Staff paper

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IFRS® Interpretations Committee meeting

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Project	**Management-defined Performance Measures—Gross profit measures (IFRS 18)**
Topic	**Initial consideration**
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Introduction

1. The IFRS Interpretations Committee (Committee) received two submissions asking whether a particular subtotal of income and expenses is similar to gross profit as described in IFRS 18 *Presentation and Disclosure in Financial Statements* and is consequently not a management-defined performance measure (MPM).

2. The objective of this paper is:

   (a) to provide the Committee with a summary of the matter;

   (b) to present our research and analysis; and

   (c) to ask the Committee whether it agrees with our conclusion that a standard-setting project is not needed to address the question and with our recommendation to publish a tentative agenda decision.

Structure

3. This paper includes:

   (a) background and summary of the matter (paragraphs 5–16);

(b) staff analysis (paragraphs 17–45); and

(c) staff conclusion and recommendation (paragraphs 46–47).

4. There are two appendices to this paper:

(a) Appendix A—suggested wording of the tentative agenda decision; and

(b) Appendix B—the submissions.

Background and summary of the matter

Applicable requirements

5. Paragraph 117 of IFRS 18 contains the definition of an MPM:

> A management-defined performance measure is a subtotal of income and expenses that (see paragraphs B113–B122):
>
> (a) an entity uses in public communications outside financial statements;
>
> (b) an entity uses to communicate to users of financial statements management's view of an aspect of the financial performance of the entity as a whole; and
>
> (c) is not listed in paragraph 118, or specifically required to be presented or disclosed by IFRS Accounting Standards.

6. Paragraph 118 says 'Subtotals of income and expenses that are not management-defined performance measures are: (a) gross profit or loss (revenue minus cost of sales) and similar subtotals (see paragraph B123)…'

7. Paragraph B123 says:

> In accordance with paragraph 118(a), subtotals similar to gross profit are not management-defined performance measures. A

subtotal is similar to gross profit when it depicts 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 income and expenses); and

(e) net rental income.

Summary of the matter

8. Paragraph 117(c) and related paragraphs of IFRS 18 exclude from the scope of MPMs, amongst other things: (a) subtotals of income and expenses specifically required to be presented or disclosed by IFRS Accounting Standards; and (b) gross profit or loss (revenue minus cost of sales) and similar subtotals of income and expenses.

9. The submissions (labelled as submission A and submission B in Appendix B) describe a subtotal of income and expenses, 'total revenues', which the submissions say is commonly used by banks. The submissions say that total revenues:

   (a) is used by a bank in its public communications outside financial statements;

   (b) is not a subtotal of income and expenses that is specifically required to be presented or disclosed by IFRS Accounting Standards; and

   (c) is not one of the subtotals that is listed in paragraphs 118(b)–118(f) of IFRS 18.

10. The submissions say total revenues depicts revenues from the bank's main business activities and directly related expenses, including interest from lending and

borrowing, fees from advisory work and fair value gains and losses from trading and managing positions on a fair value basis. Total revenues typically consists of three components:

(a) net interest income;

(b) net fee and commission income; and

(c) net income on financial instruments measured at fair value through profit or loss[1], which consists of:

(i) fair value gains and losses from measuring financial instruments that are both mandatorily at fair value and designated at fair value; and

(ii) directly associated transaction costs.

11. The submissions highlight other items that some banks include in their measure of total revenues such as ‘net gains or losses recognised on derecognition of debt instruments measured at fair value through other comprehensive income’, ‘net gains or losses recognised on debt instruments measured at amortised cost’ and residual or balancing ‘other income’, which might, amongst other things, aggregate some of these former items if they are not material.

12. Both submissions say that ‘other income’ is immaterial and therefore we have focused our analysis of the total revenues subtotal of income and expenses on the understanding set out in paragraph 10.

13. The submissions ask (directly or indirectly) whether total revenues, which would otherwise meet the definition of an MPM, is not an MPM because of the requirement in paragraph 117(c) of IFRS 18.

14. Submission A notes two of the components of total revenues described in paragraph 10—net interest income and net fee and commission income—are listed in paragraph

[1] One submission says this is commonly referred to as ‘Net trading income’.

B123 of IFRS 18 as examples of subtotals of income and expenses that are similar to gross profit. The submission specifically asks whether:

(a) the third component of total revenue—that is, net income on financial instruments measured at fair value through profit or loss (see paragraph 10(c)) is similar to gross profit as described in paragraph B123 of IFRS 18 (Question 1); and

(b) a subtotal that combines the three components described in paragraph 10 is not an MPM because:

  (i) an aggregation of subtotals similar to gross profit—which is what submission A says total revenues would be if the answer to Question 1 is yes—is also similar to gross profit as described in paragraph B123 of IFRS 18 (Question 2).

