FASB FINANCIAL ACCOUNTING STANDARDS BOARD

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Project	**Segment Reporting (SEGRPT)**
Project Stage	**Initial Deliberations**
Issue(s)	**Simplification of the Aggregation Criteria and Improving Segment Disclosures**

Introduction

1. Topic 280, Segment Reporting, and IFRS 8, *Operating Segments*, are substantially converged standards. The FASB's project is considering making some targeted changes to Topic 280. Accordingly, the purpose of this session is to provide IASB members with an update on the project, explain why the FASB decided on the current scope, and to discuss the feedback received as part of our initial deliberations.

2. The paper is structured into the following sections:

   (a) Section 1: Scope of the Project

   (b) Section 2: Purpose of the Project

   (c) Section 3: Previous Standard Setting Projects

   (d) Section 4: Aggregation Criteria and Reportable Segments Process

   (e) Section 5: Improving Segment Disclosures.

Section 1: Scope of the Project

3. In September 2017, the Board decided to add the project to the technical agenda to make targeted improvements to the segment aggregation process and the disclosure requirements.

4. For the aggregation criteria, the Board decided to focus on either of the following two alternatives for improvement:

   (a) Remove the aggregation criteria, thereby each operating segment would be reported, but retain the practical limit guidance

   (b) Re-order the process for determining reportable segments and move the quantitative thresholds earlier in that process.

5. For the segment disclosure requirements, the Board decided to focus on three areas:

   (a) Add individual pieces of segment information to the list of required disclosures

   (b) Require the disclosures in Topic 280 to be reported in a table

   (c) Require a table of regularly reviewed information based on how it relates to the lines in the financial statements.

Section 2: The Purpose of the Project

6. In deciding upon this scope, the Board was responding to feedback from users that indicated that investors are unsatisfied with the level of segment detail provided and believe that there should generally be more segments and more disclosure about those segments. This problem is driven by three main areas of the standard: (a) segment identification, (b) the application of the aggregation criteria, and (c) the segment disclosure requirements.

Segment Identification

7. An operating segment is defined as follows:

> A component of a public entity that has all of the following characteristics:
>
> (a) It engages in business activities from which it may earn revenues and incur expenses (including revenues and expenses relating to transactions with other components of the same public entity).
>
> (b) Its operating results are regularly reviewed by the public entity's chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance.
>
> (c) Its discrete financial information is available.

8. This definition underpins the core principle of the standard: the management approach. That is, operating segments are identified based on how management organizes the business activities and reviews the information. The Board decided that this approach would allow users to see the entity "through the eyes of management" and to assess the performance of individual operating segments in the same way that management reviews them in making decisions.

9. In addition to seeing the entity from management's perspective, the Board concluded that the incremental cost of providing segment information using the management approach would be low because the information is already generated for management's use.

10. Over the years, there have been competing preferences between preparers, auditors, and the SEC on how segments should be identified from the discrete reports that the chief operating decision maker (CODM) regularly reviews but at the same time reflect an entity's organizational structure. The CODM can receive a range of information at various levels of detail. Technology and modern reporting systems have increased the range, depth, and frequency in which a CODM receives information. Daily, periodic, and ad hoc reports may be sent to senior leadership for a variety of reasons. A CODM may purposefully decide to drop down into lower levels of information as a result of a business combination or a segment in difficulty.

11. Topic 280 lists three factors that entities should consider when deciding which level of information should be used as the basis for segment identification: the nature of the business activities of each component, the existence of managers responsible for them, and information presented to the board of directors. Through its comment letter process in the early 2000s, the SEC emphasized segment identification based on the information that is "regularly reviewed." The SEC's assertion was that if the CODM regularly receives a data set, then the CODM regularly reviews the information to make decisions and allocate resources at that level. This view created significant tension and cost in the system as preparers' judgments were challenged. Under that interpretation, it was suggested that the operating segments should be identified at levels within the business that were not always consistent with the overall organizational structure.

12. At the 2014 AICPA Conference, then OCA Deputy Chief Accountant observed the SEC staff's evolving views:

> Another presumption we have heard from constituents is that the CODM report is somehow the ultimate determinant of operating segments. While we may have placed emphasis on this report in the past, let me be clear there is no presumption to this effect in GAAP; rather, the CODM report, like the organizational chart, is simply one data point in the analysis.

13. Ultimately, the 2014 speech and a similar 2015 speech acknowledged that the SEC continues to place significant regulatory effort on segment identification, but the SEC has shifted its view to consider a variety of indicators and information sources as part of its compliance activities.

14. To be clear, the scope of this project is not reconsidering the basis for segment identification. That is, segments will continue to be identified using the management approach by considering information that is regularly reviewed by the CODM, the internal structure of the organization, and the existence of segment managers.

15. We acknowledge that this scope does not address some stakeholders' concerns about the inconsistency between an entity's reportable segments and how the entity might communicate its business to stakeholders, such as when an entity emphasizes the results of its products or services, rather than the results of the segments.

16. Stakeholders' views on the limitations of the management approach are not new. The FASB has heard these messages since the standard's issuance in 1997. The CODM perspective means that segments are generally identified from a very high level within the organization. Re-opening the basis for segment identification and the definition of an operating segment would involve a fundamental change to segment reporting, and there was very limited support for doing so in the 2016 Invitation to Comment (ITC), *Agenda Consultation.* The ITC asked stakeholders whether the standard should be applied from a governance perspective, rather than a CODM perspective, although there was very limited support for this idea. Said differently, this project is not seeking to solve issues related to the management approach, the CODM perspective, or the basis for identifying operating segments.

The Aggregation Criteria and Reportable Segments

17. Once the operating segments have been identified based on the management approach, they may be aggregated based on the criteria set out in Topic 280, which states:

> **280-10-50-11** Two or more operating segments may be aggregated into a single operating segment if aggregation is consistent with the objective and basic principles of this Subtopic, if the segments have similar economic characteristics, and if the segments are similar in all of the following areas…:
>
> a. The nature of the products and services
> b. The nature of the productions processes
> c. The type of class of customer for their products and services
> d. The methods used to distribute their products or provide their services
> e. If applicable, the nature of the regulatory environment, for example, banking, insurance, or public utilities.

