



STAFF PAPER

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Project	Primary Financial Statements		
Paper topic	Scope of management performance measures		
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Objective

1. This paper initiates the Board's redeliberations on management performance measures. In this paper we:
 - (a) recommend that the Board proceed with the proposal in the Exposure Draft *General Presentation and Disclosures* (the Exposure Draft) to include information about measures meeting the definition of management performance measures in the financial statements;
 - (b) ask the Board whether it wants to explore possible approaches to expanding the scope of the management performance measure requirements to include measures other than subtotals of income and expenses; and
 - (c) ask for the Board's feedback on the factors that should be used to evaluate the possible approaches, if the Board decides to explore possible approaches to expanding the scope.
2. We will follow up on this paper with further analysis depending on the Board's decision at this meeting. We plan to address the following aspects of the management performance measure proposals in future papers:
 - (a) remaining aspects of the definition of management performance measures including addressing feedback that the following components may require clarification:

- (i) the scope implied by defining management performance measures as measures of performance included in public communications;
 - (ii) the need to explicitly state that management performance measures should faithfully represent an aspect of an entity's performance given the general requirement for information in financial statements to provide a faithful representation;
 - (iii) whether defining management performance measures by reference to management's view of performance may unintentionally exclude some measures (for example industry measures); and
 - (iv) whether additional guidance may be required to help entities apply the requirement for management performance measures to complement subtotals specified in IFRS Standards;
- (b) interaction of management performance measures with other requirements including:
- (i) proposals for unusual income and expenses;
 - (ii) segment reporting;
 - (iii) other subtotals in the statement of financial performance; and
 - (iv) earnings per share measures;
- (c) disclosure requirements, including:
- (i) the proposals relating to the reconciliation;
 - (ii) the requirement to disclose tax and non-controlling interests;
 - (iii) presentation restrictions such as the restriction on the use of columns; and
 - (iv) whether specific guidance is needed for non-GAAP measures that are not management performance measures; and
- (d) requirements relating to EBITDA.

Summary of staff recommendations in this paper

3. The staff recommend:
 - (a) the Board proceed with the proposal in the Exposure Draft to include information about management performance measures in the financial statements; and
 - (b) the Board explore possible approaches to expanding the scope of the management performance measure requirements to include measures other than subtotals of income and expenses.

4. We ask the Board for feedback on the possible approaches for increasing the scope of management performance measures and the factors for evaluating them. The proposed factors are:
 - (a) the prevalence of the measure in practice;
 - (b) the usefulness of the disclosure requirements for the measure and the complexity of necessary changes to those requirements;
 - (c) the contribution that including the measure in the management performance measure proposals would make to achieving the project objective; and
 - (d) the complexity involved in developing a new definition of management performance measures.

Structure of paper

5. This paper is structured as follows:
 - (a) proposals in the Exposure Draft (paragraphs 6–7);
 - (b) should we retain the proposals to include information about management performance measures in the financial statements (paragraphs 8–28);
 - (c) should the Board consider expanding the scope of management performance measures (paragraphs 29–43);
 - (d) possible approaches and evaluation factors for expanding the scope of management performance measures (paragraphs 44–62);

- (e) Appendix A—Extracts of management performance measure requirements from the Exposure Draft; and
- (f) Appendix B—Non-GAAP measures excluded from the Exposure Draft definition of management performance measures.

Proposals in the Exposure Draft

6. The Exposure Draft proposed that an entity disclose ‘management performance measures’ in a single note and defined management performance measures as subtotals of income and expenses that:
 - (a) are used in public communications outside financial statements;
 - (b) complement totals or subtotals specified by IFRS Standards; and
 - (c) communicate to users of financial statements management’s view of an aspect of an entity’s financial performance.
7. The Exposure Draft then proposed that an entity would be required to disclose specific information about management performance measures. An extract of the full management performance measure proposals from the Exposure Draft is included in Appendix A.

Should we retain the proposals to include information about management performance measures in the financial statements?

Basis for including information about management performance measures in the financial statements

8. Paragraphs BC145–BC151 (see Appendix A) of the Basis for Conclusions on the Exposure Draft explain why the Board proposed to require entities to disclose information about management performance measures in the financial statements.
9. In summary:
 - (a) paragraphs BC145–BC147 explain that the proposals respond directly to user feedback obtained in the research performed in the Primary Financial Statements project. That feedback was that users find management-defined

performance measures useful in providing insight into aspects of the entity’s performance but are concerned about the quality of the disclosures provided about the measures.

- (b) Paragraphs BC148–BC150 explain the concerns of some stakeholders about including management performance measures in the financial statements and how the Board thought that aspects of the proposals would resolve those concerns.
- (c) Paragraph BC151 explains that the Board concluded that management performance measures can complement measures specified by IFRS Standards, providing users of financial statements with useful insight into management’s view of performance and its management of the business. Including these measures in the financial statements would make them subject to the same requirements regardless of the entity’s jurisdiction and would improve the discipline with which they are prepared and improve their transparency.

Summary of feedback on whether information about management performance measures should be included in the financial statements

- 10. Feedback on the Exposure Draft is consistent with early feedback on the project with many stakeholders, including almost all users, agreeing with the Board’s proposals to require the disclosure of management performance measures in the notes. Most of these stakeholders said they agreed because:
 - (a) management performance measures provide useful complementary information and including them in the financial statements would enhance the relevance of information in the financial statements;
 - (b) the proposed disclosures, being in many cases subject to external audit, would improve the discipline in the use of management performance measures; and
 - (c) a few respondents said that including management performance measures in the financial statements could help make the information presented outside the financial statements more consistent with the information presented inside the financial statements.

