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Accounting Standards Advisory Forum 3+4 March 2014: Agenda paper 6 D

Conceptual Framework:

How to move the section on presentation in the statement of comprehensive income forward

Preliminary remarks:

Strong support for the IASB undertaking the Framework project

Feedback Statement: Agenda Consultation 2011

- The Technical Work Programme: Conceptual Framework
Of particular importance will be how financial performance is presented, including consideration of the role of other comprehensive income (OCI) and recycling.
- Comments received:
The concept of profit or loss, the nature of OCI and the conceptual basis for recycling are given a high level of importance by the majority of respondents, across all jurisdictions. These topics are of particular relevance to investors.
- Our (IASB) responses:
We agree that performance, OCI and recycling are important and interlinked topics. We have already started work on the section of the *Conceptual Framework*.

Comment letters to the DP

- Overall strong support for undertaking the project
- Disappointment at the “catalogue of current conventions rather than concepts”
- Some views seen as a backward step from the existing Conceptual Framework

Presentation in the statement of comprehensive income cannot be discussed in isolation

Links to other parts of the Conceptual Framework

- Purpose and status

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Dr. h.c. Liesel Knorr (Präsidentin), Dr. Christoph Hütten (Vizepräsident)



Disagreement with DP 1.29 “IASB’s use only when developing new or revised IFRS, eg guidance on when an item of income or expense could be presented in OCI”

- Elements
Numerous calls for defining profit or loss as an element; calls for defining recycling adjustments
- Measurement
Taking an income statement perspective on measurement based on the proposed performance reporting model provides an alternative perspective that could be considered in developing the measurement chapter of the conceptual framework.
Should performance drive measurement or should measurement drive performance?
Measurement cannot be considered in isolation. In order to achieve useful performance reporting, it is essential to consider how remeasurements are presented in the financial statements.

General comments on section 8

- Disappointment that the DP does not define financial performance or identify the necessary and distinguishing characteristics for items to be presented in p&I or OCI
- DP does not establish a coherent principle for determining when it is more relevant to present an item in OCI rather than in profit or loss
- The CFW should require a total or subtotal for profit or loss. It is not adequate for the CFW to omit any material on its nature or purpose
- Offers of how to define / not define comprehensive income / profit or loss

“objective of the statement of profit or loss is to present income and expenses for the period in order to report the returns of the period, and facilitate an assessment of accountability and future returns”

“profit or loss represents an all-inclusive measure of irreversible outcomes of an entity’s business activities in a certain period.”

“OCI is the linkage factor that is used when the measurements relevant for the financial position differ from that relevant for financial performance”.

- Several calls for rather identifying components of income and expense than solely distinguishing between profit or loss and OCI; highlighting components such as operating result

Q 19: The IASB’s preliminary view is that the Conceptual Framework should require a total or subtotal for profit or loss. Do you agree? Why or why not?

Spectrum of views: on the surface wide spread agreement / variations of a theme with a few outlying; varying theories what should be presented in p&I / OCI



- Acknowledgement that p&l is used as primary performance metric; therefore net income should be retained
- Profit or loss needs to be robust and tinker-free
- The use of non-GAAP measures is seen as an indicator for difficulties with the current performance reporting; differing views if non-GAAP measures can be overcome
- Acknowledgement that currently the split between items to be presented in p&l and items to be presented in OCI is more of a political nature than based on a concept
- Strong disagreement by few as there is no integrated theory of presenting financial performance
- The current reporting model for net income and comprehensive income is seen as broken as it fails to provide a clean measure of operating income

Q 20: The IASB's preliminary view is that the Conceptual Framework should permit or require at least some items of income and expense previously recognised in OCI to be recognised subsequently in profit or loss, ie recycled. Do you agree? Why or why not? If you agree, do you think that all items of income and expense presented in OCI should be recycled into profit or loss? Why or why not? If you do not agree, how would you address cash flow hedge accounting?

Approach 1 – prohibit recycling

- Few proponents; recognising particular economic phenomena twice would lead to reporting items the second time around that do not meet the definition of income and expense

Approach 2 – retaining the concept of profit or loss and recycling

- Some would recycle all, some would indeed permit or require, some offer explanation with a background of timing or practical reasons

Cash flow hedge accounting

Few references as most go for approach 2 (ie recycling);

- “few will challenge the use of OCI as a parking spot for cash flow hedging instruments or foreign currency translation”
- “all forms of hedge accounting should be excluded from the CFW” / “conceptually inappropriate”

Q21: In this Discussion paper two approaches are explored that describe which item could be included in OCI: a narrow approach and a broad approach. Which of these approaches do you support, and why? If you support a different approach, please describe that approach and explain why you believe it is preferable to the approaches described in this Discussion paper.

Variety of responses: not to be dealt with in the CFW, disagreement and offer of other distinction (linkage, timing, meeting the objective), more analysis needed



What should the Conceptual Framework cover?

- Although there is broad support for maintaining a distinction between profit or loss and other comprehensive income, there is no overwhelming support for the IASB's decision not to define separate elements of income or expense to describe what should be reported in profit or loss and what should be reported in OCI or the proposed guidance addressing the distinction.
- There seem to be two different starting points for developing the objective of performance reporting: one focussing on operating profit for the period, the other on the cumulative amount of profit or loss for all accounting periods.
- Some would see timing differences arising from uncertainties about the outcome as the distinguishing characteristic between items in p&l or OCI; others would argue that this distinction is derived from the measurement in the statement of financial position rather than from the primary objective of p&l, ie reporting the performance of the reporting period. As an aside: the DP covers the role of uncertainty solely in the context of the definition of assets and liabilities and the recognition criteria; if uncertainty of outcome is a distinguishing characteristic of income and expense it might be worth acknowledging this aspect.
- Until there is a clearly articulated objective for the reporting of profit or loss (performance), there seems to be little chance of winning those over that start from a differing perspective.
- A quick fix, a readymade solution does not emerge from the comments received (other than postponing).
- There might be merit / mileage in further developing the independence of performance reporting vis-à-vis the measurement in the statement of financial position.
- Referring to the current framework does not solve a lot as the understanding seems to support diverse outcomes.

What should the Conceptual Framework not cover?

- As in all other areas of the CFW, it should not cover detailed elaborations, rather sound concepts.

What level of detail on particular issues?

It seems too early in the process to discuss the level of detail on particular issues as the issues to be solved first are likely very high level.

Conclusion: moving this section forward requires efforts and time. Not tackling the issues will haunt the development of standards.



Appendix

The following comment letters were provided by the IASB and consulted when developing the analysis:

- (1) CL 49 South African Institute of Chartered Accountants
- (2) CL 55 Financial Reporting Council UK
- (3) CL 93 Accounting Standards Committee of Germany
- (4) CL 94 Instituto de Contabilidad y Auditoria de Cuentas
- (5) CL 98 China Accounting Standards Committee
- (6) CL 118 Financial Reporting Standards Committee in South Africa
- (7) CL 129 Zambia Institute of Chartered Accountants
- (8) CL 133 Canadian Accounting Standards Board
- (9) CL 146 Group of Latin American Accounting Standard-Setters
- (10) CL 185 Accounting Standards Board of Japan
- (11) CL 186 Asian-Oceanian Standard-Setters Group
- (12) European Financial Reporting Advisory Group
- (13) Australian Accounting Standards Group

Further documents that found their way into the analysis:

- Tom Linsmeier: A Revised Model for Presentation on the Statement(s) of Financial Performance: Potential Implications for Measurement
- Hans Hoogervorst: Defining Profit or Loss and OCI...can it be done?