STAFF PAPER

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IASB® meeting

Project	**Primary Financial Statements**
Paper topic	Feedback summary—Users of financial statements

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This Agenda Paper was initially prepared for the Board's December 2020 meeting as Agenda Paper 21K. However, it was not discussed at that meeting. This Agenda Paper is identical to Agenda Paper 21K for the December 2020 Board meeting.

Objective

1. This paper analyses feedback from user comment letters and user outreach meetings on the proposals set out in the Exposure Draft *General Presentation and Disclosures*.

Key messages

2. All users expressed strong general support for the project. Most users expressed their appreciation to the Board for undertaking this project, for example saying that they expect the proposals will significantly enhance the value of financial statements for investors.

3. Users particularly welcomed the proposals on the structure of the statement of profit or loss, in particular a defined operating subtotal, and on management performance measures because of the enhanced comparability and transparency of financial information they would provide.

4. Many users asked for the Board to extend the scope of the proposals, in particular in relation to management performance measures, the statement of cash flows, segment reporting and interim reporting.

Structure of the paper

5. This paper is structured as follows:

   (a) summary of types of user feedback (paragraphs 6–9);

   (b) subtotals and categories in the statement of profit or loss (paragraphs 10–34);

   (c) equity-method accounted associates and joint ventures (paragraphs 35–45);

   (d) disaggregation principles (paragraphs 46–50);

   (e) analysis of operating expenses by nature or function (paragraphs 51–61);

   (f) unusual items (paragraphs 62–72);

   (g) management performance measures (paragraphs 73–85);

   (h) EBITDA (paragraphs 86–90);

   (i) statement of cash flows (paragraphs 91–99);

   (j) other comments (paragraphs 100–101).

Summary of types of user feedback

6. The Board received 13 comment letters from users:

   (a) eleven from representative groups; and

   (b) two from individual users or organisations (one sell-side, one buy-side).

7. In addition, between January 2020 and October 2020, the staff met with 32 individual or groups of users of financial statements to discuss feedback on the Exposure Draft. The users comprised:

   (a) CMAC;

   (b) 3 national standard setter user advisory groups;

(c) 10 representative groups of users; and

(d) 18 individual users, or a small number of users from the same or similar organisations (9 buy-side, 6 sell-side, 3 credit analysts).

8. The meetings lasted between 60 and 90 minutes. IASB staff gave a brief introduction to the main areas covered by the proposals on which we were hearing most differences in views, focusing in some jurisdictions on areas of specific interest in that jurisdiction. Those areas were defined subtotals, analysis of expenses in operating profit by function or nature, unusual items and management performance measures. Not all topics were covered in the same level of detail at all meetings.

9. The analysis in this paper includes the feedback from the comment letters and from the outreach meetings.

Subtotals and categories in the statement of profit or loss

10. The Exposure Draft proposed that an entity present the following new subtotals in the statement of profit or loss:

(a) operating profit or loss;

(b) operating profit or loss and income and expenses from integral associates and joint ventures; and

(c) profit or loss before financing and income tax.

11. In applying these proposed new subtotals, an entity would present in the statement of profit or loss income and expenses classified in the following categories:

(a) operating;

(b) integral associates and joint ventures;

(c) investing; and

(d) financing.

12. The operating category includes all income and expenses from an entity's main business activities. It excludes income or expenses classified in the other categories such as the investing category or the financing category.

13. The investing category includes returns from investments, that is, income and expenses from assets that generate a return individually and largely independently of other resources held by the entity. The investing category also includes related incremental expenses.

14. The financing category includes:

    (a) income and expenses from cash and cash equivalents;

    (b) income and expenses on liabilities arising from financing activities; and

    (c) interest income and expenses on other liabilities, for example, the unwinding of discounts on pension liabilities and provisions.

15. Because the operating category includes income and expenses from an entity's main business activities, it includes:

    (a) income and expenses from investments made in the course of an entity's main business activities; and

    (b) income and expenses from financing activities and income and expenses from cash and cash equivalents if the entity provides financing to customers as a main business activity.

16. The Board developed its proposals for the categories in the statement of profit or loss without trying to align classifications across the primary financial statements. Consequently, income and expenses classified in the operating, investing and financing categories in the statement of profit or loss do not necessarily correspond with the cash flows from operating, investing and financing activities in the statement of cash flows.

