

STAFF PAPER

March 2018

IASB Meeting

Project	Improvements to IFRS 8 <i>Operating Segments</i> arising from the post-implementation review		
Paper topic	Proposed amendment to link IFRS 8 reportable segments with other parts of the annual reporting package		
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Objective

1. The objective of this paper is to discuss how the International Accounting Standard Board (Board) should proceed with the proposal in the Exposure Draft *Improvements to IFRS 8 Operating Segments* (Proposed amendments to IFRS 8 and IAS 34) (Exposure Draft) that an entity should link its IFRS 8 reportable segments with other parts of the annual reporting package (the proposal).
2. The staff are asking the Board one question: do you agree with the staff recommendation to proceed with development of the proposal but to limit the scope of the proposal to the annual report?

Structure of the paper

3. This paper is structure as follows:
 - (a) review of the proposal in the Exposure Draft and the comments received (paragraphs 4-15);
 - (b) additional outreach (paragraphs 16-17);
 - (c) staff analysis and recommendations on how to proceed with the proposal (paragraphs 18-25).

Appendix A provides and discusses definitions of the ‘annual reporting package’ and the ‘annual report’.

Review of the proposal in the Exposure Draft and comments received

Overview of the proposal in the Exposure Draft

4. The Exposure Draft included the Board's proposal to require an explanation in the notes to the financial statements when segments identified by an entity differ between the financial statements and other parts of its annual reporting package.
5. As reported to the Board at its November 2017 meeting, the proposal raised a significant number of comments from respondents to the Exposure Draft.
6. Nearly all respondents agree that the issue of inconsistency of segment information in an entity's different reports exists in practice. They also agree with paragraph BC13 of the Exposure Draft that users of financial statements:
 - expect that when the segment information is reported using the management approach there will be consistency in applying this approach across a range of documents.¹
7. The concerns from respondents can be categorised as follows:
 - (a) the Board's mandate to link IFRS 8 segments with other parts of the annual reporting package; and
 - (b) the definition of 'the annual reporting package'.

Mandate to link IFRS 8 segments with other parts of the annual reporting package

8. As explained in agenda paper 27B of the November 2017 Board meeting, the most significant issue raised regarding the proposal was whether the Board had a mandate to introduce the proposed disclosure.
9. Preparers, national standard-setters, accounting firms and accounting associations did not support the proposal for the following reasons:
 - (a) they argue that explanations of differences in information contained in financial statements and other parts of its annual reporting package belong outside of financial statements and that ensuring consistency of information is a regulators' role; and

¹ Paragraph BC13 of the Exposure Draft.

- (b) they are concerned that the proposal will create a precedent beyond segment reporting for reconciling information between financial statements and other parts of the annual reporting package.
10. In contrast to the lack of support from preparers, national standard-setters, accounting firms and accounting associations, many investors' reactions were very positive, for example La Société Française des Analystes Financiers (SFAF) noted:
- We have heard the argument that, as the IASB is not in charge of defining information provided outside of the financial statements (ie the "annual reporting package"), it cannot link the information provided in segment reporting with the information outside of the financial statements. We believe however that since IFRS 8 is based on the management approach, it already means that there is a link between some non-financial information (non-IFRS) with the financial information as required by the IASB.
11. Although there was overall support for the proposal from investors, some investors expressed a concern that the proposal might create a disincentive for preparers to provide useful voluntary disclosures through their annual reporting packages.²
12. Overall regulators agree with the proposal. The European Securities and Markets Authority (ESMA) in its comment letter³ said:
- ESMA strongly agrees with the proposed amendment to paragraph 22(d), which goes into the direction expressed in our response to the PIR on IFRS 8 that consistency between segment information presented inside and outside the financial statements is key.
13. Some members of the Accounting Standards Advisory Forum noted that inconsistency is not problematic in their jurisdiction because preparers understand that the regulator will question differences between the financial statements and other parts of its annual reporting package.⁴

² Comment letter from CRUF.

³ Comment letter from ESMA dated July 17, 2017.

