IFRS in Focus

IASB proposes new Standard titled *General Presentation and Disclosures*

Contents

Background

The proposed amendments

Transitional provisions, effective date and comment period

This *IFRS in Focus* outlines the proposed new IFRS Standard *General Presentation and Disclosures* set out in Exposure Draft ED/2019/7 of the same title, published by the International Accounting Standards Board (IASB) in December 2019.

- The new Standard, if finalised, would replace IAS 1 *Presentation of Financial Statements*, carrying forward many of the requirements in IAS 1 unchanged and complementing them with new requirements.
- Key changes in the profit or loss statement would include:
  - Income and expenses would have to be categorised as operating, investing, financing.
  - An entity would have to provide three additional mandatory subtotals (operating profit or loss, operating profit or loss and income from integral associates and joint ventures, and profit or loss before financing and income tax).
  - Entities would be required to present their analysis of operating expenses using the method (by nature or by function) that provides the most useful information. A list of indicators would be provided to help entities assess the method that provides the most useful information.
- In the statement of financial position, entities would be required to separate goodwill from intangible assets and to distinguish integral associates and joint ventures and non-integral associates and joint ventures.
- In the statement of cash flows, entities would no longer have a choice as to where to present cash flows from dividends and interest. Dividends and interest paid would be cash flows from financing activities, while dividends and interest received would be cash flows from investing activities.
- In the notes to the financial statements, an entity would have to disclose and explain unusual items (i.e. income and expenses with limited predictive value) in a single note.
- Information that constitutes management performance measures (MPMs) would be defined and entities would be required to disclose all MPMs used in a single note to the financial statements, accompanied by disclosures aimed at enhancing their transparency.
- The new Standard would be applied retrospectively. The IASB does not propose an effective date, however preparers would be given at least 18–24 months between finalisation of the new Standard and the initial application. Earlier application is proposed to be permitted.
- The comment period for the ED ends on 30 June 2020.

For more information please see the following websites:

www.iasplus.com

www.deloitte.com

Background

The ED forms part of the IASB's work on Better Communication in Financial Reporting that includes various projects that focus on the content and delivery of information in the financial statements. This includes projects on

- Primary Financial Statements, aimed to improve how information is communicated in the financial statements, with a focus on information in the statement of profit of loss. The ED is the result of the IASB's work on this project.
- Disclosure Initiative – Accounting Policies, aimed at developing guidance and examples to help entities apply materiality judgements to accounting policy disclosures. An Exposure Draft was issued in 2019.
- Disclosure Initiative – Targeted Standards-level Review of Disclosures, aimed at improving the way the Board develops and drafts disclosure requirements. An Exposure Draft is expected in the second half of 2020.
- Management Commentary, aimed at revising and updating the IFRS Practice Statement 1 *Management Commentary* by considering how management commentary provided outside the financial statement could better complement and support the financial statements. An Exposure Draft is expected in the second half of 2020.

The proposed requirements

General presentation and disclosure requirements

The IASB proposes to define the roles of the primary financial statements and the notes to help preparers of financial statements decide in which of those parts information should be provided.

The role of the primary financial statements is to provide a structured and comparable summary of an entity's recognised assets, liabilities, equity, income, expenses and cash flows, whereas the role of the notes is to provide further information necessary to understand the line items recognised in the primary financial statements and to supplement the primary financial statements with other information that is necessary to meet the objective of the financial statements.

An entity would use the description of the roles of the primary financial statements and the notes to determine whether financial information should be included in the primary financial statements or in the notes, if there are no explicit requirements in IFRS Standards.

With regard to aggregation, the new Standard would require items to be classified and aggregated on the basis of shared characteristics. Items that do not share characteristics would not be aggregated, unless they are immaterial.

A set of illustrative examples would accompany the new Standard to help stakeholders understand the proposals and illustrate how this can be applied in practice.

Statement(s) of financial performance

The new Standard would require an entity to classify income and expenses included in profit or loss into one of the following categories:

- Operating
- Investing
- Financing
- Integral associates and joint ventures
- Income tax
- Discontinued operations

Integral associates and joint ventures are those where the activities are closely related to the reporting entity's main business activities. Non-integral associates and joint ventures are those where the activities have little or no effect on the reporting entity's main business activities and the related share of profit or loss would be presented in the investing category in the profit or loss statement.

Foreign exchange differences would be presented in the same category of the statement of profit or loss as the income and expenses that give rise to the foreign exchange differences.