11. The staff notes in particular:
- (a) feedback from regulators was generally supportive of including management performance measures in the financial statements. Nearly all regulators specifically agreed with the objectives of bringing more transparency and discipline to management performance measures and no regulators explicitly disagreed with including management performance measures in the financial statements. However, some regulators raised concerns about specific aspects of the definition and one regulator raised a concern that there could be conflicts with local regulations that prohibit non-GAAP measures in financial statements.
 - (b) the academic evidence¹ on non-GAAP measures is generally consistent with the conclusion that these measures are value relevant, that is, associated with stock prices and stock returns. Research suggests that discipline, transparency, consistency and full reconciliation to the closest equivalent measure required by applicable accounting standards are key to the decision usefulness of non-GAAP measures. There is evidence that managers disclose non-GAAP measures to convey the performance of their companies but also for opportunistic reasons. As a result, in the absence of specific guidance on non-GAAP measures' definitions and disclosure, the content of non-GAAP measures varies widely across entities.
 - (c) experience gathered during our fieldwork² showed that entities have systems and processes in place for disclosing non-GAAP measures that facilitate compliance with the proposed disclosure requirements for management performance measures. Some fieldwork participants said that systems changes would be required to disclose the tax and non-controlling interests' effects of reconciling items.
12. Feedback from some stakeholders identified benefits of including information on management performance measures in the financial statements that were not

¹ See [AP21E January 2021](#) for a summary of evidence from academic papers on topics relevant to the Exposure Draft

² See [AP21H December 2020](#) for fieldwork findings regarding management performance measures

specifically identified in the Basis for Conclusions. For example, some users emphasised the benefits of such information in assessing management’s stewardship. They said that where a link exists between management performance measures and management remuneration, they would particularly welcome the assurance that audit would provide.

13. Many accounting firms and the International Auditing and Assurance Standards Board (IAASB) agreed with the proposal to include management performance measures in the financial statements but raised concerns with particular aspects of the definition that may create audit challenges. However, many of these stakeholders also provided suggestions for how to address these concerns and said that if the concerns were addressed the measures would be auditable.
14. However, a few stakeholders included these same concerns relating to audit among the reasons they disagreed with including management performance measures in the financial statements. Those stakeholders that disagreed because of concerns about audit included mainly preparers, national standard-setters and accountancy bodies.
15. The specific concerns relating to the audit of management performance measures raised by stakeholders are:
 - (a) some stakeholders said it may be difficult to audit the completeness of management performance measures because public communications are too broad.
 - (b) a few stakeholders said that without further guidance, it is unclear how to apply the requirement for a management performance measure to faithfully represent aspects of financial performance.
 - (c) a few audit standard setters and accounting firms said they were concerned that expanding the scope of audit to management performance measures could increase confusion over which parts of an annual report are subject to audit and over the level of verification an audit can provide. A few accounting firms said they were concerned that users may incorrectly believe that the auditor agrees that a management performance measure is a good measure of performance because it has been audited, when this may not be the case.

- (d) some stakeholders said they were concerned that such measures may be difficult to audit because they may not be based on a defined accounting framework.
 - (e) some stakeholders, mainly preparers and accountancy bodies, said they were concerned about the additional costs of auditing management performance measures.
16. A few stakeholders disagreed with the Board’s conclusion to include information about management performance measures in the financial statements because they said that non-GAAP measures are not within the scope of the financial statements because, in their view:
- (a) non-GAAP measures are not useful and therefore do not meet the objective of financial statements; or
 - (b) non-GAAP measures do not provide information necessary to understand items in the primary financial statements nor do they provide supplemental information and therefore do not fall within the role of the notes.
17. In addition, some stakeholders raised objections to including information about management performance measures in the financial statements for the following reasons that were not specifically discussed in the Basis for Conclusions:
- (a) some respondents that said non-GAAP measures are not within the scope of the financial statements also said that it is not the role of the Board to define, restrict or regulate such measures. These respondents said this is the role of securities or industry regulators many of whom already provide requirements for such measures.
 - (b) a few stakeholders said it would introduce clutter to the financial statements because the interaction with existing regulatory requirements is expected to result in the duplication of disclosures.
 - (c) a few stakeholders said it would result in an increase in the complexity of financial reporting, and hence add to the costs of preparing financial statements. For example, a few respondents were concerned that the difference in scopes between regulatory measures, measures required by IFRS 8

Operating Segments and management performance measures may result in three tiers of performance measures, each with differing definitions and disclosure requirements.

Staff analysis

18. Our analysis is structured as follows:
 - (a) discussion of aspects of the explanation in the Basis for Conclusions with which stakeholders disagreed (paragraphs 19–25);
 - (b) discussion of specific concerns raised by stakeholders that were not covered in the Basis for Conclusions (paragraph 26);
 - (c) discussion of overall balance of arguments for and against including information about management performance measures in the financial statements (paragraph 27); and
 - (d) staff recommendation (paragraph 28).
19. As discussed in paragraph 15, some stakeholders disagreed with the conclusions reached by the Board in the Basis for Conclusions because of concerns regarding the audit of management performance measures.
20. Some stakeholders raised concerns that it may be difficult to provide assurance about the completeness of management performance measures because the scope of public communications is very broad (see paragraph 15(a)). A few stakeholders raised concerns over the application of the requirement for a management performance measure to faithfully represent aspects of financial performance (see paragraph 15(a)). The staff plan to address questions about the scope of public communications and guidance on faithful representation at future Board meetings.
21. A few stakeholders (an auditing standard-setter and an accounting firm) that raised the concern over the potential confusion over measures that are audited and those that are not (see paragraph 15(b)) suggested disclosures that would overcome any potential confusion. The disclosure requirements will be discussed in a paper at a later Board meeting. In the staff’s view, the suggested disclosures provide evidence that additional disclosure requirements can address this concern.

