STAFF PAPER

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Project	**Primary Financial Statements**
Paper topic	Feedback summary—Disaggregation—unusual income and expenses

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Objective

1. This paper analyses feedback from comment letters and outreach on the proposals relating to unusual items set out in the Exposure Draft *General Presentation and Disclosures*. This paper also discusses fieldwork findings related to this topic and Agenda Paper 21L *Feedback summary—Literature Review* summarised relevant academic literature.

Key messages

2. The key messages from the feedback on the proposals relating to unusual items are:
   - (a) most respondents who commented on this question, including almost all users of financial statements, agreed with the Board defining unusual items;
   - (b) however, most of these respondents, including some users, did not agree with the Board's definition of unusual items and made varying suggestions to change it. There was no clear consensus on what an alternative definition should be;
   - (c) respondents were split evenly on whether or not they agreed with the proposed disclosure in a single note.

Structure of the paper

3. This paper is structured as follows:

   (a) Proposals and questions in the Exposure Draft (paragraphs 4–5);

   (b) Comment letter and outreach feedback (paragraphs 6–22);

   (c) Fieldwork findings (paragraphs 23–46); and

   (d) Appendix A includes the relevant questions in the Exposure Draft.

Proposals and questions in the Exposure Draft

4. The Board proposed introducing a definition of 'unusual income and expenses'; and proposed requiring all entities to disclose unusual income and expenses in a single note. The Board also proposed application guidance to help an entity to identify its unusual income and expenses.

5. The proposed requirements are set out in paragraphs 100–102, B67-B75 of the Exposure Draft and paragraphs BC122–BC144 of the Basis for Conclusions describe the Board's reasons for the proposals and discuss approaches that were considered but rejected by the Board.

Comment letter and outreach feedback

Should the Board define unusual items?

6. Most respondents commented on this question. Of those that did, most, mainly from Europe, including almost all users, agreed that the Board should define unusual items. Some respondents, including a few users, did not agree with the Board defining unusual items.

   Agreement

7. Users explained that they wish to identify recurring or normalised earnings but have to rely on voluntary disclosures by an entity to do so. Defining unusual items and requiring their disclosure would provide consistent input for users' analysis. Other

respondents also indicated they expected defining unusual items would provide useful information.

8. A few respondents specifically supported the discipline that they expected a definition would provide, thus reducing opportunistic classification of items as unusual.

Concerns

9. Those respondents that did not support the Board defining unusual items gave the following reasons:

   (a) some, including a few users, said that any definition would be too restrictive—an entity should disclose information about any material income or expenses, not just those that meet the definition of unusual. They said that principles of disaggregation should be strengthened to help ensure that all material items of income or expenses are disclosed.

   (b) some said that any definition would inevitably be subject to a large degree of judgement, and that the proposals on management performance measures are sufficient to provide the information that users want.

   (c) a few said that previous experience of entities presenting items as extraordinary demonstrated that requiring or allowing items to be labelled as extraordinary/unusual is likely to lead to opportunistic use of the term by entities.

Is the proposed definition appropriate?

10. The proposed definition of unusual income and expenses is:

> *Income and expenses with limited predictive value. Income and expenses have limited predictive value when it is reasonable to expect that income or expenses that are similar in type and amount will not arise for several future annual reporting periods.*

11. Although most respondents agreed the Board should define unusual items, most, mainly preparers, but also including some users, did not agree with the proposed definition. Some, including many users, agreed.

Agreement

12. Respondents that agreed with the proposed definition said it would identify income and expenses that are not recurring which would help users assess future cash flows. They expect it to provide discipline and prevent opportunistic classification of items as unusual. Some explicitly supported the definition referring to income and expenses—they thought this was important to avoid a focus solely on unusual expenses.

Concerns

13. Respondents gave the following reasons for not agreeing with the proposed definition:

(a) many said important aspects of the definition are unclear, in particular the meaning of:

(i) limited predictive value;

(ii) similar in type and amount; and

(iii) several future annual reporting periods.