18. The aggregation criteria is another challenging area of the standard. Preparers' judgments are frequently challenged by their auditors and the SEC, and the FASB has received multiple requests over the years to improve this aspect of the literature. Users are often frustrated by a belief that the reportable segments are over-aggregated. Investors generally understand that a certain level of aggregation is permitted, but they also note that entities have the ability to use the flexibility in the standard to obscure certain segments that otherwise would be helpful if reported separately.

19. Over the years, there has been debate over what is meant by the criterion to have *similar economic characteristics*. In practice, the economic characteristics criterion is seen as a quantitative test, while the five other criteria are often viewed as qualitative in nature. Through its comment letter process in the early 2000s, the SEC had taken a narrow view on the percentage range needed to meet the test.

20. According to PwC's Accounting and Reporting Manual, the SEC staff has aggressively challenged registrant assertions, saying that the economic characteristics test was not met when the registrant otherwise believed differences in margins between segments to be relatively small. The PwC manual makes the following observation:

> When evaluating the significance in the differences in margins, registrants should consider the percent difference between the margin percentages, not just the absolute values (e.g., 55 percent vs. 50 percent margin is a 5 percent absolute value difference, but represents a 10 percent spread). Although there is no bright-line with respect to acceptable differences in long-term gross margins, registrants should carefully consider the SEC staff's views and ensure that the facts and circumstances support aggregation.

21. In the 2014 AICPA Conference speech, the SEC staff indicated that their views on this point had evolved. The then OCA Deputy Chief Accountant commented as follows:

> There are also no bright lines when assessing whether two or more operating segments have similar economic characteristics. Rather, entities should use reasoned judgment that is consistent with the objectives of the standard in determining whether the aggregation criteria have been met.

22. This 2014 SEC staff speech and a similar 2015 speech suggest an important change to the SEC's interpretation of the economic characteristics criterion that includes an investor perspective on whether segments should be aggregated.

23. This project is seeking to solve certain issues related to the aggregation criteria and the process for determining reportable segments. Although it is not seeking to clarify the meaning of similar economic characteristics.

Segment Disclosures and Reconciliations to Consolidated Amounts

24. Entities are required to provide certain disclosures by reportable segment if that selected information is regularly reviewed by the CODM or otherwise forms part of the measure of segment profit or loss or segment assets. Furthermore, segment totals are required to be reconciled to consolidated amounts if the segment totals are *significant.* This disclosure method is a cause of frustration for investors for three reasons. First, only certain disclosures are currently required by Topic 280. Users generally want more items disclosed, including gross margin, cash flow information, and working capital balances by reportable segment. Second, the disclosures are required only if the CODM regularly reviews that information. This aspect is particularly frustrating for investors who often comment that "someone in the organization must review this information." This may be true; however, the standard is applied from the CODM perspective, not the segment manager perspective. Accordingly, some investors believe that entitles use the CODM perspective to avoid providing segment disclosures. Finally, not all segment totals are reconciled to consolidated amounts and, additionally, the reconciliations are not required to be reported in a way that connects the segment data to the consolidated amounts. This limits the contextual information and causes frustration for investor modeling.

25. This project is seeking to solve some issues related to the disclosure requirements, particularly reporting additional information by segment. However, the project is not seeking to solve users' issue with the CODM perspective. Consistent with the management approach, the disclosures will continue to be required if the CODM, not the segment manager, regularly reviews the information.

26. The following table summarizes users and preparers concerns and whether this project is addressing those issues:

	Users' and Preparers' Concerns	**Cause**	**Within the Scope of This Project?**
Segment Identification			
1.	Segments are not consistent from entity to entity, making comparisons difficult. Segments seem to frequently change within the same entity.	**Management Approach**	**No**
2.	The CODM perspective is the level at which operating segments are identified. In the past, considerable regulatory effort has been spent on compliance issues in this area, which challenged preparers' judgments and emphasized the CODM reporting package.	**Management Approach / CODM Perspective**	**No**
3.	The CODM may review financial information and identify operating segments at a level that users are not satisfied with and does not necessarily match up to an entity's MD&A.	**Management Approach / CODM Perspective**	**No**
The Aggregation Criteria and Reportable Segments			
4.	Users are concerned that some entities use flexibility within the aggregation criteria to reduce the number of reportable segments.	**Aggregation Criteria**	**Yes**
5.	The application of the aggregation criteria is a compliance area that regulators challenge often, resulting in costs for preparers.	**Aggregation Criteria**	**Yes**
Segment Disclosures and Reconciliations to Consolidated Amounts			
6.	Users want more disclosures by segment than those that are currently required by Topic 280, for example, gross margin, cash flow information, and working capital balance by segment.	**Current Disclosure Requirements**	**Yes**
7.	Users are often frustrated that segment disclosures are not provided because that information is not regularly reviewed by the CODM. Users comment that "someone in the organization must look at this information."	**Management Approach / CODM Perspective**	**No**

8.	Users are often frustrated that not all segment totals are reconciled to consolidated amounts and that the reconciliations are often reported separately from the segment results, which limits the contextual information.	**Current Disclosure Requirements**	**Yes**

Section 3: Previous Standard-Setting Projects

27. Over the years, numerous standard-setting efforts to improve or clarify the standard have been undertaken. In this section of the paper, we consider the following standard-setting efforts:

    (a) 2005 proposed FASB staff position paper—meaning of similar economic characteristics

    (b) 2012 FAF Post-Implementation Review of Statement 131

    (c) 2016 Agenda Consultation.

2005 Proposed FASB Staff Position Paper—Meaning of *Similar Economic Characteristics*

28. By 2004, a number of questions had arisen in practice on how to determine whether two or more operating segments have "similar economic characteristics" for the purposes of applying the aggregation criteria.

29. In 2005, the proposed FASB staff position paper (FSP)[1] indicated, first, that both quantitative and qualitative factors could be identified when determining whether two segments have similar economic characteristics. Examples in the proposed FSP included qualitative factors such as operating risks, currency risks, and political factors. Quantitative factors included gross margins, trends in sales growth, return on assets, and operating cash flows. Secondly, the FASB staff proposed that an entity should identify its entity-specific economic factors from those primary factors that the CODM uses in allocating resources. That is, if the CODM primarily uses gross margin, sales volume, and expected future sales growth to allocate resources, then those are the economic factors that should be considered for the purposes of determining whether the operating segments have similar economic characteristics.