22. Including management performance measures in the financial statements is likely to result in increased audit work and hence increased cost (see paragraph 15(d)). However, many stakeholders identified the audit of management performance measures as a specific benefit of the proposals. In the staff's view the benefits received from including management performance measures in the financial statements outweigh the incremental costs of audit.
23. Management performance measures that are not based on a defined accounting framework may be more costly to audit (see paragraph 15(c)). However, feedback from the IAASB is that such measures would be auditable. In the staff's view the benefits of including management performance measures in the financial statements will also outweigh the increased cost in these situations. Stakeholders have also provided suggestions on disclosure requirements that may reduce the difficulty of auditing management performance measures that are not based on a defined accounting framework. The staff plan to address feedback on the disclosure requirements, including respondents' suggestions on additional disclosure requirements, in a future paper.
24. A few stakeholders expressed the view that information about management performance measures does not meet the objective of financial statements and does not fulfil the role of the notes (see paragraph 16).
25. The staff disagree with this view. Feedback from users and research undertaken when developing the Exposure Draft suggests that information about management performance measures provides information about income and expenses that is useful to users in assessing the prospects of future net cash inflows and in assessing management's stewardship of an entity's economic resources. Such information is consistent with the objective and scope of financial statements in the *Conceptual Framework for Financial Reporting*. Additionally, in providing useful information to users, information about management performance measures fulfils one of the roles of the notes, which is to supplement the primary financial statements with other information that is necessary to meet the objective of financial statements.
26. The concerns raised by stakeholders that were not specifically discussed in the Basis for Conclusions are set out in paragraph 17 of this paper:

- (a) it is not the role of the Board to define, restrict or regulate such measures (see paragraph 17(a)). In the staff’s view, the extent of stakeholder feedback agreeing with the inclusion of management performance measures in the financial statements provides evidence that the Board has a role in this area. This is also consistent with the previous arguments that such measures help meet the objective of financial statements. In addition, the definition of management performance measures and the disclosure requirements included in the Exposure Draft were drafted after consultation with regulators and considering existing regulatory requirements. As noted in paragraph 11(a), nearly all regulators specifically agreed with the objectives of bringing more transparency and discipline to management performance measures.
- (b) it would introduce clutter to the financial statements because the interaction with regulatory requirements may result in the duplication of disclosures (see paragraph 17(a)). The staff think that duplication of disclosures caused by the definition or disclosure requirements can be addressed when the Board redeliberates detailed aspects of the definition of management performance measures and disclosure requirements. For example, some solutions suggested by stakeholders include compliance by cross-reference, specific exemptions, or changes to aspects of the definition.
- (c) it would result in an increase in the complexity of financial reporting, and hence add to the costs of preparing financial statements (see paragraph 17(b)). Non-GAAP measures are already reported in other communications. In the staff’s view, including a subset of these non-GAAP measures in the financial statements does not significantly increase the complexity of reporting. As noted in paragraph 17(c), our fieldwork showed that entities did not find it difficult to identify and report management performance measures because most entities already have reporting systems and processes in place to report non-GAAP measures.

27. In the staff’s view, the extent of feedback, particularly from users, agreeing with the inclusion of information on management performance measures in the financial statements:

- (a) supports the Board’s initial conclusions that including information about management performance measures in the financial statements would provide added transparency and discipline to information that users find useful; and
 - (b) provides evidence that the benefits of including management performance measures in the financial statements would exceed additional costs.
28. On this basis and noting that specific issues raised by stakeholders regarding aspects of the definition and disclosure requirements will be addressed in future Board discussions, the staff recommend that Board proceed with the proposals in the Exposure Draft requiring an entity to include information about measures that meet the definition of management performance measures in the financial statements.

Question 1

Does the Board agree to proceed with the proposals in the Exposure Draft requiring an entity to include information about management performance measures in the financial statements?

Should the Board consider expanding the scope of management performance measures?

Basis for definition being limited to subtotals of income and expenses

29. Paragraphs BC147 and BC148 of the Basis for Conclusions to the Exposure Draft explain that the Board proposed including management performance measures in the financial statements to help address concerns raised by users of financial statements that in some cases the existing disclosure of management-defined performance measures:
- (a) lack transparency in how they are calculated;
 - (b) lack clarity regarding why the measures provide management’s view of the entity’s performance;
 - (c) create difficulties for users trying to reconcile the measures to the related measures specified by IFRS Standards; and

- (d) are reported inconsistently from period to period.
30. Paragraph BC 154 further explains that feedback from users of financial statements led the Board to focus on improvements to the reporting of financial performance in the statement(s) of financial performance and the related notes. Considering user feedback and the project focus on the statement of profit or loss, the Board's proposed definition for management performance measures was limited to subtotals of income and expenses (see paragraph 6 for the full definition), and excludes measures such as free cash flows and ratios such as return on capital employed.