(b) some said the definition should be explicitly limited to material or significant unusual items—they said that the proposals in the Exposure Draft could be interpreted as applying to immaterial items, which would be costly and add unhelpful clutter;

(c) some said unusual items should be defined in terms of income and expenses *arising from events or transactions* that are non-recurring or unusual in nature rather than focusing on the income or expenses;

(d) some said the definition should include items spanning two–three annual reporting periods, for example restructuring costs, or unusual income and expenses arising due to the pandemic;

(e) some said the definition should include a reference to past occurrence as well as future occurrence;

(f) some suggested aligning the definition of unusual items with definitions and guidance from various regulators, for example the Canadian Securities Administrator, the US Securities and Exchange Commission or the European

Securities and Markets Authorities. For example, some of this guidance prohibits labelling items as unusual if similar item arose in last two years;

(g) a few said the definition should only apply to items of operating income or expenses, or items that are unusual for an entity's main business activities;

(h) a few said management should define what is unusual for their specific entity; and

(i) many asked for more guidance and/or examples.

14. There was no clear consensus on an alternative definition. A few said that the label 'unusual' was not helpful in trying to identify the scope—it does not capture all items that they think have limited predictive value. Alternative suggestions were 'non-recurring' or 'items with low predictive value'.

15. Some respondents that agreed with the proposed definition said further clarification was needed. For example, one preparer body said that they were unclear whether the proposals would require the whole amount of a line item to be identified as an unusual expense or only the portion that was in excess of the reasonably expected amount for that line item. They also said they understood that income or expense can meet the definition of unusual only if their amounts were higher than expected (if unusual by amount), not lower than expected.

Disclose in a single note

16. Many respondents commented on the proposal that the disclosures on unusual items should be given in a single note, and expressed mixed views, with many agreeing and many disagreeing with the proposal. Some users agreed with disclosure in a single note, some said that unusual income and expenses should not be presented in the statement of profit or loss, and some asked for unusual income and expenses to be presented in the statement of profit or loss.

Agreement

17. Respondents, including users, gave the following reasons for agreeing with disclosure in a single note:

(a) a single location for the disclosures is transparent and allows easy access to the information; and

(b) a single note allows users to keep track of what items are being described as unusual, and hence enables them to determine whether the items are non-recurring.

18. Respondents also gave reasons for not presenting unusual items in the statement of profit or loss:

(a) disclosure in a note, rather than presentation in the statement of profit or loss, reduces the incentives for opportunistic labelling of items as unusual; and

(b) disclosure in a note, rather than presentation in the statement of profit or loss, avoids clutter and maintains the clear structure of operating, investing and financing categories.

Concerns

19. Respondents expressed the following concerns about disclosure in a single note:

(a) presentation in the statement of profit or loss would be more transparent, because it would be easier for users to find.

(b) presentation in the statement of profit or loss would enable entities to present a subtotals before unusual income and expenses, which would be a relevant additional subtotal that some users have asked for (for example normalised earnings).

(c) it would be more helpful to include the information in the notes for the specific items of income and expenses in question, for example the notes for IAS 37 provisions or IAS 36 impairments. One respondent suggested the accounting policy note could identify which notes included unusual items.

(d) requiring a single note for unusual items would result in duplication of information required by other IFRS Standards or regulations to be given elsewhere, for example in other notes (see subparagraph (b)) or in the management commentary. A few respondents suggested cross-references to disclosures in such other locations, but one respondent said such cross-references would add complexity and be confusing.

20. A few respondents asked for clarification of whether unusual items could be presented in the statement of profit or loss:

(a) if they are included in a single line items and hence could presented as a disaggregation of that line item; or

(b) as a separate column. These respondents said the proposed prohibition of columns seemed to apply only to management performance measures.

Disclosures

21. Many respondents did not comment on the specific disclosures proposed. Some respondents, including many users, supported the proposed disclosures. A few respondents, including users, suggested the following additional disclosures:

(a) an explanation of why the items are unusual;

(b) a five-year history of unusual items, or disclosure of whether unusual items in this period occurred in the previous five years;

(c) comparative amounts, even if the items were not unusual in the comparative period;

(d) disclosure of the tax effects of unusual items (one user also suggested disclosure of the NCI effects). In contrast, a few respondents noted that the illustrative examples accompanying the Exposure Draft included the tax effect and asked for clarification of whether that was required (the staff note that the examples in the Exposure Draft combined disclosure of management performance measures with unusual items, hence tax and NCI information was provided).