Operating profit subtotal

17. All user comment letters supported the proposal that entities should present a subtotal for operating profit or loss. They describe the role of operating profit in their analysis for example as 'an important starting point', 'a key measure', 'an essential indicator' and 'an integral component'. Many described the lack of such a defined subtotal as a significant and frustrating shortcoming in IFRS financial statements.

18. All user comment letters also agreed that the subtotal should be defined, saying that a lack of a definition hinders comparability.

19. Almost all user comment letters support defining the operating category as the default category, excluding defined items for investing and financing. They describe such an approach as straightforward and easy to understand. They regard it as robust because it removes management discretion and pragmatic because it would be impossible to develop a complete list of items to create a positive definition. Such robustness leads to greater comparability between entities.

20. A few user comment letters did not support defining operating profit as a residual. One such user suggested defining operating profit as 'income and expenses arising from main business activities, excluding unusual income and expenses', with the entity identifying what are its main business activities. The user argued that allowing the entity to identify its main business activities would provide more useful information. Another observed that the Board's research into operating profit definitions must have identified many common elements from entity-specific definitions, so the debate over any definition would only be about the uncommon elements.

21. Feedback from the outreach meetings with users on the operating subtotal was consistent with the comment letters. There was generally strong support for a defined structure for the statement of profit or loss. A few users specifically expressed support for the approach of defining investing and financing, leaving operating as the residual category. For example, one user observed doing so would reduce subjectivity and avoid frustrating past experiences with recurring items excluded from operating profit because they were described as non-recurring items.

22. However a few users at the outreach meetings expressed reservations about the approach. They described the approach as combining two aspects: (i) operating as the default category that includes everything that is not defined as investing or financing and (ii) inclusion in operating of investing and financing income and expenses when such income and expenses is generated by a main business activity. They suggested the latter aspect adds subjectivity and potential confusion over what is included in each category (see paragraph 24 of this paper for further discussion).

23. Some users made additional specific suggestions:

(a) a few users suggested operating profit should be reconciled to the amounts disclosed applying IFRS 8 *Operating Segments*;

(b) one user suggested any non-recurrent or items that might not be regarded as arising from an entity's main business activities should be disclosed;

(c) a few users suggested an alternative approach of creating a fourth category ('miscellaneous category' or 'non-core') in addition to the three categories of "operating", "investing" and "financing" set out by the Exposure Draft. This new category would include those income and expenses that are not included in either of the three other categories, and not included in unusual income and expenses. However, other users said this would complicate the profit and loss statement and expressed concern that entities would present such 'miscellaneous' or 'non-core' expenses into a non-operating category, where there is generally less scrutiny by users.

(d) one user comment letter suggested disclosure of which (and how much) of the operating costs reported in the current period are expected to result in a significant cash outflow in a future reporting period.

The investing category

24. Most user comment letters agreed in principle with the Board's proposals, but many have concerns over the identification of income and expenses generated in the course of the entity's main business activities, concerns also expressed at a few outreach meetings. They suggest that more guidance is needed to ensure that investment income is not inappropriately included in operating profit. For example, they suggest:

(a) explaining that minority holdings in entities in the same business activity are not generated in the course of the entity's main business activities;

(b) explaining that financial instrument transactions by a non-financial entity are not normally part of its main business activity, except when hedge accounting is applied; and

(c) giving guidance on how to classify income from an investment in a start-up entity that may evolve into a main business activity.

25. One user comment letter included an alternative view that the only subtotal that should be required is operating profit. Those supporting this approach suggest there is little benefit for non-financial companies to classify income and expenses not included in the operating category into other categories. Any other subtotals could be left as management performance measures, with the accompanying disclosures.

26. A few user comment letters asked for more guidance on the classification of incremental expenses.

27. Some user comment letters suggested additional disclosures:

(a) a description of the entity's main business activities, linked to the description of its business model in its annual report;

(b) what investments are made in the course of an entity's main business activities; and

(c) how the investing income links to amounts in the statement of financial position and to operating segments.

Profit or loss before financing and income tax and the financing category

28. Almost all user comment letters supported a required subtotal for profit or loss before financing and income tax, observing for example that it is 'a meaningful metric that may be particularly useful when comparing companies with similar operations and profit streams that are financed differently and/or subject to different tax jurisdictions and rates.' Comments from outreach meetings were also generally supportive of the proposed structure of the categories and subtotals. As noted in paragraph 25 of this paper, one user comment letter included an alternative view—that the only required subtotal should be operating profit.

