

# STAFF PAPER

June 2016

Prepared for the Joint Capital Markets Advisory Committee and Global Preparers Forum Meeting

<b>Paper topic</b>	<b>Follow up on issues discussed at the February 2016 CMAC meeting</b>		
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This paper has been prepared by staff of the IFRS<sup>®</sup> Foundation for discussion at a public meeting. The views expressed in this paper reflect the individual views of the author[s] and not those of the International Accounting Standards Board or the IFRS Foundation. Comments on the application of IFRS Standards do not purport to set out acceptable or unacceptable application of IFRS Standards.

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## Purpose of this paper

1. This paper provides a brief, high-level update to the Capital Markets Advisory Committee (CMAC)<sup>1</sup> and the Global Preparers Forum (GPF)<sup>2</sup> on how the staff or the International Accounting Standards Board (the Board) considered the advice received during the CMAC meeting held in February 2016. It is for information purposes only.

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<sup>1</sup> Information about the CMAC's past meetings can be found at <http://www.ifrs.org/About-us/IASB/Advisory-bodies/CMAC/past-meetings/Pages/past-meetings.aspx>.

<sup>2</sup> Information about the GPF's past meetings can be found at <http://www.ifrs.org/About-us/IASB/Advisory-bodies/GPF/Pages/GPF-meetings.aspx>

**Update on advice received at the February 2016 CMAC meeting**

Topic	Summary of CMAC views presented	Next steps / action taken by the IASB
<p><b>Different effective dates— IFRS 9 <i>Financial Instruments</i> and the new insurance contracts Standard</b></p> <p>The staff explained the proposals in the Exposure Draft <i>Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts (Proposed amendments to IFRS 4)</i>. This Exposure Draft proposes two optional approaches to address concerns raised by some interested parties, in particular insurers, about the different effective dates of IFRS 9 and the new insurance contracts</p>	<p>CMAC members provided the following comments on the proposals in the ED:</p> <ul style="list-style-type: none"> <li>• Many CMAC members said the Board should not provide any temporary approaches. Different effective dates of IFRS 9 and the new insurance contracts Standard are not problematic, they said, because:               <ul style="list-style-type: none"> <li>– continual changes in accounting are inevitable in improving accounting standards and companies are accustomed to accommodating them.</li> <li>– volatility itself is not a concern as long as companies are able to understand the sources of it.</li> <li>– the bigger concerns are the potential loss of important and relevant information and lack of</li> </ul> </li> </ul>	<p>The staff provided the Board with the feedback from users of financial statements, including CMAC, at the March 2016 meeting<sup>3</sup>.</p> <p>The Board finished deliberations on this project at its meeting in May 2016. The staff is currently drafting the final amendment to IFRS 4 and plan to publish it in September 2016.</p> <p>In summary, the Board’s tentative decisions for the amendment to IFRS 4 are:</p> <ul style="list-style-type: none"> <li>• A reporting entity that issues</li> </ul>

<sup>3</sup> <http://www.ifrs.org/Meetings/MeetingDocs/IASB/2016/March/AP14B-Insurance-and-IFRS-9.pdf>

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<p>Standard. The approaches are referred to as the overlay approach and a temporary exemption from applying IFRS 9. The proposed approaches aim to address concerns that:</p> <ul style="list-style-type: none"> <li>• users of financial statements may find it difficult to understand the additional accounting mismatches and temporary volatility that could arise in profit or loss if IFRS 9 is applied before the new insurance contracts Standard; and</li> <li>• two sets of major accounting changes in a short period of time could result in significant cost and effort for both preparers and users of financial statements.</li> </ul>	<p>comparability, especially if some entities are temporarily exempt from applying IFRS 9.</p> <ul style="list-style-type: none"> <li>• Many members said that if the Board were to adopt any approach, it should be a single, mandatory approach that would alleviate some concerns for a short period of time and not reduce comparability. Members preferred the overlay approach because it would: <ul style="list-style-type: none"> <li>– preserve comparability between all entities, because all entities would apply IFRS 9 in 2018; and</li> <li>– provide transparent information about the effects of applying IFRS 9 by reclassifying some changes to other comprehensive income (OCI).</li> </ul> </li> <li>• In general, CMAC members strongly opposed having a temporary exemption from applying IFRS 9, mainly because IFRS 9 brings vast improvements</li> </ul>	<p>insurance contracts is allowed to reclassify some effects of applying IFRS 9 from profit or loss to OCI (the overlay approach). The effect of the overlay approach would be presented in a single line item in both profit or loss and OCI.</p> <ul style="list-style-type: none"> <li>• A reporting entity with activities that are predominantly related to insurance is allowed to defer IFRS 9 until the reporting period beginning on or after 1 January 2021 (such an entity will continue to apply IAS 39 to all its financial instruments). However, for comparability purposes, such an entity will be required to provide</li> </ul>

