

STAFF PAPER

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REG IASB Meeting

Project	Clarifications to IFRS 8 <i>Operating Segments</i> arising from the post-implementation review		
Paper topic	Two sweep issues: consistent information about reportable segments and increasing the number of line items		
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Purpose of the paper

1. The Board discussed recommended amendments to IFRS 8 *Operating Segments* in May 2015 in response to the feedback received in the post-implementation review of IFRS 8. The Board decided to proceed with seven amendments to IFRS 8.¹
2. Staff is in the process of drafting the Exposure Draft of the proposed amendments. Questions have arisen about two of the seven potential amendments during the drafting process. The purpose of this paper is to ask the Board these questions. The two amendments concerned are:
 - (a) consistent identification of reportable segments; and
 - (b) increasing the number of reported line items.

Consistent identification of reportable segments

3. The Board decided to include guidance in the amendments to emphasise that, when management appropriately identifies operating segments, the application of IFRS 8 facilitates the consistent description of the entity in all presentations,

¹ <http://media.ifrs.org/2015/IASB/May/IASB-Update-May-2015.pdf>

including presentations to investors, in the management commentary and the operating segment disclosures. The Board aimed to address the concerns of investors and regulators about cases in which financial statements and management commentary identify different segments.

4. The Board's decision was that the amendment should describe a desired outcome. We think the amendment would be more effective if it included a requirement, and did not merely describe a desired outcome. We describe our recommended requirement in paragraphs 7-16 of this paper and ask if the Board agrees.

Increasing the number of reported line items

5. The Board decided to provide additional guidance about the type of information that is most useful to investors, such as information about non-cash expenses, non-recurring items and other line items that affect future cash flows. The Board aimed to address the feedback of those investors who thought that internally reported line items did not always provide them with the information they needed to make comparisons among entities.
6. The Board's decision was to provide guidance about the type of information that is useful to investors. We think the amendment would be more effective if the Board included an explicit permission for an entity to disclose additional line items if this helps the entity to meet the core principle of the Standard. We describe our recommended requirement in paragraphs 17-37 of this paper and ask if the Board agrees.

Consistent identification of reportable segments

Background

7. When the Board issued IFRS 8 in 2006, it expected management commentary and other reported information, including presentations to investors, to be based on a management approach that would be consistent with that shown in the operating segment information in the financial statements.
8. The feedback from the PIR informed us that when the basis of segmentation used in the financial statements agrees with the management commentary and financial

presentations, this results in cross-validation of the three sets of data and adds depth to the information provided. However, when the segment information and management commentary are prepared on different bases, both investors and regulators expressed concern at the difference. Further, a number of regulators reported to us that they investigate instances where the basis of segmentation differs between the financial statements and the management commentary.

Issue

9. Staff's original recommendation to the Board was that it should add additional guidance to the Standard to remind preparers that the Board expects the management commentary and other reported information to be based on the management approach that is consistent with the operating segment information shown in the financial statements. The intention behind the recommendation was to increase the consistency of the reported segments between the financial statements and the management commentary and other reported information.
10. When preparing the draft of the proposed amendments to IFRS 8 we became concerned that this amendment relating to the consistency of reported segments might not achieve the intended outcome because it is a reminder of the benefits of consistency and not a requirement.

Staff analysis

11. We think that to effect a change in response to the concerns heard in the PIR, the Board should add a requirement to the Standard rather than just remind preparers of the benefits of greater consistency to users of financial statements.
12. IFRS Standards set the requirements for financial statements and not for the management commentary or other reported information. Consequently we do not think that the Board can mandate consistency of reported segments between the financial statements and the management commentary or other reported information. Instead we recommend that the Board requires an explanation in the financial statements of any differences between the reported segments included in the financial statements and the reported segments included in the management commentary or other reported information.

13. The term ‘other reported information’ that was included in our original recommendation was in response to concerns heard through the PIR about inconsistencies in reported segments between the financial statements and presentations to analysts. We are concerned that the term ‘other reported information’ is broad and open-ended.
14. Consequently we recommend that the Board limits the explanation of differences in reported segments to segment information that is included in the management commentary, or other parts of the entity’s annual report. Although the term ‘annual report’ is not defined in IFRS Standards, we think that it is sufficiently well understood, especially by listed entities which are the focus of IFRS 8. We also note that this term has been used in a number of IFRS Standards, for example in IFRS 15 *Revenue from Contracts with Customers* and IAS 1 *Presentation of Financial Statements* as well as in Appendix A to the Basis for Conclusions on IFRS 8².