22. A few respondents suggested removing the proposed disclosure of an analysis of the unusual items by nature, if the entity presents operating expenses analysed by function on the face of the statement of profit or loss, saying it would be unduly costly. There were also concerns expressed about interaction of unusual income and expenses with management performance measures, which are discussed in Agenda Paper 21H *Feedback summary—Management performance measures.*

Fieldwork findings

23. The following section discusses the fieldwork findings related to unusual income and expenses. The findings are organised by the following categories corresponding to the objectives of the fieldwork:

    (a) observations on how the requirements were applied (paragraphs 24–33);

    (b) aspects of the Exposure Draft that participants identified as unclear (paragraphs 34–37);

    (c) extent of process or system changes that may be required (paragraphs 38–41); and

    (d) other observations (paragraphs 42–45).

24. The methodology of the fieldwork is described in Agenda Paper 21A *Feedback summary–Overview*.

Observations on how the requirements were applied

25. Most fieldwork participants provided an example note disclosure for unusual income and expenses. A few participants said that they were clear on the Exposure Draft's requirements and did not identify any unusual income or expenses. A few participants said they were not clear on the Exposure Draft's requirements and were therefore unable to identify unusual income and expenses.

26. The items that participants most often identified as unusual were:

    (a) disposals of investments;

    (b) disposals of property plant, and equipment;

    (c) restructuring;

    (d) impairments; and

    (e) litigation.

27. The items participants most often identified as unusual are included in the Exposure Draft's disaggregation guidance as items that would benefit from separate presentation or disclosure that was retained from IAS 1 *Presentation of Financial Statements*.

28. Almost all items identified as unusual income or expenses were classified in the operating category. A few participants identified expenses in the financing, investing or integral associates and joint ventures categories including refinancing expenses or impairments on investments.

29. Other than gains on disposals no participants identified unusual income.

30. Although most participants provided disclosures for unusual income and expenses, many did not include all the disclosures proposed to be required by the Exposure Draft. For example

    (a) line items in the statement of profit or loss or items in the analysis of expenses by nature affected by unusual items were not identified,

    (b) descriptions were brief or vague, or

    (c) no amounts for the unusual income and expenses were disclosed.

31. A few participants presented unusual or similar items in the statement of financial performance using a column or a line item. For example, one participant presented a line item labelled ‘separately disclosed items’ in the statement of profit or loss, which aggregated the expenses it identified as unusual income and expenses. This participant included a subtotal of profit before separately disclosed items in the statement of profit or loss.

32. Some participants said there were differences between the definition of unusual income and expenses in the Exposure Draft and terms such as unusual, infrequent or non-recurring in local regulations.

33. A few of these participants used the definitions in local regulations as the basis for identifying unusual income and expenses. Some of these participants said that the definition in the relevant local accounting standard did not consider forward looking information and provided prescriptive guidance that did not require judgement. Some of these participants incorrectly assumed that the definition used in those local regulations was equivalent to the Exposure Draft definition.

34. A few participants raised concerns over disclosing unusual income and expenses because the information about unusual income or expenses may be confidential. For example, one participant was concerned that information on whether management

expected similar transactions to occur in the future could negatively affect the terms of any potential future transactions.

Aspects of the Exposure Draft participants identified as unclear

35. Some participants said the definition of unusual income and expense was clear and, in the staff's view, made reasonable judgements about the items identified as meeting the proposed definition of unusual income and expenses.

36. However, despite being able to provide the required disclosure, many participants said that they had difficulties in applying the definition of unusual income and expenses or that doing so required significant judgement.

37. Aspects of the definition of unusual income and expenses that participants said were unclear or required significant judgement included:

    (a) the unit of account required for the analysis. For example, some participants questioned whether an individual transaction, a line item in the statement of profit or loss, or an individual segment would be the appropriate level for determining if an item was of a similar type and amount.

    (b) the application of 'several future annual reporting periods'. For example, some participants said they did not know how far into the future they would be required to consider. One participant said that they evaluated whether an item was unusual based on its nature rather than whether it was confined to a single reporting period.