Summary of feedback on the scope of management performance measures

31. A few respondents said they agreed with limiting management performance measures to subtotals of income and expenses because it is consistent with the project's focus on improvements to the statement(s) of financial performance. One respondent noted that most alternative measures used by entities relate to profit or loss.
32. However, many respondents disagreed with management performance measures being limited to subtotals of income and expenses. These respondents included many users, regulators, accountancy firms and accountancy bodies, and some preparers and standard-setting bodies. Most respondents that disagreed with limiting management performance measures to subtotals of income and expenses were concerned that other non-GAAP measures are widely used and would also benefit from the transparency and discipline provided by the proposed disclosure requirements for management performance measures—in principle, non-GAAP measures should be transparent regardless of whether they relate to financial performance, financial position, or cash flows.
33. Some respondents raised concerns that some of the measures excluded from the definition of management performance measures that could benefit from more transparency and discipline:
- (a) provide important indicators of growth and performance of an entity and provide useful insights into management's view of performance. Some of these respondents provided examples of such measures—the most frequently

mentioned were free cash flows, ratios of return such as return on equity, and adjusted revenues.

- (b) are important measures in some sectors. For example, some respondents said that net asset value was an important indicator in real estate and investing industries and ratios such as return on capital were important to understanding performance in the banking industry. Similar feedback was observed in the fieldwork. Some fieldwork participants did not provide management performance measures note disclosures because they said they currently only report non-GAAP measures that do not meet the definition of a management performance measure—many of these participants were financial institutions.
34. Some respondents that said the scope of management performance measures was too narrow raised concerns that requiring disclosure in the financial statements of only some of the non-GAAP measures included in other communications may:
- (a) make it more difficult for users to find the information and would potentially be confusing. A few of these respondents said that in their opinion financial performance could not be considered independently from other financial information about the entity. Separating non-GAAP information about some aspects of financial performance from other non-GAAP measures would provide an incomplete, and potentially misleading, picture of how management views the entity's position, performance and cash flows.
 - (b) cause confusion about which measures are subject to the requirements for management performance measures and which measures are subject to regulatory requirements only.
35. Many of these respondents, including a few users, suggested changes to the scope of management performance measures including:
- (a) some suggested including all non-GAAP measures derived from an item, subtotal or total presented or disclosed in financial statements prepared in accordance with IFRS Standards;
 - (b) a few suggested including ratios or adjusted line items based on the statement of financial performance;

- (c) a few suggested including financial ratios, measures of growth and measures of liquidity or cash flows;
 - (d) a few suggested aligning the scope of management performance measures with the scope of a regulatory definition of non-GAAP measures; and
 - (e) a few suggested including all measures determined by industry or used internally by management.
36. A few of these respondents suggested proceeding with the current definition and addressing further expansion to other measures in a separate project.

Staff analysis

37. The main argument raised by respondents that disagreed with limiting management performance measures to subtotals of income and expenses is that:
- (a) other measures also provide useful information to users. Some of these are measures frequently used to evaluate performance and others are based on the statement of financial position or cash flow statement.
 - (b) users have the same concerns about these other measures as the concerns the Board sought to address with the management performance measure proposals (see paragraph 29 of this paper). The proposals in the Exposure Draft could therefore also resolve the concerns about other measures if the scope of the proposals were expanded to include these other measures.
38. Expanding the scope of management performance measures to other measures has the potential to provide useful information to users. However, the usefulness of the additional information would depend on whether the disclosure requirements that address the user concerns in paragraph 29 for subtotals of income and expenses, can be adapted to address the same concerns for the additional measures.
39. Defining a revised scope for management performance measures and adapting the disclosure requirements will require time and resources. Any changes to the scope of management performance measures would also require sufficient stakeholder feedback to ensure that the changes would meet users’ needs and that the benefits of the changes would outweigh the cost. Depending on the extent of changes to the scope

and the disclosure requirements this may include re-exposure of the management performance measure proposals. This additional time risks delaying the implementation of the new IFRS Standard and the benefits to users of other aspects of the proposals.

40. The trade-off between providing useful information for other measures and the time and resources required to develop those proposals will vary depending on which measures are included in an expanded scope.
41. In addition, there are actions that could be taken to mitigate the risks of delay to the rest of the project. For example, expanding the scope of the management performance measure requirements could be developed separately from the finalisation of the other aspects of the proposal.
42. In the staff's view the following reasons are sufficient for the Board to explore expanding the scope of management performance measures:
 - (a) there is potential to provide useful information to users; and
 - (b) there is potential to balance the benefits and the additional time required, either through the extent of an expanded scope or mitigating the risk of delay as discussed in paragraph 41.
43. If the Board agrees with the staff recommendation, the staff will perform further work and bring to the Board a paper exploring possible approaches to expanding the scope of management performance measures. Depending on the analysis in that paper, the Board then may decide to expand the scope of the requirements for management performance measures or revert back to the scope proposed in the Exposure Draft.

Question 2

Does the Board agree to explore possible approaches to expanding the scope of the management performance measure requirements to include measures other than subtotals of income and expenses?

Possible approaches and evaluation factors for expanding the scope of the management performance measure requirements

44. We think that before performing a full analysis of the possible approaches for expanding the scope of management performance measures it would be useful to identify the range of possible approaches and set out the factors that could be used to assess these approaches. The following section provides a preliminary analysis to identify possible approaches and evaluation factors. The staff is not asking the Board to make a decision about the possible approaches (paragraph 48) or the evaluation factors (paragraph 51) at this meeting. Rather, we would like feedback on the approaches and factors we have identified to help us develop future papers.
45. The staff are proposing the Board consider measures within the scope and objective of financial statements, which is to provide **financial** information about the reporting entity's assets, liabilities, equity, income and expenses. Measures that provide non-financial information are not proposed to be considered as an approach. For example, square feet, number of customers, or number of branches. However, the Board may want to consider including the financial component of a ratio that includes both a financial and a non-financial measure. For example, adjusted revenue per square foot.

