

STAFF PAPER

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This paper has been prepared for discussion at a public meeting of the CMAC and GPF. The views expressed in this paper reflect the individual views of the author and not those of the IASB nor of the IFRS Foundation. Comments made in relation to the application of an IFRS do not purport to be acceptable or unacceptable application of that IFRS.

Purpose of the paper

1. The purpose of this paper is to get your feedback on the proposals in the IASB's Exposure Draft *Conceptual Framework for Financial Reporting* (the 'Exposure Draft') on the presentation of information about financial performance and, in particular, when income and expenses should be reported outside profit or loss—in other comprehensive income (OCI).
2. This paper provides the basis for the discussion about financial performance at this joint Capital Markets Advisory (CMAC) and Global Preparers Forum (GPF) meeting. Specifically, this paper:
 - (a) Sets out the discussion questions for the members of the CMAC/GPF.
 - (b) Provides the supporting context from the Exposure Draft to foster the discussion during the break-out session. To concentrate the discussion on the most significant aspects, the material provided omits some of the more detailed points discussed in the Exposure Draft.

Information about the Capital Markets Advisory Committee (CMAC) is available at <http://www.ifrs.org/The-organisation/Advisory-bodies/CMAC/Pages/CMAC.aspx>

Information about the Global Preparers Forum (GPF) is available at <http://www.ifrs.org/The-organisation/Advisory-bodies/Pages/Global-preparers-forum.aspx>

Questions for the members of CMAC and GPF

3. During this session we would like you to discuss the following questions:

Question 1—Description of the statement of profit or loss

Do you support the proposed description of the statement of profit or loss?
Why or why not? (See Appendix A paragraphs 7.2-7.4)

If you think that the Conceptual Framework should provide a definition of profit or loss, please explain why it is necessary and provide that definition.

Question 2—Reporting items of income or expenses in OCI

Do you agree with the proposals on the use of OCI? Do you think that they provide useful guidance for the IASB for future decisions about the use of OCI? Why or why not? (See Appendix A paragraphs 7.6-7.9)

If you disagree, what alternative do you suggest and why?

Background

4. The existing *Conceptual Framework* provides no guidance on reporting financial performance. The Exposure Draft proposes guidance to fill this gap:
- (a) it describes income and expenses included in the statement of profit or loss as the primary, although not only, source of information about an entity's financial performance for the period;
 - (b) it includes a rebuttable presumption that all income and expenses should be included in the statement of profit or loss;
 - (c) it describes the situations in which that presumption can be rebutted, resulting in income and expenses that are reported outside the statement of profit or loss—in OCI; and
 - (d) it includes a rebuttable presumption that income or expenses included in OCI will be reclassified to the statement of profit or loss in some future period and describes when that presumption can be rebutted.

5. To help you discuss the questions in this paper, Appendix A includes relevant paragraphs from the presentation and disclosure chapter of the Exposure Draft.
6. To provide you with additional background, Appendix B includes relevant paragraphs from the Basis for Conclusions on the Exposure Draft. It will help you to understand the IASB's reasons for the decisions that it made when developing the proposals on measurement
7. You will have approximately 45 minutes to discuss the questions in your group.

Appendix A – Extracts from the Exposure Draft

The following are extracts from the Exposure Draft *Conceptual Framework for Financial Reporting*.

Chapter 7—Presentation and disclosure

Paragraphs 7.1-7.18 not reproduced in this paper.

Information about financial performance

- 7.19 In order to communicate information about financial performance more efficiently and effectively, income and expenses in the statement(s) of financial performance are classified into either:
- (a) the statement of profit or loss, which includes a total or subtotal for profit or loss;¹ or
 - (b) other comprehensive income.
- 7.20 The purpose of the statement of profit or loss is to:
- (a) depict the return that an entity has made on its economic resources during the period; and
 - (b) provide information that is helpful in assessing prospects for future cash flows and in assessing management's stewardship of the entity's resources.
- 7.21 Hence, income and expenses included in the statement of profit or loss are the primary source of information about an entity's financial performance for the period.
- 7.22 The total or subtotal for profit or loss provides a highly summarised depiction of the entity's financial performance for the period. Many users incorporate that total or subtotal in their analysis of the entity's financial performance for the period and in their analysis of management's stewardship of the entity's resources, using it either as a starting point for further analysis or as the main indicator of the entity's financial performance for the period. Nevertheless, understanding an entity's financial performance for the period requires an

¹ This [draft] *Conceptual Framework* does not specify whether the statement(s) of financial performance comprise a single statement or two statements. For brevity, this [draft] *Conceptual Framework* uses the term 'statement of profit or loss' to refer both to a separate statement (showing a total for profit or loss) and to a separate section (showing a subtotal for profit or loss) within a single statement.

analysis of all recognised income and expenses (including income and expenses included in other comprehensive income), as well as an analysis of other information included in the financial statements.

