STAFF PAPER

March 2022

IASB® meeting

Project	**Primary Financial Statements**
Paper topic	Entities with specified main business activities—General issues

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Objective of this paper

1. This paper sets out the staff analysis and recommendations relating to some of the proposals in the Exposure Draft *General Presentation and Disclosures* for entities that:
   (a) invest in the course of main business activities in assets that generate a return individually and largely independently of other resources held by the entity (referred to as 'entities that invest in the course of main business activities'); or
   (b) provide financing to customers as a main business activity.
2. This paper is the first in a series of papers on entities that invest in the course of main business activities or provide financing to customers as a main business activity (referred to combined as 'entities with specified main business activities'). It considers the feedback on the key concept of 'main business activities' that is related to both the investing category and the financing category.
3. In future papers, we plan to discuss:
   (a) the feedback on main business activities specific to the investing and financing categories, including whether and what changes are required for the accounting policy choice for entities that provide financing to customers as a main business activity;

(b) the consequences of the redeliberations on the investing and financing categories for entities with specified main business activities, including the change in category for income and expenses from cash and cash equivalents and the change in how interest expense on trade payables and lease liabilities is captured within the financing category;

(c) the classification of income and expenses from associates and joint ventures accounted for using the equity method that are held by entities with specified main business activities;

(d) insurance finance income and expenses included in profit or loss;

(e) application of the proposals in separate financial statements;

(f) disclosure of significant judgements made in applying presentation and disclosure requirements; and

(g) feedback related to consequential amendments to IFRS 8 *Operating Segments*.

Summary of staff recommendations

4. The staff recommend that the International Accounting Standards Board (IASB):

(a) provide additional guidance on 'main business activities' by clarifying that:

(i) the role of main business activities in the requirements of the Accounting Standard is limited;

(ii) when an entity has a reportable segment that constitutes a single business activity it indicates that the business activity of the reportable segment is a main business activity of the entity;

(iii) when an entity has an operating segment that constitutes a single business activity, but it does not meet the requirements to be a reportable segment, that operating segment is not precluded from being a main business activity when the operating performance of the operating segment is an important indicator of operating performance of the entity;

(iv) the assessment of main business activities is not only a matter of judgement, but should also be observable through the operating performance communicated to users in public communications; and

(v) the specified subtotals similar to gross profit in paragraph B78 of the Exposure Draft are examples of important indicators of operating performance for entities that invest in the course of main business activities or provide financing to customers as a main business activity;

(b) clarify that the assessment of whether an entity invests in the course of main business activities or provides financing to customers as a main business activity is performed at the reporting entity level;

(c) clarify that when there is a change in the assessment of whether an entity invests in the course of main business activities or provides financing to customers as a main business activity, the change is made prospectively and thus restatement of comparatives is not required; and

(d) require that when there has been a change in the assessment of whether an entity invests in the course of main business activities or provides financing to customers as a main business activity, the entity shall disclose that fact.

Structure of the paper

5. This paper is structured as follows:

(a) background (paragraphs 7–23):

(i) proposals in the Exposure Draft (paragraphs 7–8);

(ii) feedback on the Exposure Draft (paragraphs 9–18);

(iii) summary of tentative IASB decisions (paragraphs 19–23);

(b) staff analysis, staff recommendations and questions for the IASB (paragraphs 24–81):

(i) whether the IASB should provide additional guidance on main business activities (paragraphs 25–56);

(ii) whether the IASB should clarify the level for assessing main business activities (paragraphs 57–69);

(iii) whether restatement of comparatives is required when main business activities change (paragraphs 70–76); and

(iv) whether additional disclosures about changes in the assessment of main business activities are required (paragraph 77–81).

6. There are three appendices to this paper:

(a) Appendix A— Summary of the proposals for the structure of the statement of profit or loss

(b) Appendix B—Paragraphs from the Exposure Draft

(c) Appendix C—Paragraphs from IFRS Accounting Standards

Background

Proposals in the Exposure Draft

7. The Exposure Draft describes a 'general model' for the structure of the statement of profit or loss. In addition, the Exposure Draft proposes specific requirements for entities that invest in the course of main business activities or provide financing to customers as a main business activity to ensure that the operating category includes all income and expenses from their main business activities[1]. For entities applying these specific requirements, the Exposure Draft proposes that the operating category include the following:

(a) income and expenses from individual investments made in the course of the entity's main business activities (paragraph 48 of the Exposure Draft);

(b) for an entity that provides financing to customers as a main business activity, as an accounting policy choice, either:

[1] Except for income and expenses from associates and joint ventures accounted for using the equity method which are classified outside of the operating category regardless of their relationship to main business activities.

(i) income and expenses from financing activities, and from cash and cash equivalents, that relate to the provision of financing to customers; or

(ii) all income and expenses from financing activities and all income and expenses from cash and cash equivalents (paragraph 51 of the Exposure Draft);

(c) income and expenses from cash and cash equivalents if an entity invests in financial assets that generate a return individually and largely independently of other resources held by an entity in the course of its main business activities (paragraph 52(a) of the Exposure Draft);

(d) income and expenses on liabilities arising from issued investment contracts with participation features recognised applying IFRS 9 *Financial Instruments* (paragraph 52(b) of the Exposure Draft); and

(e) insurance finance income and expense included in profit or loss (paragraph 52(c) of the Exposure Draft).

8. Appendix A summarises these requirements and explains how they relate to the general model.

Extract of the feedback on the proposals in the Exposure Draft

Comment letter feedback

9. Many respondents said the IASB should provide further guidance to help an entity identify its main business activities, because this assessment plays an important role in the determination of operating profit. Without further guidance, they are concerned entities would apply the proposals inconsistently, which would undermine the comparability of the operating profit subtotal.

10. A few respondents suggested additional indicators that could help an entity identify a main business activity—for example, they suggested an activity is likely to be a main business activity if:

(a) the income or expenses from the activity are reviewed by the chief operating decision maker in assessing the entity's operating performance;

(b) the income or expenses from the activity are considered in determining key management personnel compensation; or

(c) the activity is included in the entity's business purpose as described in its articles of association (or similar documents).