    (c) the role that event plays in determining if an item of income or expense is unusual. For example, some participants questioned whether the event giving rise to an impairment expense could be considered in determining if the impairment expense was unusual. (The staff note that discussion of why the event itself is not part of the definition of unusual income and expenses including how it might be considered is included in the Basis for Conclusions but not within the proposed IFRS Standard or Application Guidance).

    (d) the application of materiality. For example, some participants said that they interpreted the Exposure Draft to require a lower quantitative threshold of materiality for unusual income and expenses than for the application of other IFRS Standards.

(e) the circumstances and types of remeasurements that would be permitted to be classified as unusual. For example, one participant questioned whether and under what circumstances foreign exchange differences could be classified as unusual.

(f) the differences in judgements that would be required to identify unusual income and expenses in annual financial statements compared to interim financial statements. For example, some participants questioned whether an item might meet the definition of unusual in an interim period but not meet the definition of unusual for the annual financial statements.

38. Some participants said they were unclear on the amount of unusual income and expenses to disclose. For example, some participants questioned whether they were required to disclose the whole amount of a line item identified as an unusual expense or only the portion of that line item that was determined to be unusual.

Extent of process or systems changes that may be required

39. Most participants said that changes to systems and processes would be required to identify all unusual income and expense at the subsidiary and at the group level.

40. A few participants said that they had all of the information required to identify unusual income and expenses using existing systems and processes. For example, one participant said that their routine variance analysis would identify unusual income and expenses. Another participant said that they prepared a budget by line item of the statement of profit or loss that could serve as a basis for identifying unusual income and expenses.

41. Some participants that present the analysis of operating expenses in the statement of financial performance using the function of expense method said that they will require system changes to be able to identify which items in the disclosure of expenses by nature are affected by unusual income and expenses. These participants said that systems changes would be required because existing systems do not track expenses by nature.

42. Some participants expressed concerns over the ability to provide sufficient evidence to their auditors for unusual income and expenses. For example, some participants were concerned with being able to justify their estimations of reasonable expectations of future occurrence both for expenses judged to be unusual and those judged not to be unusual.

Other observations

43. Some participants said that the definition of unusual income and expenses was clear but that it was too narrow. Some participants said that the definition was too narrow because it did not capture income and expenses that might occur for a limited timeframe that either cross a period end or last for more than one year. They gave as an example a restructuring that occurs over two periods.

44. Some participants said they were concerned the differences between the proposed definition and the definitions used in local guidance or regulatory requirements may result in non-compliance with local regulations or cause confusion for users of their financial statements. For example, one participant said that the ESMA guidelines for alternative performance measures state that items that affected past periods and will affect future periods will rarely be considered as non-recurring, infrequent or unusual (such as restructuring costs or impairment losses), which is different from the proposed definition of unusual income and expenses.

45. A few participants read the examples in the Exposure Draft as prescriptive rather than demonstrating the underlying principles. For example, one participant said that there was a risk that the example of a fire giving rise to unusual expenses may be read as meaning that expenses related to fires are always classified as unusual.

46. One participant raised a concern that the requirement to include unusual income and expenses in a single note disclosure would lead to duplication of disclosures because most of the items classified as unusual were already required to be disclosed in other notes.

Question for the Board

Does the Board have any comments or questions on the feedback discussed in this paper? Specifically:

a) Is there any feedback or fieldwork evidence that is unclear?

b) Are there any points, or fieldwork evidence, you think the Board did not consider in developing the Exposure Draft but should consider in the re-deliberations?

c) Are there any points, or fieldwork evidence, you would like staff to research further for the re-deliberations?

Appendix A—Relevant questions in the Exposure Draft

Question 10—unusual income and expenses
(a) Paragraph 100 of the Exposure Draft introduces a definition of 'unusual income and expenses'. (b) Paragraph 101 of the Exposure Draft proposes to require all entities to disclose unusual income and expenses in a single note. (c) Paragraphs B67–B75 of the Exposure Draft propose application guidance to help an entity to identify its unusual income and expenses. (d) Paragraphs 101(a)–101(d) of the Exposure Draft propose what information should be disclosed relating to unusual income and expenses. Paragraphs BC122–BC144 of the Basis for Conclusions describe the Board's reasons for the proposals and discuss approaches that were considered but rejected by the Board. Do you agree with the proposals? Why or why not? If not, what alternative approach would you suggest and why?