29. Users raised some specific points (from comment letters and outreach meetings):

(a) a few users explicitly supported including the unwinding of the discounting of pension and decommissioning liabilities in financing, whereas some preferred it to be included in operating profit. A few stated they did not mind which category it was in as long as the disclosure was clear. Many did not express a view.

(b) one user asked for clarity on the location of the effect of changes in discount rates, impairment losses recognised applying IFRS 9 *Financial Instruments* and gains and losses on the disposal of financial assets measured at amortised cost.

(c) one user commented that inclusion of amounts determined applying IFRS 16 *Leases* for depreciation in operating profit or loss and for interest expense in financing distorted both operating and financing categories.

Inclusion of income and expenses from financing activities in operating profit if an entity provides financing to customers as a main business activity

30. All user comment letters supported including income and expenses from financing activities in operating profit if an entity provides financing to customers as a main business activity.

31. Many agreed with the option to include in operating profit either all income and expenses from financing activities or only that which relates to the provision of financing to customers. Many said that options were not ideal but regarded this option as the only viable approach. The same view was expressed at the few outreach meetings (with users of banks' statements) where this question was raised, but the users at those meetings said they expected banks would include all income and expenses from financing activities in operating profit. A few users noted that clear disclosure would be needed of the policy chosen and the amounts included in each category.

32. About half the users disagreed with the option, arguing that operating profit should include only income and expenses from financing activities relating to the provision of financing to customers. One user observed that the identification of such income and expenses would typically be clear, another that the identification might be subjective but it would not be arbitrary.

33. One user comment letter suggested some finance income recognised applying IFRS 15 *Revenue from Contracts with Customers* should be considered to be operating income when it is a key component of the contract;

34. Only one user comment letter commented on the proposals for income and expenses from cash and cash equivalents. That user agreed with the proposals in relation to financial institutions. However, for other entities, the user observed that investors rarely view balances of cash and cash equivalents as 'operating assets'. The user therefore suggested that the final standard instead introduces a rebuttable presumption that assumes that income and expenses from cash and cash equivalents are not part of the operating category. If that presumption is rebutted because it is evident that the income and expenses from cash and cash equivalents are mainly related to the provision of financing to customers, the entity should be required to include all related income and expenses in the operating category. The user argues that this modification would be easier to apply and would cause less divergence in application.

Equity-method accounted associates and joint ventures

35. The Board proposed to define 'integral associates and joint ventures' and 'non-integral associates and joint ventures', and to require an entity to classify its equity-accounted associates and joint ventures as either integral or non-integral to the entity's main business activities. The Board also proposed to require an entity to provide information about integral associates and joint ventures separately from that for non-integral associates and joint ventures. The Board proposed that an entity would be required to:

    (a) classify, in the integral associates and joint ventures category of the statement of profit or loss, income and expenses from integral associates and joint ventures, and present a subtotal for operating profit or loss and income and expenses from integral associates and joint ventures (paragraphs 53 and 60(b) of the Exposure Draft);

    (b) present, as cash flows from investing activities in the statement of cash flows, cash flows from investments in integral associates and joint ventures separately from the cash flows from investments in non-integral associates and joint ventures (proposed new paragraph 38A of IAS 7);

(c) present, in the statement of financial position, investments in integral associates and joint ventures separately from investments in non-integral associates and joint ventures (paragraphs 82(g)–82(h) of the Exposure Draft); and

(d) disclose, in the notes, information required by paragraph 20 of IFRS 12 for integral associates and joint ventures separately from non-integral associates and joint ventures (proposed new paragraph 20E of IFRS 12).

Split between integral and non-integral

36. Most user comment letters disagreed with the split between integral and non-integral proposed in the Exposure Draft. They thought the proposed split would require arbitrary judgements that would not capture the sometimes complex relationships between an entity and its associates and joint ventures. The resulting reporting would not be meaningful and could lead to a lack of comparability.

37. Some user comment letters indicated that although they did not agree with the proposals as set out in the Exposure Draft, users would be interested in information about how an entity thinks its equity-accounted associates and joint ventures fit within its business model. Some such users suggested additional guidance on the proposed split, to overcome the concerns about arbitrary judgements set out in paragraph 36 of this paper.

38. A few user comment letters suggested alternative approaches:

(a) include no requirements on how to split associates and joint ventures because an entity can develop a management performance measure to present a split of the results if necessary;

(b) define integral as the most important associates and joint ventures; or

(c) reform equity accounting.