11. Some respondents suggested the IASB should clarify:

(a) the relationship between 'main business activities' and similar concepts in other IFRS Accounting Standards, such as 'ordinary activities' (used in the definition of revenue in IFRS 15 *Revenue from Contracts with Customers*) and 'principal revenue-producing activities' (used in the definition of cash flows from operating activities in IAS 7 *Statement of Cash Flows*);

(b) the level at which 'main business activities' are assessed in a group. They questioned whether the assessment should be made from the perspective of the reporting entity—that is, the group—or the individual subsidiaries. Some of those respondents said the IASB should clarify whether differences in classification can arise between consolidated and separate financial statements due to different activities being identified as main business activities;

(c) how an entity should identify and present changes in its main business activities. Some respondents said it was unclear whether comparative figures would need to be restated to reflect changes in main business activities; and

(d) how an entity's main business activities relate to its operating segments. For example, paragraph B31 of the Exposure Draft proposed that '[i]f, applying IFRS 8 *Operating Segments*, an entity reports a segment that constitutes a single business activity, that may indicate that that business activity is a main business activity.' A few respondents suggested the IASB should clarify whether an *operating* segment can represent a main business activity, even if it does not meet the criteria in IFRS 8 to be a *reportable* segment.

12. A few respondents said that the following disclosure requirements—which the Exposure Draft proposes to carry over from IAS 1 *Presentation of Financial Statements*—would provide sufficient information about how an entity has identified its main business activities:

(a) the requirement for an entity to describe its main business activities (paragraph 138 of IAS 1, paragraph 99 of the Exposure Draft); and

(b) the requirement to disclose information about significant judgements (paragraph 122 of IAS 1, proposed to be moved to paragraph 27E of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*).

13. However, some other respondents suggested strengthening the proposed disclosure requirements by:

(a) giving the requirement to describe the entity's main business activities more prominence in the Accounting Standard—it is currently at the end of the [draft] Accounting Standard in the 'other disclosures' section.

(b) introducing a specific disclosure requirement for judgements made in identifying an entity's main business activities. One accounting firm suggested clarifying that the requirement to disclose information about significant judgements described in paragraph 12(b) includes significant judgements made in applying presentation and disclosure requirements. They said this requirement is read by some as only relating to judgements made in applying recognition and measurement requirements.

Feedback from fieldwork participants[2]

14. Most participants were able to identify and classify in the operating category:

(a) income and expenses from investments made in the course of the participants' main business activities; and

(b) all income and expenses from financing activities and cash and cash equivalents or the portion of these income and expenses related to the provision of financing to customers when providing financing to customers was a main business activity.

15. Some participants said that significant judgements were required in determining whether investments were made in the course of an entity's main business activities or

[2] Paragraphs 26–35 in Agenda Paper 21A of the December 2020 IASB meeting describe the methodology of the fieldwork.

provision of financing to customers was a main business activity. For example, when an entity makes an investment in a customer or supplier or sells products or services to customers on extended credit terms.

16. Some participants said that they were unclear on whether different main business activities could be identified in the consolidated financial statements and the subsidiary financial statements. For example, some participants were unclear whether having a subsidiary with a main business activity of provision of financing to customers meant that providing financing to customers was required to be a main business activity in the consolidated financial statements.

17. Some participants raised concerns that having different main business activities in the consolidated financial statements and the subsidiary financial statements may cause practical difficulties. For example, one participant was required to present financial statements for both the consolidated group and for the non-consolidated parent company. The non-consolidated parent company was a holding company and would therefore have a different main business activity from the consolidated group. This participant said that the different main business activities would make it difficult to:

    (a) continue its current practice of presenting the group and parent statements of profit and loss in a single statement;

    (b) consolidate the parent and subsidiary accounts without additional processes and systems changes; and

    (c) explain the differences between the main business activities to investors and regulators.

18. Some participants that said they would have different main business activities in the group financial statements and in the subsidiary financial statements said that systems and process changes would be required to reclassify income and expenses on consolidation.

Summary of related IASB tentative decisions from redeliberations to date

19. In March 2021, the IASB tentatively decided to require an entity to present an operating profit subtotal and confirm that the operating category:

(a) includes all income and expenses recognised in profit and loss that are not classified in the investing, financing, income tax and discontinued operations categories;

(b) comprises all income and expenses arising from an entity's operations including volatile and unusual income and expenses arising from an entity's operations; and

(c) includes, but is not limited to, income and expenses from an entity's main business activities (See Agenda Paper 21A of the March 2021 IASB meeting).

20. In May 2021, the IASB tentatively decided to:

(a) retain the proposal to introduce separate investing and financing categories in the statement of profit or loss;

(b) retain the proposal to define the 'profit or loss before financing and income tax' subtotal and require it to be presented in the statement of profit or loss; and

(c) require an entity to classify income and expenses from cash and cash equivalents in the investing category rather than the financing category (see Agenda Paper 21B of the May 2021 IASB meeting).

21. In July 2021, the IASB tentatively decided to:

(a) require an entity to classify in the financing category all income and expenses from liabilities that arise from transactions that involve only the raising of financing and specified income and expenses from other liabilities;

(b) change the 'default category' for the classification of fair value gains and losses on derivatives and hedging instruments used for risk management from the investing category to the operating category; and

(c) change the classification of fair value gains or losses on derivatives not used for risk management from the investing category to the operating category (see Agenda Paper 21B of the July 2021 IASB meeting).

22. In October 2021, the IASB tentatively decided to:

(a) proceed with the proposal to require an entity to classify income and expenses from associates and joint ventures accounted for using the equity method outside the operating category;

(b) not to proceed with the proposal to require an entity to present the subtotal 'operating profit or loss and income and expenses from integral associates and joint ventures'; and

(c) not to proceed with the proposal to require an entity to identify and present income and expenses from integral associates and joint ventures separately from income and expenses from non-integral associates and joint ventures (see Agenda Paper 21A of the October 2021 IASB meeting).

23. In December 2021, the IASB tentatively decided to:

(a) retain the proposal for entities to classify in the investing category income and expenses from assets that generate returns individually and largely independently of other resources held by the entity; and

(b) classify income and expenses from associates and joint ventures accounted for using the equity method in the investing category (see Agenda Paper 21B of the December 2021 IASB meeting).

Staff analysis, staff recommendations and questions for the IASB

24. In this paper we analyse:

(a) whether the IASB should provide additional guidance on main business activities (paragraphs 25–56);

(b) whether the IASB should clarify the level for assessing main business activities (paragraphs 57–69);

(c) whether restatement of comparatives is required when there is a change in main business activities (paragraphs 70–76); and

(d) whether additional disclosures about changes in the assessment of main business activities are required (paragraph 77–81).

