Primary Financial Statements

Project summary

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This paper has been prepared for discussion at a public educational meeting of the US Financial Accounting Standards Board (the FASB) and the International Accounting Standards Board (the IASB). It does not represent the views of the boards or any individual member of either board. Comments on the application of IFRS® Standards or US GAAP do not purport to set out acceptable or unacceptable application of IFRS Standards or US GAAP. Technical decisions are made in public and reported in FASB Action Alert or in IASB Update.
Agenda

- Project objective and scope 3-10
- Tentative IASB decisions – improving disaggregation 11-16
- Future topics for discussion 17-20

Questions for the FASB are on slides 10, 16 and 20
Project objective and scope
Central theme of the IASB’s work

Better Communication in Financial Reporting

Content
- Primary Financial Statements
- Disclosure Initiative
- Management Commentary

Delivery
- IFRS Taxonomy

Financial statements

Information outside the financial statements
Agenda Consultation
Respondents identified the project as a priority and recommended focusing on the statement(s) of financial performance.

Project timeline

July 2014
- Added to the IASB research agenda

2015
- IASB decision on project scope
  - Targeted improvements, mainly to the presentation of the statement(s) of financial performance

Dec 2016
- IASB discussions on topics in project scope

H1 2019
- Publish Exposure Draft or Discussion Paper
Problems with the statement(s) of financial performance

- Structure and content of statement(s) of financial performance varies even within the same industry
- Inconsistencies in calculation of subtotals, even within the same industry (e.g., treatment of associates/JVs)
- Insufficient disaggregation of information
- Presentation alternatives reduce comparability
- Some companies communicate performance mainly through Alternative Performance Measures
Increasing use of alternative performance measures indicates that financial statements are losing their relevance.

Alternative performance measures can provide relevant information.

Alternative performance measures are misleading investors.

By presenting more alternative performance measures in financial statements, transparency and discipline will be enhanced and measures will be audited.

The IASB should develop mechanisms to allow preparers to present more alternative performance measures in financial statements.
Comparability vs flexibility – feedback

- Lack of comparability negatively affects usefulness of IFRS financial information
- Due to lack of comparability, users prefer financial statements ‘standardised’ by data aggregators
- Recognition and measurement should be principles-based but presentation should be more structured

- Flexibility allows preparers to tell their own story
- As long as necessary information is available in the notes, primary financial statements can be concise
- IFRS Standards should keep their principles-based nature
### Scope of the project

#### Statement(s) of financial performance
- Subtotals & categories facilitating comparisons between entities:
  - Finance income/expense
  - Income/expenses from investments
  - Presentation of associates/JVs
- Management performance measures
- Better ways to communicate OCI

#### Statement of cash flows
- Eliminating classification options (interest/dividends)
- Consistent starting point for the indirect method
- Cash flows related to associates/JVs

### Improving disaggregation in financial statements

<table>
<thead>
<tr>
<th>Principles of disaggregation in financial statements</th>
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<tbody>
<tr>
<td>Disaggregation by nature and by function in the statement(s) of financial performance</td>
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<tr>
<td>Minimum line items in primary financial statements</td>
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<tr>
<td>Templates for primary financial statements</td>
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**All tentative decisions on project apply to non-financial entities only**
Question 1 for the FASB

• Before we discuss the IASB’s work on improving disaggregation, do the FASB members have questions or comments on the project scope or the IASB’s tentative decisions in other project areas (Agenda Paper 21A provides a comprehensive overview of the IASB’s tentative decisions)?
Tentative IASB decisions—Improving disaggregation
## Improving disaggregation

### Principles of disaggregation in the financial statements

- Develop **principles** for aggregation and disaggregation in the financial statements;
- Develop **guidance on the steps involved** in applying ‘classification’, ‘aggregation’ and ‘disaggregation’ when preparing financial statements.

### Disaggregation by nature/by function within the business profit subtotal

- **Describe** the by-nature method and by-function method
- **Develop guidance** for determining whether a by-function or by-nature method provides the **most useful information** to users (see slide 14)
- **Require additional information on the nature** of expenses when an entity uses the by-function method (see slide 15)

### Minimum lines items in primary financial statements

- Explore amendments to minimum lines items required in IAS 1

### Developing templates for primary financial statements

- Explore development of templates for a small number of industries.
Quantitative thresholds

• The IASB considered, but tentatively decided not to introduce quantitative thresholds to promote more disaggregation.

<table>
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<tr>
<th>Advantages</th>
<th>Disadvantages</th>
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<tr>
<td>• potentially ‘forces’ greater disaggregation, resulting in more relevant information</td>
<td>• may override materiality judgements</td>
</tr>
<tr>
<td>• more enforceable than qualitative requirements or principles</td>
<td>• it could be difficult for the IASB to develop quantitative thresholds</td>
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• Instead, the IASB asked the staff to explore whether principle-based guidance could be developed to encourage further disaggregation of large residual balances or ‘other’ balances.
Analysis of expenses in the statement(s) of financial performance

Determine whether by function or by nature method provides the most useful information.

Factors to consider:

- Which method provides best information about the key components or drivers of profitability?
- Which method matches internal reporting best?
- What is peer industry practice?
- Can allocation of expenses to functions faithfully represent those functions?
The IASB considered the following approaches for disclosing additional information in the notes when an entity uses a by-function approach in the statement(s) of financial performance:

A. require disaggregation by nature for each functional line item
   entity has flexibility to decide which natural components are disclosed

B. require disaggregation by nature for each functional line item
   IASB specifies which natural components should be disclosed

C. require additional information by nature at an entity level, not as a breakdown of each functional line presented

This is the IASB’s preferred approach
Question 2 for the FASB

• In the light of FASB’s work on disaggregation, do FASB members have thoughts or comments on the IASB’s preferred approach to disaggregation of functional line items on slide 15?
Future topics for discussion
Future topics for discussion

**Disaggregation**
- Industry-specific illustrative examples/templates
- Further guidance on disaggregation

**Financial performance**
- Guidance on the presentation and definition of EBITDA
- Disclosure of information about unusual or infrequently occurring items

Application of proposals to financial entities

First due process document—Discussion Paper or Exposure Draft?
The IASB will discuss application of project proposals to financial entities and decide whether to:

– apply the same principles to financial entities
– adjust the principles/specific provisions for application by financial entities
– scope out/have different principles for financial entities

Financial entities have been excluded so far (banks, insurers, investment entities, investment property companies, some conglomerates)
Question 3 for the FASB

• Do the FASB members have any thoughts or comments on the application of the respective projects to financial entities?
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