30. In total, six comment letters were received: one each from the major accounting firms and two from preparers. In general, the respondents supported both aspects of the proposed FSP. However, the respondents' principal concern was centered on how those factors should be evaluated for similarity once they are identified, that is, whether all identified factors must be evaluated individually for similarity

[1] Proposed FASB Staff Position (FSP) on Statement 131; FSP FAS No. 131-a, *Determining Whether Operating Segments have "Similar Economic Characteristics" under Paragraph 17 of FASB Statement No. 131,* Disclosures about Segments of an Enterprise and Related Information http://www.fasb.org/cs/ContentServer?site=FASB&c=Document_C&pagename=FASB%2FDocument_C%2FDocumentPage&cid=1176157360527

or a weighing of all factors and the implications of concluding that one individual or one weighted factor is not similar in a given reporting period. Diversity in practice would continue without additional guidance on how to perform the evaluation. The Board decided not to finalize the FSP because it believed that any additional guidance would not reduce the level of judgment required to apply the final standard.

2012 FAF Post Implementation Review of Statement 131

31. In 2012, the FAF published its Post-Implementation Review (PIR) Report[2] on Statement 131. At a similar time, the IASB also published its Report and Feedback Statement, *Post-Implementation Review: IFRS 8 (Feedback Statement).*

32. The FAF Report concluded that, overall, Statement 131 has achieved the objectives that the Board intended when it was issued and has improved financial reporting. Both PIRs indicated that the standards are, in general, working effectively and have enhanced the relevance of segment reporting and promoted greater alignment between the financial statements, management commentary, and analyst presentations. Moreover, the PIRs did not call for a reconsideration of the core principle on which the standards are based—the management approach. However, PIR respondents suggested several issues for improvement.

33. One of the main concerns raised by U.S. respondents was on the aggregation criteria. The PIR Report commented that guidance for aggregating segments can be difficult for entities to apply in part because of the principle-based nature of the standard. The PIR Report observed that some entities reported only one segment. These entities were using the flexibility in the standard to reduce the number of reportable segments. A substantial majority of entities that reported a single reportable segment under the previous standard continued to report a single reportable segment under Topic 280. Academic researchers believe that some of those entities resisted providing more disaggregated segment because of competitive harm concerns or to mask poor performing businesses.

34. The PIR Report also observed that there is considerable regulatory effort spent toward compliance issues. It observed that the system could benefit from additional guidance on applying the aggregation criteria and segment identification because these are the compliance areas that regulators challenge most often.

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[2] FAF PIR Report
http://www.accountingfoundation.org/cs/ContentServer?c=Document_C&cid=1176160621900&d=&pagename=Foundation%2FDocument_C%2FFAFDocumentPage

35. The FASB staff prepared an analysis of each of the issues from both PIR Reports and identified potential improvements to Topic 280. Ultimately, the FASB decided not to add a segment reporting project to its agenda at that time. While aspects of the segment reporting standard could be improved, the Board agreed with the conclusions reached in the PIR Report that Statement 131 is effective and achieving its expected benefits.

2016 FASB Agenda Consultation (ITC)

36. In August 2016, the ITC invited feedback from stakeholders on the accounting issues that potentially are most in need of improvement. The ITC discussed three areas of segment reporting for which there is a perceived need for improvement:

    (a) The aggregation criteria: Preparers express concern that their judgments are often open for challenge by their auditors and the SEC. Users are concerned that entities often combine individual segments for which information would be useful if shown separately.

    (b) Segment disclosures: Many users would like more performance and balance sheet information by segment and want that information to be reported in a way that enhances the contextual relationships with the consolidated amounts. The ITC discussed several ways the guidance could be improved by expanding the disclosure requirements while adhering to the management approach.

    (c) Finally, many users commented that changing the composition of reportable segments and individual segment disclosures results in a loss of important trend data over longer periods of time. Those users would prefer more consistency in segment information over longer time periods. The ITC considered whether segments could be identified from the level of the governing body, such as the board of directors or trustees, instead of the CODM perspective, because that level may have a more consistent segment composition over time.

37. Most respondents did not consider segment reporting to be a major area in need of improvement and a fundamental change to the standard was not necessary. However, many acknowledged that improvements to the guidance were still warranted. In deciding upon the scope of the project, the FASB sought to strike a balance by retaining the management approach while also responding to users' request that entities disclose more reportable segments and more disclosures about those segments.

Question for the IASB—Background and Scope
1. Do IASB members have questions on the background and scope of the project?

38. The remaining sections of this paper discuss the staff's initial deliberations for (a) addressing the aggregation criteria and reportable segments process and (b) improvements to the segment disclosure requirements.

Section 4: Aggregation Criteria and Reportable Segments Process

39. We are considering either of the two alternatives for improvement:
    (a) Remove the aggregation criteria, thereby each operating segment would be reported, but retain the practical limit guidance
    (b) Re-order the process for determining reportable segments and move the quantitative thresholds earlier in that process.

40. To understand the effect of each alternative, the staff batched the technical issues associated with each approach. The Board decided this project should undertake a field testing program at the beginning of the deliberations to understand any operability issues. In our most recent Board meeting, the staff presented the Board an analysis of the technical issues and a working draft of the field testing materials.

41. For the purposes of this paper, we thought it might be helpful to explain to IASB members the substance and follow-on issues related to each alternative.

Re-Order the Size Tests within the Reportable Segments Process

42. As a quick reminder, the process for determining reportable segments under current guidance can be summarized in the following steps:
    (a) *Identify Operating Segments*: Based on a management approach, centered around the CODM function.
    (b) *Step One: Aggregate Segments That Meet All Aggregation Criteria*: After segments are identified, an entity may aggregate two or more segments into a single segment if they meet all of the aggregation criteria in paragraph 280-10-50-11. These segments are not yet deemed reportable. Aggregation is permitted not required.
    (c) *Step Two: Apply the Size Tests to Segments to Determine Reportability*: An entity applies the quantitative thresholds in paragraph 280-10-50-12 to determine which of the segments from (a) and/or (b) are reportable.
    (d) *Step Three: Aggregate Segments That Do Not Meet 10 Percent Tests If Meet Majority of Aggregation Criteria*: An entity may aggregate two or more remaining segments that do not meet the 10 percent tests in the previous step if both of the following apply: (i) the segments have similar economic characteristics and (ii) the segments meet a *majority* of the aggregation

criteria in paragraph 280-10-50-11. Again, it is an option to aggregate, not a requirement. Segments that are aggregated in this step are reportable.

