STAFF PAPER

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IASB Meeting

Project	**Disclosure Initiative**
Paper topic	Principles of Disclosure—Non-IFRS information

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Introduction

1. The reporting of non-IFRS information, and in particular the reporting of alternative performance measures (APMs), is currently the focus of much debate.[1] The fact that many preparers present alternative performance measures, and that data aggregators and analysts adjust numbers reported by entities, suggests that alternative measures can be useful. However, recent press articles on how some entities report these measures, and publication of guidelines by regulators about their use, paint them in a negative light.

2. Discussions about non-IFRS information are broader than merely covering alternative performance measures, and can also focus on whether information belongs in financial statements or in other reports. Decisions about the scope of information to be included in financial statements can have implications for whether information is audited and for where it is placed within an entity's package of general purpose financial reports.

[1] The term *alternative performance measure* is the most common descriptor. However, PwC uses the term adjusted performance measure.

Overview of the package of papers

3. For this meeting we have four papers covering the topic of **non-IFRS information**. This paper (11A) introduces the general topic of non-IFRS information to help us have a common understanding of what is meant by that term. This paper does not contain any questions for the IASB.

4. The papers that seek the preliminary views of the IASB are papers 11B and 11C. In those papers we discuss **alternative performance measures** and **other non-IFRS information** as follows:

   Paper 11B: Alternative Performance Measures

   (a) the disclosure of alternative performance measures;

   (b) depiction of non-recurring, unusual or infrequently occuring transactions and events; and

   (c) EBIT and EBITDA

   Paper 11C: Other Non-IFRS Information

   (a) non-IFRS information as part of a complete set of financial statements; and

   (b) placement of non-IFRS information inside financial statements.

   Paper 11D provides extracts from resource material that we reference in these papers:

   (a) an extract from IAS 1 on the objective of financial statements and fair presentation;

   (b) illustrative examples of additional disclosures in the primary financial statements that are not specified in IFRS; and

   (c) extracts from regulatory guidance regarding non-GAAP and non-IFRS measures with reference to the financial statements.

Scope of the discussion

5. This paper deals with the presentation and disclosure of 'non-IFRS information' in IFRS financial statements. This paper does not deal with the disclosure of 'non-IFRS information' in other financial reports such as management commentary, earnings releases and investor presentations.

6. We are aware that several national securities regulators have issued guidance dealing with the disclosure of some types of non-IFRS/non-GAAP information. Some of this guidance limits, or even prohibits, an entity from including non-IFRS financial information in the primary financial statements or the notes (see Paper 11D).

7. Any guidance that the IASB develops on non-IFRS information may have implications for existing regulatory guidance. However, we think that guidance on non-IFRS information in IFRS financial statements should be addressed by the IASB. Others have the same view. For example, in its response to ESMA's recent consultation on Alternative Performance Measures (APMs), the Investment Management Association (IMA) stated that:

> 'As regards applying the guidelines to the financial statements, we consider that such guidance should be for accounting standard setters such as the IASB to provide.'[2]

8. Bearing in mind this context, in this paper we consider and build on relevant regulatory guidance where possible.

Current IFRS

9. IAS 1 *Presentation of Financial Statements* provides that '[t]he application of IFRSs, with additional disclosure when necessary, is presumed to result in financial statements that achieve a fair presentation.'[3] Furthermore, with the aim of achieving fair presentation, IAS 1 states that additional disclosure is required when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's

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[2] IMA letter- ESMA Consultation Paper: 'Guidelines on Alternative Performance Measures', 13 May 2014

[3] IAS 1, paragraph 15 (reproduced in the appendix to this paper).

financial position and financial performance. (See Paper 11D for paragraphs 15-24 of IAS 1 regarding fair presentation and compliance with IFRSs.)

10. In addition, it is a specific requirement in IFRS that an entity provides:

    (a) additional line items, headings and subtotals in the statement of financial position when such presentation is relevant to an understanding of the entity's financial position (IAS 1.55);

    (b) additional line items, headings and subtotals in the statement(s) presenting profit or loss and other comprehensive income when such presentation is relevant to an understanding of the entity's financial performance (IAS 1.85); and

    (c) information in the notes that is not presented elsewhere in the financial statements, but is relevant to an understanding of any of them (IAS 1.112(c)).

11. The IASB has already published, in December 2014, narrow-focus amendments to IAS 1, clarifying the presentation of additional line items in the statements of financial position and statement of comprehensive income that are relevant to an understanding of the entity's financial position, and financial performance, respectively.

12. Furthermore, paragraph 49 of IAS 1 emphasises that an entity shall clearly identify the financial statements and distinguish them from other information in the same published document. There is no specific guidance on to what extent the entity may or may not embed information that is not required by an IFRS in a complete set of financial statements. For example, IFRS guidance does not address whether information that is relevant, but that is not within the scope of financial statements, can be embedded in financial statements.

The set of non-IFRS information

13. The *possible* set of non-IFRS measures is equal to APMs plus other non-IFRS information.

14. APMs tend to be presented in the (primary) financial statements and are additional subtotals or aggregations beyond those specified by IFRS. Other non-IFRS information is that which is not a part of the information required to be presented in the (primary) financial statements—ie they tend not to be recognised elements and could include things such as handset churn rates or measures of return on assets.[4] It is APMs that attract the most commentary and concern, although it is not always clear that all APMs are non-IFRS information.