Staff recommendation

15. We recommend that the Board amends IFRS 8 to require an entity to explain why the reported segments in the financial statements differs from that included in the management commentary or other parts of the entity’s annual report.
16. Such an explanation will help users understand the relationship between the bases of segmentation in the financial statements and in the management commentary or other parts of the entity’s annual report when these are different.

Question 1 – requirement to explain the difference in reported segments

Do you agree that the Board should amend IFRS 8 to require an entity to explain why the reported segments in the financial statements differs from that included in the management commentary or other parts of the annual report?

² *Background information and basis for conclusions of the US Financial Accounting Standards Board on SFAS 131*

Increasing the number of reported line items

Background

17. Paragraph 23 of IFRS 8 requires an entity to disclose specified amounts³ about each reportable segment, if the specified amounts are:
 - (a) included in the measure of segment profit or loss and *are reviewed by the chief operating decision maker*; or
 - (b) *otherwise regularly provided to the chief operating decision maker*, even if not included in the measure of segment profit or loss. [emphasis added]
18. Paragraph 24 of IFRS 8 contains a similar disclosure requirement for specified amounts that are included in the measure of segment assets.
19. Some respondents to the PIR thought that disclosure of these specified items was not always sufficient to provide them with the information they needed to make comparisons among entities. Many investors wanted the Board to mandate particular line items – or, using the terminology of IFRS 8, ‘specified amounts’ – for disclosure.
20. The Board decided not to add line items to the disclosure requirements in IFRS 8 because:
 - (a) mandating the disclosure of line items that are not used in internal decision-making would go against the management approach used in IFRS 8;
 - (b) it would be difficult to decide which line items should be mandated because some line items are more relevant for some sectors than for others;

³ Paragraph 23 of IFRS 8 requires to disclose the following specified amounts:

(a) revenues from external customers; (b) revenues from transactions with other operating segments of the same entity; (c) interest revenue; (d) interest expense; (e) depreciation and amortisation; (f) material items of income and expense disclosed in accordance with paragraph 97 of IAS 1 *Presentation of Financial Statements*; (g) the entity’s interest in the profit or loss of associates and joint ventures accounted for by the equity method; (h) income tax expense or income; and (i) material non-cash items other than depreciation and amortisation.

- (c) additional disclosure would be burdensome to preparers if it included line items that are not already presented and reviewed internally; and
- (d) mandating an extended list of line items for disclosure could result in an increase in less relevant, 'boilerplate' disclosures.

21. Instead, the Board agreed with the staff's original recommendation to provide additional guidance about the type of information most useful to investors.

Issue

22. Staff's expectation behind the original recommendation was that preparers would present more relevant information about operating segments if the Board reminded them about what information is useful to investors and why.

23. During the drafting process and discussions with Board members, we identified three questions about the Board's decision to provide additional guidance about the type of information most useful to investors:

- (a) Is it permissible for segment information disclosed in financial statements to include additional information that is not reviewed by or regularly provided to the chief operating decision maker?
- (b) Should the Board permit or require entities to disclose such additional information that is not reviewed by or regularly provided to the chief operating decision maker if it helps to meet the core principle of IFRS 8?
- (c) How does 'the *type of information* that is useful for investors' reconcile with IFRS 8, given that IFRS 8 uses a 'specified amounts' approach for its disclosure requirements?

Staff analysis

24. We start our analysis with the core principle of IFRS 8 (paragraphs 1 and 20):

An entity shall disclose information to enable users of its financial statements to evaluate the nature and financial effects of the business activities in which it engages and the economic environment in which it operates.

25. However, IFRS 8 also refers to the ‘management approach’, ie the requirements of IFRS 8 are based on the way that management regards the entity, focusing on information about the components of the business that management uses to make decisions about operating matters.⁴ This approach is demonstrated in the disclosure requirements of paragraphs 23 and 24, ie the specified amounts must be disclosed if they ‘are reviewed by or otherwise regularly provided to the chief operating decision maker’.