Additional guidance on main business activities

25. In this section of the paper, we analyse whether the IASB should add additional guidance on:

    (a) the role of main business activities (see paragraphs 26–29);

    (b) the relationship between main business activities and similar concepts used in other IFRS Accounting Standards (paragraphs 30–35);

    (c) the relationship between main business activities and operating segments (paragraphs 36–46); and

    (d) important indicators of operating performance for entities with specified main business activities (paragraphs 47–56).

Role of main business activities

26. Many respondents said the IASB should provide further guidance to help an entity identify its main business activities, because this assessment plays an important role in the determination of operating profit (see paragraph 9).

27. Paragraphs 48 and 51 of the Exposure Draft require an entity to assess whether it:

    (a) invests in the course of its main business activities in assets that generate a return individually and largely independently of other resources held by the entity; or

    (b) provides financing to customers as a main business activity.

28. In performing this assessment, an entity is only required to identify whether it conducts business activities that constitute (a) or (b) in paragraph 27. An entity is not required to identify all business activities and assess whether each activity constitutes a main business activity.

29. As the operating category is the residual category that includes, but is not limited to, income and expenses from an entity's main business activities (see paragraph 19) and the requirement to assess main business activities is limited to the two specified business activities in paragraph 27, the staff recommend that the IASB clarify in the application guidance that the role of main business activities in the requirements of the Accounting Standard is limited and that an entity is not required to identify

all business activities and assess whether each activity constitutes a main business activity.

Relationship with concepts used in other IFRS Accounting Standards

30. Some respondents suggested the IASB should clarify the relationship between 'main business activities' and similar concepts in other IFRS Accounting Standards, such as 'ordinary activities' used in the definition of revenue in IFRS 15 and 'principal revenue-producing activities' used in the definition of cash flows from operating activities in IAS 7 (see paragraph 11).

31. The Exposure Draft uses the concept 'business activities' because it is used in the *Conceptual Framework for Financial Reporting (Conceptual Framework)*. The Conceptual Framework does not define business activities, but paragraph BC0.32 explains that the concept of business activities can be further explained and developed in a particular IFRS Accounting Standard.

32. In April 2019, the IASB discussed whether to develop further guidance on main business activities, including a principle-based definition of 'main business activities'. However, the staff did not recommend pursuing such an approach because it would be similar to the IASB trying to define 'ordinary activities', which the IASB has found challenging in the past (see Agenda Paper 21B of the April 2019 IASB Meeting).

33. IFRS Accounting Standards acknowledge that revenue from ordinary activities may be broader than those activities generating revenue from contracts with customers in the scope of IFRS 15 (see paragraph BC247 of IFRS 15 and Appendix A, paragraphs B7(c) and BC21S of IFRS 3 *Business Combinations*). Entities that invest in the course of main business activities or provide financing to customers as a main business activity often generate revenue which is not accounted for in accordance with IFRS 15. As a result, any clarification of the relationship between 'main business activities' and 'ordinary activities' in IFRS 15 is likely to be of limited use.

34. 'Principal revenue-producing activities' is included in the definition of operating activities in paragraph 6 of IAS 7. In December 2017, the IASB decided not to align the operating category in the statement of cash flows with the operating category in the statement of profit or loss. In analysing whether to seek alignment, the staff considered and rejected an approach to defining the operating category in the

statement of profit or loss based on the definition of operating activities in paragraph 6 of IAS 7. The staff also noted that the statement of cash flows and statement of financial performance have different purposes. Attempting alignment will therefore always be at best partial and will not necessarily aid understanding of either statement or the performance of the entity more generally (see Agenda Paper 21D of the December 2017 IASB meeting).

35. The comments from stakeholders on clarifying the relationship between 'main business activities' and similar concepts in other IFRS Accounting Standards do not provide any new information that suggests that the IASB should change the approach that it has taken in the Exposure Draft. Hence, the staff recommend that the IASB not clarify the relationship between 'main business activities' and 'ordinary activities' in IFRS 15 and 'principal revenue-producing activities' in IAS 7.

Relationship with operating segments

36. Some respondents suggested the IASB should clarify how an entity's main business activities relate to its operating segments. A few respondents suggested the IASB should clarify that an operating segment can represent a main business activity, even if it does not meet the criteria in IFRS 8 to be a reportable segment (see paragraph 11(d)).

37. Paragraph B31 of the Exposure Draft describes the relationship between main business activities and segment reporting as follows.

> B31 If, applying IFRS 8 *Operating Segments*, an entity reports a segment that constitutes a single business activity, that may indicate that that business activity is a main business activity.

38. The staff note that it is not clear from the wording in paragraph B31 of the Exposure Draft whether 'reports a segment that constitutes a single business activity' is referring to an 'operating segment' or a 'reportable segment' in IFRS 8. The Basis for Conclusions does not contain a summary of the considerations of the IASB when developing the proposal in paragraph B31 of the Exposure Draft. However, the staff note that when discussing this proposal prior to issuing the Exposure Draft:

(a) the concept discussed by the IASB was 'separate reportable segment'; and

(b) the IASB did not propose a separate reportable segment should be a criterion that is required to be met for a business activity to be a main business activity because not all entities identify segments on the basis of products or services provided—for example some entities identify geographical segments (see Agenda Paper 21B of the April 2019 IASB meeting).

39. Appendix A and paragraph 5 of IFRS 8 define an 'operating segment' as follows *(emphasis added)*.

> An operating segment is a component of an entity:
>
> (a) that engages in *business activities* from which it may earn revenues and incur expenses (including revenues and expenses relating to transactions with other components of the same entity),
>
> (b) whose operating results are regularly reviewed by the entity's chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance, and
>
> (c) for which discrete financial information is available.