7.23 Because the statement of profit or loss is the primary source of information about an entity's financial performance for the period, there is a presumption that all income and all expenses will be included in the statement of profit or loss. That presumption cannot be rebutted for:

- (a) income or expenses related to assets and liabilities measured at historical cost; and
- (b) components of income or expenses related to assets and liabilities measured at current values if the components are separately identified and are of the type that would arise if the related assets and liabilities were measured at historical cost. For example, if an interest-bearing asset is measured at a current value and if interest income is identified as one component of the change in the carrying amount of the asset, that interest income would need to be included in the statement of profit or loss.

7.24 The presumption that all income and all expenses will be included in the statement of profit or loss can only be rebutted if:

- (a) the income or expenses (or components of them) relate to assets or liabilities measured at current values and are not of the type described in paragraph 7.23(b); and
- (b) excluding those income or expenses (or components of them) from the statement of profit or loss would enhance the relevance of the information in that statement for the period.

When this is the case, those income or expenses (or components of them) are included in other comprehensive income.

7.25 One example of when income and expenses will be included in other comprehensive income is when a current value measurement basis is selected for an asset or a liability for the statement of financial position and a different measurement basis is selected for determining the related income and expenses in the statement of profit or loss.

7.26 If income or expense are included in other comprehensive income in one period, there is a presumption that it will be reclassified into the statement of profit or

loss in some future period. That reclassification occurs when it will enhance the relevance of the information included in the statement of profit or loss for that future period.

- 7.27 The presumption that such a reclassification will occur could be rebutted, for example, if there is no clear basis for identifying the period in which reclassification would enhance the relevance of the information in the statement of profit or loss. If no such basis can be identified, this may indicate that the income or expenses should not be included in other comprehensive income.

Appendix B – Extracts from the Basis for Conclusions

The following are extracts from the Basis for Conclusion on the Exposure Draft *Conceptual Framework for Financial Reporting*.

The information in this Appendix will help you to understand the IASB’s reasons for the decisions that it made when developing the proposals on measurement.

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Basis for Conclusions

Information about financial performance (paragraphs 7.19–7.27)

Terminology

BC7.24 The Exposure Draft uses the term ‘statement(s) of financial performance’ to refer to the combination of the statement of profit or loss and the statement of other comprehensive income.² The Exposure Draft uses this term because it is consistent with the term ‘statement of financial position’ that is used in existing Standards and is clearer than the term ‘comprehensive income’.

BC7.25 Existing Standards use the term ‘other comprehensive income’ to refer to income and expenses recognised outside the statement of profit or loss. Feedback on the Discussion Paper suggested that this term is not particularly descriptive or well understood, particularly by investors. Nonetheless, the IASB considers that avoiding the use of the term or using a different term to refer to income and expenses recognised outside profit or loss could be confusing. Hence, the Exposure Draft refers to ‘other comprehensive income’.

Discussion Paper

BC7.26 The Discussion Paper³:

- (a) discussed principles that could be used to determine whether income and expenses should be included in the statement of profit or loss or in other comprehensive income (‘OCI’). In particular the Discussion Paper suggested that:
 - (i) income and expenses included in the statement of profit or loss provide the primary source of information about the return that an entity has made on its economic resources in a period; and
 - (ii) all income and expenses should be included in the statement of profit or loss unless including an item in OCI enhances the relevance of the statement of profit or loss for that period.

² The Exposure Draft does not specify whether the statement(s) of financial performance comprise a single statement or two statements.

³ References to the Discussion Paper are to the Discussion Paper *A Review of the Conceptual Framework for Financial Reporting* published in July 2013.

- (b) suggested that the *Conceptual Framework* should permit or require at least some OCI items to be reclassified (recycled) from OCI to profit or loss.
- (c) suggested that the *Conceptual Framework* should require a total or subtotal for profit or loss.

