

# Primary Financial Statements

*Project overview*

September 2018

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# Agenda

2

Slides

Project background & overview

3–8

Tentative Board decisions

9–25

Statement(s) of financial performance

9–17

Statement of cash flows

18–20

Improving disaggregation

21–24

Remaining topics for Board discussion

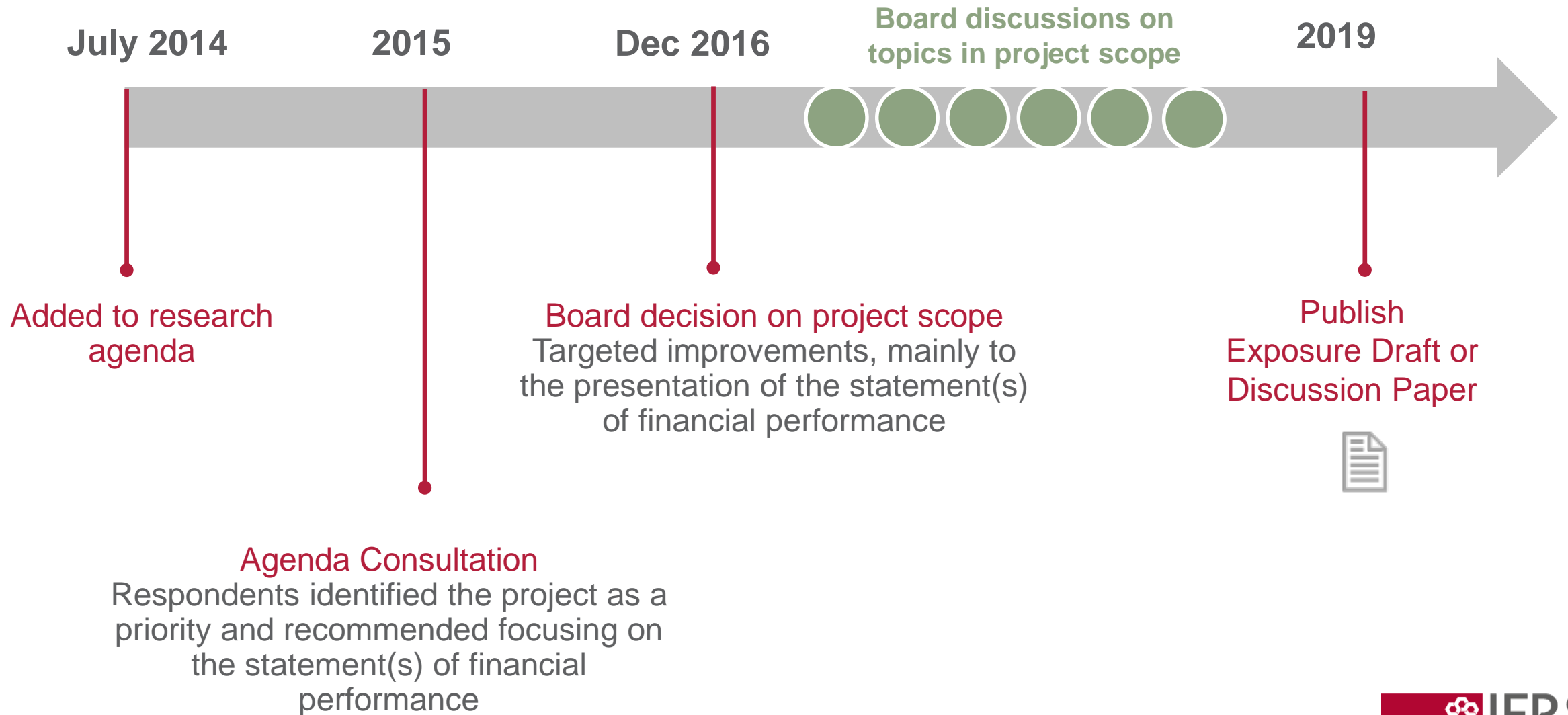
25–26

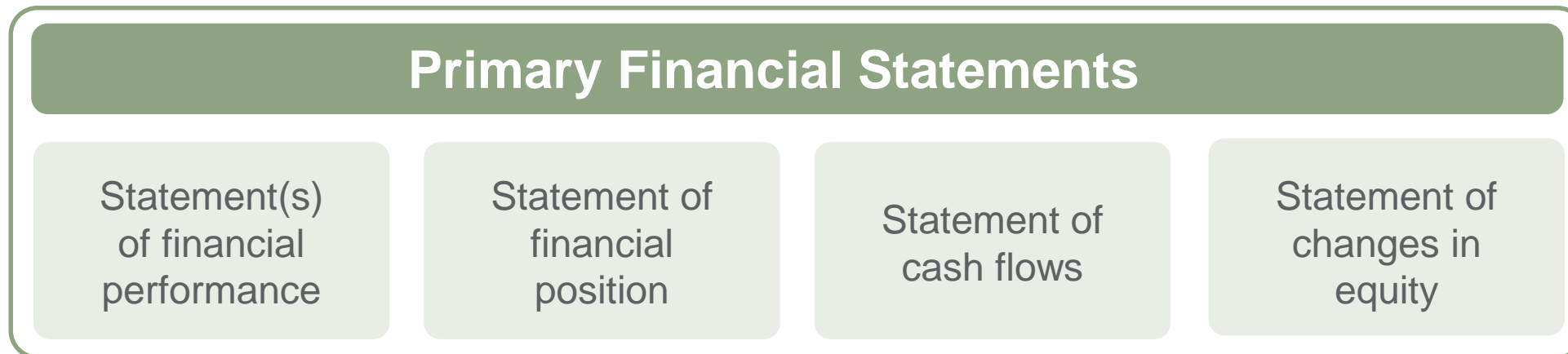
# Project background & overview

## Better Communication in Financial Reporting



# Project timeline





## Objective of the Primary Financial Statements project

Targeted improvements to the primary financial statements with a focus on the statement(s) of financial performance

# Stakeholder feedback and key project proposals



Statements of financial performance are not sufficiently comparable between different companies

Introduce **defined subtotals** in the statement(s) of financial performance



Non-GAAP measures can provide useful information, but transparency needs to be improved

Proposals on **Management Performance Measures**



Preparers

I need flexibility to tell my company's story

Proposals to **improve disaggregation**



There is insufficient disaggregation in financial statements

# Scope of the project

Statement(s) of financial performance
Subtotals & categories facilitating comparisons between entities: <ul style="list-style-type: none"><li>• Finance income/expense</li><li>• Income/expenses from investments</li><li>• Presentation of associates/JVs</li></ul>
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
Principles of disaggregation in financial statements
Disaggregation by nature and by function in the statement(s) of financial performance