40. Paragraphs 11–19 of IFRS 8 contain quantitative thresholds and aggregation criteria for determining a 'reportable segment'. In summary, an entity:

(a) reports information about an operating segment separately as a reportable segment when it meets any of the 10% quantitative thresholds for revenue, profit or loss and assets (paragraph 13 of IFRS 8);

(b) may consider an operating segment to be a reportable segment when these quantitative thresholds are not met, if management believes information about that segment may be useful to users (paragraph 13 of IFRS 8);

(c) identifies additional operating segments as reportable segments if total external revenue reported by operating segments constitutes less than 75 per cent of the entity's revenue (paragraph 15 of IFRS 8);

(d) may combine information about operating segments to produce a reportable segment if the operating segments have similar economic characteristics and share a majority of the aggregation criteria (paragraph 14 of IFRS 8);

(e) combines and discloses information about other business activities and operating segments in an ‘all other segments’ category when they do not meet the criteria to be reportable segments (paragraph 16 of IFRS 8); and

(f) should consider whether the number of reportable segments that are separately disclosed is beyond the practical limit at which segment information becomes too detailed if an entity has more than ten reportable segments (paragraph 19 of IFRS 8).

41. An operating segment is a component of an entity that engages in ‘business activities’, ie it may constitute one or more of its business activities. A component of a reporting entity, such as a subsidiary, that constitutes a single business activity will meet the definition of an operating segment if it earns revenues and incurs expenses from that business activity, its results are regularly reviewed by the entity’s chief operating decision maker and discrete financial information is available. Hence, the bar to meeting the definition of an operating segment is comparatively low.

42. By contrast, the bar to meeting the requirements to be a reportable segment is higher. A reportable segment may be a single operating segment or a combination of two or more operating segments depending on how the quantitative thresholds and aggregation criteria are applied. For example, a reporting entity may have a single business activity that meets the definition of an operating segment. After application of the quantitative thresholds and aggregation criteria the business activity may either be disclosed as a separate reportable segment, combined with other operating segments to produce a reportable segment or disclosed in the ‘all other segments’ category.

43. The staff think that when a reportable segment constitutes a single business activity, that is an indicator that the business activity of that reportable segment is a main business activity. However, the staff do not think that the IASB intended that the application of the quantitative thresholds and aggregation criteria for determining reportable segments in IFRS 8 should preclude an entity from judging that an operating segment with a single business activity constitutes a main business activity. Rather, what matters is whether the operating performance of that operating segment is an important indicator of the operating performance of the entity (see paragraphs 47–56 for discussion of important indicators of operating performance).

44. Therefore, the staff agree with the respondents that suggested the IASB clarify that an operating segment can represent a main business activity, even if it does not meet the quantitative thresholds and aggregation criteria in IFRS 8 to be a reportable segment (see paragraph 11(d)).

45. The general disclosure requirements in paragraph 22 of IFRS 8 require an entity to disclose the factors used to identify the entity's reportable segments, including whether operating segments have been aggregated, the judgements made in applying the aggregation criteria and the types of products and services from which each reportable segment derives its revenues. The staff expect that these disclosures will help to ensure that transparency is not compromised when an entity judges that an operating segment that is not a separate reportable segment represents a main business activity.

46. Therefore, the staff recommend that the IASB clarify that:

(a) when an entity has a reportable segment that constitutes a single business activity it indicates that the business activity of the reportable segment is a main business activity of the entity; and

(b) when an entity has an operating segment that constitutes a single business activity, but it does not meet the requirements to be a reportable segment, that operating segment is not precluded from being a main business activity if the operating performance from that operating segment is an important indicator of operating performance of the entity.

Important indicators of operating performance

47. Some participants in the fieldwork said that significant judgements were required in determining whether investments were made in the course of an entity's main business activities or providing financing to customers was a main business activity (see paragraph 15). A few respondents also suggested additional indicators that could be used in the assessment (see paragraph 10).

48. Paragraphs B27 and B29 of the Exposure Draft explain that determining whether an entity invests in the course of main business activities or provides financing to customers as a main business activity is a matter of judgement. Both paragraphs also

provide examples of entities that conduct such business activities and explain that in general:

(a) investments are likely to have been made in the course of an entity's main business activities when investment returns are an important indicator of operating performance; and

(b) providing financing to customers is likely to be a main business activity when the difference between interest income and the related interest expense is an important indicator of operating performance.

49. The staff considered whether the following three indicators suggested by respondents in paragraph 10 could enhance this guidance:

(a) income or expenses from the activity are reviewed by the chief operating decision maker in assessing the entity's operating performance – a similar indicator is used in the assessment of operating segments in paragraph 5 of IFRS 8. The staff do not think it is necessary to introduce this as an indicator given the clarification of the relationship between main business activities and segment reporting discussed above in paragraphs 36–46;

(b) income or expenses from the activity are considered in determining key management personnel compensation – a similar indicator is used in the business model assessment in IFRS 9 which is discussed below in paragraphs 50–53; and

(c) whether the activity is included in the entity's articles of association or similar documents – the staff note that this may not be a suitable indicator for all entities to consider when assessing whether the entity invests in the course of main business activities or provides financing to customers as a main business activity because such documents are prepared in accordance jurisdiction specific laws and regulations and contain varying degrees of granularity.

50. In considering the indicator suggested by respondents in paragraph 49(b), the staff considered the overall business model assessment in IFRS 9. The business model assessment in paragraph B4.1.2B of IFRS 9 is written in the context of the objectives of IFRS 9 and is one of the key factors which determines the measurement basis for financial assets, the income and expenses recognised from financial assets and

whether those income and expenses are recognised in profit or loss or other comprehensive income.

51. Paragraph B4.1.2B of IFRS 9 explains that the business model is 'a matter of fact not merely an assertion' and is 'typically observable through the activities that the entity undertakes to achieve the objective of the business model'. It also explains that in exercising judgement the entity should consider 'all relevant evidence that is available at the date of the assessment' and provides examples of relevant evidence, including how managers of the business are compensated.

52. Given the limited role of the assessment of main business activities in the requirements for this [draft] Accounting Standard (see paragraph 28), to keep the requirements balanced the staff do not think that guidance of the level of detail in IFRS 9, including consideration of how managers of the business are compensated is appropriate. However, similar to the business model in IFRS 9, whether an entity invests in the course of main business activities or provides financing to customers as a main business activity should not be an assertion by management.

53. Therefore, the staff think that the IASB could enhance the guidance in paragraphs B27 and B29 of the Exposure Draft (see paragraph 48) by using the concept of 'observable' and clarifying that whether an entity invests in the course of main business activities or provides financing to customers as a main business activity should be observable through the operating performance which the entity communicates to users in public communications (see Agenda paper 21B of the November 2021 IASB meeting for discussions on public communications). This guidance would also be applied in judging whether the operating performance of an operating segment that is not a reportable segment is an important indicator of operating performance of the entity (see paragraph 46(b)). The operating performance of a reportable segment will be directly observable in the segment reporting note.