BC7.27 In addition, the Discussion Paper discussed an alternative approach whereby:

- (a) income and expenses included in OCI would not be recycled to the statement of profit or loss;
- (b) the *Conceptual Framework* would not require a total or subtotal for profit or loss; and
- (c) the *Conceptual Framework* would not describe which items of income and expenses should be included in the statement of profit or loss.

Feedback on the Discussion Paper

BC7.28 Some respondents to the Discussion Paper agreed with the proposal to address the reporting of income and expenses in the statement of profit or loss, and OCI, in the *Conceptual Framework*. However, others stated that it is more appropriate to address those topics in particular Standards.

BC7.29 Respondents also expressed mixed views on most of the proposals on the reporting of income and expenses in the statement of profit or loss and OCI. Some respondents supported more extensive use of OCI whereas others advocated less use of OCI. Some respondents supported subsequent recycling of some, or all, income and expenses included in OCI to the statement of profit or loss. However, their views varied on which items should be recycled and on when those items should be recycled to the statement of profit or loss. Other respondents opposed recycling in principle.

BC7.30 Regardless of their views on the types of income and expenses that should be included in OCI and on recycling, most respondents agreed that the *Conceptual Framework* should refer to a total or subtotal for profit or loss. The few respondents who disagreed with requiring such a total or subtotal instead advocated a single statement of performance that would not draw a line between profit or loss and OCI (ie they favoured the alternative approach described in paragraph BC7.27).

BC7.31 Many respondents stated that the use of profit or loss and OCI requires further thought and analysis. Some urged the IASB either to define financial performance or OCI or to define, or directly describe, profit or loss and its purpose. Other respondents acknowledged the difficulty of developing such definitions and pointed out that decades of research and numerous attempts at producing such definitions have not yielded a satisfactory result. Only a few respondents suggested how the IASB might approach developing such definitions. Most of those suggestions did not extend beyond the approaches already considered and rejected by the IASB in developing the Discussion Paper. A few respondents proposed variations of those approaches or new approaches. For example, one respondent suggested describing profit or loss as an all-inclusive measure of irreversible outcomes. These suggestions were considered by the IASB as part of the feedback on the Discussion Paper.

BC7.32 Views expressed by investors and analysts were also mixed and were generally consistent with other feedback received. In addition, many investors and analysts made the following comments:

- (a) there are many facets to an entity's performance and no single performance number would be suitable for all users' needs;
- (b) the use of OCI and of recycling are not well understood by the user community and OCI is not looked at by many users; and
- (c) users need transparency and meaningful disaggregation of information in financial statements, including the appropriate use of totals and subtotals, regardless of whether OCI exists as a separate category.

Approach to reporting financial performance

BC7.33 Having considered the feedback received on the Discussion Paper, the IASB discussed whether to explore the use of the statement of profit or loss and OCI in a separate research project instead of providing guidance in the *Conceptual Framework*. However, the IASB concluded that conceptual guidance on this issue is urgently needed.

BC7.34 The IASB noted that respondents to the Discussion Paper and others have consistently asked the IASB to define, or better describe, profit or loss or OCI or to define financial performance. However, the IASB's previous work on

presentation and disclosure, as well as its work in developing the Discussion Paper, has shown that no single characteristic can be used to separate items of income and expenses usefully into two clear-cut categories, with all items within one category sharing the same characteristic. For example, many items currently included in OCI are remeasurements of assets or liabilities expected to be held for a long period. However, some such remeasurements are currently included in the statement of profit or loss. Feedback from users suggests that there is little appetite for including those particular remeasurements in OCI. The conclusion that income and expenses cannot be divided consistently into two categories in a manner that would provide useful information is also consistent with the idea that there are many facets of an entity's financial performance (see paragraph BC7.32).

BC7.35 In addition, in developing proposals for the use of OCI, the IASB has considered the current and proposed use of OCI in Standards. The IASB notes that whereas each use of OCI has an explanation, there is no single conceptual basis that underlies all of those cases.

BC7.36 Accordingly, the IASB decided that it is not feasible or appropriate to attempt to define, or precisely describe, in the *Conceptual Framework* when an item of income and expenses should be included in the statement of profit or loss or OCI. Instead, the IASB proposes to include in the *Conceptual Framework* high level guidance on this topic and on subsequent reclassification.