Possible approaches for expanding the scope of management performance measures

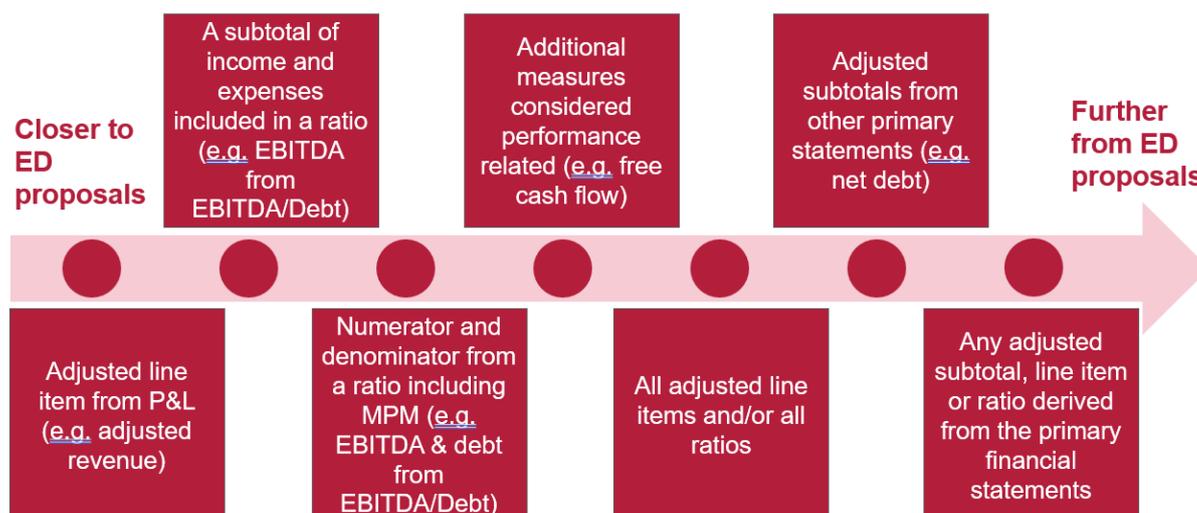
46. To better understand the implications of a possible expansion of the scope of the management performance measure requirements, the staff have researched the use of non-GAAP financial measures excluded from the Exposure Draft definition of management performance measures. The staff reviewed the annual reports and earnings releases of a sample of 100 entities³. In addition, the staff reviewed the annual reports and earnings releases of 38 entities that participated in the fieldwork and were not included in the sample of 100. Appendix B provides a table of the non-GAAP financial measures excluded from the Exposure Draft definition of management performance measures identified in the reviewed reports and earnings releases of the 138 entities.

³ We used the same sample as was used in the Exposure Draft effects analysis.

47. Our research indicates that entities use a wide range of individual measures. However, many of these measures can be classified into a few types:
- (a) measures based on the statement(s) of financial performance (152 instances of these types of measures used in the sample of 138 entities in appendix B⁴)—includes adjusted line items and ratios with both a numerator and denominator based on the statement(s) of financial performance;
 - (b) measures based on the statement of financial position (206 instances of these types of measures used in the sample of 138 entities in appendix B)—includes adjusted line items, adjusted subtotals and ratios consisting of both a numerator and denominator based on the statement of financial position;
 - (c) measures based on the cash flow statement (145 instances of these types of measures used in sample of 138 entities in appendix B)—adjusted subtotals based on the cash flow statement; and
 - (d) ratios with a numerator and denominator based on different primary financial statements (170 instances of these types of measures used in sample of 138 entities in appendix B).
48. There is a wide range of potential approaches for expanding the scope of management performance measures. It might be possible to include specific measures, categories of measures such as those based on a specific statement, or combinations of these different types of measures. For example, figure 1 sets out a number of possible approaches.

⁴The data in Appendix B includes only those measures that do not meet the Exposure Draft definition of management performance measures. There are 152 such measures based on the statement of financial performance. In addition, there are 164 instances of measures based on a subtotal in the statement of financial performance which are not included in Appendix B for a total of 316 measures based on this statement.

Figure 1:



49. To make the assessment of this wide range of possible approaches more manageable, the staff intend to use the four categories in paragraph 47 to assess groups of measures that share common characteristics collectively. That analysis will assess measures based on line items, subtotals or ratios within each category and then consider the benefits and challenges of combining any of these groups of measures within an extended scope.

Potential evaluation factors

50. As discussed in paragraph 40, there is a trade-off between:
- (a) the additional benefits to users of financial statements from expanding the scope; and
 - (b) the additional time and resources required to address that expansion as part of this project.
51. The staff have identified the following factors for the Board to consider when assessing whether a particular approach achieves the appropriate balance of benefits and costs:
- (a) the prevalence of the measure in practice (see paragraphs 52–54);

- (b) the usefulness of the disclosure requirements for the measure and the complexity of necessary changes to those requirements (see paragraphs 55–58);
- (c) the contribution that including the measure in the management performance measure proposals would make to achieving the project objective (see paragraph 59); and
- (d) the complexity involved in developing a new definition of management performance measures (see paragraph 60).

