STAFF PAPER

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Prepared for Capital Markets Advisory Committee Meeting

Project	**Post-implementation review of IFRS 8 *Operating Segments***		
Paper topic	Use of segment disclosures		
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Purpose of this paper

1. The purpose of this paper is to ask for CMAC members' views on the usefulness of segment disclosures. Specifically, the staff would like to know whether:
   (a) the change in the basis of segmentation introduced with IFRS 8 *Operating Segments* provides better information for understanding the business and its performance (Issue 1 below); and
   (b) the use of management's own accounting line items provides better information for understanding the business and its performance (Issue 2 below).

Background

What is a post-implementation review?

2. The IASB reviews each new IFRS or major amendment approximately two years after global implementation.
3. Post-implementation reviews provide an opportunity to assess the effect of new requirements:
   (a) the goal of improving financial reporting underlies any new IFRS
   (b) important or contentious issues identified during development of the standard, or subsequently
   (c) unexpected costs or implementation problems encountered

4. The post-implementation review of IFRS 8 is the first that has been conducted by the IASB.

What was the effect of the change in accounting rules on how operating segments are reported?

5. The following table summarises the differences between IFRS 8 ("new rules") and IAS 14 *Segment Reporting* ("old rules"):

New rules	Old rules
• Segment operations on the basis of internal reporting used by chief operating decision maker. • Each reported item is measured on the basis used for management reporting, eg operating profit at budget costing rates.	• Segment operations by goods and services provided to customers or by geography. Matrix not allowed. • Each reported item is measured on the basis used in preparing the group's financial statements, ie IFRS.

Issue 1: Change in the basis of segmentation

6. We would like to understand whether CMAC members think that the change in the basis of segmentation provides better information for your understanding of the business and its performance. (See examples on the next few pages.)

Benefits	Concerns
• "Through management's eyes' perspective – highlights risks that are important – helps investors predict profits and cash flows – commentary, segments and presentations will all agree • Fewer single-segment companies • Basis of segmentation same as US GAAP requirements • Easier for interim reporting	• Inconsistent segments between companies • Frequent internal reorganisations may mean it is hard to see trends within a company • Geographical analyses not available

(a) Does it provide more relevant information for your analysis?

(b) Does it enable preparers to communicate more effectively with investors?

(c) Does the gain in entity-specific information outweigh the potential loss of comparability across entities?

Examples of operating segments from recent interim reports

7. We discussed telecommunications and construction at the February CMAC meeting. Consider two further sectors:

(a) Food products sector

(b) Pharmaceutical sector

Food products sector example

8. The basis of segmentation varies.

9. In our examples, Nestlé segment using a matrix basis and Associated British Foods disaggregate by product:

Nestlé **Associated British Foods***

Revenue (H1) CHF m	***2012***	***2011***	***Revenue (H1) £m***	***2012***	***2011***
Europe	7379	7521	Grocery	1813	1743
Americas	13419	12769	Sugar	1203	1024
Asia, Oceania, Africa	9192	7466	Agriculture	597	507
Waters	3555	3372	Ingredients	538	527
Nutrition	3831	3725	Retail	1615	1406
Other	6721	6151	Central		
Unallocated					
Total	**44097**	**41004**	**Total**	**5766**	**5207**

**ABF shows its UK reporting history by also providing an equivalent geographical analysis, which has been required since 1990 under UK GAAP.*

Questions for CMAC members

1. How important is comparability of segments between market participants?
2. Do you value the business segment-by-segment or at a 'total' level?

Pharmaceutical sector example

10. Participants in this market are very product focused (although we note that GlaxoSmithKline, not shown below, is split geographically):

Novartis **Roche**

Revenue (H1) $ m	***2012***	***2011***	***Revenue (H1) m CHF***	***2012***	***2011***
Pharmaceuticals	16094	16036	Pharmaceuticals	17409	16815
Vaccines and diagnostics	648	670	Diagnostics	5014	4856
Alcon	5189	5041	Corporate		
Sandoz	4271	4839			
Consumer health	1836	2356			
Total	**28038**	**28942**		**22423**	**21671**

All participants provide very detailed information not only by product type but often by individual compound within each product range.

Questions for CMAC members

3. How useful is segment information in this sector or is the valuation basis compound-by-compound?

Issue 2: Use of management's own accounting line items

11. We would like to understand whether CMAC members think that the use of management's own accounting line items provides better information for your understanding of the business and its performance. The following table summarises some of the main benefits and concerns we have heard from stakeholders.

Benefits	Concerns
• Reported lines items are those used by company decision maker – Tells you how they track performance	• Various definitions for 'operating results' – adjusted operating profit – EBITDA • Key lines may be omitted: – Cash generated – Working capital

Questions for CMAC members

4. Does the required use of internally-reported line items provide you with relevant information? Is the information more relevant than the use of standard, defined line items, previously required?
5. Recent analyses of European reported results identified up to 15 different ways of reporting operating results. Do these alternative line items, such as EBITDA, provide more useful information to investors than IFRS operating profit? Why?