54. The Exposure Draft does not provide examples of operating performance of entities with specified main business activities. However, paragraph B78 of the Exposure Draft provides examples of specified subtotals similar to gross profit. Such subtotals represent the difference between a type of revenue and directly related expenses incurred in generating that revenue. The examples given are:

(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.

55. Entities that invest in the course of main business activities or provide financing to customers as a main business activity generally manage and communicate one or more of these specified subtotals similar to gross profit as a measure of operating performance. For example, if an entity provides financing to customers as a main business activity, it generally manages net interest margin and communicates 'net interest income' to users as a measure of operating performance. Conversely, if an entity provides financing to customers as a business activity, but the entity does not manage or communicate with users on net interest margin, then 'net interest income' is not an important indicator of its operating performance.

56. The staff recommend that the IASB provide additional application guidance clarifying that:

(a) the assessment of main business activities is not only a matter of judgement, but should also be observable through the operating performance communicated to users in public communications; and

(b) the specified subtotals similar to gross profit in paragraph B78 of the Exposure Draft are examples important indicators of operating performance for entities that invest in the course of main business activities or provide financing to customers as a main business activity.

Question for the IASB
Q1 Does the IASB agree with the staff recommendation to provide additional guidance on 'main business activities' by clarifying that: (a) the role of main business activities in the requirements of the Accounting Standard is limited; (b) if an entity has a reportable segment that constitutes a single business activity, that indicates that the business activity of the reportable segment is a main business activity of the entity; (c) if an entity has an operating segment that constitutes a single business activity, but it does not meet the requirements to be a reportable segment, that operating segment is not precluded from being a main business activity when the operating performance of the operating segment is an important indicator of operating performance of the entity; (d) the assessment of main business activities is not only a matter of judgement, but should also be observable through the operating performance communicated to users in public communications; and (e) the specified subtotals similar to gross profit in paragraph B78 of the Exposure Draft are examples of important indicators of operating performance for entities that invest in the course of main business activities or provide financing to customers as a main business activity.

Level for assessing main business activities

57. Some respondents and fieldwork participants raised concerns or asked for clarity about whether different main business activities could be identified in the consolidated financial statements of a group and the separate or consolidated financial statements of entities within the group (see paragraphs 11(b), 16–18).

Assessment of main business activities at the reporting entity level

58. The Exposure Draft does not contain specific guidance on the level at which to assess whether an entity or group invests in the course of main business activities or provides financing to customers as a main business activity. The following paragraphs in the Exposure Draft implicitly require the assessment to be performed at the level of the reporting entity preparing the consolidated and separate financial statements.

    (a) Paragraph 2 of the Exposure Draft which explains that the requirements of the [draft] IFRS Accounting Standard are to be applied by all entities in presenting and disclosing information in financial statements prepared applying IFRS Accounting Standards.

    (b) Paragraph 6 of the Exposure Draft which explains that the [draft] IFRS Accounting Standard is applied equally to all entities, including those that present consolidated financial statements and separate financial statements.

59. If the assessment of whether a group invests in the course of main business activities or provides financing to customers as a main business activity differs from the assessment by individual entities within the group, it would result in items of income and expenses being classified in different categories within the statements of profit or loss for the group and the individual entities within the group. However, if the important indicators of operating performance (see paragraph 54) differ between the group and individual entities within the group, then classification of income and expenses in different categories would be an appropriate outcome.

60. Similar issues about different outcomes in consolidated and separate financial statements arise in other IFRS Accounting Standards. The staff have considered:

    (a) segment reporting in IFRS 8 (paragraphs 61–65); and

    (b) accounting by a non-investment entity parent and an investment entity subsidiary in IFRS 10 *Consolidated Financial Statements* (paragraphs 66–69).

Segment reporting

61. In many instances reportable segments in the consolidated financial statements of a group would differ from reportable segments assessed at a lower level within the group. In practice, such cases are limited because:

(a) IFRS 8 limits the scope of its application – an entity or group is only required to disclose segment information when it has debt or equity instruments traded in a public market or it files, or is in the process of filing financial statements for the purpose of issuing instruments in a public market (paragraph 2 of IFRS 8); and

(b) segment information is not required for the separate financial statements of a parent that is required to present segment information in its consolidated financial statements if those separate financial statements are contained in the same financial report as the consolidated financial statements (paragraph 4 of IFRS 8).

62. The exemption in paragraph 61(b) was carried forward from IAS 14 *Segment Reporting* on practical grounds (paragraph BC21 of IFRS 8). However, there is no similar exemption when a group that is required to disclose segment information contains a subsidiary that is also required to disclose segment information. For example, when a parent and a subsidiary both have publicly traded debt or equity instruments. In such a case, the reportable segments at the group level and the subsidiary level may differ and this can result in similar practical issues to those raised by fieldwork participants about reclassifying information on consolidation (see paragraphs 17–18).

63. The Exposure Draft does not contain requirements for determining which entities are required to prepare financial statements and what financial statements entities are required to, or can elect to, prepare. Such requirements are contained in other IFRS Accounting Standards, for example paragraphs 4–4B of IFRS 10 determine the entities which are required to present consolidated financial statements.

64. As a result, the staff do not think that it would be appropriate to introduce similar exemptions to IFRS 8 as it would have a disproportionate outcome. Exempting a parent company from presenting the statement of profit or loss in the separate financial statements if those separate financial statements are presented in the same financial report as the consolidated financial statements would result in the separate financial statements being incomplete (paragraph 10 of the Exposure Draft).

65. The staff note that the proposed clarification in paragraph 46 that an operating segment is not precluded from being a main business activity, even if it does not meet the quantitative thresholds and aggregation criteria in IFRS 8 to be a reportable segment will to some extent address the practical concerns raised by fieldwork participants (see paragraphs 17–18) as the hurdle to being an operating segment is lower than the hurdle to being a reportable segment.

Non-investment entity parent and investment entity subsidiary

66. Paragraph 31 of IFRS 10 requires an investment entity to measure an investment in a subsidiary at fair value through profit or loss in accordance with IFRS 9 instead of consolidating it. Paragraph 33 of IFRS 10 does not permit a parent of an investment entity to carry through the consolidation exception in paragraph 31 for an investment entity subsidiary unless the parent is itself an investment entity. This results in:

   (a) the investment entity subsidiary measuring investments in subsidiaries at fair value in its financial statements; and

   (b) the non-investment entity parent consolidating the investments in subsidiaries of its investment entity subsidiary.

