



CMAC Meeting, March 2018

Agenda paper 2A

Primary Financial Statements Requirements for management performance measures and adjusted EPS

The views expressed in this presentation are those of the presenter, not necessarily those of the International Accounting Standards Board (the Board) or IFRS Foundation.

Purpose and structure of this meeting

- To seek input from CMAC members on introducing into the financial statements
 - management performance measures (MPMs), and
 - management-defined adjusted earnings per share (adjusted EPS)
- The slides are structured as follows:
 - background – slides 4-5
 - proposed structure for the statement(s) of financial performance – slides 7-8
 - MPMs – slides 10-12
 - adjusted EPS – slides 14-16
 - questions to CMAC members – slides 18-19
 - appendix – slide 22

Background

Previous staff proposals for two subtotals

Flexibility - Performance measure that management uses to communicate progress towards its business objective or strategy

Items between two subtotals show how an entity's MPM is different from EBIT

Comparability - Introducing a comparable performance measure among entities as an 'anchor'

Revenue	10,000
Cost of goods sold	<u>-4,000</u>
Gross profit	6,000
Selling, general and admin costs (SG&A)	<u>-2,500</u>
Management performance measure	3,500
Restructuring expenses	<u>-500</u>
EBIT	3,000
Finance income	200
Finance expenses	<u>-1,200</u>
Pre-tax profit	2,000
Taxation	<u>-600</u>
Profit	1,400



Feedback at June 2017 CMAC/GPF meeting

- 3 of 4 groups supported proposal to present MPM in statement(s) of financial performance
 - merits include scope of audit, transparency, consistency over time and additional disclosures
 - noted we should limit constraints on MPM so it reflects management's view of performance
- Other group opposed proposal because felt MPMs do not belong in financial statements
 - instead supported greater disaggregation, including separate presentation of infrequent items



Proposed structure for the statement(s) of financial performance

Illustration of proposed structure

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Prioritise introduction of comparable subtotals over MPM

New category 'income/expenses from investments'

Revenue	10,000
Cost of goods sold	<u>-4,000</u>
Gross profit	6,000
Selling, general and admin costs (SG&A)	<u>-2,000</u>
Profit before investing, financing and income tax	3,000
Dividends from equity instruments	250
Other investing income	50
Profit before financing and income tax (EBIT)	3,300
Interest income from cash and cash equivalents calculated using effective interest method	80
Other income from cash and cash equivalents and financing activities	20
Expenses from financing activities	(1,000)
Other finance income	50
Other finance expense	(350)
Pre-tax profit	2,100



Description of proposed structure

- Proposed structure for the statement(s) of financial performance:
 - by function or by nature analysis of expenses
 - profit before financing, investing and income tax subtotal
 - income/expenses from investments category
 - profit before financing and income tax (EBIT) subtotal
 - finance income/expenses category
- Existing requirements for additional subtotals would continue to apply (paragraph 85A of IAS 1):
 - comprised of line items of amounts recognised and measured in accordance with IFRS
 - presented and labelled in clear and understandable manner
 - consistent from period to period
 - not more prominent than subtotals/totals required by IFRS



Management performance measures (MPMs)





What is a MPM?

- We are proposing to require an entity to identify its key financial performance measures in the financial statements (identified as management performance measures)
- The Board is discussing whether to either:
 - require MPM to be presented in the statement(s) of financial performance if it fits the proposed structure (slides 7-8), or otherwise disclosed in the notes as part of a reconciliation with the most appropriate subtotal/total specifically required in IFRS Standards (eg EBIT, profit before investing, financing and tax, profit); or
 - always require MPM to be disclosed in a reconciliation in the notes

Should we require a MPM subtotal if it 'fits' our proposed structure?