Presentation of unusual/infrequently occurring items
Minimum line items in the primary financial statements
Templates for primary financial statements for a small number of industries



# Tentative Board decisions: statement(s) of financial performance

# Three defined subtotals in the statement of profit or loss

10

## 1 Profit from consolidated entities, before investing, financing and income tax (business profit)

Excludes share of profit from ALL joint ventures and associates

## 2 Profit before investing, financing and income tax

- Excludes income/expenses from investments, which are defined as 'income/expenses from assets that generate a return individually and largely independently of other resources held by the entity'
- Excludes share of profit from non-integral joint ventures and associates

## 3 Profit before financing and income tax

Excludes finance income and expenses which include:

- expenses on liabilities arising from financing activities (definition based on existing definition of financing activities for the statement of cash flows)
- unwinding of discount on other liabilities (see illustrative example)



Defined  
bottom-up

# Presentation of associates and JVs



Preparer A

My associates and JVs are a part of my main business, so I want to include my share of their results in my key performance measures.

The share of associates' and joint ventures' profit is after financing and after tax so I want to analyse them separately.



User B

## Tentative Board decisions

Requirement to separately present 'integral' and 'non-integral' associates and joint ventures in statements of financial performance and cash flows.

Indicators for determining whether a joint venture or associate is 'integral' or 'non-integral'.