67. Paragraph BC276 of IFRS 10 explains that the majority of respondents to the Exposure Draft on investment entities disagreed with the proposal not to retain the investment entity's accounting in the financial statements of a non-investment entity parent as they think that fair value information is also relevant information at the non-investment entity parent level. However, the IASB decided to proceed with the requirement for various reasons, including the likelihood that a non-investment entity parent could otherwise achieve different accounting outcomes by holding subsidiaries directly or indirectly through an investment entity (paragraphs BC280 of IFRS 10).

68. Similarly, if the [draft] Accounting Standard were to permit a group to carry through the accounting from entities within the group, there is a risk that the category in the consolidated statement of profit or loss in which the income and expenses are classified would be driven by the legal structure of the business activity, rather than by whether the return on an investment or the difference between interest income and the related interest expense (see paragraph 48) is an important indicator of operating performance of the group.

69. Based on the analysis in paragraphs 58–68, the staff think that an approach similar to IFRS 10 is appropriate for entities with specified main business activities. Therefore, the staff recommend that the IASB:

    (a) clarify that the assessment of whether an entity invests in the course of main business activities or provides financing to customers as a main business activity is assessed at the reporting entity level; and

    (b) explain in the Basis for Conclusions that the outcome of that assessment may differ at the group level and at the level of individual entities within the group, and that such an outcome is expected.

Question for the IASB
Q2 Does the IASB agree with the staff recommendation to clarify that the assessment of whether an entity invests in the course of main business activities or provides financing to customers as a main business activity is assessed at the reporting entity level?

Restatement of comparatives

70. Some stakeholders asked for clarity on how an entity should identify when main business activities have changed and how to present those changes, in particular whether comparative figures would need to be restated to reflect changes in main business activities (see paragraph 11(c)).

71. As an entity is not required to identify all business activities and assess whether each activity constitutes a main business activity (see paragraph 28), the staff do not think that the IASB needs to develop indicators for an entity to identify when main business activities have changed.

72. Changes to main business activities will impact on the application of the [draft] IFRS Accounting Standard when an entity begins or ceases to invest in the course of main business activities or provides financing to customers as a main business activity. When such changes occur, in many cases an entity will apply the requirements of IFRS 3 and IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*,

respectively. However, there may be changes that are not within the scope of these IFRS Accounting Standards, for example, when providing financing to customers grows from being an ancillary business activity to a main business activity. To determine whether or not restatement should be required the staff considered the approaches taken in IFRS 8 for changes in reportable segments (see paragraph 73) and IFRS 9 for changes in business model (see paragraph 74).

73. IFRS 8 requires restatement of previously reported information if an entity changes the structure of its internal organisation in a manner that causes the composition of its reportable segments to change, unless the information is not available and the cost to develop it would be excessive. If the entity does not restate, it is required to disclose segment information for the current period on both the old and new basis of segmentation (paragraphs 29–30 of IFRS 8).

74. IFRS 9 requires reclassification of financial assets when an entity changes its business model for managing those assets. The reclassification is applied prospectively from the reclassification date because reclassification retrospectively would not reflect how the financial assets were managed in the prior reporting periods (paragraphs 4.4.1, 5.6.1 and BC4.118 of IFRS 9). Paragraphs 12B–12D of IFRS 7 *Financial Instruments: Disclosures* contain disclosure requirements for reclassifications.

75. The staff think that changes arising from a change in the assessment of whether an entity invests in the course of main business activities or provides financing to customers as a main business activity are akin to changes in the business model in IFRS 9, rather than changes in the way information is aggregated period-to-period for segment reporting. Hence, the staff think that the change in presentation of income and expenses arising from a change in the assessment of whether an entity invests in the course of main business activities or provides financing to customers as a main business activity should be applied prospectively in order to appropriately reflect the business activities as they were in the prior reporting period.

76. The staff recommend that the IASB clarify that a change in the assessment of whether an entity invests in the course of main business activities or provides financing to customers as a main business activity is applied prospectively and thus restatement of comparatives is not required. The staff will consider whether additional disclosures should be required when such changes occur in the next section on disclosures.

Question for the IASB
Q3 Does the IASB agree with the staff recommendation to clarify that a change in the assessment of whether an entity invests in the course of main business activities or provides financing to customers as a main business activity is applied prospectively and thus restatement of comparatives is not required?

Disclosures about changes in the assessment of main business activities

77. A few respondents said that the disclosure requirements proposed in the Exposure Draft related to main business activities and significant judgements would provide sufficient information about how an entity has identified its main business activities. However, some other respondents suggested strengthening the proposed disclosure requirements (see paragraphs 12–13).

78. Paragraph 99 of the Exposure Draft requires an entity to disclose a description of the entity's operations and its main business activities. There is no application guidance or illustrative examples which provide additional clarity on what should be included in this disclosure, in particular whether an entity is required to disclose when it changes its main business activities.

79. For most entities changes in its main business activities will not result in changes in classification in the statement of profit or loss. However, the classification in the statement of profit or loss will change from period to period when there are changes in the entity's assessment of whether it invests in the course of main business activities or provides financing to customers as a main business activity. The fact that such changes have occurred may provide material information to users. Hence, the staff recommend that the IASB require that when there has been a change in the assessment of whether an entity invests in the course of main business activities or provides financing to customers as a main business activity, the entity shall disclose that fact.

