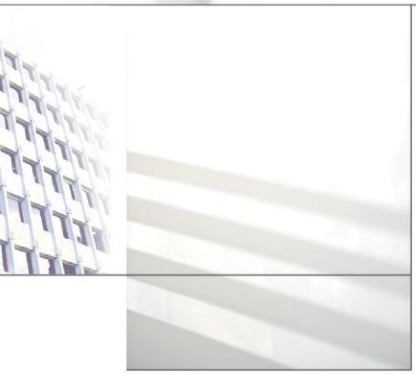

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European Financial Reporting Advisory Group

Filipe Alves & Albert Steyn

EFRAG CFSS Primary Financial Statements

22 February 2017

Objective of the session

The objective of the session is to discuss:

- The key findings of the IASB Staff's research activities
- The key findings of EFRAG's evidence finding activities
- The IASB's tentative decisions on the scope of this project

Latest developments

- In November 2016 the IASB discussed the outcome of the research work undertaken by the IASB Staff and subsequently in December 2016 the IASB discussed the scope of the project.

- The IASB will decide at a later stage whether the next step is the publication of a Discussion Paper or an Exposure Draft.

- EFRAG TEG and EFRAG User Panel have recently discussed the outcome of the research work and scope of the project.

IASB Staff findings: Presentation of PFS

The IASB Staff analysed 25 entities that report in accordance with IFRS Standards. The key findings are:

Statement(s) of financial performance

- Variations in the structure and content, even for entities within the same industry
- Many entities present an “operating profit” that corresponds broadly to EBIT. However, these subtotals were often calculated differently
- Many entities present an adjusted operating profit but the adjustments vary, lack transparency and are presented differently (e.g. non-recurring)

IASB Staff findings: Presentation of PFS

Statement of cash flows

- The starting point for determining net cash flow from operating activities varies (the indirect method). For example, entities used either “profit or loss”, “profit attributable to shareholders” or “operating profit”.
- The presentation of interest and dividends in the statement of cash flows varies

Statement of financial position

- No major inconsistencies in the presentation of the statement of financial position. Nonetheless, some entities had large “other” items.

Segment information

- The number of line items presented in segment information varies

IASB Staff findings: Performance measures

Performance measures used:

- IFRS-specified information" (e.g. revenue);
- "not explicitly required IFRS information" (e.g. gross profit)
- "non-IFRS information" (e.g. adjusted revenue)

Some non-IFRS measures can conflict with IFRS Standards

measured on a different basis to IFRS or provide information that undermines information provided in accordance with IFRS

Widespread use of performance measures based on non-IFRS information outside the financial statements.

These are sometimes also presented in the financial statements.

Commonly used non-IFRS performance measures include revenue growth rate excluding some effect (eg currency), adjusted EBITDA and adjusted profit.

Still, these performance measures are often calculated differently.

IASB Staff findings: Literature review

Issues that arise in practice, US SEC Staff Paper (2011) :

- Nature of subtotals reported varied by company
- Different classifications to report share of profit or loss from associates
- Presentation of alternative earnings per share measures

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IASB Staff findings: Literature review

Studies focused on possible improvements:

- Users need more subtotals, disaggregation and structure. Aligning financial statements can also add value
- Separating operating from financing is relevant
- Investors often do not use OCI
- Allowing choice in reporting interest in the statement of cash flows hinders comparability
- Primary financial statement information is used differently for different industries
- More detail in the segments notes

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IASB Staff findings: Outreach activities on scope

Outreach activities on the scope of the project

Users including EFRAG User Panel, IFRS Advisory Council, Accounting Standards Advisory Forum, Capital Markets Advisory Committee, Global Preparers Forum and IFRS Taxonomy Consultative Group

- Support for a project to improve the structure and content of the primary financial statements beginning with the statement of financial performance
- This statement contains the least structure under IFRS and most APMs are based on these numbers
- Fewer concerns about the structure and content of other PFSs

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IASB Staff findings: Outreach activities on scope

Suggestions received for improvements for PFS:

- More guidance on minimum line items and subtotals for the statement of financial performance – principle basis vs detailed rules
- Add new EPS measure that reflects management's view of profit
- Alignment between "operating profit" in statement of financial performance and "cash flows from operating activities" in cash flow statement
- Removing presentation options for dividends and interest in cash flow statement
- Developing templates
- Additional line items and subtotals in the segments notes

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IASB Staff findings: Outreach activities on the scope

Other feedback received

- Some users stated that APMs were useful and should not be prohibited
- There is divergence and lack of transparency in the calculation of APMs
- Some suggested having principle basis guidance on their presentation
- Many users did not understand what is currently presented in OCI and did not include OCI items in their analysis

EFRAG Staff findings: Presentation of PFS

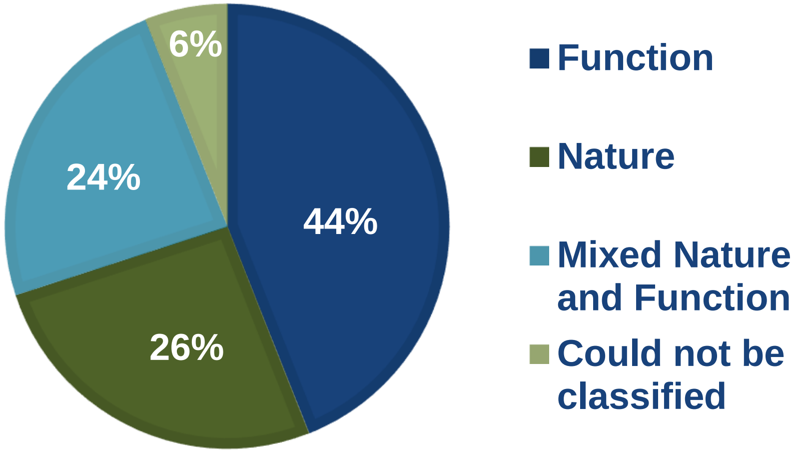
EFRAG Staff analysed 34 entities that report in accordance with IFRS Standards and are included in the S&P Europe 350
The key findings are:

Statement(s) of financial performance

- **Companies presented the expenses by their function, nature and a mixture of both**
- **The majority of the companies did not include an explicit reference to the term "non-recurring" or "exceptional"**
- **Companies use many different subtotals**
- **Almost all the companies used two statements**
- **Presentation of results of associates and joint ventures varied**
- **In some cases the number of line items was limited and disaggregation level was low**

EFRAG Staff findings: Statement of financial performance

1. PRESENTATION CHOICE



2. Use of performance measures

- 76% did not include an explicit reference to the term non-recurring, exceptional, non- core items or extraordinary
- Companies that made explicit reference:
  - amounts disclosed in a separate note
  - different labelling on the face
  - their location on statement of financial performance varied
  - the nature of line items varied

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EFRAG Staff findings: Statement of financial performance

3. USE OF SUBTOTALS

Gross profit

Operating profit

EBIT

Finance results

Profit before tax

Profit for the year

4. SINGLE OR TWO STATEMENTS

- **Percentage of companies using 2 statements:**

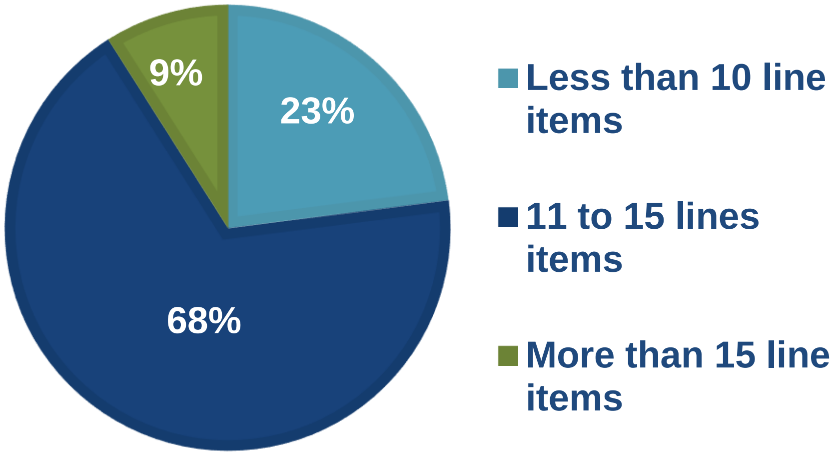
97%

EFRAG Staff findings: Statement of financial performance

5. PRESENTATION OF RESULTS OF ASSOCIATES AND JOINT VENTURES

- Presentation varied
- 59% within profit before tax
- 2 cases included it in total revenue and other income
- Separate subtotal created
- Presented as a figure net of tax