The new Standard would require an entity to present the following new subtotals in the statement of profit and loss:

- Operating profit or loss
- Operating profit or loss and income and expenses from integral associates and joint ventures
- Profit or loss before financing and income tax

If the proposals are finalised, a statement of profit or loss would have the following basic structure:

	Revenue	**Operating**
-	Operating expenses	
=	Operating profit or loss	
+/-	Share of profit or loss of integral associates and joint ventures	**Integral associates and joint ventures**
=	Operating profit or loss and income and expenses from integral associates and joint ventures	
+/-	Share of profit or loss of non-integral associates and joint ventures	**Investing**
+	Income from investments	
=	Profit or loss before financing and income tax	
+	Interest revenue from cash and cash equivalents	**Financing**
-	Expenses from financing activities	
-	Unwinding of discount on pension liabilities and provisions	
=	Profit or loss before tax	

Observation

In its deliberations leading up to the ED, the IASB considered requiring an 'earnings before interest and tax' (EBIT) subtotal. However, the IASB found that EBIT and similar subtotals are not comparable between entities, because of the diverse ways in which entities classify items between finance income and expenses and other income and expenses. Many calculations of EBIT also include some items of interest income or expense, which is incompatible with describing EBIT as a subtotal before interest. To avoid this, the IASB decided to propose "profit or loss before financing and income tax" as a required subtotal that serves a similar purpose as EBIT as it allows users of financial statements to compare entities independently of how they are financed.

Operating category

The IASB proposes to require an entity to classify income and expenses from its main business activities into an operating category and present an operating profit or loss subtotal in the statement of profit or loss. The operating category comprises income and expenses that are not classified as investing or financing, or are not included in income taxes or discontinued operations, in other words: operating profit or loss is defined as a residual.

Depending on the entity's main business activities, some types of income or expenses would be categorised differently for different entities. For example:

- Interest expenses are typically categorised as financing. However, they may be included in operating if an entity provides financing to customers as a main business activity. An entity that includes all expenses from financing activities in the operating profit or loss subtotal would not present a subtotal of profit or loss before financing and income tax.
- Interest income is typically categorised as investing. However, they are included in operating if an entity, in the course of its main business activities, invests in assets that generate a return independently of other entity resources or if they result from a significant balance of cash and cash equivalents and the entity's operations require such a balance.

Investing category

The IASB proposes to require entities to present an investing category in the statement of profit or loss that gives information about returns from investments that are generated individually and largely independently of other resources held by the entity. The category contains income and expenses from investments that are not classified as operating, including incremental expenses incurred generating income and expenses from investments.

Financing category

The IASB proposes to require an entity to classify income and expenses from assets and liabilities related to its financing into a financing category. An entity would include the following items in the financing category, unless they relate to the entity's main business activities (see above):

- Income and expenses from cash and cash equivalents
- Income and expenses on liabilities from financing activities
- Interest income and expenses on other liabilities

Financing activities are those involving the receipt or use of a resource from a provider of finance with the expectation that the resource will be returned to the provider of finance and the provider of finance will be compensated through the payment of a finance charge that is dependent on both the amount of the credit and its duration.

Before the financing category, an entity would present a profit or loss before financing and income tax subtotal in its statement of profit or loss. The proposed subtotal would include an entity's operating profit or loss; income and expenses from its integral associates and joint ventures; and income and expenses included in the investing category. The subtotal would exclude an entity's financing, income tax and discontinued operations.

Observation

Although the categories have the same labels, the IASB is not seeking full alignment between the categories in the statement of profit or loss and those in the statement of cash flows. The IASB has intentionally defined the investing categories in the two statements with different objectives. For example, cash flows from property, plant and equipment are included in the investing category in the statement of cash flows, but income and expenses from those assets would generally be included in the operating category in the statement of profit or loss.

Analysis of operating expenses

The new Standard would clarify that entities would either use the nature of expense method or the function of expense method when presenting the analysis of expenses included in operating profit or loss. An entity would be required to use the method that provides the most useful information.

In determining this, an entity would consider their key components or drivers of profitability, which method most closely matches the way the business is managed and how management reports internally to the board or key decision makers, industry practice, and whether the allocation of expenses to functions would be so arbitrary that it would not provide a sufficiently faithful representation of the line items presented.

A mix of both methods would be prohibited.

Statement of financial position

The IASB decided to propose to require an entity to present goodwill separately from intangible assets as its characteristics as an asset that is not identifiable and is measured only as a residual are sufficiently different to those of intangible assets.

In line with the proposals for the profit or loss statement, an entity would be required to present investments in integral associates and joint ventures separately from investments in non-integral associates and joint ventures.

Observation

The IASB is currently conducting a project on Goodwill and Impairment. As part of that project, the IASB is exploring whether it should require an entity to present a subtotal of equity before goodwill in its statement of financial position. This is expected to be one of the topics in the upcoming Discussion Paper on Goodwill and Impairment.

Statement of cash flows

The IASB also proposes consequential amendments to IAS 7 *Statement of Cash Flows*. In particular, when using the indirect method to determine operating cash flows, an entity would start with its operating profit or loss subtotal. This would limit the number of adjustments that are currently required to derive this figure.

Furthermore, an entity would no longer have a choice as to how to classify dividends and interest. For most entities, the new Standard would require the following:

- Dividends and interest paid would be cash flows from financing activities
- Dividends and interest received would be cash flows from investing activities

An entity would classify as cash flows from investing activities dividends received from associates and joint ventures accounted for using the equity method. Cash flows in respect of investments in integral associates and joint ventures would be presented separately from cash flows in respect of investments in non-integral associates and joint ventures.

Entities that provide financing to customers as a main business activity or invest in the course of their main business activities in assets that generate a return individually and largely independently of other resources held by the entity would instead refer to the classification of the income and expenses corresponding to such cash flows in the statement of profit or loss.