Regulator and data aggregator definitions and descriptions

15. The Australian Securities & Investments Commission (ASIC) describes non-IFRS financial information as 'any financial information that is presented other than in accordance with all relevant accounting standards'. (See Paper 11D)

16. What constitutes non-IFRS/non-GAAP information has also been more narrowly interpreted. Specifically, we have heard non-IFRS information described as information that is not defined or specified in IFRS.[5] For example, when discussing 'earnings before interest, taxes, depreciation, and amortisation' (EBITDA), Standard &Poor's Ratings Services state:

> However, neither U.S. generally accepted accounting principles (GAAP) nor International Financial Reporting Standards (IFRS) define how companies should calculate EBITDA, which makes it a non-GAAP measure...[6]

17. Under this interpretation any measure not specified or defined in IFRS would be considered non-IFRS. We think this narrower interpretation is incorrect and unhelpful. This is because IFRS is principle-based and much of the information provided in a set of IFRS financial statements is not defined or specified. Others share this view. For example, the Canadian Securities regulator's guidance on non-GAAP financial measures states that:

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[4] These other non-IFRS measures might nevertheless be reported on the Statement of Comprehensive Income or in the notes.

[5] *Finance costs* are required to be presented in the Statement of Comprehensive Income but IFRS does not define the term. This would be considered to be an IFRS measure even though it is not defined.

[6] *EBITDA It's All in the Definition,* Standard & Poor's Rating Services *CreditWeek*, February 26, 2014, pg 17

> IFRS mandates certain minimum line items for financial statements and requires presentation of additional line items, headings and subtotals when such presentation is relevant to an understanding of an entity's financial position and performance. IFRS also requires the notes to financial statements to provide information that is not presented elsewhere in the financial statements, but is relevant to an understanding of them. Because IFRS requires such additional GAAP measures, they are not non-GAAP financial measures.[7]

18. Typical examples of information that is not defined or specified in IFRS are aggregation and disaggregation requirements that do not define or specify the items of disclosure individually, for example:

    (a) disclosure of additional subtotals and totals in the primary financial statements if they are relevant to an understanding of the entity's financial performance or financial position;

    (b) disclosure of material classes of assets and liabilities in the notes or in the primary financial statements, for example machinery as a component of property, plant and equipment; and

    (c) providing additional disclosures when compliance with the specific requirements in IFRSs is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance.

19. ESMA has recently described APMs as:

> '… any numerical measure of historical, current or future financial performance, which relates to the financial position, comprehensive income or cash flows, other than a measure defined by the applicable financial reporting framework.'[8]

20. ESMA's definition illustrates that APMs are seen as presenting an alternative to the measures that are defined (or specified) in IFRS. The definition also illustrates that a

[7] Canadian Securities Administrators' Staff Notice 52-306 (REVISED) - Non-GAAP Financial Measures and Additional GAAP Measures - *35 OSCB*, 2012, pg 1631

[8] ESMA consultation paper, [Draft] Guidelines—paragraph 21

measure that is not defined or specified in IFRS, even if it is in accordance with IFRS, could be viewed as an alternative performance measure. Examples include many of the subtotals commonly reported in an entity's financial statements that are not defined in IFRS, such as total assets, gross margin, operating profit and EBITDA.

21. The Canadian Securities Regulator uses a more targeted description to differentiate between non-GAAP financial measures (not presented in an issuer's financial statements) and additional GAAP measures presented under IFRS (presented in financial statements in accordance with IFRS). For the purposes of its guidance, it defines a non-GAAP financial measure as:

> '… a numerical measure of an issuer's historical or future financial performance, financial position or cash flow, that does not meet one or more of the criteria of an issuer's GAAP for presentation in financial statements, and that either:
>
> (i) excludes amounts that are included in the most directly comparable measure calculated and presented in accordance with the issuer's GAAP, or
>
> (ii) includes amounts that are excluded from the most directly comparable measure calculated and presented in accordance with the issuer's GAAP.'[9]

Summary

22. The guidelines developed by some regulators, and comments in the Press, show that there is no common notion of non-IFRS (non-GAAP) information. As we have explained, IFRS does not provide a list of all specific items that qualify as IFRS measures or information. In fact, IFRS **requires** an entity to disclose disclosure additional information that is 'relevant to an understanding of the entity's financial position and financial performance'. As you will see in Paper 11B, the debate about what constitutes an IFRS number is particularly contentious when we look at the Statement of Comprehensive Income and 'alternative performance measures'.

[9] Canadian Securities Administrators' Staff Notice 52-306 (REVISED) - Non-GAAP Financial Measures and Additional GAAP Measures - *35 OSCB*, 2012, pg 1630

23. What is clear however, is that all regulators, and the IASB, start off with the presumption that financial statements prepared using IFRS (or other applicable accounting framework) provide a fair presentation of an entity's performance and position. Put simply, revenue, for example, measured and presented in accordance with IFRS is presumed to provide better information than revenue measured and presented by an entity on some other basis. That presumption extends to expenses, profit or loss, total comprehensive income, assets, liabilities and so on.

24. General Purpose Financial Statements provide information that is standardised, neutral and verifiable and in many cases subject to external audit and regulation. Measures defined or specified by IFRS (or other applicable accounting framework) are particularly standardised, because the calculation and presentation has been independently prescribed and is widely known and understood.

25. In the next two papers (11B and 11C) we look at whether additional measures of performance and supplementary information could undermine the IFRS information.