6. NUMBER OF LINE ITEMS



EFRAG Staff findings: Statement of financial performance

6. USE OF SUBTOTALS

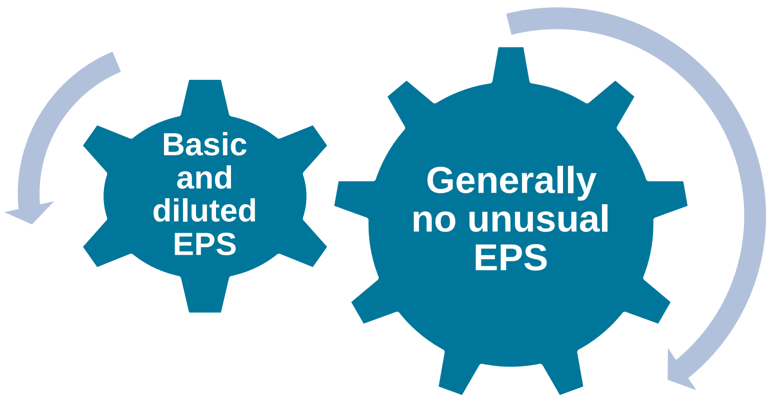
- 68% had at least 4 subtotals:
  - Gross profit
  - Operating profit
  - Profit before tax
  - Profit for the year
- There were subtotals within other subtotals
- Limited use of a separate line item for interest from defined benefit plans

7. PERFORMANCE MEASURES USED IN TWO PUBLIC DATABASES

- Only profit and loss part displayed (No OCI items)
- Many subtotals used, including EBITDA
- Use of extraordinary items and unusual items

EFRAG Staff findings: Statement of financial performance

8. EARNINGS PER SHARE



9. OTHER COMPREHENSIVE INCOME

- Started with profit after tax
- Separated:
    - Items that can not be reclassified to profit and loss
    - Items that may be reclassified to profit and loss
- Presentation of recycling to profit and loss
- No other APMs used

EFRAG Staff findings: Statement of financial position

1. SEPARATION AND ORDER

- **All entities separated**:

Current / Non-Current

- **Order of liquidity used**:

79%

2. SUBTOTALS AND LINE ITEMS

A few entities used a “Net assets” subtotal

A few entities disaggregated the discontinued operations subtotal

Some entities presented additional information within separate columns

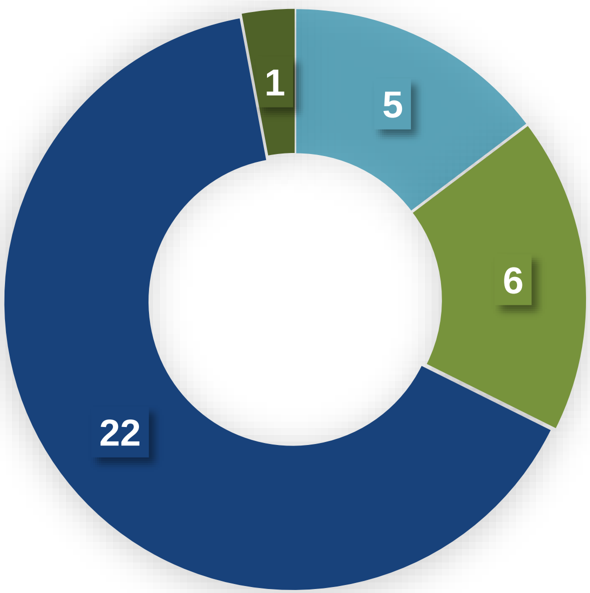
All used total assets, liabilities and equity

