; and

(g) the structure of the statement of profit or loss would be significantly predetermined due to the requirements in IFRS 9, IFRS 17 and paragraph 65 of the ED. Such predetermined structure would imply the use of a mixed approach. Considering this, it was not clear how entities that are required to use a mixed approach shall apply the requirements regarding the additional disclosures by nature, which would be costly to comply with.

Management performance measures ('MPMs')

29 In general, stakeholders acknowledged and agreed that non-IFRS measures are often used in practice and more discipline could bring transparency and consistency on their use. Stakeholders, particularly users of financial statements, also acknowledged the benefit of having such measures being audited.

30 In general, stakeholders did not raise significant issues in regard to identifying MPMs, which could be found in the notes, management commentary, presentation to analysts, guidance for the year and mid-term plan. Nonetheless, many stakeholders called for the IASB to clarify what 'public communication' was.

31 When referring to the scope of the IASB proposals on MPMs in terms of the location of the performance measures (i.e. public communication, annual report, financial statements), EFRAG received mixed views:

(a) some (mainly users) considered appropriate to go for the performance measures presented in the communications issued jointly with the annual or interim results, particularly users of financial statements, as this approach would bring the benefit of these measures being audited;

(b) some (mainly preparers) would prefer disclosures only for the performance measures that an entity presents in the financial statements. These cautioned about requiring the inclusion of MPMs in the financial statements as in the end there would be many types of performance measures located in different parts of the annual reports, including IFRS performance measures, management performance measures, alternative performance measures, unusual items and integral and non-integral subtotals; and

(c) some suggested having all the information about alternative performance measures in a single place (i.e. management commentary) to avoid confusion, the use of non-defined measures within the financial statements and the increase of disclosures in the future.

32 Nonetheless, when referring to the scope of the IASB proposals on MPMs in terms of type of performance measures, in general stakeholders:

(a) noted that the definition seemed to be narrow (e.g. does not include measures from balance sheet) and explained that only disclosing a narrow number of MPMs would provide an incomplete picture of the entity's performance (both users and preparers). Nonetheless, some stakeholders were concerned about presenting performance measures that would be difficult to reconcile with IFRS numbers (e.g. organic growth);

(b) many questioned whether other non-GAAP measures that did not meet the definition of MPMs could be presented together with MPMs;

(c) if the IASB allowed the presentation of other non-GAAP measures, some questioned whether MPMs could be presented in an appendix to the financial statements (it could be a comprehensive amount of information) or whether cross references to management report could be made;

(d) questions on the interaction of MPMs with several other regulatory requirements (e.g. ESMA guidelines and local management report requirements) given their different scope; and

(e) suggested that regulatory reporting and other mandatory frameworks should be excluded from the MPMs reconciliation.

33 Not much debate about more or less MPM. Only few shared the view that there is a risk of more MPM after applying the upcoming standard on PFS.

34 Finally, stakeholders provided a number of other comments:

(a) some stakeholders noted that the computation of income tax effect can be complex, particularly when there are many different tax jurisdictions and when using constant currency performance measures;

(b) some stakeholders noted that they might revisit their performance measures considering the new proposed subtotals;

(c) a number of stakeholders considered that the IASB has not sufficiently articulated the link between MPMs and IFRS 8 *Operating Segments* (in line with EFRAG DCL);

(d) importance of the notion of 'neutrality' for the MPMs as the non-IFRS earnings were often significantly higher than IFRS earnings; and

(e) European preparers which currently provide information to adjustments per share (adjusted EPS) mentioned that the requested disclosures were easy to prepare as they already had the information.

Unusual income and expenses

35 The majority of stakeholders agreed that disclosing unusual items in the notes would provide useful information to users of financial statements. Some stakeholders in the field-test already provided information about non-recurring or unusual items. However, it was noted that the IASB proposals would change current practice.

36 When referring to the IASB's proposed definition of unusual items, stakeholders provided mix views on how unusual items should be defined:

(a) a majority considered that the IASB definition is too narrow as it only focused on whether expenses/income would occur in the future. The definition would restrict the number of unusual items identified and, consequently, disclosures would have limited added value. For example, the definition excludes expenses caused by a restructuring program which takes two years. Some agreed with EFRAG suggestion for the IASB to consider not only items that 'will not arise for several future annual reporting periods' but also items that presently occur in the business, but only for a limited period of time;

(b) some were concerned that it could be too wide; the definition should be narrow to avoid abuse. Similarly, some noted that the definition of usual and unusual items needed to be further clarified as there was still a leeway for companies on the use of this definition;

(c) some considered that there should be a list of line items for which entities have to provide disclosures (e.g. restructurings, impairments, litigations, etc);

(d) some considered that it was difficult to agree on a common definition and management should provide its own definition of unusual items (particularly when considering that this would not impact the presentation of the income statement);

(e) some, particularly users, questioned the need for the IASB to define and require entities to disclose unusual items, particularly when considering:

  (i) the IASB proposals on MPMs;

  (ii) the semantics of unusual, non-recurring, extraordinary and other similar words which could potentially confuse users of financial statements;

  (iii) potential translation issues;

  (iv) the subjectivity involved as there is always uncertainty on whether similar events or transactions will take place in the future (e.g. covid19); and

  (v) the difficulties of implementing such concept in practice.

