STAFF PAPER

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Prepared for the Capital Markets Advisory Committee Meeting

Paper topic	**Follow up on issues discussed at the March 2018 CMAC meeting**		
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Purpose of this paper

1. This paper provides a brief, high-level update to the Capital Markets Advisory Committee (CMAC)[1] and the Global Preparers Forum (GPF)[2] on how the staff or the International Accounting Standards Board (the Board) considered the advice received during the CMAC meeting held in March 2018. It is for information purposes only.

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[1] 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.

[2] 2 Information about the GPF's past meetings can be found at https://www.ifrs.org/groups/global-preparers-forum/#meetings

Update on advice received at the March 2018 CMAC meeting

Topic	Summary of CMAC views presented	Next steps / action taken by the IASB
Primary Financial Statements	The purpose of this session was to seek feedback from CMAC members on: (a) introducing management performance measures and management-defined adjusted earnings per share (adjusted EPS) into financial statements; and (b) proposed improvements to the presentation of the share of profit or loss of associates and joint ventures in the statement(s) of financial performance. ***Management performance measures and adjusted EPS*** ***Management performance measures*** Some CMAC members supported the overall approach of introducing management performance measures into the financial statements with the aim of: (a) enhancing the transparency of such measures through presentation and disclosure requirements such as a reconciliation to the most appropriate subtotal or total required by IFRS Standards; and (b) making management performance measures subject to external audit. However, a few CMAC members were concerned that including management performance measures in financial statements could be misleading. They said users could wrongly assume that management performance measures are comparable across entities if different entities use the same labels for their management performance measures. In response to this concern, one CMAC member suggested that the Board define some commonly used adjustments, such as 'restructuring expenses'. This member also questioned whether management performance measures would be auditable without such definitions. However, another CMAC member said that if management	The Board considered the feedback received about the MPM and adjusted EPS proposals at its April 2018 meeting. The Board will consider the other feedback received at future meetings and/or during development of the first due process document.

	performance measures are meant to represent management's true view of performance, the Board should not provide any definitions for management performance measures. In this member's view, management performance measures can be audited without the Board providing definitions—for example auditors can assess whether management's definition of management performance measures has been consistently applied over time. With regard to reconciling an entity's management performance measure to the most appropriate subtotal or total required by IFRS Standards: (a) a few CMAC members said a separate reconciliation should always be presented in the notes, even when the management performance measure meets the requirements to be presented as a subtotal in the statement(s) of financial performance. One of these members expressed the view that some reconciliations would be too complex to be provided in the statement(s) of financial performance. They also said they prefer having a consistent location—i.e. the notes—for the reconciliation across all entities, because it would facilitate mass processing of data. (b) a few CMAC members said that such a reconciliation should be presented below the statement(s) of financial performance, rather than in the notes, so it is easier for users to find. (c) one CMAC member suggested entities should be required to disclose the allocation of the reconciling items to the entity's segments. ***Adjusted EPS*** Some CMAC members supported staff proposals for: (a) providing an adjusted EPS that is calculated consistently with the entity's management performance measures; and (b) an accompanying reconciliation showing the tax effect and the share of non-controlling interests of adjustments made in calculating adjusted EPS.	

	One CMAC member said these proposals would be useful because many users focus on EPS. A few CMAC members said the tax effect should be disclosed separately from the share of non-controlling interests. ***Presentation of the share of profit or loss of associates and joint ventures in the statement(s) of financial performance*** ***Distinction between 'integral' and 'non-integral' associates and joint ventures***. CMAC members expressed mixed views about the proposed distinction between the share of profit or loss of integral and non-integral associates and joint ventures in the statement(s) of financial performance. However, most CMAC members did not support this distinction for the following reasons: (a) any definition of 'integral' and 'non-integral' the Board develops would require high levels of judgement and entities would use this flexibility to obtain the most favourable presentation. (b) if the classification of investments by an entity as 'integral' or 'non-integral' changed frequently, users would have difficulty analysing the performance of a particular investment over time. (c) presentation in the statement(s) of financial performance should depend only on whether the entity has control over an investment (as defined in IFRS 10 Consolidated Financial Statements), without a further categorisation of investments outside the entity's control. (d) it does not seem appropriate to develop such a distinction in the Primary Financial Statements project, because this project should only address presentation issues. If such a distinction is made, it should be part of the Post-implementation Reviews of IFRS 10 Consolidated Financial Statements, IFRS 11 Joint Arrangements and IFRS 12 Disclosure of Interests in Other Entities. A few CMAC members said such a distinction could provide useful information to investors, but those members also had concerns about the practicability of such a distinction.	