(e) *Step Four: Report Additional Segments until 75 Percent of External Revenue Reported:* After considering the segments that were deemed reportable at step two and step three, entities must continue to report additional segments until 75 percent of external revenue is reported. If 75 percent of external revenue is already reported based on steps two and three, this step may be skipped.

(f) *Step Five: Aggregate Remaining Segments into "All Other" Category:* Segments that are not reportable by earlier steps may be combined into an "All Other" category separate from reconciling items.

(g) *Step Six: Apply a Practical Limit to the Number of Reportable Segments:* As the number of reportable segments increases above 10, the entity considers whether a practical limit has been reached.

43. The appendix of this memo includes an illustration from Topic 280 of these steps.

What Would Be the Main Change under This Alternative?

44. In simple terms, the main change would involve moving step two to step one. Segments would continue to be identified in accordance with the management approach. However, this alternative would require any operating segment that meets and exceeds the quantitative thresholds to be reportable. Segments that fall below the size tests may be aggregated in the later steps of the process. Within this alternative, we also are considering making changes to the size tests.

45. In effect, this alternative would ensure that the largest operating segments are separately reported and are not aggregated with other segments. We think it will result in additional reportable segments compared to today.

Technical Issues Associated with This Approach

46. Should the Board decide to proceed with this approach, the key follow-on technical decisions include:

(a) Issue 1: What should be the threshold bases?

(b) Issue 2: What size (percentage) should be used?

(c) Issue 3: Restatement of prior reporting periods for the threshold effect.

(d) Issue 4: Determining reportable segments after the size test.

Issue 1: What Should Be the Threshold Bases?

47. GAAP currently requires the size tests to be applied on three bases—segment revenue, profit or loss, and assets. In re-ordering the quantitative thresholds to appear earlier in the reportable segments process, there is also an opportunity to reconsider these bases.

48. The staff identified two options: (a) retain the current threshold bases or (b) require additional bases. We do not think it is necessary to remove any of the current bases because they are readily understood by preparers, auditors, and users.

49. At the February 2018 Board meeting at which this issue was discussed, there appeared to be consensus among Board members that the purpose of including additional threshold bases would be to report segments that are (a) currently allocated significant resources by the CODM but are not captured by the current thresholds or (b) expected to be the major growth areas of the business. Research and development expense and capital expenditure are examples of allocated resources not directly captured by the current thresholds.

50. In our field testing materials, we are asking preparers to provide information about the effect on the number of reportable segments when the size tests are applied earlier and the effect of including research and development expense and capital expenditure as additional size tests.

Issue 2: What Size (Percentage) Should Be Used?

51. The second key technical issue considers what size (percentage) should be used on the threshold bases. In re-ordering the reportable segments process, there is also an opportunity to reconsider the percentage used. Under current GAAP, if an operating segment meets or exceeds 10 percent of any of the thresholds, that segment automatically becomes reportable and the segment cannot be aggregated with other operating segments.

52. In the February 2018 Board meeting, FASB members discussed alternatives to using 10 percent. However, the Board signaled that it does not intend to modify this percentage and directed the staff use 10 percent in all thresholds in the field testing materials.

Issue 3: Restatement of Prior Reporting Periods for the Threshold Effect

53. The third key technical issue considers the requirement to restate prior comparative periods because of an operating segment moving above or below a threshold percentage. An operating segment could exceed a size test based on current period segment information and, therefore, be reportable, or could be below the thresholds in the next. The inverse also could occur.

54. We think restatements of comparative information will occur more frequently as a result of an operating segment moving above or below a threshold percentage in the current period.

55. The staff identified two options for this issue. The first is to retain current GAAP, that is, restate prior periods to be consistent with current period reportable segments.

56. The second is to restate prior periods only for segments that exceed the thresholds. If a segment falls below the size tests in the current period, restatement of prior comparative periods would not be permitted. A disclosure would explain that the segment was aggregated in the current year because it fell below the size test. Comparative period segment data would continue to disclose information as if the segment was reportable. If a segment exceeds the size test in the current period, comparative period information is restated to be consistent with the newly reportable current period segment.

57. In the field testing materials, we are asking participants of the advantages and disadvantages of these two options.

Issue 4: Process for Reporting Information about Segments That Fall below the Size Tests

58. The fourth key technical issue, if the Board decides to pursue this approach, is the steps followed to report information about segments that fall below the size tests.

59. We acknowledge that this issue is quite complex and involves multiple steps. However, it is a feature of current GAAP. The staff is uncertain how to simplify this issue beyond the options already identified. In the February 2018 Board meeting, the staff provided two recommendations for the field testing.

Option One: Size Tests → Aggregate All → 75% Test → Aggregate Majority → All Other

60. Under this option, the process for reporting information about segments that fall below the size tests is as follows:

    (a) *Step One:* First apply the size tests. Segments that meet or exceed the size tests are reportable.

    (b) *Step Two:* Segments that fall below the size test may be aggregated into a single operating segment if the segments meet *all* of the aggregation criteria. This step does not necessarily determine whether the aggregated segment is reportable.

    (c) *Step Three:* Report additional segments until 75 percent of external revenue reported. Any segments identified at this step are reportable.

    (d) *Step Four:* Any remaining operating segments would be permitted to apply a second round of aggregation if those segments share a *majority* of the aggregation criteria. The economic characteristics criterion would be evaluated as part of that majority and would not be an additional test. The segments identified at this step are reportable.

(e) *Step Five:* Information about other segments that are not otherwise reportable at earlier steps should be combined in an "All Other" Category separate from other reconciling items.

(f) *Step Six:* Consider whether a practical limit of 10 reportable segments has been reached.