(f) Some requested clarification in the guidance: unusual in amount and/or type?

(g) Some users suggested, instead of defining the unusual items, to provide an option to show more disaggregated information on the face of the income statement. More disaggregation would allow analysts to take their own decisions of what was 'unusual' based on the more granular information provided by companies.

37 In addition, many stakeholders considered that:

(a) it would involve a significant degree of judgement and discretion to determine whether an item is unusual (e.g. the term 'several future annual reporting periods' and 'predictive value' will involve significant judgement);

(b) questions on how to report the unusual amounts (part that is usual and the excess that is unusual) and how unusual items would be monitored and considered by the auditors. This is particularly relevant when considering, for example, loan impairment losses (normal vs unusual due to covid19);

(c) many questioned the applicability and interaction/added value in conjunction with the IASB proposals on MPMs (likely to capture the same items); and

(d) importance of neutrality of unusual items (both income and expenses are considered unusual).

Roles of the primary financial statements and the notes, aggregation and disaggregation

38 In general, stakeholders welcomed the new guidance on the roles of the primary financial statements and the notes, aggregation and disaggregation.

39 The users were particularly supportive for more disaggregation and noted that it could also eliminate the need for defining unusual items, as the necessary information would already be available in the financial statements.

40 Nonetheless, some stakeholders questioned whether this new guidance would significantly change current practice.

Other comments: Statement of cash flows

41 In general, the IASB proposals on cash flow statement were very well received, although participants acknowledged there was still some work to do.

42 Most comments on the statement of cash flows were related to the labelling. Many stakeholders noted that both the statement of financial performance and the statement of cash flows will have three different categories with similar labelling (operating, investing and financing) even if they are not aligned. These stakeholders considered that this would be confusing and could be misleading.

43 Mainly labelling was questioned, but cohesiveness between the statement of cash flows and the statement of financial performance was not requested as part of this project. Only for the IASB to align the statements to the extent possible.

44 Further inconsistencies were noted for example in classification of the dividends from the integral associates and joint ventures as investing activities in the cash flow statement, as they were more of an operating nature according to management.

45 Many supported the IASB's proposal to require entities to use 'operating profit or loss' as the starting point for the indirect reconciliation of cash flows from operating activities in the statement of cash flows ('the most natural way of presenting the information, even though the categories of the two statements were not aligned'). However, some users of financial statements were concerned that this would lead to loss of information as the reconciliation of 'net profit' with 'operating activities' provided more information than the reconciliation of 'operating profit or loss' with 'operating activities'.

46 In general, stakeholders did not raise significant concerns on the removal of options for the classification of interest and dividends in the statement of cash flows and considered that such an approach would improve comparability. Nonetheless, there were a few concerns about the requirement to separately present cash flows from integral and non-integral associates and joint ventures, particularly when taking into account materiality considerations.

47 Finally, some stakeholders suggested that the IASB has a separate project on IAS 7 *Statement of Cash Flows* with the objective of having a comprehensive review of the challenges that arise in practice (e.g. financial institutions) and improve consistency with the new content and structure of the statement of profit or loss.

Other comments: presentation of revenue and costs in different business lines

48 Many stakeholders agreed that, currently, there is diversity in practice in how entities that operate business activities in different industries present their performance and it could be useful if the IASB could further explain how entities with different business activities should prepare their financial statements (similar to EFRAG DCL).

Other comments

49 Many users highlighted the importance of having more guidance on disclosures and the accounting for on reverse factoring. Users of financial statements considered that the lack of information about such transactions was a widespread issue that involved significant amounts. In particular, users of financial statements mentioned the current asymmetry of information between banks (involved in the reverse factoring) and bondholders.

50 Some requested guidance on classification of items recycled from OCI.

51 Some questioned the title “Profit before tax” as it was meant to be “Profit before income tax”.

52 Some noted that the implementation period of 18-24 months might be challenging if a significant change to the IT systems is required. This is, in particular, relevant for some industries that use by function presentation and where users do not demand by-nature presentation of costs In complex groups with a long delivery chain, the type-of-cost tracking functionality has not been implemented and it would take a long time to change their systems.

Appendix 1

EFRAG TEG preliminary reactions on September 24

53 EFRAG TEG discussed the feedback from outreaches and field-tests in their meetings on 2 July, 2 September and 24 September 2020.

54 The following is a summary of their initial reactions on 2 July 2020:

(a) Members noted that many criticisms were arising about the IASB proposal to define integral and non-integral associates and joint ventures and to separately present their results on the face of the income statement. EFRAG initially supported this proposal and already anticipated the need to test in practice these new concepts. Considering the amount of comments on this topic, the initial support may be re-discussed in a next meeting. The following comments were made during the discussion:

(i) One EFRAG TEG member appreciated the separate presentation of equity accounted investments but questioned the need to separate presentation of integral and non-integral associates and joint ventures as users valued them similarly without making such distinction.