	A few members suggested that instead, entities could include the share of profit or loss of some associates and joint ventures in the calculation of their management performance measure. That way, they can provide this information if they wish to do so in a way that makes it clear to users that it represents a management view. ***Location in the statement(s) of financial performance*** A few CMAC members did not support presenting the share of profit or loss of associates and joint ventures near the beginning of the statement(s) of financial performance (for example, as part of an 'operating' or similar section) because: (a) post-tax and post-NCI amounts would be mixed with pre-tax and pre-NCI amounts; and (b) this might confuse some users and lead to double-counting of associates and joint ventures in valuations, for example when enterprise value methodologies are used. A few CMAC members added to perform margin calculations on a like for like basis (for example, comparing consolidated revenues to a profit subtotal from consolidated activities), users need a 'clean' subtotal that excludes the share of all equity-accounted investments. ***Other comments*** A few CMAC members expressed interest in having more disclosures about the financial performance, financial position and cash flows (including segmental information) of 'integral' associates and joint ventures, for example about their indebtedness. A Board member suggested the Board could explore linking the requirements for 'integral' associates and joint ventures to the disclosure requirements in IFRS 12 Disclosure of Interests in Other Entities for associates and joint ventures that are material to the reporting entity (IFRS 12 paragraphs 21 and B12–B13).	
Principles of Disclosure	The purpose of this session was to provide CMAC members with a brief summary of the feedback on Discussion Paper Disclosure Initiative—Principles of Disclosure (Discussion Paper) and to seek their advice on the next steps for the project.	At the March 2018 Board Meeting, the Board decided:

	Specifically, CMAC members discussed: (a) preparers' views on addressing the disclosure problem; (b) the relative prioritisation of five specific topics included in the Discussion Paper; and (c) the effect of technology and digital reporting on the project. ***Addressing the disclosure problem*** CMAC members had the following responses to preparers' views on addressing the disclosure problem through a review of disclosure requirements in IFRS Standards: (a) some members viewed the disclosure problem as a result of the inappropriate application of the concept of materiality and not as a direct result of the specific disclosure requirements in IFRS Standards. These members said preparers should view financial statements as an opportunity to communicate useful and material information to users rather than as a compliance exercise. They suggested that preparers apply the requirement in IAS 1 to disclose only material information when deciding whether to provide the disclosures in each Standard. One of these members added that the Board could provide additional principlebased guidance to reiterate the importance of providing relevant information. (b) one member suggested that the Board undertake a review of its disclosure requirements to justify why those requirements are necessary. Another member suggested that the Board could review disclosure requirements in individual standards as part of its postimplementation reviews. (c) a few members said that they are more concerned about missing disclosures than about excessive disclosures. A few other members, however, highlighted that standing data—that is, explanatory information that remains unchanged from year to year—does not provide any useful information. These members thought such information could be removed to simplify financial statements.	1) To undertake a Targeted Standards-level review of Disclosures. Specifically, the Board will develop guidance for the Board itself to use to improve the way that it develops and drafts disclosure objectives and requirements in future. The Board will also select one or two IFRS Standards on which to test and improve that guidance. This is expected to lead to improvements in the disclosure requirements in the selected Standards. 2) To perform further analysis before deciding upon next steps relating to the location of information, accounting policy disclosures and the effects of

	(d) a few members were concerned that a user's ability to choose from a wide range of information in and across financial statements would be hindered if a standards-level review were to reduce the disclosure requirements in the standards. ***Projects—determining priorities*** CMAC members were asked to comment on the relative prioritisation of the following topics from the Discussion Paper: (a) which accounting policies to disclose; (b) information outside the financial statements that is required by IFRS Standards; (c) information inside the financial statements that is not required by IFRS Standards; (d) formatting; and (e) the location of accounting policies. One CMAC member said the Board should provide guidance or requirements on each topic because the topics all address relevant issues in financial statements. A few members commented on the content of the guidance for some of the topics and: (a) expressed concerns over fragmentation of information when information that is required by IFRS Standards is provided outside a company's financial statements, for example, on the company's website. Some of these members said it would be important to ensure that financial statements are in a single document, which serves as a single repository of a company's annual disclosures. (b) suggested ways in which formatting can be improved in financial statements provided in PDF form, for example, using hyperlinks to link to related pieces of information and using tables to provide a disaggregation of line items in the primary financial statements.	technology and digital reporting. 3) To consider whether to perform any further activities relating to materiality when the Board has more information about the practical effects of recent Board publications relating to the application of materiality.

