PFS – Preliminary Thoughts from South Africa

EEG- MAY 2020

Primary Financial Statements (PFS)

General

- Well rounded support in principle.
- Agree with the need for better performance measurement principles and analysis.
- Backing from regulators such as the JSE.
- A few areas (non exhaustive list) highlighted as per below.

Primary Financial Statements (PFS)

(1) Subtotal for operating profit or loss:

- Well rounded support in principle.
- Definition of the operating category appears to be contradictory - It first states that it includes information about income and expenses from an entity's main business activities and then the second part of the definition appears to make the operating category a residual category.
- Consider an EBITDA line item.
- Consider the definition of operating category if it can be aligned with the IAS 7 definition of 'operating activities'.

Primary Financial Statements (PFS)

(2) Operating Activities as a default ?

- "Operating activities are the principal revenue-producing activities of the entity **and other activities that are not investing or financing activities**."
- Possibly only a need for 2 categories i.e. operating and financing since distinguishing between investing and operating is not always clear, for example in the case of buying or selling property, plant and equipment that is part of an entity's operation. OR
- the IASB should either align the definitions per the ED with the definition in IAS 7 to provide clarity and consistency

Primary Financial Statements (PFS)

(3) Operating category: income and expenses from investments made in the course of an entity’s main business activities?

- General agreement with this principle.
- Consider providing clarity or guidance on ‘entity’s main business activity’ , or;
- align the terminology to ‘principal revenue-producing activities’ as used in the definition of ‘operating activities’ under IAS 7.

Primary Financial Statements (PFS)

(4) The operating category: an entity that provides financing to customers as a main business activity

- Paragraph 51 of the Exposure Draft proposes that an entity that provides financing to customers as a main business activity classify in the operating category either:

1. income and expenses from financing activities, and from cash and cash equivalents, that relate to the provision of financing to customers; or
2. all income and expenses from financing activities and all income and expenses from cash and cash equivalents.

Primary Financial Statements (PFS)

(4) CONTD:

Respondents agree with the IASB’s proposal for an entity that provides financing to customers as a main business activity to include income and expenses from financing activities in the operating category since such entities are already including income and expenses from financing activities in operating profit. However, respondents are concerned that the IASB’s proposal includes accounting policy choices. For example, within the financial services sector, one institution, may have centralised treasury functions that raise general borrowings and then pool them together before using the funds such that the funds cannot be identified with specific activities, while another peer might not have such centralised treasury function and the funds do not lose their respective identity.

Primary Financial Statements (PFS)

(4) CONTD:

In addition, if the entity with the centralised treasury function choose option 1 (paragraph 51(a) of ED) above in the statement of financial performance, for purposes of the statement of cash flows, the entity will have to either classify all borrowings as financing activities or all borrowings as operating activities because the amendment to IAS 7 does not allow a split between operating and financing.

This may create a mismatch between the income statement and the statement of cash flows. Although the respondents understand the IASB's rationale for including the option, the respondents strongly believe that accounting policy choices may result in the undermining of comparability between peers. Therefore, the respondents are proposing that the IASB eliminate accounting policy choices by retaining option 2 (paragraph 51(b) of ED) only unless it is impracticable to eliminate the choices.

Primary Financial Statements (PFS)

(5) **integral and non-integral associates and joint ventures:**

– differing views on the proposed presentation of a subtotal for operating profit or loss and income and expenses from integral associates and joint ventures present in the statement of profit or loss.

Primary Financial Statements (PFS)

(5) **integral and non-integral associates and joint ventures contd:**

– Some respondents viewed the proposed presentation by the Board to be appropriate since the measurement of the share in the profit or loss from associates and joint ventures i.e. the equity method application, is different to the measurement applied in general to items presented as operating activities. These respondents argued that due to the distinction in measurement, it is important for analysis purposes that results of investments in associates and joint ventures accounted for using the equity method are separately presented from the results of an entity's operating activities.

Primary Financial Statements (PFS)

(5) Integral and non-integral associates and joint ventures contd:

– Other respondents argued that in the case where entities invest in integral associates and joint ventures in the course of their main business activities, the result of these type of investments are operating activities and should be presented as such. It was proposed by these respondents that separate presentation in the statement of financial performance was unnecessary since IFRS 12 – *Disclosures of Interests in Other Entities* already requires comprehensive disclosures. If further disclosure is required to aid in analysis between income from integral and non-integral associates and joint ventures, these respondents proposed that the distinction between integral and non-integral associates and joint ventures be made in the notes to the statement of financial performance.

– In general more guidance required to assist in classifying between integral and non integral.

THE SOUTH AFRICAN INSTITUTE OF CHARTERED ACCOUNTANTS

develop.influence.lead.

Thank you