(ii) One EFRAG TEG member referred to paragraph BC 87 of the ED and noted that joint ventures would normally be considered as integral. This member asked if users were valuing associates differently from joint ventures.

(iii) Another EFRAG TEG member responded that the valuation technics for all equity accounted investments were the same, but the more granular information would be welcome. This member highlighted that having the results of associates and joint ventures in operating profit was distorting future projections.

(iv) Some EFRAG TEG members noted that for insurance companies in some cases it would be relevant to present the results of associates and joint ventures in the operating section of the income statement, as important components of the operating business were often realised through this mean.

(v) One EFRAG TEG member observed that this was similar to what manufacturing entities do with distribution channels, such as operating through associates or joint ventures (for example in China where setting up a fully integrated subsidiary may be more difficult due to entry barriers in that country). This member asked if it made sense not to reflect the incremental margin in operating profit in such cases. He also concluded that focusing on a better conceptual principle for the operating category (less focus on the "integration" element) and in particular for the definition of "main business activity" would support a clearer identification of the dividing line between integral and non-integral. Another EFRAG TEG member suggested to enlarge the scope of MPMs by including the balance sheet and any other performance measures used in public communication.

(b) Two EFRAG TEG members considered the distinction between APMs and MPMs as artificial, on the one side there were GAAP measures linked to IFRS numbers, but performance measures used in public communication were different.

(c) Another EFRAG TEG member noted that the valuation adjustments required by the IAS 40 *Investment Property* could be included as a separate subtotal within the operating profit.

(d) Another EFRAG TEG member suggested that it could be explained in the notes to the financial statements.

55 The following is a summary of their initial reactions on 2 September 2020:

(a) EFRAG TEG members welcomed the feedback received from EFRAG's stakeholders in the outreach activities.

(b) EFRAG TEG members acknowledged that preparers agreed with EFRAG DCL that the proposed scope on management performance measures seemed to be narrow, as it is limited to subtotals of income and expenses and excludes indicators of the financial position and cash flows. One EFRAG TEG member noted also the there is an interaction in practice today between the reconciliation required by ESMA, which will probably also be applicable under the IASB MPM proposal, and the requirement to disclose unusual income/expenses.

(c) One EFRAG TEG members expected to see commonalities on the implementation at segment or country level.

(d) EFRAG TEG members acknowledged the application challenges related to the descriptions of analysis of expenses by function and by nature. One EFRAG TEG member mentioned two challenging items that demonstrated that the proposal was not clear: impairment losses of goodwill and restructuring cost. These are not "inputs" to the operating process, so they were not strictly speaking "expenses by nature", however presenting them separately may conflict with the impossibility to have mixed presentation, while mixed presentation would help in these two cases/ .

(e) On the distinction of integral and non-integral associates and joint ventures, it was noted that management will always have to use judgement when applying IFRS Standards however the underlying principles have to be clear. One EFRAG TEG member reiterated a message that was already emerging in previous outreaches: that the lack of clarity of how to implement this distinction was confirming the lack of full clarity on the concept of operating category.

(f) It was noted in conclusion, that the main messages and challenges were in line with the initial key points identified in EFRAG DCL. However, the participants to the roundtables had brought to the table a number of practical suggestions to overcome the issues that EFRAG could further consider in the final comment letter, as possible examples of solutions.

56 The following is a summary of their initial reactions on 24 September 2020:

(a) EFRAG TEG observed that stakeholders had provided a wide variety of views, including on the topics that EFRAG had requested for constituents' views, and acknowledged the challenges of seeking a compromise solution on areas where there is considerable diversity of views such as the distinction between integral and non-integral associates and joint ventures.

(b) some EFRAG TEG members also provided the following suggestions on how to improve EFRAG DCL:

(i) the need for having (ii) a better conceptualisation of the distinction between the analysis of the operating expenses by nature and by function and (ii) more guidance on the presentation of certain items by function (e.g. 'cost of sales' and 'administrative expenses');

(ii) to include a rebuttable presumption to classify at least joint ventures as integral;

(iii) to identify cases where associates and joint ventures should be presented within operating profit or loss (e.g. insurance industry);

(iv) to clarify the interaction between the ED and long-term interest notion in accordance with IAS 28 (e.g. would the income from the long-term interest be aggregated into the results from the integral associates on the face of the income statement);

(v) to provide more guidance on the classification within the different categories on the face of the profit or loss of some specific items such as those related to contingent consideration from business combinations and goodwill impairment;

(vi) more guidance on the definition of incremental expenses in the investing category a; and

(vii) to encourage a separate project on IAS 7 Statement of Cash Flows to address the IASB's proposals included in the ED on the statement of cash flows, to improve consistency with the new structure of the statement of profit or loss and have a comprehensive review of the challenges that arise in practice.