⁴ <http://www.ifrs.org/news-and-events/calendar/2017/july/accounting-standards-advisory-forum/>

Annual reporting package

14. Regulators, preparers, national standard-setters, accounting firms and accounting associations requested implementation guidance for the term ‘the annual reporting package’. They suggested that the Board addresses:
- (a) What information constitutes the annual reporting package?
 - (b) What does ‘published at approximately the same time’ mean?
 - (c) What constitutes a ‘segment’ in other parts of the annual reporting package?
 - (d) What types of differences would require disclosure (for example, differences that arise from different aggregations)?
15. All groups of respondents questioned whether auditors would be able to audit the proposed disclosure that entities would provide.⁵ In response, we discussed the concern with the International Auditing and Assurance Standards Board (IAASB). The Liaison Working Group of the IAASB believes that the required disclosures in the financial statements could be audited providing the annual reporting package is available to the auditor in sufficient time before the auditor issues the auditor's report.

Additional outreach

16. Since we presented the comment letter summary to the Board in November 2017, we have undertaken further outreach with regulators. As noted above, some regulators will challenge entities to explain differences between the segment disclosures in the financial statements and other parts of its annual reporting package, however, regulators noted that it can be difficult to enforce consistency of information.

⁵ In accordance with the International Standard on Auditing 720 (Revised) *The Auditor's Responsibilities Relating to Other Information in Documents Containing Audited Financial Statements* (ISA 720), auditors have responsibility to review information included in ‘annual reports (or similar documents), that are issued to owners (or similar stakeholders) containing audited financial statements and the auditor's report thereon’.

17. Regulators provided some of the reasons for differences between segment disclosures in financial statements and other parts of its annual reporting package, including:
- (a) different aggregation of operating segments into reportable segments;
 - (b) using the legal entity approach outside of financial statements;
 - (c) presenting business segments in the financial statements and geographic segments outside the financial statements; and
 - (d) highlighting a separate operation(s) within a reportable segment.

Staff analysis and recommendations

Scope of the proposal

18. We believe that constituents raised valid concerns about the definition of the annual reporting package and thereby the scope of the proposal.
19. Some respondents, including auditors, pointed out that many of the challenges listed in paragraph 14 would fall away if the Board restricted the proposal to link segments in financial statements only to the annual report (vs the annual reporting package).
20. The staff acknowledge some challenges will remain even with limiting the scope of the proposal to the annual report; the Board will still need to address:
- (a) What constitutes a ‘segment’ in other parts of the annual report?
 - (b) What types of differences require disclosure? For example, differences that arise from different aggregations or disaggregations might not require disclosure.
21. We also acknowledge, as some respondents pointed out, that limiting the scope of the proposal to the annual report from the original proposal will affect the usefulness of the overall proposal.
22. Nevertheless, for practical reasons, we recommend limiting the scope of the proposal to the annual report.
23. If the Board decides to proceed with the recommendation to limit the scope of the proposal, we recommend the Board ensure that the definition of the ‘annual report’

is aligned across all relevant IFRS Standards and if possible with International Standards on Auditing. Appendix A provides and discusses definitions of the ‘annual reporting package’ and the ‘annual report’.

Recommendation

24. We recommend proceeding with the development of the proposal but restricting the scope of the proposal for the following reasons:
- (a) There is general agreement that the proposal will:
 - (i) provide useful information for users of financial statements;
and
 - (ii) enhance consistency of segment information throughout the annual report.
 - (b) We note that some investors are concerned that this proposal might create a disincentive for preparers to provide useful voluntary disclosures as mentioned in paragraph 11 of this paper. However, as paragraph BC18 of the Exposure Draft explains, the Board is not mandating consistency of information, but requiring an explanation of differences in various sets of similar information. We also believe that additional information is most useful if users of financial statements can put the information into context with the financial statements.
 - (c) We believe that the benefits of information provided in accordance with the proposal will outweigh the costs. Whilst we accept there will be some costs for preparers, the proposed disclosure will not require changes to information systems.
 - (d) We believe that preparers’ concerns that the proposal will create a precedent beyond segment reporting for reconciling information between financial statements and other parts of the annual report (or the annual reporting package) mentioned in paragraph 9(b) is not justified. This is

because introducing the disclosure is specific to IFRS 8, which is based on the management approach.⁶

- (e) Adding the proposed disclosure to IFRS 8 will not lead to divergence with US GAAP.

Next Steps

- 25. If the Board agrees with the staff recommendation we will bring a paper to a future Board meeting discussing the definition of the annual report.

Question for Board members

Question

Do you agree with the staff recommendation to proceed with development of the proposal but to limit the scope of the proposal to the annual report?