Required subtotal for operating profit or loss and income and expenses from integral associates and joint ventures

39. Most user comment letters disagreed with the proposals to have a subtotal for operating profit or loss and income and expenses from integral associates and joint ventures. They argued that such a subtotal would not provide useful information for financial statement analysis because:

   (a) it combines amounts that exclude tax and financing effects with amounts that include such effects; and

   (b) the net amounts from the equity-accounted associates and joint ventures would distort any analysis of gross margins or ratios such as return on capital employed.

40. Some of these users also stated that the inclusion of such a subtotal adds undue complexity to the structure of the statement of profit or loss.

41. A few user comment letters supported the subtotal saying that it would improve comparability.

42. Almost all user comment letters agreed that the results of equity-accounted associates and joint ventures should be excluded from operating profit for the reasons set out in paragraph 39 of this paper. A few users suggested requiring the results of all equity-accounted associates and joint ventures to be presented in a single line outside operating profit.

Disclosures

43. Many user comment letters requested more disclosures on associates and joint ventures. Some users that did not support presenting the proposed split in the statement of profit or loss did support such a split in the disclosures, and a few asked for disclosure of the reasons why an entity decided an associate or joint venture was integral or non-integral. Others suggested additional disclosure requirements, for example disclosure of separate pre and post-tax amounts or disclosures for each associate or joint venture individually.

Cash flow statement

44. Many user comment letters did not explicitly comment on the proposals for associates and joint ventures in the cash flow statement. A few user comment letters explicitly supported the proposals and a few explicitly disagreed, because of the subjectivity they perceived in making the distinction. One user comment letter suggested that the cash flows from integral associates and joint ventures should be in a separate 'operating subtotal', because that would be consistent with the approach proposed for the statement of profit or loss.

Feedback from outreach meetings

45. Feedback from the user outreach meetings was broadly consistent with the comment letters. All users who commented wanted income and expenses from equity-accounted associates and joint ventures shown separately from operating profit. There were mixed views on whether the split between integral and non-integral would be helpful—some said it could be helpful, especially if entities explained how they had applied the distinction, but others were concerned that management could misuse the distinction to manage results. Some were neutral, indicating good disclosures on equity-accounted joint ventures and associates generally were more important than the split or presentation in the statement of profit or loss.

Disaggregation principles

46. The Board proposed to describe the roles of the primary financial statements and the notes. The Board also proposed principles and general requirements on the aggregation and disaggregation of information; the principles would be applicable both to presentation in the primary financial statements and disclosures in the notes. The Board proposed specific requirements to provide more useful information about aggregations of dissimilar immaterial items that are currently often described as 'other'.

47. Most user comment letters agreed with the description of the roles of the primary financial statements and the disaggregation principles, a few explicitly commenting

that the latter should resolve the problem of amounts described as 'other'. A few user comment letters argued that the principles were too vague and needed to be strengthened to achieve more and better disaggregation. Some of these suggested a quantitative threshold should be used to determine when an item should be disaggregated and shown separately.

48. A few user comment letters disagreed with the proposals on aggregations of dissimilar immaterial items, commenting 'If immaterial items have been aggregated, we do not see how their disaggregation and disclosure in the notes would be useful. In particular, the disclosure of immaterial information can obscure the more relevant information and undermine the usefulness of the financial statements.'

49. A few user comment letters commented that the statement of financial position is often insufficiently disaggregated at present and encouraged the Board to consider more minimum line items for that statement.

50. One user comment letter asked for the description of the roles of the primary financial statements to be linked more closely to the *Conceptual Framework for Financial Reporting*, for example by noting the financial statements should be comparable and understandable. One user comment letter commented that the description of the roles of the primary financial statements inappropriately limits the role of financial statements in determining distributions.

Analysis of operating expenses by nature or function

51. The Board proposed to continue to require entities to present in the statement of profit or loss an analysis of operating expenses using either the nature of expense method or the function of expense method.

52. The Board proposed the method presented should be the one that provides the most useful information to users of financial statements and that entities should not present line items mixing the two methods, with the exceptions of required line items. In addition, the Board proposed to describe the factors to consider when deciding which method of operating expense analysis should be used.

53. An entity that presents an analysis of operating expenses using the function of expense method in the statement of profit or loss would also be required to disclose in a single note an analysis of its total operating expenses using the nature of expense method.