BC7.37 In developing the Exposure Draft, the IASB built on the high level principles discussed in the Discussion Paper (see paragraph BC7.26). However, it did not develop further the more specific suggestions in the Discussion Paper on the types of income and expenses that could be included in OCI and the related approaches to recycling. Respondents did not generally find those more specific suggestions helpful as a way of analysing this topic.

Describing the statement of profit or loss (paragraphs 7.19–7.22)

BC7.38 The Exposure Draft proposes that the *Conceptual Framework* should:

- (a) describe the statement of profit or loss as the primary source of information about an entity's financial performance for the period;

- (b) require a total or subtotal for profit or loss; and
- (c) state explicitly that the purpose of the statement of profit or loss is to both:
 - (i) depict the return that an entity has made on its economic resources during the period; and
 - (ii) provide information that is helpful in assessing prospects for future cash flows and in assessing management's stewardship of the entity's resources.

The IASB thinks that it is important to emphasise this dual purpose of the statement of profit or loss to prevent excessive focus on one purpose over another.

BC7.39 Describing the statement of profit or loss in this way would reflect the feedback from some respondents who argued that profit or loss is the primary measure of performance and, for that reason, its prominence should be established in the *Conceptual Framework*. The IASB noted that such a description would also be consistent with how the statement of profit or loss is used in practice. That is, many users incorporate the total or subtotal for profit loss in their analysis, either as a starting point or as the main indicator of an entity's financial performance.

BC7.40 On the other hand, the Exposure Draft emphasises that the statement of profit or loss is not the only source of information about an entity's financial performance for the period. An in-depth understanding of performance requires an analysis of all recognised income and expenses (including income and expenses included in OCI), as well as other information included in the financial statements.

BC7.41 The IASB acknowledges that merely describing the statement of profit or loss would be unlikely to satisfy those who asked for a definition of 'profit or loss'. However, as discussed in paragraphs BC7.34–BC7.36, the IASB did not think that a robust and appropriate definition of profit or loss would be feasible for the *Conceptual Framework*.

Presumption of inclusion in the statement of profit or loss (paragraph 7.23)

BC7.42 If the statement of profit or loss is the primary source of information about an entity's financial performance for the period, it follows that excluding income and expenses from that statement without compelling reasons could undermine the usefulness of that statement. That is, the statement of profit or loss should be as inclusive as possible.

BC7.43 Accordingly, the Exposure Draft includes a presumption that income and expenses will be included in the statement of profit or loss. Only in limited circumstances could the IASB require, or permit, income and expenses (or a component of income and expenses) to be excluded from the statement of profit or loss and, hence, be included in OCI. Those circumstances would be when the IASB concludes that doing so would enhance the relevance of the information in the statement of profit or loss for the period.

BC7.44 Only the IASB when setting Standards would be able to rebut the presumption that an item of income or expenses should be reported in the statement of profit or loss. Preparers would not be able to rebut that presumption, because IAS 1 prohibits the inclusion of items of income and expenses in OCI when no Standard permits or requires this.

Types of income and expenses (paragraphs 7.23–7.24)

BC7.45 The IASB discussed whether the *Conceptual Framework* should require the following types of income and expenses to be included in the statement of profit or loss:

- (a) income and expenses arising on initial recognition of an asset or a liability;
- (b) income and expenses arising on assets and liabilities measured at historical cost;
- (c) the following types of income and expenses arising on assets and liabilities carried at current values:
 - (i) consumption of the economic resource that constitutes the asset (depreciation or amortisation);
 - (ii) accrual of interest, accretion of a discount or amortisation of a premium on acquisition; or

(iii) impairment of assets or increases in the carrying amount of liabilities that have become onerous.

(d) dividend income.

BC7.46 The IASB considers that a detailed list would be inappropriate in the *Conceptual Framework*. However, the IASB noted that the items listed in paragraph BC7.45 relate to transactions and events of the period, such as consumption of an asset or interest income and expenses, but not to other changes in the value of assets and liabilities. Classifying income and expenses arising from transactions and events separately from changes in value can provide useful information.