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Revenue	10,000
Cost of goods sold	<u>-4,000</u>
Gross profit	6,000
Selling, general and admin costs (SG&A)	<u>-2,000</u>
Management performance measure	4,000
Restructuring expenses	<u>-1,000</u>
Profit before investing, financing and income tax	3,000
Dividends from equity instruments	250
Other investing income	50
Profit before financing and income tax	3,300
Interest income from cash and cash equivalents calculated using effective interest method	80
Other income from cash and cash equivalents and financing activities	20
Expenses from financing activities	(1,000)
Other finance income	50
Other finance expense	(350)
Pre-tax profit	2,100

MPM in a separate reconciliation

Reconciled to most appropriate subtotal or total required by IFRS Standards

Management performance measure reconciliation	
Profit before investing, financing and income tax	3,000
Restructuring expenses	1,000
Net interest income on net defined benefit assets (part of other finance income)	(100)
Management performance measure	<u>3,900</u>

This MPM does not 'fit' proposed structure for the statement(s) of financial performance because it adjusts for an item of finance income/expense

Adjusted EPS



Feedback from investors

- From our research and outreach we have identified three main concerns
 - many entities only present adjusted EPS outside the financial statements without sufficient information and transparency
 - an entity's adjusted EPS is sometimes not consistently calculated with its MPM, such as operating profit, and this has the potential to mislead
 - existing IFRS disclosures about adjusted EPS do not provide enough information, for example about non-controlling interest (NCI) and tax effects of adjustments



Possible approach to address this feedback

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- Require adjusted EPS to be included in the financial statements and for it to be consistently calculated with MPM
- Require information about the NCI and tax effects of items excluded from adjusted EPS
- Prohibit other adjusted EPS amounts in the financial statements to avoid confusion

Possible disclosure?

Category	Items excluded	Gross	Tax and NCI	Net
Items excluded from the management performance measure	Restructuring expenses	-300	30	-270
	Amortisation of intangibles	-200	20	-180
	Share-based payment	-400	40	-360
	subtotal	-900	90	-810
Items excluded from finance income/expenses	Early redemption of debt	-50	5	-45
	subtotal	-50	5	-45
Items excluded from the adjusted EPS		-950	95	-855

'Items excluded' from the management performance measure

Slide 22 provides a possible alternative layout for the disclosure which provides more detail

'Items excluded' from adjusted EPS (all adjustments, net of tax and NCI)

Questions for CMAC members

Q1

Should the MPM be required to be presented as a subtotal in the statement(s) of financial performance if it fits the proposed structure for the statement(s) (see slides 7-8)?

If the MPM does not fit into the proposed structure for the statement(s) of financial performance, would you prefer the reconciliation between the MPM and the most appropriate subtotal or total required by IFRS Standards (see slide 12) to:

- form part of the primary financial statements (eg present the reconciliation below the statement(s) of financial performance); or
- be disclosed in the notes?

Note: Because of our proposed restrictions on the structure of the statement(s) of financial performance we think many MPMs will not fit into the proposed structure for the statement(s) for financial performance.

Q2

Would you find an adjusted EPS that is consistently calculated with the MPM useful? Would you find the disclosure about the tax and NCI effects of adjustments to the MPM and adjusted EPS on slide 16 helpful? How would you use this information?

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Appendix

Alternative possible disclosure for adjusted EPS

	IFRS subtotal	Adjustments to reach MPM			Further adjustment for adjusted EPS	MPM
	Profit before investing, financing and tax	Restructuring changes	Amortisation of intangibles	Share-based payment expenses	Early redemption of debt	Adjusted operating profit
Profit before investing, financing and tax/ Adjusted operating profit	1,000	300	200	400		1,900
Income/expenses from investments	100					100
Finance income/expenses	-100				50	-50
Income tax	-160	-24	-16	-32	-5	-237
NCI	-40	-6	-4	-8	-1	-59
Profit/Adjusted profit attributable to ordinary equity holders of the parent entity	800	270	180	360	44	1,654
EPS/Adjusted EPS	0.08	0.027	0.018	0.036	0.004	0.165