# Defined subtotals —illustration for general corporates

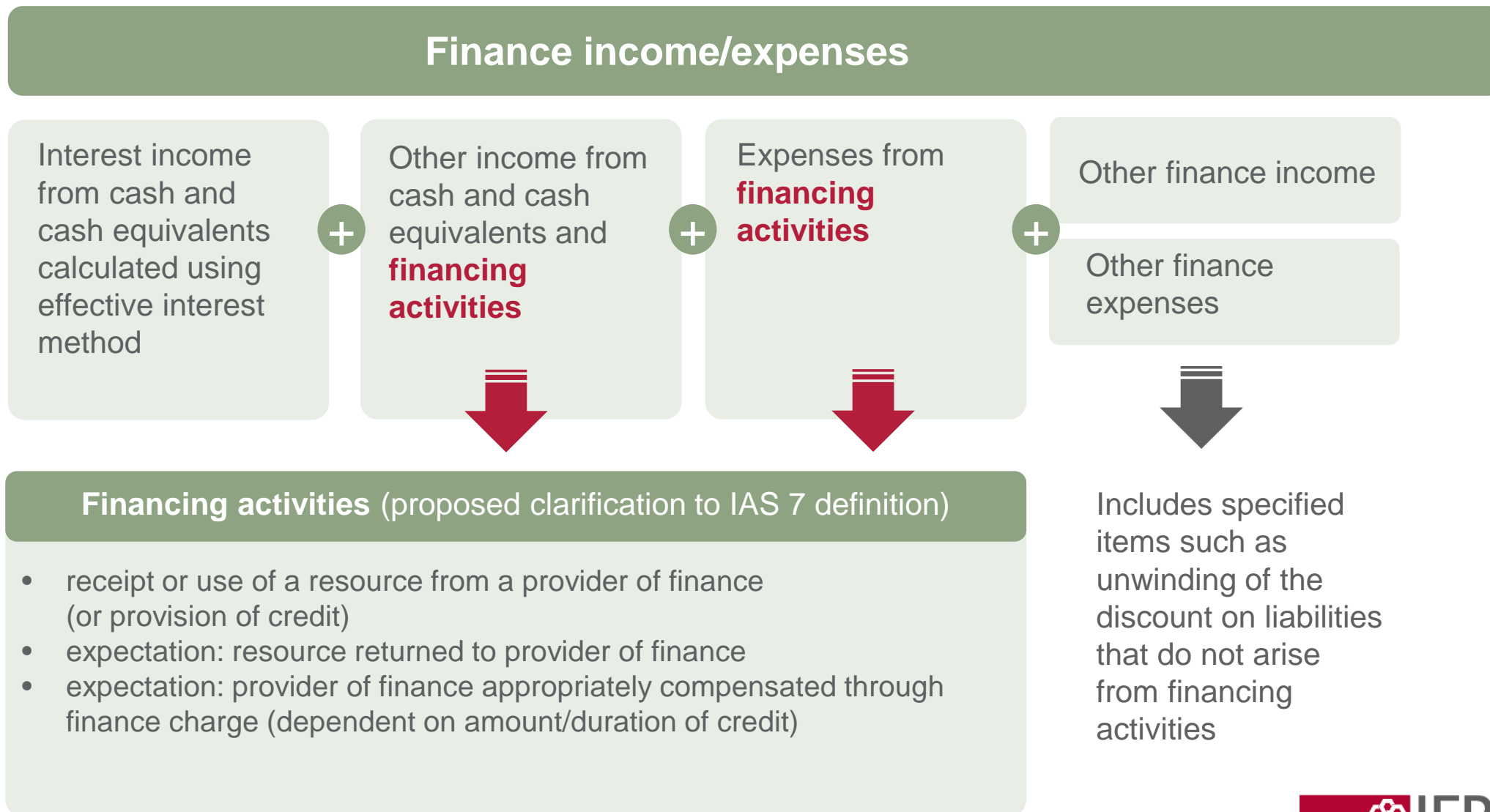
Revenue	10,000
Cost of goods sold	-4,000
Gross profit	6,000
Selling, general and admin costs (SG&A)	-3,000
<b>Business profit (from consolidated entities)</b>	<b>3,000</b>
Share of profit of <b>integral</b> joint ventures and associates	500
<b>Profit before investing, financing and income tax</b>	<b>3,500</b>
Changes in the fair value of financial assets	250
Dividend income	50
Share of profit of <b>non-integral</b> joint ventures and associates	100
<b>Profit before financing and income tax (EBIT)</b>	<b>3,900</b>
Interest income from cash and cash equivalents calculated using effective interest method	80
Other income from cash and cash equivalents and financing activities	20
Expenses from financing activities	-1000
Other finance income	50
Other finance expenses	-350
Profit before tax	2,700

Income/  
expenses from  
investments

Finance income/  
expenses

# Subtotals – finance income/expenses

13



# Scope of subtotals

	Business profit from consolidated entities Includes...		Profit before investing, financing and tax	Profit before financing and tax (EBIT)
General corporates	✓	no income or expenses relating to financing or investing activities	✓	✓
Entities whose main business activity is providing financing to customers (eg traditional banks)	✓	all income/expenses from financing activities and cash and cash equivalents	✓	✗
Entities who invest* in the course of their main business activity (eg investment property companies)	✓	income/expenses from investments made in the course of their main business activity	✗	✓
Entities whose main business activities are <u>both</u> investing* and provision of financing to customers	✓	<ul style="list-style-type: none"> <li>income/expenses from financing activities and cash and cash equivalents</li> <li>income/expenses from investments made in the course of their main business activity</li> </ul>	✗	✗
Entities with more than one main business activity incl. investing* <u>and/or</u> provision of financing to customers	✓	<ul style="list-style-type: none"> <li>income/expenses from financing activities and cash and cash equivalents related to the provision of financing to customers</li> <li>income/expenses from investments made in the course of their main business activity</li> </ul>	✓	✓

\*in assets that generate a return individually and largely independently from other resources held by the entity.