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	<p style="text-align: center;"><i>over IAS 39 Financial Instruments: Recognition and measurement .</i></p> <p>The CMAC members provided the following comments on the details of the proposed approaches:</p> <ul style="list-style-type: none"> <li>• On the overlay approach some commented that only one presentation of the effect of the overlay approach should be allowed, because options, in general, decrease comparability. They recommended presenting the effects of the overlay approach as a single line item in the statement of profit or loss to allow comparability with entities that will apply IFRS 9 without any delay and to clearly show the adjustment that is reclassified to OCI.</li> <li>• If the temporary exemption from applying IFRS 9 were provided, they unanimously supported the ED</li> </ul>	<p>disclosures to help users of financial statements to assess the effect that applying IFRS 9 would have on the financial statements (including information that will help users of financial statements better assess the credit risk of the financial assets held by the entity).</p>

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	<p>proposals that:</p> <ul style="list-style-type: none"> <li>- the predominance criterion should be applied at the reporting entity level; otherwise, financial assets in one set of financial statements will be accounted for using two accounting Standards, which will be complex to understand;</li> <li>- the exemption from applying IFRS 9 should have an expiry date. This is because the exemption from applying IFRS 9 is temporary and should be treated as such; and</li> <li>- entities that apply the exemption should disclose more IFRS 9 information than proposed in the ED, especially information about expected credit losses. This is because CMAC members believed that such information is an important improvement compared to what is currently required, and should already be produced by</li> </ul>	

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	most entities for management purposes.	
<p><b>Structured Electronic Reporting— What do investors need?</b></p> <p>The purpose of this session was to discuss CMAC members’ views about structured electronic reporting. In particular, CMAC members were asked:</p> <ul style="list-style-type: none"> <li>• whether they use structured electronic data in their analysis; and</li> <li>• how structured electronic reporting could be made more useful to investors and analysts.</li> </ul> <p>CMAC members discussed the topic in two break-out groups. Group 1 focussed on the current and potential use of structured electronic reporting. Group 2 discussed whether structured electronic</p>	<p><b>Report back from Group 1</b></p> <p>Members of Group 1 reported that their use of structured electronic data is relatively limited, and that any such usage is mainly through data aggregators. They identified implementation costs (versus expected benefits), data reliability and specific technical issues as factors in explaining their limited use of structured electronic data. One member of Group 1 noted that investors are making more use of XBRL data in Japan. In the view of this member, this is due to the more structured disclosure regime in Japan, which makes the data more reliable.</p> <p>Most members of Group 1 expressed the view that some degree of data input automation could be beneficial. However, they also emphasised that structured electronic reporting is not a substitute for</p>	<p>Comments from CMAC members have been fed into the follow-on work resulting from the IFRS Foundation’s Review of Structure and Effectiveness and will also be used to help staff direct activities to improve the IFRS Taxonomy. In particular the resulting strategy includes:</p> <ul style="list-style-type: none"> <li>• Increased IFRS Taxonomy outreach with investors with the aim to identify specific improvements to the way we support investor use of IFRS data.</li> <li>• Investor outreach on the wider topic of the use of Technology and if there</li> </ul>

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<p>reporting can work for principle-based IFRS financial reporting (including any risks of using structured electronic data).</p>	<p>data interpretation and analysis and that data context (including narrative explanations) would remain important. Other technical advances (including, but not limited to, artificial intelligence) would need to be considered, especially for data that is less structured.</p> <p><b>Report back from Group 2</b></p> <p>Members of Group 2 expressed the view that structured electronic reporting can work for principle-based reporting.</p> <p>These CMAC members stated that the use of (and the need for) structured electronic reporting differs among investors, with some using it on an extensive basis whereas others mainly use it for benchmarking. One member of this group reported using US XBRL data extensively. Those members of the group that make extensive use of structured electronic data stated that</p>	<p>could be any resulting impact on standard-setting.</p> <ul style="list-style-type: none"> <li>• Looking into the perception that there is a conflict between principle-based reporting and electronic reporting and if there are actions we can take to mitigate any issues.</li> </ul> <p>Comments relating to challenges identified by CMAC members are also being used to guide our more immediate work to help improve data quality. This includes taxonomy improvements to help preparers tag accurately and working with XBRL International to improve how XBRL works with entity-specific disclosures (or extensions).</p>