80. The staff think that the proposals in this paper in combination will help to reduce the significant judgements that fieldwork participants said was required to determine whether the entity invests in the course of main business activities or provides

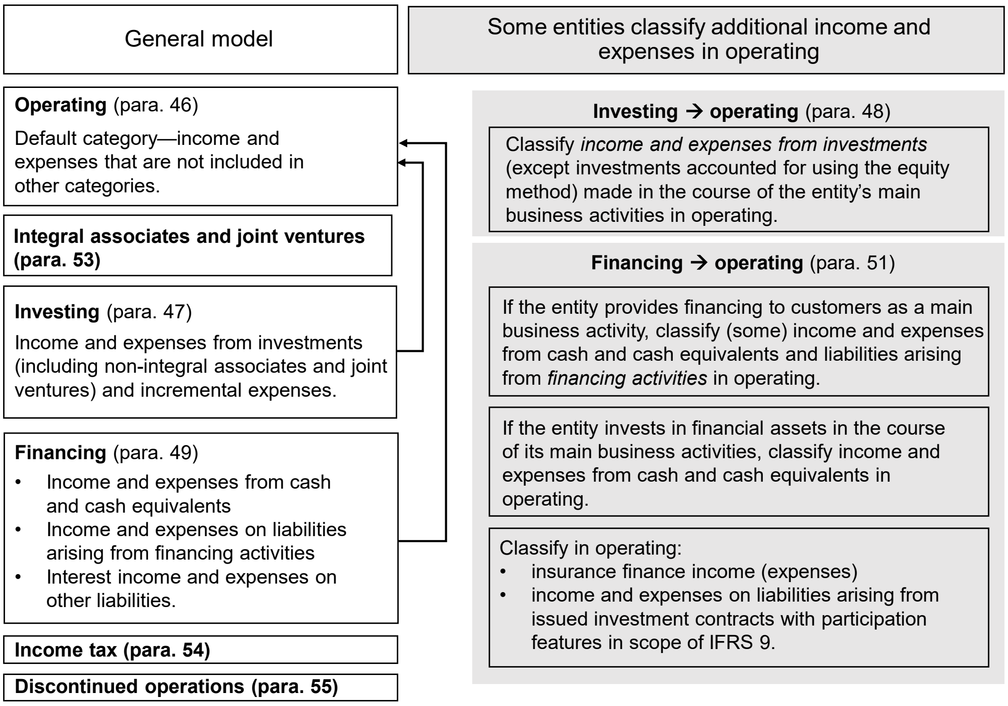
financing to customers as a main business activity (see paragraph 15). The staff expect that in many cases whether an entity invests in the course of main business activities or provides financing to customers as a main business activity to be a matter of fact. However, the staff acknowledge that there may still be some cases where significant judgement is required.

81. The staff do not think that introducing a specific disclosure requirement for judgements made in the assessment of an entity's main business activities is required. However, the staff will consider in a separate paper whether the IASB should clarify that the requirement to disclose information about significant judgements described in paragraph 12(b) includes significant judgements made in applying presentation and disclosure requirements.

Question for the IASB
Q4 Does the IASB agree with the staff recommendation to require that when there has been a change in the assessment of whether an entity invests in the course of main business activities or provides financing to customers as a main business activity, the entity shall disclose that fact?

Appendix A—Summary of the proposals for the structure of the statement of profit or loss

A1. The following figure summarises the requirements for classification of income and expenses into categories in the statement of profit or loss as proposed in paragraph B24 of the Exposure Draft.



Appendix B—Paragraphs from the Exposure Draft

B1. The paragraphs from the Exposure Draft are reproduced below.

2 [IAS 1.2] An entity shall apply this [draft] Standard in presenting and disclosing information in financial statements prepared applying IFRS Standards.

6 [IAS 1.4 partial] This [draft] Standard applies equally to all entities, including those that present consolidated financial statements in accordance with IFRS 10 *Consolidated Financial Statements* and those that present separate financial statements in accordance with IAS 27 *Separate Financial Statements*.

10 [IAS 1.10] A complete set of financial statements comprises:

(a) a statement(s) of financial performance for the reporting period (see paragraph 13);

(b) […]

48 An entity shall not classify in the investing category income and expenses specified in paragraphs 47(a)–47(b) generated in the course of its main business activities. Such income and expenses are instead classified in the operating category. An entity shall not classify income and expenses from non-integral associates and joint ventures in the operating category.

51 If an entity provides financing to customers as a main business activity, it shall make an accounting policy choice to not classify in the financing category either (see paragraphs B28–B29):

(a) income and expenses from financing activities, and from cash and cash equivalents, that relate to the provision of financing to customers; or

(b) all income and expenses from financing activities and all income and expenses from cash and cash equivalents.

Such income and expenses are instead classified in the operating category.

52 An entity also excludes the following income and expenses from the financing category and classifies them in the operating category:

(a) income and expenses from cash and cash equivalents if the entity, in the course of its main business activities, invests in financial assets that generate a return individually and largely independently of other resources held by the entity (see paragraph B30);

(b) income and expenses on liabilities arising from issued investment contracts with participation features recognised applying IFRS 9 *Financial Instruments*; and

(c) insurance finance income and expenses included in profit or loss applying IFRS 17 *Insurance Contracts*.

99 [IAS 1.138] An entity shall disclose in the notes the following, if not disclosed elsewhere in information published with the financial statements:

(a) […]

(b) a description of the nature of the entity's operations and its main business activities;

(c) […]

B27 Paragraph 48 requires an entity to classify in the operating category income and expenses from investments in the course of its main business activities. Whether income and expenses from investments arise in the course of an entity's main business activities is a matter of judgement. In general, investments are likely to have been made in the course of an entity's main business activity when investment returns are an important indicator of operating performance. Examples of entities that invest in the course of their main business activities may include:

(a) investment entities as defined by IFRS 10 *Consolidated Financial Statements*;

(b) investment property companies; and

(c) insurers.

B29 Whether an entity provides financing to customers as a main business activity is a matter of judgement. In general, providing financing to customers is likely to be a main business activity when the difference between interest income and the related interest expense is an important indicator of operating performance. Examples of entities that provide financing to customers as a main business activity may include:

(a) banks;

(b) entities that provide financing to customers to enable those customers to purchase the entity's products; and

(c) lessors that provide finance leases to customers.

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.

IAS 8.27E [IAS 1.122] An entity shall disclose in the notes, along with its significant accounting policies or other notes, the judgements, apart from those involving estimations (see paragraph ~~125~~31A), that management has made in the process of applying the entity's accounting policies and that have the most significant effect on the amounts recognised in the financial statements.

Appendix C – Paragraphs from IFRS Accounting Standards

C1. The paragraphs from IFRS 3 are reproduced below.

Appendix A definition of a business

An integrated set of activities and assets that is capable of being conducted and managed for the purpose of providing goods or services to customers, generating investment income (such as dividends or interest) or generating other income from ordinary activities.

B7 A business consists of inputs and processes applied to those inputs that have the ability to contribute to the creation of outputs. The three elements of a business are defined as follows (see paragraphs B8–B12D for guidance on the elements of a business):

(a) […]

(b) […]

(c) Output: The result of inputs and processes applied to those inputs that provide goods or services to customers, generate investment income (such as dividends or interest) or generate other income from ordinary activities.