⁶ Paragraph BC13 of IFRS 8 states that when the Board issued IFRS 8, it expected that a benefit of the management approach would be that entities would report segment information in a manner consistent with the way they reported similar information in other parts of the annual report.

Appendix A

Definitions of the ‘annual reporting package’ and the ‘annual report’

A1. This appendix provides and discusses the following definitions:

- a. the annual reporting package in the Exposure Draft;
- b. the annual report in:
 - (i) the *Disclosure Initiative—Principles of Disclosure* Discussion Paper; and
 - (ii) International Standard on Auditing (ISA) 720 (Revised).

Exposure Draft

A2. Paragraph 19B of the Exposure Draft proposed introducing and defining the term of the ‘annual reporting package’ as follows:

An entity’s annual reporting package is a set of one or more documents that:

- (b) is published at approximately the same time as the entity’s annual financial statements;
- (c) communicates the entity’s annual results to users of its financial statements; and
- (d) is publicly available, for example, on the entity’s website or in its regulatory filings.

In addition to the annual financial statements, the annual reporting package may include a management commentary, press releases, preliminary announcements, investor presentations and information for regulatory filing purposes.

A3. The staff paper presented to the Board in October 2016⁷ noted that that the term ‘annual report’ – albeit undefined - had been used in a number of IFRS Standards, for example in IFRS 15 *Revenue from Contracts with Customers* and IAS 1

⁷ <http://www.ifrs.org/-/media/feature/meetings/2016/october/iasb/amendments-to-ifrs-8-and-ias-34/ap27-ifrs-8-two-sweep-issues.pdf>

Presentation of Financial Statements as well as in Appendix A to the Basis for Conclusions on IFRS 8.

The Disclosure Initiative—Principles of Disclosure Discussion Paper

A4. *The Disclosure Initiative—Principles of Disclosure* Discussion Paper (Discussion Paper) says that the term ‘annual report’ is not currently defined in IFRS Standards. The Board’s preliminary view is that an entity’s annual report should be described as:

a single reporting package issued by that entity that includes the financial statements and has boundaries similar to those described in the International Standard on Auditing (ISA) 720 (Revised) *The Auditor’s Responsibilities Relating to Other Information*.⁸

A5. Some respondents to the Discussion Paper expressed concerns about the Board using the term ‘annual report’. In particular, these respondents thought ‘annual report’ might be difficult to apply consistently because it means different things in different jurisdictions.

A6. A few respondents suggested the Board should retain the reference to the ‘annual report’ but suggested aligning its definition with the ISAs. These respondents thought that a consistent definition of ‘annual report’ across auditing and accounting standards would make the term easier to apply.⁹

ISA 720

A7. ISA 720 (Revised) deals with the auditor’s responsibilities relating to other information included in an entity’s annual report. It also describes other information by reference to the definition of an annual report.

A8. Paragraph 12(a) of ISA 720 (Revised) defines the annual report as follows:

Annual report – A document, *or combination of documents*, prepared typically on an annual basis by management or those charged with governance in accordance with law,

⁸ Paragraph 4.11 of the Discussion Paper.

⁹ <http://www.ifrs.org/-/media/feature/meetings/2018/february/iasb/ap11h-disclosure-initiative.pdf>, paragraphs 16-19

regulation or custom, the purpose of which is to provide owners (or similar shareholders) with information on the entity’s operations and the entity’s financial results and financial position as set out in the financial statements. An annual report contains or accompanies the financial statements and the auditor’s report thereon and usually includes information about the entity’s developments, its future outlook and risks and uncertainties, a statement by the entity’s governing body, and reports covering governance matters.

- A9. ISA 720 (Revised) does not apply to preliminary announcements of financial information or securities offering documents, including prospectuses. Application guidance of ISA 720 (Revised) provides further guidance to support the description of an annual report, including examples of documents that can form part of the annual report and other stand-alone reports that typically do not.
- A10. This table provides a high level comparison of documents includes in the scope of:
- a. the annual reporting package as proposed in the Exposure Draft; and
 - b. the annual report in described in ISA 720 (Revised).

Documents may include:	Annual reporting package	Annual report per ISA 720 (Revised)
Management commentary	✓	✓
Press releases	✓	-
Preliminary announcements	✓	-
Investor presentations	✓	-
Information for regulatory filings	✓	- However, depends on the filing
The Chairman’s statement Statements on corporate governance	Not addressed	✓

Internal control and risk assessment		
Securities offering documents	- However, not addressed explicitly	-