54. Many user comment letters supported the use of a single method of analysis of operating expenses in the statement of profit or loss. A few user comment letters supported allowing a limited mix of methods in the statement of profit or loss, specifically to enable those entities using a functional analysis to separately present specific items analysed by nature, for example amortisation, depreciation and impairments. Feedback from outreach meetings was similar—some users expressed strong support for requiring the use of a single method, to avoid incomplete line items, but some users expressed concern about the interaction with regulations in specific jurisdictions and one user explicitly expressed concern about the loss of trend information if a mixed analysis in the statement of profit or loss was prohibited.

55. Some user comment letters did not support the proposal for an entity to determine which method provides the most useful information. They argued that this proposal effectively gives an entity a free choice because the criteria for adopting a method are not sufficiently robust, with a resulting loss of comparability. Most of these users expressed a preference for a requirement to give an analysis by nature in the statement of profit or loss.

56. A few user comment letters supported the proposal for an entity to determine which method provides the most useful information but also asked for a matrix so that each line item of expenses analysed by nature was analysed by function, or vice versa. One user comment letter suggested such a matrix be presented in the statement of profit or loss, unless the cost of doing so was prohibitive. Again, feedback from outreach meetings was similar—some users expressed interest in a matrix approach whereby a by nature analysis would be given of each functional line item, or a partial matrix. The suggestions for a partial matrix varied—some wanted a by nature analysis of cost of sales, others wanted only some by nature items, for example depreciation and amortisation split across functions.

57. One user comment letter suggested an entity should be required to disclose the reason for its choice of method of analysis of operating expenses in the statement of profit or loss. Another suggested the analysis of operating expenses should also be given at a reporting segment level in the segment note.

58. Almost all user comment letters (except a few that did not express a view) supported disclosure of an analysis by nature in the notes if the analysis in the statement of profit or loss were by function, as did the feedback in many outreach meetings.

59. A few user comment letters and discussions at outreach meetings suggested a requirement to disclose an analysis by function in the notes if the analysis in the statement of profit or loss were by nature, because the functional analysis enables gross profit information to be compared. A few user comment letters suggested requiring all entities to provide an analysis by nature in the statement of profit or loss and an analysis by function in the notes.

60. A few users acknowledged there could be allocation problems with a functional analysis. One user comment letter requested more guidance on identifying an entity's functions and how costs should be allocated to them. This was consistent with feedback from outreach meetings where some users commented on the lack of comparability of items included in cost of sales, and hence of gross margin. Some suggested disclosure should be required of how expenses are allocated to functions.

61. Some user comment letters suggested the analysis by nature should be given in interim as well as annual reports. Disclosure in the interim reports, and in the segment analysis, was also raised in some outreach meetings.

Unusual items

62. The Board proposed introducing a definition of 'unusual income and expenses'; and proposed requiring all entities to disclose unusual income and expenses in a single note. The Board also proposed application guidance to help an entity to identify its unusual income and expenses.

Should the Board define unusual items?

63. Almost all user comment letters agreed that the Board should define unusual items. There was also a high-level of support expressed in the outreach meetings. Users explained that they wish to identify recurring or normalised earnings but have to rely on voluntary disclosures by an entity to do so. A definition of unusual items that have to be disclosed will result in greater consistency in reporting.

64. A few user comment letters and a few comments from the outreach meetings disagreed, saying instead that entities should always give disclosures about individually material items of income and expenses. Hence, the Board should strengthen the general requirements on disaggregation rather than try to define unusual items (see paragraph 46 of this paper).

Is the proposed definition appropriate?

65. Many user comment letters agreed with the proposed definition, but a few of these thought further guidance would be helpful, for example on whether the amount described as unusual should be the whole amount or just the unusual portion, or what was meant by not recurring for 'several future years'. Some thought it important to emphasise that unusual items could be income as well as expenses.

66. Other user comment letters suggested changes to the definition:

    (a) many thought the definition should focus on the nature of the event causing the item of income or expenses, rather than on whether the item was expected to recur in the future. They gave as examples the costs of a restructuring that was expected to take several years, or costs of a disaster that were expected to last for several years.

    (b) a few questioned whether an item which by nature was not unusual should ever be regarded as unusual because of its size.

    (c) a few thought the definition should be restricted to 'significant' unusual items.