	Effect of technology One member expressed the view that ESMA's requirement for financial statements to be reported in Inline XBRL would improve the accessibility of information for investors in Europe. One member said that sell-side research is investing more in natural language processing software that can allow computers to read financial statements. One member said that it would be important to ensure that data aggregators can easily extract data and information from financial reports.	
Goodwill & Impairment	The staff sought feedback on: (a) their proposal about an approach to the impairment testing of goodwill that considers movements in headroom. Headroom is the excess of the recoverable amount of a cash-generating unit (or group of units) over the carrying amount of that unit. (b) the requirement in IFRS 3 Business Combinations to recognise all identifiable intangible assets acquired in a business combination separately from goodwill, specifically whether: (i) recognising all identifiable intangible assets separately from goodwill provides useful information; (ii) the reason for investors' concerns about using fair value measurement for recognising intangible assets is insufficient disclosure about the valuation methodology and about the inputs used in valuing the intangible assets; and (iii) there are ways of allowing some identifiable intangible assets to be included within goodwill without losing information that is currently provided. ***Using movements in headroom in testing goodwill for impairment (headroom approach)*** In November and December of 2017, the staff had one-to-one calls with 11 CMAC members to discuss the headroom approach. At this meeting, the staff summarised	The staff considered the comments from the members in their research and presented them to the Board in its April 2018 meeting. In relation to the separate recognition of intangibles in a business combination, the Board tentatively decided not to pursue allowing some intangible assets to be included within goodwill. The Board will continue to discuss the next stage of the project at a future meeting.

	the feedback received during the calls and asked the CMAC to provide any incremental feedback. Paragraphs 27–32 set out the feedback received both during the calls and at this meeting. A majority of CMAC members supported the headroom approach. One of the important aspects of the headroom approach that garnered support from CMAC members was that it could remove the shielding effect that is created by internally-generated goodwill in the current impairment testing requirements. That shielding effect arises because, in current requirements, any decrease in total headroom is attributed first to unrecognised internally-generated goodwill; an impairment loss is recognised on acquired goodwill only if the value of unrecognised internally-generated goodwill has first been entirely eliminated by a decrease in total headroom. Some members supported the Board's idea to require disclosure of the basis for attributing the decrease in headroom. Those members thought such disclosure would provide useful information to investors. Some members indicated a preference for disclosure of headroom instead of using the headroom approach for impairment testing. However, those members thought that companies are likely to apply a disclosure-only requirement less rigorously than if they have to use the headroom for impairment testing purposes. The headroom approach contains a presumption that a company would attribute all of any decrease in total headroom to acquired goodwill. However, a company could rebut the presumption if there is evidence that all or part of the decrease should instead be attributed to unrecognised headroom. One member cautioned the staff that a rebuttable presumption could lead to decreases in total headroom being attributed to acquired goodwill even if the decrease was caused by reasons not connected to the acquired goodwill. Some members suggested reintroducing amortisation of goodwill.	

	One member thought that, instead of pursing any of the approaches mentioned by the staff, the Board should consider requiring: (a) further componentisation of goodwill on initial recognition; and (b) depending upon the nature of the component, either amortising the component, writing it off against equity or only testing it for impairment. ***Recognising all identifiable intangible assets acquired in a business combination*** In relation to whether useful information is provided by the recognition of all identifiable intangible assets separately from goodwill: (a) one member commented that the requirement in IFRS 3 provided useful information to investors. (b) another member said that identifying and valuing some of the intangible assets requires high levels of judgement. That member does not, therefore, believe that separate recognition of those intangible assets provides useful information. That member also views a business combination as a type of transaction different from purchase of assets. (c) one member said that recognising only those intangible assets for which there is an active market provides useful information because a reliable measure of fair can be attained. (d) some members with experience of the banking sector said they ignore intangible assets acquired in a business combination because regulatory capital requirements require those intangible assets to be deducted from equity to determine regulatory capital. (e) some members said that they were indifferent between recognising and not recognising identifiable intangible assets. An investor's assessment of whether an acquisition increases value or diminishes value and whether the investor should invest in any capital raising by an entity to fund the acquisition is made when the acquisition is announced, at which time detailed information about values of intangible assets acquired is generally not available.	