61. The advantage of this option is that it is the least disruptive to the Topic 280 literature. In essence, all of the current steps are retained, but reordered as the size tests appear earlier in the process.

Option Two: Size Tests → Aggregate Majority → 75% Test → All Other

62. Under option two, the process for reporting information about segments that fall below the size tests is as follows:

(a) *Step One:* First apply the size tests. Segments that meet or exceed the size tests are reportable.

(b) *Step Two*: Segments that fall below the size test may be aggregated into a single operating segment if the segments meet the *majority* of the aggregation criteria. The economic characteristics criterion would be evaluated as part of the majority and would not be an additional test. This step does not necessarily determine whether the aggregated segment is reportable.

(c) *Step Three*: Report additional segments until 75 Percent of external revenue reported. Any segments identified at this step are reportable.

(d) *Step Four:* Information about other segments that are not otherwise reportable at earlier steps should be combined in an "All Other" category separate from other reconciling items.

(e) *Step Five:* Consider whether a practical limit of 10 reportable segments has been reached.

63. The advantage of this option is that it simplifies the reportable segment process the most. The *aggregate all* test is removed and the process involves five steps, rather than six.

64. In the field testing materials, we are asking participants to explain the effect on the number of reportable segments under both options.

Question for the IASB—Re-order the Reportable Segments Process
3. Do IASB members have questions on this Alternative?

Remove the Aggregation Criteria and Retain the Practical Limit Guidance

What Would Be the Main Change under This Alternative?

65. This approach would remove the aggregation criteria from Topic 280 and an entity would be required to report its operating segments unless it reaches a practical limit, such as 10 reportable segments. Segments would continue to be identified based on the management approach; however, those operating segments would then become an entity's reportable segments.

66. In developing the present standard, the FASB concluded that requiring an entity to report all of the information that is reviewed by the CODM in a so-called pure management approach could lead to a level of detail that may not be useful to investors and may be cumbersome for the entity to report. For that reason, the Board decided that permitting, but not requiring, the aggregation of segments and providing mechanisms to determine when a segment is reportable would help provide for the right amount of detail. As a result, the Board specifically acknowledged that they were adopting a "modified management approach" when determining which segments to report.

67. Removing the aggregation criteria would revert the standard to a purer form of the management approach. It would permit users to view the business more in line with how management views the entity and is, arguably, closer to the original principle of the standard.

68. The Board's original conclusion in 1997 that the level of detail may not be useful to users under a pure management view may no longer hold true in 2018. Both technology and how users consume segment information have evolved. Electronic data has enabled greater consumption of information that can be mapped more efficiently into investors' models and forecasts. However, the Board's original conclusion that a pure management approach may result in cumbersome reporting of numerous segments for the entity likely holds true. The staff, therefore, thinks it is important that this approach retain some sort of practical limit.

69. We acknowledge that the decision to remove the aggregation criteria, in itself, is a significant change to current GAAP. We expect to receive preparers' feedback on the merits of this decision during the field testing, and there will likely be strong points of view on this matter.

Technical Issues Associated with This Approach

70. Should the Board decide to proceed with this approach, the key follow-on technical decisions include:

    (a) Issue 1: What should be the practical limit?

    (b) Issue 2: What should be the basis of reporting segments when an entity exceeds the practical limit?

(c) Issue 3: Restatement of prior reported periods when there is a change in the composition of the “all other” reportable segment.

Issue 1: What Should Be the Practical Limit?

71. Topic 280 currently has a practical limit of 10 reportable segments. In removing the aggregation criteria, the Board has an opportunity to reconsider that limit. Given preparers’ experience with the practical limit, we neither think it should be lowered nor do we think it should be eliminated. In the staff’s view, there needs to be a mechanism that limits the number of reportable segments, otherwise the cost to report the information would not justify the benefits.

72. Two options were identified by the staff. The Board could retain the practical limit at 10 reportable segments. This means that Segments 1–9 are separately reported, and any remaining segments are aggregated into the tenth, “All Other” reportable segment. Alternatively, the Board would increase the practical limit to, say, 15 reportable segments. This means that Segments 1–14 are separately reported, and any remaining segments are aggregated into the fifteenth, “All Other”, reportable segment.

73. In our field testing materials, we are asking preparers to provide information about the number and size of operating segments identified. We are specifically seeking participants who are engaged in retail operations and real estate because those entities often identified large numbers of operating segments.

Issue 2: What Should Be the Basis for Reporting Segments When an Entity Exceeds the Limit?

74. The second key technical issue under this alternative is determining the basis for reporting the operating segments when an entity’s segments exceed the practical limit. In other words, how to decide which of the operating segments should be reported separately and which should be aggregated into the “All Other” segment. In removing the aggregation criteria and retaining a practical limit, the Board has an opportunity to address this issue.

75. Topic 280 does not explain how to determine which reportable segments should be reported if an entity exceeds the practical limit. That said, it is implicit that individual segments or aggregated segments that exceed the 10 percent quantitative thresholds should be reported.

76. We think that the existing quantitative thresholds—revenue, profit or loss, and assets—encourage the largest segments to be first reported. However, in choosing a quantitative basis to determine which operating segments to report, the Board will have to pick one of these bases to prioritize.

77. As illustrated below, an entity would not know which segments to separately report if each quantitative basis had equal priority when ranking the individual operating segments.

Operating Segments by ranking											
	A	B	C	D	E	F	G	H	I	J	K
Revenue	1	2	3	4	5	6	7	8	9	10	11
Profit/Loss	3	1	2	4	6	7	5	9	11	8	10
Assets	10	5	4	1	2	7	6	3	8	11	9

**Operating Segments (A-K) are ranked 1-11 from largest to smallest respective of each basis. The practical limit in this illustration is assumed to be 10.*

78. If revenue was chosen as a basis, Segments A–I would be reported separately, and Segments J and K would be aggregated into the "All Other" category. If profit or loss was the basis, Segments B to H and J would be separately reported, and Segments I and K would be aggregated into the "All Other" category.