Prevalence of the measure in practice

52. The more prevalent a measure, the more benefits users will have from including it in the scope of management performance measures. Some measures are used more than others. For example, in our research sample of 138 entities, we identified 15 entities that used one non-GAAP measure based on adjustments to a line item in the primary financial statements. We identified 80 entities that used one or more ratios of return. (This is close to the number of entities in this sample that use operating profit.) The limited use of adjusted line items and frequent use of ratios of return could suggest greater benefit in including ratios than in including adjusted line items in the definition of management performance measures.
53. The most frequently used measures in our research were as follows:
- (a) For the 113 non-financial entities:
 - (i) a margin ratio (e.g. EBITDA margin) —used in 92 instances by 63 entities;
 - (ii) a ratio of return (e.g. return on capital employed) —used in 84 instances by 58 entities;
 - (iii) net debt—used by 68 entities; and
 - (iv) free cash flow—used by 67 entities.
 - (b) For the 25 financial entities:
 - (i) a ratio of return (e.g. return on tangible equity) —used in 38 instances by 22 entities;

- (ii) ratio of regulatory capital (e.g. CET1)—used in 24 instances by 21 entities; and
- (iii) cost to income ratio—used by 15 entities.

54. To compare the frequency of these measures to those based on subtotals in the statement of profit or loss, of these same entities 81 of 113 non-financial and 12 of 25 financial entities use operating profit as a performance measure either presented in the statement of profit or loss, disclosed in the notes, or included in the annual report.

Usefulness of the disclosure requirements for the measure and the complexity of necessary changes to those requirements

55. Disclosures for management performance measures address user concerns that management-defined measures lack transparency and clarity, their relationship to measures specified in IFRS Standards is unclear and they are reported inconsistently from period to period (see paragraph 29).
56. The disclosure requirements were developed specifically for subtotals of income and expenses. The usefulness of these disclosure requirements for other measures will depend on the extent the same disclosure requirements can be applied to effectively address the concerns described in paragraph 55.
57. Some requirements, such as consistency in calculation and explanation of any changes in the calculation could equally apply to any measure. However, some requirements may not apply as easily to other measures and may need to be revised. For example, tax and non-controlling interest relating to reconciling items would not be relevant to measures based on the statement of financial position or the cash flow statement. The extent and complexity of any revisions to the disclosure requirements required for a particular measure will be a factor contributing to the additional time and resources required.
58. In the staff's view the disclosure requirement that will be the most complex to apply to other measures is the requirement to reconcile the measure to the most directly comparable subtotal or total specified by IFRS Standards. The reconciliation requirement will be the most challenging to adapt because in some cases a management-defined measure may not have a directly comparable equivalent measure

that is specified in IFRS Standards. For example, IFRS Standards do not define a subtotal that is equivalent to net debt.

Contribution that including the measure in the management performance measure proposals would make to achieving the project objective

59. The project objective is to improve how information is communicated in the financial statements, with a focus on information in the statement of profit or loss. In line with this objective the definition of management performance is limited to subtotals of income and expenses that communicate an aspect of an entity's financial performance. If we focus on communicating financial performance as the implied objective of management performance measures, we find that some measures excluded from the definition of management performance measures are closer to this objective than others. For example, measures such as ratios that express a return relative to a balance sheet measure are generally considered measures of performance and often include a numerator that would meet the existing definition of a management performance measure. However other measures, such as a debt-to-equity ratio are not generally considered measures of performance and are further away from the objective. The closer a measure is to the project objective the greater it will contribute to addressing the original concerns of users about performance reporting. Measures closer to the scope of management performance measures proposed in the Exposure Draft will require fewer changes to requirements.

Complexity involved in developing a new definition of management performance measures

60. Drafting a definition in way that includes specific measures while excluding others may not be straightforward. Individual measures may have different uses, different ways of being calculated and different labels. These differences may cause challenges in defining the line between those measures intended to be included and those intended to be excluded and may require further research on current practice. For example, if a decision were made to include financial ratios in the definition but to exclude other measures based on the statement of financial position, the definition would need to be drafted in a way that includes the element of a ratio derived from the

statement of financial position while excluding measures other than ratios that are based on the statement of financial position.

Summary

61. We plan to analyse the following possible approaches to expanding the scope of management performance measures, expanding the scope to include:
 - (a) measures based on the statement(s) of financial performance—including adjusted line items and ratios;
 - (b) measures based on the statement of financial position—including adjusted line items, adjusted subtotals and ratios;
 - (c) measures based on the cash flow statement—including adjusted subtotals; and
 - (d) ratios with a numerator and denominator based on different primary financial statements.

62. We have identified the following factors to use when assessing these possible approaches:
 - (a) the prevalence of the measure in practice;
 - (b) the usefulness of the disclosure requirements for the measures and the complexity of necessary changes to those requirements;
 - (c) the contribution that including the measure in the management performance measure proposals would make to achieving the project objective; and
 - (d) the complexity involved in developing a new definition of management performance measures.

Question 3

- (a) Does the Board have any comments or questions on the possible approaches to expanding the scope of management performance measures discussed in paragraph 61?
- (b) Does the Board agree the staff should use the factors identified in paragraph 62 to assess the possible approaches in paragraph 61 for expanding the scope of management performance measures? Are there any other factors the Board would like the staff to include in such an analysis? Are any of the factors more important than others?