Core principle and management approach

26. The first question is whether segment information disclosed in financial statements may include information that is not reviewed by or regularly provided to the chief operating decision maker?
27. Another way of looking at this question is whether the specific requirements set out in paragraphs 23 and 24 of IFRS 8 merely support the application of the core principle in paragraphs 1 and 20 of IFRS 8 or whether they limit its application.
28. One view is that, because the core principle of IFRS 8 requires entities to disclose information that allows users of financial statements to evaluate the nature and financial effects of the business activities in which it engages and the economic environment in which it operates, the entity may provide more information than that specified in paragraphs 23 and 24 of IFRS 8.
29. An opposing view, however, is that providing such additional information is a departure from the management approach in IFRS 8. In other words, providing such additional information will represent a misrepresentation of what the chief operating decision maker actually reviews.
30. We think that IFRS 8 sets out the minimum requirements needed to meet the core principle of the Standard and that it may include additional information that is not reviewed by or regularly provided to the chief operating decision maker. We think that this would not only allow an entity to better meet the core principle of IFRS 8 but it would also be consistent with the more general requirements of paragraph 17 of IAS 1 that an entity shall ‘provide additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable users to

⁴ BC4 of IFRS 8.

understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance'.

Permit or require?

31. If the Board agrees that segment information may include information that is not regularly provided to the chief operating decision maker, the second question is whether the Board should require an entity to disclose information about its reportable segments beyond that specified in paragraphs 23 and 24 of IFRS 8 if this helps to meet the core principle in paragraphs 1 and 20 of IFRS 8?
32. If the Board added a requirement to IFRS 8 that an entity should disclose any additional segment information needed to comply with the core principle of the Standard this might lead to more line items being reported for each reportable segment. Consequently, some people might argue that including the requirement about additional information in IFRS 8 would enhance the application of the Standard's core principle.
33. We see the merits of this argument. However we think that requiring an entity to disclose information that is not reviewed by or otherwise regularly provided to the chief operating decision maker would be a departure from the management approach adopted in IFRS 8. This view is consistent with the Board's previous tentative decision as described in paragraph 20(a) of the paper.
34. Because we see benefits of entities providing additional segment information, whilst at the same time realising that IFRS 8 is based on the management approach, we recommend that the Board amends IFRS 8 to state that an entity is permitted to provide such additional information. In other words, we do not recommend that the Board requires an entity to disclose additional information that is not reviewed by or otherwise regularly provided to the chief operating decision maker.

Type of information useful for users of financial statements

35. The third question relates to the additional guidance about the type of information most useful to users of financial statements. It would be difficult to decide which line items should be mandated because some line items are more relevant to some entities than others. In other words, what is most useful depends on the activities

and economic environment of an entity. Both, ie the activities and economic environment of an entity, are already mentioned in the core principle of IFRS 8. In addition, paragraphs 23 and 24 of IFRS 8 already require disclosure of a broad range of information, including material items of income and expense disclosed to comply with paragraph 97 of IAS 1 and material non-cash items. Consequently, staff recommend the Board provide no additional guidance on the type of useful information in IFRS 8.

Staff recommendation

36. On the basis of the above analysis, we recommend that the Board amends IFRS 8 to state that:
- (a) an entity can disclose additional information about its reportable segments if this helps to meet the core principle in paragraphs 1 and 20 of IFRS 8; and
 - (b) this additional information may include information that is not reviewed by or otherwise regularly provided to the chief operating decision maker.
37. This permission would address concerns of users of financial statements, which they expressed during the PIR, because this permission would improve the quality of segment information for users of financial statements.

Question 2 – permission to disclose additional information

- (a) Do you agree that an entity may disclose additional segment information that includes information that is not reviewed by, or regularly provided to, the chief operating decision maker?
- (b) Do you agree to include in IFRS 8 an explicit permission to disclose such additional information if this helps to meet the core principle in paragraphs 1 and 20 of IFRS 8?
- (c) Do you agree that the Board should provide no additional guidance in IFRS 8 on the type of segment information that would be helpful to meet that core principle?