  (ii) an aggregation of subtotals that are not MPMs for different reasons does not meet the criterion in paragraph 117(c) of IFRS 18 and is therefore not an MPM (Question 3). In particular, submission A says if the answer to Question 1 is no, then total revenues is comprised of two subtotals that are similar to gross profit (net interest income and net fee and commission income) and a line item (net income on financial instruments measured at fair value through profit or loss) that the submission says is required by IFRS 7 *Financial Instruments: Disclosures*.

15. Both submissions say that there might be practical challenges for entities disclosing the information about MPMs required by IFRS 18 if total revenues is considered to be an MPM. The submissions also question whether the resulting information would be useful. For example, the submissions say there would be challenges in identifying the most directly comparable subtotal (paragraph 123(c) of IFRS 18). Submission B says that if the Committee concludes total revenues is an MPM, it should clarify what the most directly comparable subtotal to total revenues would be.

16. Appendix B reproduces the submissions, which provide further background about the questions and the different views identified by the submitters.

Staff analysis

Criteria for a standard-setting project

17. Paragraph 5.19 of the IFRS Foundation *Due Process Handbook* (*Handbook*) states that the Committee assesses the need for a standard-setting project based on whether:

    (a) the matter has widespread effect—that is:

        (i) the circumstance or transaction is prevalent, or is expected to be prevalent; and

        (ii) there is diversity, or expected diversity, in the application of IFRS Accounting Standards that has, or is expected to have, a material effect on those affected;

    (b) it is necessary to add or change requirements in IFRS Accounting Standards to improve financial reporting—that is, the principles and requirements in IFRS Accounting Standards do not provide an adequate basis for an entity to determine the required accounting;

    (c) the matter can be resolved efficiently within the confines of the existing Standards and the *Conceptual Framework for Financial Reporting*; and

    (d) the matter is sufficiently narrow in scope that the International Accounting Standards Board (IASB) or the Committee can address it efficiently, but not so narrow that it is not cost-effective for the IASB or the Committee and stakeholders to undertake the due process required to amend an IFRS Accounting Standard.

Does the matter have widespread effect? (paragraph 5.19(a))

18. The purpose of any information request we send to stakeholders is to understand whether a submission meets the criterion in paragraph 5.19(a) of the *Handbook*—that is, whether the matter set out in the submission has widespread effect. We consider:

    (a) the prevalence, or expected prevalence, of the transaction or fact pattern submitted; and

    (b) whether there is diversity, or expected diversity, in the application of IFRS Accounting Standards to that transaction or fact pattern that has, or is expected to have, a material effect on those affected.

19. We did not send an information request related to these submissions for the following reasons:

    (a) most entities are in the process of applying—but have not yet applied—IFRS 18. Accordingly, stakeholders would be unable to comment on the existence of diversity in the application of the applicable requirements.

    (b) the submitters provided us with evidence of reporting practices of banks in various jurisdictions using subtotals similar to total revenue.

    (c) we have had informal feedback from some stakeholders (including, for example, regulators, national standard-setters, large accounting firms and preparers) that confirmed the widespread effect of the question. Those stakeholders informed us of discussions they have had on similar questions, and these conversations confirmed that stakeholders understand the applicable requirements differently.

20. In our view, the evidence gathered indicates the matter could have widespread effect because:

    (a) subtotals similar to total revenues are being used by many banks.

(b) differences in applying the requirements could result in diversity in whether an entity discloses the information about MPMs required by IFRS 18 for these subtotals.

21. In our view, the criterion set out in paragraph 5.19(a) of the *Handbook* is met for this matter. Therefore, we have proceeded to analyse the question submitted.

Is it necessary to add to or change the Standards? (paragraph 5.19(b))

22. In this section we first analyse some aspects of how an entity considers the applicable requirements more generally (paragraphs 23–35); and then assess how the entity described in the submissions applies the applicable requirements to the total revenues subtotal discussed in the submissions (paragraphs 36–41).

How to consider the applicable requirements

23. Paragraphs 5–7 summarise the applicable requirements. An entity assesses whether a subtotal of income and expenses meets the criterion of the definition of an MPM in paragraph 117(c) of IFRS 18 separately for each subtotal of income and expenses. Therefore, in the context of the submission, an entity would consider whether total revenues—the subtotal of income and expenses used in public communications outside financial statements—is a subtotal similar to gross profit.

24. We consider below:

(a) how an entity assesses whether a subtotal is similar to gross profit (paragraphs 25–30);

(b) whether and how to consider components of a subtotal (paragraphs 31–32); and

(c) commonly used subtotals other than those listed in paragraph 118 of IFRS 18 (paragraphs 33–35).

Assessing whether a subtotal is similar to gross profit

25. This section sets out some general considerations an entity would apply when assessing whether a subtotal of income and expenses (for example, total revenues) is similar to gross profit.