BC21S In the 2018 Amendments, […]. The Board also amended the definition of a business to make it consistent with the narrowed definition of outputs. The Board made these changes because:

(a) IFRS 15 *Revenue from Contracts with Customers* focuses on goods or services that are an output of an entity's ordinary activities. Nevertheless, because not all businesses have revenue within the scope of IFRS 15, the revised definition also includes outputs that are investment income or other income from ordinary activities.

(b) […]

C2. The paragraphs from IFRS 8 are reproduced below.

2 This IFRS shall apply to:

(a) the separate or individual financial statements of an entity:

(i) whose debt or equity instruments are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets), or

(ii) that files, or is in the process of filing, its financial statements with a securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market; and

(b) the consolidated financial statements of a group with a parent:

(i) whose debt or equity instruments are traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets), or

(ii) that files, or is in the process of filing, the consolidated financial statements with a securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market.

4 If a financial report contains both the consolidated financial statements of a parent that is within the scope of this IFRS as well as the parent's separate financial statements, segment information is required only in the consolidated financial statements.

22 An entity shall disclose the following general information:

(a) factors used to identify the entity's reportable segments, including the basis of organisation (for example, whether management has chosen to organise the entity around differences in products and services, geographical areas, regulatory environments, or a combination of factors and whether operating segments have been aggregated);

(aa) the judgements made by management in applying the aggregation criteria in paragraph 12. This includes a brief description of the operating segments that have been aggregated in this way and the economic indicators that have been assessed in determining that the aggregated operating segments share similar economic characteristics; and

(b) types of products and services from which each reportable segment derives its revenues.

29 If an entity changes the structure of its internal organisation in a manner that causes the composition of its reportable segments to change, the corresponding information for earlier periods, including interim periods, shall be restated unless the information is not available and the cost to develop it would be excessive. The determination of whether the information is not available and the cost to develop it would be excessive shall be made for each individual item of disclosure. Following a change in the composition of its reportable segments, an entity shall disclose whether it has restated the corresponding items of segment information for earlier periods.

30 If an entity has changed the structure of its internal organisation in a manner that causes the composition of its reportable segments to change and if segment information for earlier periods, including interim periods, is not restated to reflect the change, the entity shall disclose in the year in which the change occurs segment information for the current period on both the old basis and the new basis of segmentation, unless the necessary information is not available and the cost to develop it would be excessive.

C3. The paragraphs from IFRS 9 are reproduced below.

4.4.1 When, and only when, an entity changes its business model for managing financial assets it shall reclassify all affected financial assets in accordance with paragraphs 4.1.1–4.1.4. See paragraphs 5.6.1–5.6.7, B4.4.1–B4.4.3 and B5.6.1–B5.6.2 for additional guidance on reclassifying financial assets.

5.6.1 If an entity reclassifies financial assets in accordance with paragraph 4.4.1, it shall apply the reclassification prospectively from the reclassification date. The entity shall not restate any previously recognised gains, losses (including impairment gains or losses) or interest. Paragraphs 5.6.2–5.6.7 set out the requirements for reclassifications.

BC4.118 The IASB considered how reclassifications should be accounted for. Almost all respondents said that reclassifications should be accounted for prospectively and should be accompanied by robust disclosures. The IASB reasoned that if classification and reclassification are based on the business model within which they are managed, classification should always reflect the business model within which the financial asset was managed at the reporting date. To apply the reclassification retrospectively would not reflect how the financial assets were managed at the prior reporting dates.

B4.1.2B An entity's business model for managing financial assets is a matter of fact and not merely an assertion. It is typically observable through the activities that the entity undertakes to achieve the objective of the business model. An entity will need to use judgement when it assesses its business model for managing financial assets and that assessment is not determined by a single factor or activity. Instead, the entity must consider all relevant evidence that is available at the date of the assessment. Such relevant evidence includes, but is not limited to:

(a) how the performance of the business model and the financial assets held within that business model are evaluated and reported to the entity's key management personnel;

(b) the risks that affect the performance of the business model (and the financial assets held within that business model) and, in particular, the way in which those risks are managed; and

(c) how managers of the business are compensated (for example, whether the compensation is based on the fair value of the assets managed or on the contractual cash flows collected).

C4. The paragraphs from IFRS 10 are reproduced below.

31 Except as described in paragraph 32, an investment entity shall not consolidate its subsidiaries or apply IFRS 3 when it obtains control of another entity. Instead, an investment entity shall measure an investment in a subsidiary at fair value through profit or loss in accordance with IFRS 9.1

33 A parent of an investment entity shall consolidate all entities that it controls, including those controlled through an investment entity subsidiary, unless the parent itself is an investment entity.

BC276 The Board noted that the majority of respondents disagreed with the proposal, arguing that if fair value information is more relevant than consolidation at an investment entity subsidiary level, it is also more relevant information at the non-investment entity parent level.

BC280 The Board was concerned that some of these changes would increase the likelihood that a non-investment entity parent could achieve different accounting outcomes by holding subsidiaries directly or indirectly through an investment entity. The Board noted that, for example, a non-investment entity parent may elect to hold subsidiaries through an investment entity subsidiary in order to hide leverage or loss-making activities.

C5. The paragraphs from IFRS 15 are reproduced below.

BC247 The boards noted that some entities (for example, banks and other entities with similar types of operations) regularly enter into financing transactions and, therefore, interest represents income arising from ordinary activities for those entities. The boards noted that the requirements in paragraph 65 of IFRS 15 do not preclude an entity from presenting interest as a type of revenue in circumstances in which the interest represents income from the entity's ordinary activities.

C6. The paragraphs from IAS 7 are reproduced below.

> **6** The following terms are used in this Standard with the meanings specified:
>
> […]
>
> *Operating activities* are the principal revenue-producing activities of the entity and other activities that are not investing or financing activities.

C7. The paragraphs from the *Conceptual Framework for Financial Reporting* are reproduced below.

> **BC0.32** The concept of business activities is discussed in the 2018 Conceptual Framework to assist the Board in developing Standards. In a particular Standard, the concept of business activities can be further explained and developed. The discussion of business model in IFRS 9 Financial Instruments is one example of how the Board has applied the concept of business activities.