67. Feedback from the outreach meetings on the definition of unusual items was also mixed:

(a) many buy-side analysts and credit analysts supported the narrow definition in the Exposure Draft because they welcomed the consistency it would bring but some preferred a broader definition, for example including items that might occur over more than one period;

(b) many sell-side analysts preferred a broader definition (or an approach strengthening the disaggregation requirements so that all material items would be appropriately disclosed), commenting that additional information about large or lumpy expenses was always useful in forecasting future cash flows;

(c) some analysts of both types specifically wanted the definition to cover expected multi-period expenses—sometimes it is the nature of the item that is important rather than whether it will recur next period;

(d) a few users thought the definition was unclear and more guidance was needed; and

(e) One user pointed out the definition needed to capture information useful for both forecasting future cash flows and assessing management's use of resources.

Should unusual items be presented in the statement of profit or loss or in a single note?

68. Some user comment letters explicitly said that unusual items should not be presented in the statement of profit or loss. They want to preserve the structure of operating, investing and financing. They observed that including unusual items in the statement within that structure would make the statement too complex, especially if there were unusual items in all three categories. They also observed that an entity could create a management performance measure excluding unusual items from operating profit (or other subtotal) if it wished.

69. In contrast, some user comment letters and comments from outreach meetings explicitly supported the presentation of unusual items in the statement of profit or loss. A few noted that if there were a single line item for unusual items presented after operating profit, operating profit would become the measure of normalised profit they have been asking for. One user suggested unusual items should be presented in

the statement of profit or loss, analysed as a nature or function item consistent with the entity's analysis of operating expenses. One user suggested a columnar approach to presenting unusual items in the statement of profit or loss.

70. Some user comment letters explicitly supported disclosure in a single note, commenting that it was helpful to know where to find the information, and that it would enable users to better determine whether the items were non-recurring. One user comment letter said it would be more helpful to include disclosure about an unusual item in the note for the relevant line item.

Disclosures

71. Many user comment letters and comments from the outreach meetings welcomed the proposed disclosures related to unusual items. Some suggested additional disclosures:

    (a) why are the items unusual;

    (b) a five year history of unusual items, or disclosure of whether unusual items this period occurred in the previous five years;

    (c) comparative amounts, even if the items were not unusual in the comparative period; and

    (d) disclosure of tax and non-controlling interest related to unusual items because that would enable them to calculate adjusted earnings per share when the unusual item is not included in management performance measure.

72. One user comment letter opposed the proposed removal of paragraph 97 of IAS 1 that requires the separate disclosure of the nature and amount of material items of income and expenses, noting that not all material items would meet the definition of unusual items.

Management performance measures

73. The Board proposed to introduce a definition of 'management performance measures' and require an entity to disclose them in a single note. Management performance measures are subtotals of income and expenses that:

(a) are used in public communications outside financial statements;

(b) complement totals or subtotals specified by IFRS Standards; and

(c) communicate to users of financial statements management's view of an aspect of an entity's financial performance.

74. An entity would comply with the general requirements in IFRS Standards for information included in financial statements when it provides these measures; for example, each performance measure must faithfully represent an aspect of the financial performance of the entity. However, the Board does not propose additional restrictions on management performance measures, such as only allowing an entity's management to provide measures based on amounts recognised and measured in accordance with IFRS Standards (paragraphs BC155 and BC158–BC162).

75. The Exposure Draft also proposed to specify the information an entity would be required to disclose about management performance measures, including a reconciliation to the most directly comparable total or subtotal specified by IFRS Standards.

Information to be included in the financial statements

76. All but one user comment letter supported the proposals to include information about management performance measures in the financial statements. This level of support was also demonstrated in the outreach meetings where many users expressed very strong support for the proposals on management performance measures. For example, one user stated this is the 'most important IASB proposal in 20 years'. Some users encouraged the Board not to be deterred by possible pushback on the proposals from preparers. Reasons given for the support are that the proposals respond to requests from users over many years. Management performance measures have a significant influence on how an investor perceives an entity's results. The proposals would result in transparency over what is included in management performance measures and would provide some discipline over their use:

(a) many users welcomed the fact that the information about management performance measures would be audited. Some buy-side analysts stated in particular that having audited information on management performance measures would be a big improvement from a stewardship perspective, particularly in those jurisdictions where there is a link between such measures and management remuneration.

(b) some users commented that the requirements to explain any changes in management performance measures would add discipline on the consistent use of the measures and transparency over any changes.

(c) many users specifically commented that having the management performance measures in a single note would be helpful.