Appendix A—Extracts of management performance measure requirements from Exposure Draft

Management performance measures

103 *Management performance measures* are subtotals of income and expenses that (see paragraphs B76–B81):

- (a) are used in public communications outside financial statements;
- (b) complement totals or subtotals specified by IFRS Standards; and
- (c) communicate to users of financial statements management’s view of an aspect of an entity’s financial performance.

104 Subtotals specified by IFRS Standards that are not management performance measures include:

- (a) a total or subtotal required by paragraphs 60 and 73;
- (b) gross profit or loss (revenue less cost of sales) and similar subtotals (see paragraph B78);
- (c) operating profit or loss before depreciation and amortisation;
- (d) profit or loss from continuing operations; and
- (e) profit or loss before income tax.

105 Management performance measures shall:

- (a) faithfully represent aspects of the financial performance of the entity to users of financial statements; and
- (b) be described in a clear and understandable manner that does not mislead users.

106 **An entity shall disclose information about any management performance measures in a single note to the financial statements. That note shall include a statement that the management performance measures provide management’s view of an aspect of the entity’s financial performance and are not necessarily comparable with measures sharing similar descriptions provided by other**

entities. In addition, for each management performance measure an entity shall disclose in the notes (see paragraphs B82–B85):

- (a) a description of why the management performance measure communicates management’s view of performance, including an explanation of:

 - (i) how the management performance measure is calculated; and**
 - (ii) how the measure provides useful information about the entity’s performance;****
- (b) a reconciliation between the management performance measure and the most directly comparable subtotal or total included in paragraph 104;**
- (c) the income tax effect and the effect on non-controlling interests for each item disclosed in the reconciliation required by paragraph 106(b); and**
- (d) how the entity determined the income tax effect required by paragraph 106(c).**

107 An entity shall determine the income tax effect required by paragraph 106(c) on the basis of a reasonable pro rata allocation of the current and deferred tax of the entity in the tax jurisdiction(s) concerned or by another method that achieves a more appropriate allocation in the circumstances.

108 If an entity changes the calculation of its management performance measures, introduces a new management performance measure or removes a previously disclosed management performance measure from its financial statements, it shall:

- (a) disclose sufficient explanation for users of financial statements to understand the change, addition or removal and its effects;
- (b) disclose the reasons for the change, addition or removal; and
- (c) restate its comparative information, including in the required note disclosures, to reflect the change, addition or removal.

109 A subtotal included in the statement(s) of financial performance applying paragraph 42 may be a management performance measure (see paragraph B81).

110 An entity shall not use columns to present management performance measures in the statement(s) of financial performance.

Management performance measures

Identifying management performance measures

B76 Paragraph 103 defines management performance measures. Some entities may have more than one management performance measure. However, not all entities will have management performance measures. For example, if an entity publicly communicates its financial performance to users of its financial statements, using only totals and subtotals specified by IFRS Standards, it will not have a management performance measure.

B77 Paragraph 104 specifies subtotals that are not management performance measures. An entity is not required to provide the disclosures specified in paragraph 106 for these subtotals.

B78 In accordance with paragraph 104(b) subtotals similar to gross profit are not management performance measures. A subtotal is similar to gross profit when it represents the difference between a type of revenue and directly related expenses incurred in generating that revenue. Examples include:

- (a) net interest income;
- (b) net fee and commission income;
- (c) insurance service result;
- (d) net financial result (investment income minus insurance finance expenses); and
- (e) net rental income.

B79 Only subtotals that management uses in public communications outside financial statements, for example, in management commentary, press releases or in investor presentations, meet the definition of management performance measures.

B80 A management performance measure is a subtotal of income and expenses. Examples of measures that are not management performance measures include:

- (a) individual items or subtotals of only income or expenses (for example, adjusted revenue as a stand-alone measure);
- (b) assets, liabilities, equity or combinations of these elements;
- (c) financial ratios (for example, return on assets);
- (d) measures of growth;
- (e) measures of liquidity or cash flows (for example, free cash flow); or
- (f) non-financial performance measures.

B81 A subtotal presented in the statement(s) of financial performance to comply with paragraph 42 may meet the definition of a management performance measure. When such a subtotal meets that definition, an entity shall disclose all the information required by paragraph 106.

Management performance measures note disclosure

B82 All information required to be disclosed about management performance measures shall be included in a single note.

B83 In some cases, one or more of an entity's management performance measures may be the same as part of the operating segment information disclosed by the entity in applying IFRS 8. In such cases, the entity may disclose the required information about those management performance measures in the same note that it uses to disclose information about its operating segments provided the entity either:

- (a) includes in that note all of the information required by paragraph 106 for management performance measures; or
- (b) provides a separate note that includes all of the information required for management performance measures.

B84 Paragraph 106(a)(i) requires an explanation of how a management performance measure is calculated. To comply with this requirement an entity shall explain the specific principles, bases, conventions, rules and practices it applies in calculating its management performance measures.

B85 Paragraph 106(b) requires an entity to reconcile its management performance measure(s) to the most directly comparable subtotal or total specified by IFRS

Standards. For example, an entity that discloses in the notes adjusted operating profit or loss as a management performance measure would reconcile to operating profit or loss as the most directly comparable subtotal. In aggregating or disaggregating the reconciling items disclosed an entity shall apply the requirements in paragraphs 25–28.

Management performance measures (Basis for Conclusions)

BC145 When an entity provides one or more performance measures that meet the definition of management performance measures, the Board proposes to require entities to disclose information about such measures in their financial statements.