26. Paragraph B123 of IFRS 18 (reproduced in paragraph 7):

    (a) describes subtotals of income and expenses that are similar to gross profit. It says a subtotal is similar to gross profit if 'it depicts the difference between a type of revenue and directly related expenses incurred in generating that revenue'.

    (b) provides examples of subtotals of income and expenses that meet the description of subtotals similar to gross profit in paragraph B123.

27. An entity considers whether a subtotal of income and expenses is similar to gross profit by considering whether that subtotal meets the description in paragraph B123 of IFRS 18 of subtotals of income and expenses that are similar to gross profit. In doing so, an entity assesses whether:

    (a) revenue included in that subtotal is 'a type of revenue'; and

    (b) that subtotal includes directly related expenses incurred in generating that revenue.

28. Submission A notes that some view a subtotal that aggregates different components to be reflective of multiple revenue streams and therefore not 'a type of revenue'. IFRS 18 does not define or describe 'type of revenue'. We see no basis to restrict the reading of 'type of revenue' to only one particular revenue stream and think 'a type of revenue' could include revenue from multiple revenue streams as long as the combined revenue stream represents a type of revenue. For example, net interest income, an example of a subtotal similar to gross profit listed in paragraph B123 of IFRS 18, could include revenue from different revenue streams such as retail, commercial and investment banking revenue streams.

29. Additionally, we think the examples in paragraph B123 of IFRS 18 should not be read as an exhaustive list of subtotals that are similar to gross profit. The list in paragraph B123 is a list of examples.

30. One of the examples in paragraph B123 of IFRS 18, net financial result (investment income minus insurance finance income and expenses), might include gains and losses from measuring financial instruments at fair value. Therefore, we think including gains and losses from measuring financial instruments at fair value in a subtotal of income and expenses does not prevent that subtotal from being similar to gross profit.

Considering components of a subtotal

31. Questions 2 and 3 in submission A ask about a subtotal of income and expenses that aggregates components:

    (a) Question 2 asks whether a subtotal of income and expenses that is an aggregation of different components that are individually similar to gross profit is consequently also similar to gross profit. We think that in assessing whether a particular subtotal is similar to gross profit, an entity would consider whether *that subtotal* meets the description in paragraph B123 of IFRS 18 of subtotals of income and expenses that are similar to gross profit (see paragraph 27). While adding up a number of subtotals similar to gross profit could also be similar to gross profit, we think an entity is required to assess whether the aggregated subtotal it is assessing is similar to gross profit (see paragraphs 25–29).

    (b) Question 3 asks whether a subtotal of income and expenses would be an MPM if the subtotal aggregates component parts that individually would not be considered an MPM for different reasons listed in paragraph 117(c) of IFRS 18.

32. As noted in paragraph 23, we think an entity considers each subtotal separately. Therefore, for both questions 2 and 3, an entity would consider whether the subtotal it

is assessing (total revenues in the context of the submission) meets the criteria in paragraph 117(c). In our view, whether the subtotal is a sum of component subtotals that individually would not be MPMs for different reasons listed in paragraph 117(c) of IFRS 18 is irrelevant to this assessment. The entity would assess whether the aggregated subtotal is similar to gross profit or required by another IFRS Accounting Standard.

Commonly used subtotals other than those listed in paragraph 118

33. In discussing the questions and the different views, both the submissions highlight paragraph BC362 of the Basis for Conclusions on IFRS 18:

> The IASB decided subtotals listed in paragraph 118 of IFRS 18 or specifically required to be disclosed by IFRS Accounting Standards are not management-defined performance measures. Some subtotals are not defined by IFRS Accounting Standards, but are commonly used in financial statements and are well understood by users of financial statements—for example, a gross profit subtotal. In the IASB's view, providing the management-defined performance measures disclosures for such measures would not provide useful information because their purpose and relationship to totals or subtotals defined by IFRS Accounting Standards are well understood or would usually be apparent from their presentation in the statement(s) of financial performance…

34. The submissions say some consider the reasoning described in paragraph BC362 (related to subtotals that are commonly used in financial statements) as justification for not considering as an MPM an aggregation of subtotals of income and expenses that are not themselves MPMs.

35. In our view, the basis for conclusions on an IFRS Accounting Standard explains why the IASB developed a specific requirement. However, the basis for conclusions

contains no requirements on how an entity applies an IFRS Accounting Standard. Therefore, in assessing whether a subtotal is similar to gross profit, an entity considers only the requirements in paragraph 117 and related paragraphs of IFRS 18. Whether that subtotal is commonly used is irrelevant to that assessment.