79. The staff identified two options for this issue. The Board could require that the largest segments based on revenue (internal and external) would be first reported. Any remaining segments above the practical limit would be aggregated into an "All Other" category. Topic 280 currently emphasizes segment revenue in two ways. First, the quantitative thresholds currently include segment revenue as a basis for determining reportable segments and, second, the 75 percent revenue test ensure that at least 75 percent of segment revenue is disclosed. This alternative is a continuation of that emphasis.

80. Alternatively, the Board could require that the entity decides, through an accounting policy, which segments are the most useful to users to report separately based on the objective of the standard in paragraph 280-10-10-1.[3] The entity would disclose the rationale in the notes. The advantage of this alternative is that it may revert the standard to a purer form of the management approach and would rely on the standard's objective. The disadvantage of this alternative is that management could obscure the largest, most significant segments or could mask poor performing segments in the "All Other" category.

81. In the field testing materials, we asked participants about the operability of these two alternatives.

Issue 3: Restatement of Prior Reporting Periods for Changes to the "All Other" Segment

82. Stakeholders have raised concern about the increased frequency of having to restate prior reporting periods, which are shown for comparative purposes, under this approach. For example, assume in

[3] **280-10-10-1** The objective of requiring disclosures about segments of a public entity and related information is to provide information about the different types of business activities in which a public entity engages and the different economic environments in which it operates to help users of financial statements do all of the following:

(a) Better understand the public entity's performance
(b) Better assess its prospects for future net cash flows
(c) Make more informed judgments about the public entity as a whole.

Issue 2 that the Board decides that segments with the largest revenue are first reported. Any remaining segments that exceed the practical limit are included in the "All Other" category. Over time, the segment revenues may change with a larger percentage of revenue in one of the segments previously included in the "All Other" category, necessitating that segment moving out of "All Other" in the current reporting period.

83. Considering whether or when to require restatements only arises for restatements that result from operating segments that move in or out of the "All Other" category. It does not apply to restatements that result from internal reorganizations. In the latter case, the guidance in paragraphs 280-10-50-34 through 50-36 continues to apply.

84. Topic 280 currently requires that if a new reportable segment is identified in the current reporting period, an entity is required to restate the newly reported segment in prior periods even if that segment would not have met the criteria for reportability in the prior period. This means that comparative period reportable segments are required to be consistent with the current period reportable segments.

85. Given that this issue only arises when an entity exceeds the practical limit of say 10 or 15 segments, the staff recommended that the current restatement requirements in Topic 280 continue to apply for this issue. That is, prior period segments are consistent with current period reportable segments.

86. However, FASB members suggested an additional alternative, specifically that operating segments that *move out* of the "All Other" category as a result of a change in ranking require restatement of comparative periods. Operating segments that otherwise would *move in* the "All Other" category, as a result of a change in ranking, continue to be reportable until the segment is divested or the entity undertakes a reorganization. In other words, this would be an exception to the practical limit.

87. In our field testing materials, we are asking preparers to provide information about the advantages and disadvantages of restating comparative period information.

Question for the IASB—Remove the Aggregation Criteria and Retain Practical Limit
2. Do IASB members have questions on this alternative?

Section 5: Segment Disclosures

88. Users have said that they want more disclosures by segment and they want that information to be reported in a way that enhances the relationship between the segment information and the consolidated information. To address this issue, we are focused on three alternatives for improvement:

(a) Add individual pieces of segment information to the list of required disclosures

(b) Require the disclosures in Topic 280 to be reported in a table that reconciles segment totals to consolidated totals

(c) Require a table of regularly reviewed information in the format of the entity's financial statements.

Adding Items in the Current List of Disclosure Requirements

What Would Be the Main Change under This Alternative?

89. The Board could decide to add specific individual pieces of information to the current list of required segment disclosures in Topic 280. These disclosures would be required only if the information is regularly reviewed by the CODM, and the amounts would be based on the entity's internal measures, not GAAP measurement methods.

90. Topic 280 currently requires the following segment disclosures:

> **280-10-50-22** A public entity shall report a measure of profit or loss and total assets for each reportable segment. A public entity also shall disclose all of the following about each reportable segment if the specified amounts are included in the measure of segment profit or loss reviewed by the chief operating decision maker or are otherwise regularly provided to the chief operating decision maker, even if not included in that measure of segment profit or loss:
>
> a. Revenues from external customers
> b. Revenues from transactions with other operating segments of the same public entity
> c. Interest revenue
> d. Interest expense
> e. Depreciation, depletion, and amortization expense
> f. Unusual items as described in paragraph 220-20-45-1
> g. Equity in the net income of investees accounted for by the equity method
> h. Income tax expense or benefit
> i. Subparagraph superseded by Accounting Standards Update No. 2015-01
> j. Significant noncash items other than depreciation, depletion, and amortization expense.
>
> **280-10-50-25** A public entity shall disclose both of the following about each reportable segment if the specified amounts are included in the determination of segment assets reviewed by the chief operating decision making or are otherwise regularly provided to the chief operating decision making, even if not included in the determination of segment assets:
>
> a. The amount of investment in equity method investees
> b. Total expenditures for additions to long-lived assets other than any of the following…:
>   1. Financial instruments
>   2. Long-term customer relationships of a financial institution
>   3. Mortgage and other servicing rights
>   4. Deferred policy acquisition costs
>   5. Deferred tax assets.
>
> **280-10-50-26** If no asset information is provided for a reportable segment, that fact and reason for its exclusion shall be disclosed

91. At present, the staff is considering three additional pieces of segment information: (a) gross margin, (a) inventory and research and development expense, and (c) cash flow.

Gross Margin

92. The staff will present to the Board proposals that would require disclosure of gross margin by reportable segment if that amount is reviewed by the CODM. This measure of gross margin would be self-defined, based on the measure the CODM reviews.

93. Users have consistently requested more granular profitability information on a segment basis, specifically gross margin. Gross margin is less affected by internal cost allocations and is considered a better measure of the segment's performance.

94. Disclosure of segment gross margin also would be internally consistent within the standard because the aggregation criteria already suggests that similar economic characteristics is an evaluation of long-term average gross margin.

Other Asset and Profit or Loss Information

95. The staff will present to the Board a proposal to address the internally consistency with the potential changes to the quantitative thresholds (discussed in paragraphs 47 to 50). If regularly reviewed by the CODM, research and development expense also could be disclosed by reportable segment and reconciled to the consolidated amount. Capital expenditure by segment is currently required.