BC146 Research undertaken as part of the Primary Financial Statements project, feedback received on the 2017 Discussion Paper *Disclosure Initiative—Principles of Disclosure* and the 2015 Agenda Consultation indicated that:

- (a) many entities disclose financial information outside the financial statements by providing management-defined performance measures in communications with users of financial statements; and
- (b) users consider that information provided by such measures can be useful because it provides insight into:
 - (i) how management views the entity’s financial performance;
 - (ii) how a business is managed; and
 - (iii) the persistence or sustainability of an entity’s financial performance.

BC147 However, users of financial statements expressed concerns about the quality of disclosures provided about these measures. According to users, in some cases, the disclosures:

- (a) lack transparency in how the management-defined performance measures are calculated;
- (b) lack clarity regarding why these measures provide management’s view of the entity’s performance;
- (c) create difficulties for users trying to reconcile the measures to the related measures specified by IFRS Standards; and

- (d) are reported inconsistently from period to period.

BC148 Including disclosures about these measures in the financial statements could help address some of the concerns expressed by users of financial statements. However, some stakeholders raised concerns about including management-defined performance measures in financial statements prepared applying IFRS Standards, which were that:

- (a) management-defined performance measures may be incomplete or biased and therefore including them in the financial statements may be misleading to users of financial statements;
- (b) management-defined performance measures may be given undue prominence or legitimacy by including them in the financial statements; and
- (c) some adjustments made in calculating management-defined performance measures may be difficult to audit—for example, adjustments made when an entity calculates its performance measures using accounting policies that do not comply with IFRS Standards.

BC149 The Board considered the concerns raised, noting that management-defined performance measures that meet the definition of management performance measures, and would thus be included in the financial statements:

- (a) would be subject to the general requirement for information to faithfully represent what it purports to represent, which would not be met if measures were misleading (see paragraph BC158).
- (b) would rarely be presented in the statement(s) of financial performance (see paragraphs BC163–BC166).
- (c) are similar to segment measures of profit or loss in that they are based on management’s view. Segment measures of performance are included in the financial statements and are audited.

B150 Some stakeholders also expressed concerns that management performance measures may proliferate if they are included in the financial statements. The Board noted that it is difficult to predict the effect of the proposals on the number of management performance measures an entity would use. While it is possible that the use of such measures would increase as a result of the Board’s proposals, it is also possible that

the use of management performance measures would decline if entities choose to use the proposed new subtotals to communicate their performance instead. Paragraphs BC304–BC307 include further discussion of the expected effects of the proposals for management performance measures on the use of performance measures defined by management.

BC151 The Board acknowledges the concerns of some stakeholders, but concluded that management performance measures can complement measures specified by IFRS Standards, providing users of financial statements with useful insight into management’s view of performance and its management of the business. Including these measures in the financial statements would make them subject to the same requirements regardless of the entity’s jurisdiction and would improve the discipline with which they are prepared and improve their transparency.

Appendix B—Non-GAAP measures excluded from the Exposure Draft definition of management performance measures

B1. The following table summarises the number of instances of each non-GAAP measure identified in the most recently published annual reports and/or related earnings announcements of the 50 entities that participated in our fieldwork and a sample of 100 entities used in the Exposure Draft effects analysis. The sample includes entities from a range of industries and geographies. The total number of entities in the table is 138 as 12 fieldwork participants are included in our sample of 100 companies. The table excludes any non-GAAP measure that, in the staff’s view, would meet the definition of a management performance measure or is included in the list of measures specified in IFRS Standards in the Exposure Draft.

Sector		Measures based on the statement of financial performance	Measures based on the statement of financial position	Measures based on the cash flow statement	Measures based on multiple financial statements
Non-Financial (113 entities)	Line items	Adjusted revenue (10)			
	Subtotals		Net debt (68) Risk-weighted assets (1)	Free cash flow (67) Capital expenditure (52) Funds from operations (14) Net cash before changes in working capital (10)	
	Ratios	Operating margin (34) EBITDA margin (22) Gross margin (18) EBIT margin (11) Net profit margin (7) Interest Coverage ratio (13)	Gearing (Liabilities/equity) (28) Debt to equity ratio (20) Equity ratio (Equity/Total Assets) (14) Leverage ratio (Liabilities/Equity) (6) Current ratio (5) Debt to asset ratio (3)		Return on equity (33) Return on capital employed (21) Return on assets (13) Return on invested capital (12) Return on average capital employed (5) Net debt/EBITDA (28) Cash conversion ratio (free cash flow/adjusted net profit) (7) Net debt to funds from operations (3)

Financial (25 entities)	Line items	Adjusted revenue (5)			
	Subtotals		Loans and deposits (6) Risk-weighted assets (5)	Free cash flow (1) Capital expenditure (1)	
	Ratios	Cost to income ratio (15) Combined operating ratio (4) Net interest margin (10) Operating margin (1) EBIT margin (1) Net profit margin (1)	CET 1 capital ratio* (18) Leverage ratio (10) Loan to deposit ratio (8) Non-performing loan ratio (6) Total capital ratio (3) Solvency II capitalisation ratio (3) Equity ratio (1) Gearing (1)		Return on equity (19) Return on tangible equity (10) Return on assets (4) Return on risk-weighted assets (4) Return on invested capital (1) Liquidity coverage ratio (7) Coverage ratio (3)

* Common equity tier 1 capital (CET 1) net of regulatory adjustments divided by risk-weighted assets.