Notes to the financial statements

Unusual income and expenses

The IASB proposes to define unusual items as income or expenses with limited predictive value, i.e. 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.

An entity would, in a single note covering all unusual income and expenses, disclose the following:

- The amount of each item of unusual income or expense recognised in the period
- A narrative description of the transactions or other events that gave rise to that item and how it satisfies the definition of unusual
- The line item(s) in the statement(s) of financial performance in which each item of unusual income and expense is included
- An analysis of the included expenses using the nature of expense method, when an entity presents an analysis of expenses in the statement of profit or loss using the function of expense method

It is proposed to clarify that income and expenses from the recurring measurement of items measured at current value would not normally be classified as unusual.

Observation

It is important to note that income or expenses are classified as unusual based on expectations about the future rather than past occurrences. Therefore, it is possible for income or expenses similar to income or expenses reported in previous reporting period(s) to be classified as unusual.

Management performance measures

The IASB proposes to define management performance measures (MPMs) as subtotals of income and expenses that are used in public communications with users of financial statements, complement totals or subtotals in the IFRS Standards, and communicate to users of financial statements management's view of an aspect of an entity's financial performance. Subtotals that are defined in IFRS Standards would not be considered MPMs.

It is proposed that an entity disclose MPMs and all related information in a single note. That note would include a statement that the MPMs provide management's view of an aspect of the entity's financial performance and are not necessarily comparable with measures with a similar description provided by other entities.

In addition, an entity would disclose the following for each MPM:

- A description of why the MPM communicates management's view of performance including an explanation of how the MPM is calculated and how it provides useful information about the entity's performance
- A reconciliation between the MPM to the most directly comparable IFRS-total or subtotal
- The income tax effect and the effect on non-controlling interests for each item disclosed in the reconciliation, including how the tax effect is determined

If an entity changes the calculation of an MPM, introduces a new MPM or removes a previous MPM, an entity would explain the change, addition or removal and its effects, including its reasons for changing, adding or removing it.

The IASB is not proposing to entirely prohibit presentation of MPMs in the statement(s) of financial performance as this might otherwise prevent entities from complying with the requirement to present line items, headings and subtotals that are relevant to an understanding of the entity's financial performance. However, the IASB expects that only few MPMs would meet the criteria for presentation as a subtotal.

To restrict the circumstances in which such measures may be presented on the face of the profit or loss statement, it is also proposed to prohibit presenting MPMs in columns in the statement(s) of financial performance. In the IASB's view, presentation in columns would give these measures undue prominence.

Observation

The IASB considered but rejected describing operating profit or loss before depreciation and amortisation as EBITDA as users have no consensus about what EBITDA represents. Consequently, EBITDA may meet the definition of MPM.

However, the IASB proposes to include "operating profit or loss before depreciation and amortisation" in the list of subtotals defined by IFRS Standards. It would therefore not represent an MPM.

Transitional provisions, effective date and comment period

Should the new Standard be finalised, the IASB proposes that an entity applies the new Standard retrospectively in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

The IASB does not propose an effective date, but proposes to set the effective date so that the new Standard is applied after a transition period of 18–24 months starting on the date of publication. Earlier application is proposed to be permitted.

The comment period for the ED ends on 30 June 2020.

Further information

If you have any questions about the Exposure Draft *General Presentation and Disclosures*, please speak to your usual Deloitte contact or get in touch with a contact identified in this *IFRS in Focus.*

Key contacts

Global IFRS Leader
Veronica Poole
ifrsglobalofficeuk@deloitte.co.uk

IFRS Centres of Excellence

Americas		
Argentina	Fernando Lattuca	arifrscoe@deloitte.com
Canada	Karen Higgins	ifrsca@deloitte.ca
Mexico	Miguel Millan	mx_ifrs_coe@deloittemx.com
United States	Robert Uhl	iasplus-us@deloitte.com
Asia-Pacific		
Australia	Anna Crawford	ifrs@deloitte.com.au
China	Gordon Lee	ifrs@deloitte.com.cn
Japan	Shinya Iwasaki	ifrs@tohmatsu.co.jp
Singapore	James Xu	ifrs-sg@deloitte.com
Europe-Africa		
Belgium	Thomas Carlier	ifrs-belgium@deloitte.com
Denmark	Jan Peter Larsen	ifrs@deloitte.dk
France	Laurence Rivat	ifrs@deloitte.fr
Germany	Jens Berger	ifrs@deloitte.de
Italy	Massimiliano Semprini	ifrs-it@deloitte.it
Luxembourg	Martin Flaunet	ifrs@deloitte.lu
Netherlands	Ralph Ter Hoeven	ifrs@deloitte.nl
Russia	Maria Proshina	ifrs@deloitte.ru
South Africa	Nita Ranchod	ifrs@deloitte.co.za
Spain	José Luis Daroca	ifrs@deloitte.es
Switzerland	Nadine Kusche	ifrsdesk@deloitte.ch
United Kingdom	Elizabeth Chrispin	deloitteifrs@deloitte.co.uk