96. Similarly, if regularly reviewed by the CODM, the other asset information could be disclosed segmentally and reconciled to the consolidated amount. Specifically, the Board directed the staff to consider the decisions made in the Disclosure Framework: Disclosure Review—Inventory project.

97. In January 2017, the Board's Exposure Draft for Disclosure Review—Inventory project proposed the following additional disclosures by reportable segment in the underlined text:

> **280-10-50-25** A public entity shall disclose both of the following about each reportable segment if the specified amounts are included in the determination of segment assets reviewed by the chief operating decision making or are otherwise regularly provided to the chief operating decision making, even if not included in the determination of segment assets:
>
> a. ….
>
> b. ….
>
> <u>c. **Inventory,** only if such information is reviewed by or regularly provided to the chief operating decision maker by segment (see Example 4 in paragraphs 280-10-55-53 through 55-54):</u>
>
> 1. <u>In total. If any portion of inventory is not allocated to a segment, that amount shall be classified as unallocated.</u>
> 2. <u>By major component (such as raw materials, work-in-process, finished goods, and supplies). If any portion of inventory is not allocated to a segment or to a component, that amount shall be classified as unallocated.</u>

98. The Board discussed including this inventory disclosure proposal within the segment reporting project, rather than making a standalone change to Topic 280 within the Disclosure Review—Inventory project.

Cash Flow

99. Users have told us they would like to review segment cash flow information. In our discussion with preparers, we understand that segment cash flow information is almost never prepared in accordance with Topic 230, Statement of Cash Flows, if it is prepared segmentally at all. If segment cash flow information is available, it is almost never reconciled to amounts presented in the cash flow statement.

100. The staff will present to the Board proposals that (a) require disclosure of a measure of segment cash flow, if that measure is reviewed by the CODM, and (b) require an entity to explain the composition of that measure. However, total segment cash flows would not be reconciled to any consolidated amount. The cash flow measure would be self-defined based on what the CODM regularly reviews.

Question for the IASB—Additional Segment Disclosures
4. Do IASB members have questions on the ideas for additional segment disclosures?

Reporting Topic 280 Disclosures and Reconciliations in a Table

What Would Be the Main Change under This Alternative?

101. Segments would continue to be identified based on the management approach and the segment disclosures in Topic 280 would continue to be required if those amounts are regularly reviewed by the CODM. However, this approach would require the Topic 280 disclosures and the reconciliations to be reported in a table.

102. Consistent with many other standards, Topic 280 does not require segment disclosures to be reported in a single location. It is not uncommon for segment information to be reported in (a) a segment note, (b) the goodwill impairment note, and (c) revenue disclosure note. Furthermore, often the segment reconciliations are reported in a separate manner to the segment results, and the standard does not require all segment totals to be reconciled to consolidated amounts. GAAP requires reconciliations for segment revenue, profit and loss, assets and “significant” segment amounts. All of these features limit the contextual value of how segment results relate to consolidated amounts.

103. In other parts of GAAP, the FASB has decided to require disclosures to be reported in a tabular format and in one location, for example, hedging disclosures and the reporting of amounts within accumulated other comprehensive income. The Board has done this for particular reasons, specifically to enable users to understand the connectivity of the reported information.

104. The Board included the following example in the 2016 Agenda Consultation:

<See next page for the illustration>

Alternative B: Illustrative Table Based on Existing Topic 280, Segment Reporting, Disclosures XYZ Company, Inc.

Note: Supplemental segment items in the illustration below, such as gross margin, working capital, and cash flow from operating activities, are not currently required by Topic 280 but could be required in the future.

	Segment Information							
	Reportable Segment A	Reportable Segment B	Other Segments (a)	Total of Segments	Amounts Not Allocated to Segments (b) (c) (d)	Elimination of Intersegment Amounts	Entity-Wide Total	Financial Statement Caption
Information about Segment Profit								
Revenues from external customers	$ 17,500	$ 17,000	$ 1,000	$ 35,500				
Intersegment revenues	3,000	1,500	-	4,500				
Segment revenues	20,500	18,500	1,000	40,000	$ -	$ (4,500)	$ 35,500	Revenue
Interest expense	-	-	-	-	850	-	850	Interest expense
Interest income	400	500	-	900	75	-	975	Interest income
Depreciation and amortization	350	2,600	-	2,950	425	-	3,375	Costs of goods sold, SG&A
Segment profit	1,470	2,500	100	4,070	200	(1,200)	3,070	Income before income taxes
Other significant noncash items:								
Cost in excess of billings on long-term contracts	200	-	-	200	-	-	200	SG&A
Goodwill impairment	500	-	25	525	-	-	525	Goodwill impairment
Information about Assets and Capital Expenditures								
Segment assets	11,450	39,900	1,850	53,200	66,800	(2,000)	118,000	Total assets
Capital expenditures	-	-	-	-	3,900	-	3,900	Capital expenditures
Supplemental Segment Information								
Gross margin	7,180	4,420	300	11,900	(425)	(2,475)	9,000	Gross margin
Working capital	1,800	4,350	50	6,200	3,600	(3,000)	6,800	N/A
Cash flow from operating activities	-	-	-	-	5,500	-	5,500	Cash flow from operating activities

Reconciliation and Segment Notes

(a) Other segments include a small real estate business, a warehouse leasing operation, an electronics equipment rental business, and a software consulting practice.

(b) Certain income statement amounts are not allocated to reportable segments and are reviewed by the CODM at the consolidated level. The following amounts are not allocated to reportable segments: $850 related to interest expense, $75 related to interest income, and $425 related to cost of goods sold for depreciation and amortization.

(c) Certain assets, liabilities, and capital expenditures are not allocated to reportable segments and are managed at the consolidated level. Unallocated amounts include $66,800 in assets and $3,900 in capital expenditures.

(d) Certain supplemental segment information amounts are not allocated to reportable segments because they relate to assets and liabilities that are managed at the consolidated level. The following amounts are not allocated to reportable segments: $425 related to cost of goods sold for depreciation and amortization, $3,600 in working capital, and $5,500 in cash flow from operating activities.