77. In contrast, one user comment letter disagreed with the proposals, describing them as ‘mission creep’, and some users at one outreach meeting questioned whether such information was appropriate for the financial statements.

78. Many user comment letters supported the proposal that the information about management performance measures would be provided in a single note, observing that would address one of the biggest practical challenges that users face currently with alternative performance measures being presented in multiple locations or documents. A few user comment letters suggested that the note should be required to be presented immediately below the statement of profit or loss.

79. All the user comment letters that supported the inclusion in the financial statements of information about management performance measures supported the proposed disclosures of reconciliations to an IFRS subtotal and the reasons why the performance measure communicates management’s view of performance.

80. A few user comment letters emphasised the importance of the tax and non-controlling interest effects, with one suggesting that disclosure of different tax effects on items of income and expenses should be improved more generally. In the outreach meetings, some users explicitly stated that the tax and non-controlling interest information would be useful but a few indicated they were not particularly concerned whether that information was given.

81. A few user comment letters suggested additional disclosures related to management performance measures:

(a) disclosure of management performance measures at a segment level;

(b) a history of the measures for some period (suggestions included 3, 5, or 10 years);

(c) disclosure of a management performance measure in the year after to ceases to be a management performance measure, with an explanation of why it has ceased to communicate management's view of performance; and

(d) any link between a management performance measure and executive remuneration plans.

Definition of management performance measures

82. Many user comment letters and comments from user outreach meetings disagreed with the proposed definition of management performance measures, arguing that the definition should be extended to cover:

(a) measures that are not subtotals of income and expenses, for example free cash flows and ratios such as return on capital employed—such measures are equally important and in need of the same improvements to transparency, consistency and auditing; and

(b) IFRS subtotals—although a reconciliation to an IFRS subtotal is not necessary, the description of why the measure communicates management's view of performance is useful. A few users specifically highlighted EBITDA as an example.

83. In contrast, a few user comment letters and comments from outreach meetings accepted the scope of the definition for practical reasons, acknowledging there could be difficulties in extending the scope. They supported the proposed scope as a good first step.

84. One user comment letter suggested excluding from the scope items required to be disclosed by other bodies, for example regulators. Another user comment letter suggested the scope should be limited to items disclosed in the interim or annual reporting packages in the same period.

85. One user comment letter suggested that alternative performance measures that were not management performance measures should be identified as such in the document in which they were used. That would alert users to the different requirements applying to the measures. The user acknowledged that achieving such disclosure would require the involvement of parties other than the IASB.

EBITDA

86. The Board does not propose to define earnings before interest, tax, depreciation and amortisation (EBITDA) in this project. The Board considered, but rejected, describing operating profit or loss before depreciation and amortisation as EBITDA. However, the Board proposed to exempt from the disclosure requirements for management performance measures a subtotal calculated as operating profit or loss before depreciation and amortisation (paragraph 104(c) of the Exposure Draft).

87. Most user comment letters agreed that the Board should not define EBITDA, agreeing that entities that wished to use such a measure could create one as a management performance measure that could be reconciled to the Board's proposed specified subtotal of operating profit before depreciation and amortisation. Comments from a few outreach meetings with sell-side analysts also supported not defining EBITDA—they commented it is not a useful measure of performance.

88. In contrast, some user comment letters argued that the Board should define EBITDA. They observed that EBITDA is a measure used almost universally by both preparers and users. By virtue of its use in key leverage and valuation ratios, it is also used to compare between companies. They noted that a standard definition of EBITDA would not prevent entities from diverging via the publication of their own management performance measure 'adjusted EBITDA' if they wished, but it would provide a comparable benchmark against which users could evaluate the entity-adjusted measure. Comments from a few outreach meetings with buy-side analysts and credit analysts indicated they also thought a standardised measure similar to EBITDA would be useful (especially for credit analysts), for similar reasons, but they added that operating profit or loss before depreciation and amortisation would fill that role.

89. A few user comment letters disagreed with paragraph BC173 of the Exposure Draft, which explains that an EBITDA measure that equalled operating profit or loss before depreciation and amortisation would not be a management performance measure. They observed it is useful for financial statement users to know what measures management uses as key performance indicators, even if they happen to match subtotals defined by IFRS Standards.

90. A few user comment letters suggested that the proposed IFRS specified subtotal 'operating profit or loss before depreciation and amortisation' should be amended to also exclude impairments because they said that would make it closer to how most users define EBITDA. One user comment letter suggested that 'operating profit or loss before depreciation and amortisation' should be a required line item. One user comment letter suggested that 'operating profit or loss before depreciation and amortisation' should be required to be disclosed by reporting segment.