Line items referred to as “other” sometimes significant

82% did not use additional subtotals (from those already required by IFRS)

EFRAG Staff findings: Statement of financial position

3. PRESENTATION OF EQUITY



- Split of equity attributable to owners of the parent and non-controlling interest but no other disaggregation
- No separation of retained earnings and other reserves that would include OCI items
- Separation of retained earnings and other reserves that would include OCI items
- Separate reserve for every OCI item

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IASB's tentative decisions on the project

Statement(s) of financial performance	Statement of cash flows	Statement of financial position and changes in equity
• Requiring additional subtotals; EBIT and/or operating profit • Providing guidance on the performance measures that exclude non-recurring items etc. • Better ways to communicate OCI	• Eliminating options for the classification of interest and dividends • Aligning the operating section between the statements of cash flows and financial performance • Requiring a consistent starting point for the reconciliation	✘ No specific change is planned in this project, except for possible development of template for all primary financial statements and greater disaggregation

- Developing a template for primary financial statements

- Achieving greater disaggregation

Key messages from EFRAG TEG discussions

- EFRAG TEG highlighted the importance of this project and generally agreed with the IASB's tentative decisions on its scope.
- EFRAG TEG members emphasised the importance of non-GAAP measures for investors and the need for guidance on their use within the financial statements.
- Some EFRAG TEG questioned the relationship between this project and the IFRS Taxonomy and the influence of taxonomy on this project. Nonetheless, it was noted that standards should drive the IFRS Taxonomy and not the other way around.
- Highlighted the potential tension existing between comparability and relevance and the need for the IASB to balance competing expectations.
- Some EFRAG TEG members were of the view that the IASB should address the issues that arise in the cash flow statement of financial institutions
- Finally, EFRAG TEG members considered that, for transparency purposes, it could be useful to have a Discussion Paper as a next step.

Key messages from EFRAG User Panel discussion

- General agreement that the project was currently focusing on the right issues.
- Comparability of financial statements is very important for users and further consistency needs to be achieved through, for example, additional guidelines on the content and structure of financial statements and elimination of presentation options.
- Some EFRAG User Panel members highlighted the need for the IASB to clarify the linkage between the different primary financial statements. This would improve comparability and transparency of the information.
- EFRAG User Panel members favoured having strong principles for the definition of subtotals, such as EBIT, with limited choices for preparers in terms of allocation of line items so that users obtain a comparable starting point for their analysis.
- One EFRAG User Panel member highlighted the importance of discussing the definition of performance, use of OCI and the need for recycling.

Key messages from EFRAG User Panel discussion

- EFRAG User Panel members considered that there was room to improve the *Statement of Cash Flows* and highlighted a number of specific issues that needed to be addressed, including some of the definitions and options that exist in IAS 7 and better linkage to other primary financial statements.

- EFRAG User Panel members emphasised the importance of non-GAAP measures and the need for guidance on their use within the financial statements.

- There were some concerns about having a new Adjusted Earnings Per Share figure as it would not beneficial for users and would create room for misuse by preparers. Nonetheless, Panel members highlighted the need for a definition of financial debt.

- One EFRAG User Panel member highlighted that relevant information about OCI was also provided in the statement of financial position (e.g. separate components of equity) and that this information was particularly relevant for financial institutions.

Next steps

- The IASB will start to discuss the different issues under the scope of the project in future meetings.
- The IASB staff has already considered input from EFRAG User Panel on the use and calculation of the subtotal EBIT, including:
  - its definition; and
  - whether the IASB should require a specific treatment, recommend specific treatment or allow accounting policy choice on the line items to be included or excluded (e.g. interest cost pension) from the subtotal.

Questions

Questions to EFRAG CFSS members

- Do EFRAG CFSS members agree with the scope of the project as proposed by the IASB? If not, do you consider that there is a topic that should be removed from, or included in, the scope of the project?
- Do EFRAG CFSS members consider that the IASB should explicitly address issues that arise in specific type of industries, including banks and insurance companies?