105. Should the Board decide to proceed with this approach, some of the key follow-on technical decisions include:

(a) Issue 1: Requiring reconciliations for all segment totals

(b) Issue 2: How to report reconciling items within a table that is consistent with the management approach

(c) Issue 3: Page break concerns—reporting in a split table or single table.

106. We have not completed our analysis for each of these issues.

Question for the IASB—Reporting the Segment Disclosures and Reconciliations in a Table
5. Do IASB members have questions on reporting the segment disclosures and reconciliations within a table?

Reporting Segment Information in a Financial Statement Format

What Would Be the Main Change under This Alternative?

107. Segments would continue to be identified based on the management approach. However, this approach would require the segment amounts to be reported based on how those amounts relate to the lines presented in the income statement and the assets and liabilities in the balance sheet. For example, the CODM may regularly review (a) occupancy expenses, (b) employee expenses, and (c) depreciation expense by segment. The segment information would be reported based on how those amounts are allocated to the Cost of Goods Sold line and the Selling, General, and Administrative line presented in the income statement. For income statement lines, or components thereof, that are not allocated segmentally or are not regularly reviewed by the CODM segmentally, this approach would require reporting of those amounts within an unallocated column.

108. In effect, this alternative would provide users with segment information in a table in a way that enhances the contextual relationships to the consolidated amounts.

109. The following example was included in the 2016 Agenda Consultation:

<See next page for the illustration>

Alternative C: Illustrative Table Based on Captions in the Consolidated Income Statement and Balance Sheet XYZ Company, Inc.

Note: This illustration was developed with the following assumptions: (1) only income statement and asset and liability lines and captions are required to be displayed on a segment basis, (2) only subtotals for total assets and total liabilities from the consolidated balance sheet are displayed on a segment basis, and (3) supplemental information for segment items such as capital expenditures, depreciation, and amortization may also be provided under this alternative.

				Segment Information			
	Consolidated Total	Amounts Not Allocated to Segments (a) (b) (c)	Elimination of Intersegment Amounts	Total of Segments	Reportable Segment A	Reportable Segment B	Other Segments (d)
Income Statement							
Revenue	$ 35,500	$ -	$ 4,500	$ 40,000	$ 20,500	$ 18,500	$ 1,000
Cost of goods sold	26,500	(425)	2,025	28,100	13,320	14,080	700
Selling, general, and administrative	7,030	500	1,275	8,805	5,610	3,020	175
Goodwill impairment	525	-	-	525	500	-	25
Interest expense	850	(850)	-	-	-	-	-
Interest income	975	(75)	-	900	400	500	-
Other income, net	1,500	(900)	-	600	-	600	-
Income before income taxes	3,070	(200)	1,200	4,070	1,470	2,500	100
Income tax expense	750	(750)	-	-	-	-	-
Net income	2,320	550	1,200	4,070	1,470	2,500	100
Information about Assets and Liabilities							
Cash and cash equivalents	15,050	(14,000)	-	1,050	300	550	200
Available-for-sale investment securities	4,250	(4,250)	-	-	-	-	-
Accounts receivable	17,100	(16,050)	2,000	3,050	1,300	1,650	100
Inventories	16,850	(5,000)	-	11,850	2,200	9,200	450
Prepaid expenses and other current assets	11,750	(8,500)	-	3,250	700	2,350	200
Property, plant, and equipment, net	31,000	(4,000)	-	27,000	3,500	23,000	500
Goodwill	5,000	(2,500)	-	2,500	2,400	-	100
Trademarks and other intangible assets	9,500	(7,500)	-	2,000	600	1,300	100
Deferred tax assets	4,500	(4,500)	-	-	-	-	-
Other assets	3,000	(500)	-	2,500	450	1,850	200
Total assets	118,000	(66,800)	2,000	53,200	11,450	39,900	1,850
Accounts payable	30,600	(22,000)	(1,000)	7,600	1,450	5,750	400
Accrued and other liabilities	22,400	(17,000)	-	5,400	1,250	3,650	500
Debt due within one year	5,200	(5,200)	-	-	-	-	-
Long-term debt	12,200	(12,200)	-	-	-	-	-
Deferred tax liabilities	7,300	(7,300)	-	-	-	-	-
Other noncurrent liabilities	10,300	(10,300)	-	-	-	-	-
Total liabilities	88,000	(74,000)	(1,000)	13,000	2,700	9,400	900
Supplemental Segment Information							
Capital expenditures	3,900	(3,900)	-	-	-	-	-
Depreciation and amortization	3,375	(425)	-	2,950	350	2,600	-

Reconciliation and Segment Notes

(a) Certain income statement amounts are not allocated to reportable segments and relate to amounts that are managed at a consolidated level. The following amounts are not allocated to reportable segments: $425 related to cost of goods sold for depreciation and amortization, $500 related to selling, general, and administrative expenses comprising a net of (i) $750 for litigation settlement received and (ii) $250 for a measurement adjustment to pension expense, $850 related to interest expense, $75 related to interest income, and $900 related to other income for lease rentals.

(b) Certain assets and liabilities are not allocated reportable segments and are managed at the consolidated level. Unallocated assets and liabilities are managed through the corporate headquarters.

(c) Certain supplemental segment information amounts are not allocated to reportable segments and are managed at the consolidated level. The following amounts are not allocated to reportable segments: $3,900 in capital expenditures and $425 for depreciation and amortization.

(d) Other segments include a small real estate business, a warehouse leasing operation, an electronics equipment rental business, and a software consulting practice.

110. Should the Board decide to proceed with this approach, some of the key follow-on technical decisions include:

(a) Issue 1: How to report segment amounts when those items are allocated to multiple income statement or balance sheet lines

(b) Issue 2: How to report the measure of segment profit or loss that does not have an equivalent consolidated profit or loss measure

(c) Issue 3: How to report reconciling items in the table

(d) Issue 4: Should the table reconcile all asset and liability lines, only income statement lines or some other option.

111. Again, we have not completed our analysis for each of these issues.

Question for the IASB—Reporting Segment Information in a Financial Statement Format
6. Do IASB members have questions on this alternative?

APPENDIX: Process for Determining Reportable Segments