Preparers

I need flexibility to tell my company's story

## Tentative Board decisions

Entities are allowed to present 'Management performance measures' in the **notes**

MPMs **complement** subtotals or totals specified by IFRS Standards

**No specific constraints** on the calculation of MPMs



Users

Non-GAAP measures can provide useful information, but transparency needs to be improved

## Tentative Board decisions

Disclose a **reconciliation** in the **notes** between the MPM and the most directly comparable subtotal or total specified by IFRS Standards

**Describe why** the MPMs provide management's view of performance and **how** they have been **calculated**

Disclose the **effect of tax and non-controlling interests** separately for each reconciling item

**Label** MPMs in a **clear** and **understandable** way



# Management performance measures (3)

## Example of reconciliation

The management performance measure is presented in a **separate reconciliation in the notes**:

### Management performance measure reconciliation (extract from notes)

<b>Management performance measure</b>	<b>4,900</b>
Restructuring expenses for the closure of Factory A	-1,000
Litigation settlement related to court case B	-400
<b>Profit before investing, financing and income tax</b>	<b>3,500</b>

# Tentative Board decisions: statement of cash flows

# Statement of cash flows

- Eliminating **classification options** (interest/dividends):

Cash flows	Classification
Interest incurred on financing activities	Financing cash flows
Interest paid that is capitalised as part of the cost of an asset	Financing cash flows
Dividends paid	Financing cash flows
Dividends received	Investing cash flows
Interest received	Investing cash flows

- **Consistent starting point** for the **indirect method** for reporting operating cash flows: ‘profit before investing, financing and income tax’
- **Separate presentation** of cash flows from integral and non-integral **associates and JVs** within investing cash flows

# Statement of cash flows – illustration (indirect method)

Profit before investing, financing and income tax	X
Adjustments for:	
Depreciation	X
Share of profit from integral associate A	(X)
[...]	
Income taxes paid	(X)
<b><u>Net cash from operating activities</u></b>	<b><u>X</u></b>
Acquisition of integral joint venture X	(X)
Acquisition of non-integral associate Y	(X)
Dividends received from integral associate A	X
Dividends received from non-integral associate B	X
Purchase of property, plant and equipment	(X)
[...]	
<b><u>Net cash used in investing activities</u></b>	<b><u>(X)</u></b>
[...]	
<b><u>Net cash used in financing activities</u></b>	<b><u>(X)</u></b>
<b><u>Net increase in cash and cash equivalents</u></b>	<b><u>X</u></b>

Consistent starting point for the indirect method for reporting operating cash flows

Separate presentation of cash flows from integral and non-integral associates and joint ventures within investing cash flows

# Tentative Board decisions: improving disaggregation

# Disaggregation (1)



Users

Some entities present large, unexplained  
'other' balances

<b>Extract from the notes—Other expenses</b>	(In million €)
Losses on asset disposals	(200)
Foreign exchange losses	(100)
Other expenses	(700)
<b>Total 'Other expenses' presented in P&amp;L</b>	<b>(1000)</b>

A large part of 'other expenses' remains unexplained



Users

There is insufficient disaggregation in financial statements

Principles of disaggregation in the financial statements

Proposals to improve disaggregation of expenses by nature / by function

Guidance on unusual/infrequently occurring items

Consider expanding the list of required minimum line items in the primary financial statements

Consider templates for the primary financial statements for a small number of industries



Users

Information about unusual or infrequent items is useful but transparency needs to be improved.

## Tentative Board decisions

Requirement for all entities to disclose information about unusual or infrequent items in the notes irrespective of whether an entity chooses an MPM.

Note disclosure required to attribute unusual or infrequent items to line items in the statement(s) of financial performance.

Proposals to develop principles-based guidance for identifying unusual or infrequent items.



# Remaining topics for Board discussion

# Remaining topics for Board discussion

## Not discussed yet

Industry-specific illustrative examples/templates

Minimum line items

Guidance on the presentation and definition of EBITDA

First due process document—  
Discussion Paper or Draft?

## Further discussion of outstanding issues on:

Application of project proposals to financial entities

Disaggregation of information

Subtotals (incl. review of labelling)

Unusual/infrequent items

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