Cash flow statement

91. The Board proposed requiring an entity to use the operating profit or loss subtotal as the starting point for the indirect method of reporting cash flows from operating activities.

92. The Board also proposed reducing the presentation alternatives currently permitted by IAS 7 and requiring that, in the statement of cash flows, an entity classifies interest and dividend cash flows as shown in Figure 1.

Figure 1—Classification of interest and dividend cash flows

Cash flow item	Most entities	Specified entities[1]
Interest paid	Financing	Accounting policy choice, possible location depends on the classification of the related income and expenses in the statement of profit or loss
Interest received	Investing	
Dividends received	Investing	
Dividends paid	Financing	

Comment letters

93. Almost all user comment letters supported using operating profit as the starting point for the indirect method reporting cash flows from operating activities. They observed doing so would result in a better link between operating cash flows and operating profit and a shorter cash flow statement.

94. A few user comment letters disagreed, arguing that net profit was a more intuitive place to start, easier for users to understand and consistent with US GAAP.

95. Most user comment letters supported removing the options in IAS 7 over the presentation of interest and dividend cash flows, observing that options are confusing and hamper comparability. A few users preferred to include interest paid in operating, wanting to maintain consistency with US GAAP. One user observed that including in investing activities all dividends received from equity-accounted associates and joint ventures is inconsistent with the split proposed in the statement of profit or loss for income and expenses from such associates and joint ventures.

96. Some user comment letters asked the Board to align the categories in the statement of profit or loss and the statement of cash flows. Suggestions to achieve this included presenting income and expenses or cash flows from all equity-accounted associates and joint ventures in a single line, or splitting the investing category in the cash flow

[1] An entity that provides financing to customers as a main business activity or in the course of its main business activities invests in assets that generate a return individually and largely independently of the entity's other resources.

statement into two categories, one for capital expenditure and one for other investing cash flows.

97. Many user comment letters asked for a comprehensive review of IAS 7 as a separate project, to achieve more consistency and alignment with the statement of profit or loss and statement of financial position.

98. One user comment letter asked for investment entities that satisfy specific conditions to be exempt from producing cash flow statements, consistent with US GAAP.

Outreach meetings

99. These proposals were discussed in detail at relatively few of the meetings with users. Comments were:

    (a) one group of users gave mixed views on the starting point of the reconciliation to operating cash flows:

        (i) some see the purpose of the cash flow statement is to compare with the statement of profit or loss. They fear a loss of information about cash flows relating to amounts outside operating profit if operating profit is the starting point. They also think the starting point should be aligned with US GAAP.

        (ii) others think the cash flow statement is for understanding actual cash flows for purpose of forecasting and therefore they prefer comparability across entities and support the IASB proposals.

    (b) there were mixed views on the treatment of interest and dividends. Some supported removing the options but a few supported a choice. Some explicitly stated they preferred them to be included in operating, but a few explicitly supported the proposal to include them in financing. One suggested it would be helpful to align the categories in the statement of cash flows and the statement of profit or loss.

    (c) some users expressed strong support for a separate project on the cash flow statement. One user suggested eliminating the options in IAS 7 relating to the presentation of discontinued operations and the use of the direct or indirect method.

Other comments

100. Many users suggested the Board start work on other projects:

(a) many users suggested a comprehensive review of IAS 7;

(b) many users suggested further work linking presentation of items in the statements of financial performance, financial position and cash flows, and segment disclosures;

(c) many users suggested improving the disclosures required by IAS 34 *Interim Financial Reporting*;

(d) some users suggested improving disclosure of tax effects, including the effect of different tax rates on items of income and expenses and the tax included in equity-accounted associates and joint ventures;

(e) a few users suggested a review of the use of other comprehensive income and recycling;

(f) a few users suggested a review of IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*;

(g) one user suggested a review of reporting of unrealised gains and losses;

(h) one user suggested developing proposals for the presentation and disclosure of supply chain finance; and

(i) one user suggested revising IFRS Standards generally because they are not grounded in principles of business, investment or the legal frameworks underpinning accounts.

101. A few users commented on the increasing use of digital communication, for example the need to have consistent inputs into information providers such as Bloomberg.

Question for the Board
Does the Board have any comments or questions on the feedback discussed in this paper?