	CMAC members did not reach a clear position on whether investors' concerns about using fair value measurement for recognised intangible assets would be resolved by improving disclosure about the valuation methodology and inputs used in valuing the intangible assets. In relation to possible ways of allowing some identifiable intangible assets acquired in a business combination to be included within goodwill without losing information that is currently provided: (a) one member did not support allowing any identifiable intangible assets to be included within goodwill. (b) one member thought that an acquiring entity should recognise only those intangible assets that have already been recognised as assets by the acquired entity, and include all other identifiable intangible assets within goodwill. (c) one member supported a staff member's suggestion to segregate intangible assets into wasting assets and organically-replaced assets, and require recognition of only wasting intangible assets acquired in a business combination. The CMAC member's preference was based on the view that amortisation of wasting intangible assets provides useful information about potential future cash outflows required for replacing those assets. On the other hand, some members discouraged this approach. (d) one CMAC member with experience of the banking sector thought that a staff member's suggestion to allow indefinite-lived intangible assets to be included within goodwill is not worth pursuing. In that CMAC member's experience, few indefinite-lived intangible assets were recognised in acquisitions, and consequently, the member's view was that this approach may not result in saving costs for preparers.	

Rate-regulated Activities	The purpose of this session was to obtain CMAC members' views on a preliminary set of disclosures being considered for the accounting model the Board is developing for rate-regulated activities (model). The staff provided CMAC members with an overview of the model and asked for their views on: (a) whether using the disclosure objective in IFRS 14 *Regulatory Deferral Accounts* would be a good starting point for developing the disclosure objective for the model; (b) the usefulness of the preliminary set of disclosures; and (c) whether entities should be required to provide all the resulting information within their financial statements, rather than in another location, such as in management commentary. ***Disclosure objective*** Some members suggested that the disclosure objective in IFRS 14 would be a good starting point for developing the disclosure objective of the model. A few members commented that information about rate-regulated entities is currently scattered across various sources and, sometimes, in different languages. These members welcomed a disclosure objective that would contribute to bringing together information that is currently dispersed. ***Usefulness of the preliminary set of disclosure requirements for the model*** Some members indicated that disclosing information relating to regulatory matters, such as the regulatory environment and the entity's relationship with the rate regulator, should be required because this information helps investors understand an entity's financial statements. One member thought that requiring disclosure about the inputs used in the rate formula calculation, especially assumptions about timing and volumes, is very important.	The staff will use this feedback when developing disclosure requirements for the model in its future discussions with the Board.

	Some members identified other disclosure requirements that would result in useful information: (a) separate disclosures for regulatory as compared to non-regulatory revenue and regulatory as compared to non-regulatory capital expenditure—a member indicated that rate-regulated activities benefit from what is, in effect, a sovereign guarantee; thus, separate disclosures would allow investors to understand the different credit environments of those activities and the rate of return that the rate regulator allows on capital expenditure. According to this member, entities typically provide this information as non-GAAP financial information only. (b) the effect of changes in the regulatory environment—one member recommended requiring entities to disclose the changes in the regulatory environment and the effect of these changes in their financial statements. (c) reconciliation of the regulatory balances to the reported balances required by IFRS Standards—a few members stated that equity analysts use mainly entities' regulatory balances when carrying out their analyses. For these analysts, it would be useful to understand the key differences between the balances reported in accordance with IFRS Standards and the regulatory balances that they use in their equity valuations. Taking this approach would enhance analysts' understanding of the balances required by IFRS Standards. ***Should IFRS Standards require all the information to be provided in entities' financial statements?*** A few members expressed the view that entities should provide information relating to regulatory matters in their financial statements because this information contributes to the financial statements' completeness and understandability. One of these members thought that it could be appropriate to provide the information about regulatory matters in the financial statements by cross referencing from another section of the annual report.	

	As mentioned in above, some members commented on the need to bring together information about regulatory matters in a single document. According to these members, doing so would enhance the accessibility of information that is relevant to decisions investors make on the basis of entities' financial statements. In addition, a member indicated that entities' own summaries of the key terms of their regulatory agreements could help investors understand the entities' regulatory environments by decreasing the need for investors to interpret the implications of the entities' agreements by themselves.	