BC7.47 Hence, consistently with the suggestions in the Discussion Paper, the IASB proposes to specify that only income and expenses related to changes in current value measures of assets and liabilities (remeasurements), or components of such income and expenses, could be included in OCI. Income and expenses related to changes in a historical cost measure of assets and liabilities would need to be included in the statement of profit or loss. Likewise, if an asset or a liability is being measured on a current value basis, but components of income and expenses of the type that would arise if the asset or liability were measured at historical cost are identified separately, those components would need to be included in the statement of profit or loss. This is because excluding such items from the statement of profit or loss would not enhance the confirmatory or predictive value of the information included there.

BC7.48 Recognising some components of income and expenses in the statement of profit or loss, and some components in OCI, is a particular case of classification, namely classification between two separate statements (or, within a single statement between profit or loss and OCI). As stated in paragraph 7.11 of the Exposure Draft, separate classification is appropriate when the components have such different characteristics that classifying them separately would enhance the relevance and understandability of financial information. Paragraph 7.10 notes that such characteristics include, but are not limited to, the role (function) of the item within the business activities conducted by the entity and how it is measured.

Use of more than one measurement basis (paragraph 7.25)

BC7.49 One example of when components of income and expenses will be included in OCI is when the IASB selects a current measurement basis for an asset or a liability in the statement of financial position and selects a second measurement basis for determining the related income and expenses in the statement of profit or loss (a ‘dual measurement’ approach). When such an approach is used:

- (a) the current measurement basis is used in the statement of financial position.
- (b) the income and expenses included in the statement of profit or loss are determined by measuring the asset or the liability on the second measurement basis.
- (c) the cumulative amount of that income or expense is the same as if the second measurement basis had also been used in the statement of financial position. Thus, the cumulative amount of income and expenses included in other comprehensive income equals the difference between the two measures of the asset or the liability.
- (d) the measure of the asset or the liability on the second measurement basis needs to have an independent meaning and not be a mere accumulation of amounts included in the statement of profit or loss.

BC7.50 For example:

- (a) measuring a financial asset at fair value in the statement of financial position and related income and expenses at historical cost in the statement of profit or loss is a case of dual measurement.
- (b) but the treatment of a pension liability applying IAS 19 *Employee Benefits* is not a case of dual measurement. This is because the income and expenses included in the statement of profit or loss in each period reflect assumptions (including discount rates) for that period. Thus, the cumulative amounts included in that statement reflect different assumptions (including discount rates) for each period. Those cumulative amounts correspond to a measure for the pension liability that has no independent meaning and can be described only as the accumulation of the amounts included in the statement of profit or loss.

Reclassifying items into the statement profit or loss (paragraphs 7.26–7.27)

- BC7.51 The IASB considered whether items of income and expenses included in OCI should be subsequently reclassified into the statement of profit or loss. Such reclassification is often described as recycling.
- BC7.52 When the dual measurement approach described in paragraph BC7.49 is used, reclassification of the cumulative amount included in OCI over the holding period of the asset or the liability is a necessary consequence of that approach. This is because the income or expenses included in profit or loss on derecognition of the asset or the liability (for example, on sale) includes any income and expenses relating to the asset or the liability that have not already been included in the statement of profit or loss. Hence, any income and expenses previously included in OCI will, unless it has already reversed, now be included in profit or loss.
- BC7.53 However, when income and expenses are included in OCI in cases other than dual measurement, such reclassification is not a necessary consequence of the approach adopted.
- BC7.54 If the amounts included in the statement of profit or loss are the primary source of information about an entity's financial performance for the period, it follows that the cumulative amounts included over time in that statement should also be as complete as possible. Hence, no income and expenses should be excluded from the statement of profit or loss permanently, unless there is a compelling reason to do so.
- BC7.55 Accordingly, the IASB proposes to include in the *Conceptual Framework* a presumption that income and expenses included in OCI must subsequently be reclassified to the statement of profit or loss. Reclassification takes place in the period when including the income and expenses in the statement of profit or loss enhances the relevance of the information included in that statement for that period.
- BC7.56 However, in some cases, reclassifying the income and expenses to the statement of profit or loss may not enhance the relevance of the information in that statement in any period. Thus, there would be no appropriate basis for

reclassification. In such cases, the presumption of reclassification can be rebutted because reclassification could occur only on an arbitrary basis, which would not provide useful information. The absence of an appropriate basis for reclassification may be an indication that this particular item of income and expenses should not be included in OCI in the first place.

BC7.57 The IASB does not propose to include in the *Conceptual Framework* specific guidance on when reclassification may be appropriate. The IASB expects to take that decision when developing particular Standards.