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	<p>its main advantage is the cost-effective extraction of highly detailed quantitative and qualitative data ('the footnote information') over a period of time.</p> <p>Members of this group identified the following risks of using structured electronic data:</p> <ul style="list-style-type: none"> <li>• a risk of it being misleading, for example a disclosure tagged with the same IFRS Taxonomy element does not necessarily imply comparability;</li> <li>• a risk of it leading to undue standardisation in financial reporting ('template thinking');</li> <li>• a risk of it not being easily reconcilable to the PDF filing; and</li> <li>• a risk of it being overwhelming and being complicated and costly to use; the implementation has to work for investors, or else it will not be used.</li> </ul> <p>A Board member asked CMAC members whether they thought that structured electronic reporting has</p>	



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	<p>implications for Standard setting. The Board and the IASB staff often hear that effective communication involves giving a certain degree of freedom to entities regarding what to disclose and how to present information, but the Board needs to balance this freedom with the need for comparability. It is not clear whether structured electronic reporting can help to achieve this balance. CMAC members had a variety of views on this question.</p> <ul style="list-style-type: none"> <li>• A few CMAC members stated that structured electronic reporting should follow standard-setting. It does not make information inherently more useful, but it can help analysis. For example, entities could provide a computer-readable link to an IFRS Taxonomy element, thereby making entity-specific detail more easily accessible. Another example is that entities could provide a computer readable (complete)</li> </ul>	

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	<p>disaggregation of IFRS disclosures, thereby facilitating data standardisation by investors.</p> <ul style="list-style-type: none"> <li>• One CMAC member warned against giving preparers too much freedom to choose how to present and disclose information. This member expressed the view that some level of standardisation in presenting and disclosing information should be required.</li> <li>• One CMAC member stated that in order to protect the relevance of IFRS Standards, the Board should take on some responsibility for how IFRS disclosures will be represented electronically.</li> <li>• One CMAC member warned about the risk of structured electronic reporting undermining the usefulness of information; in the view of this member financial reporting remains very much about the narrative and the story.</li> </ul>	

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<p><b>Primary Financial Statements—An information gathering session on users’ views on operating profit</b></p> <p>The purpose of the session was to obtain the CMAC members’ views on the use of the operating profit subtotal, as a part of the staff’s initial research work on the Primary Financial Statements project.</p> <p>During the meeting, the staff asked CMAC members whether they employ the operating profit subtotal in their analysis and whether the Board should develop a standard definition of this subtotal.</p>	<p>The resulting discussion highlighted the following points:</p> <ul style="list-style-type: none"> <li>• Many CMAC members mentioned that they use the operating profit subtotal. However, they observed that this subtotal is not consistently defined.</li> <li>• Many CMAC members suggested that it would be very difficult for the Board to define operating profit because it is likely to vary from entity to entity. Some members expressed the view that deriving an appropriate operating profit subtotal for an entity requires considerable judgement and is a key part of an analyst’s job. Consequently, a standardised operating profit figure would be unlikely to be useful.</li> <li>• However, others suggested that a standardised operating profit subtotal might be useful for less sophisticated investors or for company communications with the press. Some CMAC</li> </ul>	<p>In April 2016 the Board discussed the feedback received on the Primary Financial Statements project in response to the 2015 Agenda Consultation and the online investor survey. The papers incorporated the feedback provided by CMAC members at the February 2016 CMAC meeting.</p> <p>In May 2016, the Board discussed its approach to research in the Primary Financial Statement Project. The purpose of this research is to develop in detail the scope for the project.</p> <p>The Board tentatively decided that initial research work should focus on the structure and content of the</p>

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	<p>members suggested that guidance on what could and what could not be included in arriving at operating profit or ‘Earnings Before Interest and Taxes’ (EBIT) might be useful.</p> <ul style="list-style-type: none"> <li>• Many CMAC members thought that a standardised EBIT subtotal could be useful as a starting point for their analysis.</li> <li>• A few CMAC members questioned the need for operating profit or EBIT subtotals if a standardised taxonomy is used for electronic reporting.</li> <li>• CMAC members also commented on whether particular items should be included in the calculation of EBIT:               <ul style="list-style-type: none"> <li>– Many thought that the interest cost of a defined benefit pension scheme should be presented as a finance cost.</li> <li>– Some CMAC members thought that any share of</li> </ul> </li> </ul>	<p>statement(s) of financial performance, including whether there should be a requirement to include a defined subtotal for operating profit and the use of alternative performance measures.</p> <p>The Board also decided to undertake research to establish whether there is any demand for changes to the statement of cash flows and the statement of financial position.</p> <p>The staff will continue their research to develop in detail the scope of the Primary Financial Statements project.</p>

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	<p>profit of associates should be presented below the EBIT subtotal:</p> <ul style="list-style-type: none"> <li>▪ One CMAC member observed that inclusion of share of profit of associates in EBIT distorts the EBIT margin.</li> <li>▪ Another CMAC member thought that the inclusion of share of profit of associates in EBIT distorts future cash flow projections, because cash is received from associates through dividends.</li> </ul>	