Analysis of fact pattern in the submission

36. Submission B asks directly whether total revenues is a subtotal similar to gross profit and consequently not an MPM. Question 1 of submission A asks whether 'net income on financial instruments measured at fair value through profit or loss' is a subtotal that is similar to gross profit but does so in the context of assessing whether total revenues is not an MPM. As noted in paragraph 23, we think an entity assesses each subtotal of income and expenses separately. Our analysis therefore focuses on total revenues as described in paragraph 10—which is the subtotal used in public communications outside financial statements. We have not separately analysed whether 'net income on financial instruments measured at fair value through profit or loss' is a subtotal that is similar to gross profit.

37. Paragraph 117(c)—reproduced in paragraph 5—says an MPM is a subtotal of income and expenses that 'is not listed in paragraph 118 or specifically required to be presented or disclosed by IFRS Accounting Standards'.

38. We understand from the submitters that total revenues is a subtotal of income and expenses that is:

    (a) not specifically required to be presented or disclosed by IFRS Accounting Standards; and

    (b) not one of the subtotals that is listed in paragraphs 118(b)–118(f) of IFRS 18.

39. Therefore, in assessing whether total revenues meets the requirement in paragraph 117(c), the entity considers whether total revenues is a subtotal listed in paragraph 118(a) of IFRS 18—that is, whether it is a subtotal that is similar to gross profit.

40. As paragraphs 25–29 note, the entity assesses whether a subtotal of income and expenses like total revenues is similar to gross profit by considering whether it depicts 'the difference between a type of revenue and directly related expenses incurred in generating that revenue'.

41. As noted in paragraph 10, from the submissions, we understand total revenues depicts the difference between total revenues from a bank's main business activities—in our view, an example of a type of revenue—and directly related expenses incurred in generating that revenue. Because total revenues is a subtotal of income and expenses that depicts the difference between 'a type of revenue' and directly related expenses incurred in generating that revenue, in our view, total revenues is similar to gross profit and is therefore not an MPM applying paragraph 117 of IFRS 18.

Conclusion

42. Based on our analysis in paragraphs 22–41, we think:

(a) an entity analyses each subtotal of income and expenses used in public communications outside financial statements separately. Therefore, the analysis of whether a subtotal meets the criteria in paragraph 117 of IFRS 18 is done for each subtotal, regardless of the components of that subtotal.

(b) in assessing whether a subtotal is similar to gross profit, an entity assesses whether that subtotal 'depicts the difference between a type of revenue and directly related expenses incurred in generating that revenue'.

(c) the examples of subtotals similar to gross profit in paragraph B123 of IFRS 18 are examples and not an exhaustive list.

(d) a subtotal that depicts the difference between revenue from an entity's main business activities—in our view, an example of a type of revenue—and directly related expenses incurred in generating that revenue is a subtotal similar to gross profit and therefore not an MPM.

43. We have not analysed questions about the application of the MPM requirements to total revenues (see paragraph 15) because of our conclusion in paragraph 42(d).

Question 1 for the Committee
1. Does the Committee agree with our analysis of the application of the requirements in IFRS 18 summarised in paragraph 42 of this paper?

Is the criterion in paragraph 5.19(b) met?

44. Based on our analysis in paragraphs 22–41, and as summarised in paragraph 42, we think the principles and requirements in IFRS 18 provide an adequate basis for an entity to determine whether a subtotal of income and expenses is similar to gross profit as described in IFRS 18.

45. Accordingly, we conclude that the criterion in paragraph 5.19(b) of the *Handbook* is not met. Therefore, in accordance with paragraph 5.22 of the *Handbook*, a standard-setting project is not needed to address the question submitted.

Staff conclusion and recommendation

46. Based on our assessment of the criteria in paragraph 5.19 of the *Handbook*, we recommend that the Committee publish a tentative agenda decision explaining its decision that a standard-setting project is not needed. In accordance with paragraphs 8.2–8.3 of the *Handbook*, we also recommend that the tentative agenda decision explains how an entity determines whether a subtotal is similar to gross profit as described in IFRS 18.

47. Appendix A sets out the suggested wording of the tentative agenda decision. In our view, the suggested tentative agenda decision (including the explanatory material

contained within it) would not add or change requirements in IFRS Accounting Standards.[2]

Questions for the Committee

Questions 2 and 3 for the Committee
2. Does the Committee agree with our conclusion that the criterion in paragraph 5.19(b) of the *Handbook* is not met and, consequently, there is no need for a standard-setting project? 3. Does the Committee have any comments on the suggested wording of the tentative agenda decision in Appendix A?

[2] Paragraph 8.4 of the *Due Process Handbook* states: 'Agenda decisions (including any explanatory material contained within them) cannot add or change requirements in IFRS Accounting Standards. Instead, explanatory material explains how the applicable principles and requirements in IFRS Accounting Standards apply to the transaction or fact pattern described in the agenda decision.'

Appendix A—Suggested wording of the tentative agenda decision

This appendix sets out the suggested wording of the tentative agenda decision. Paragraph numbers are included to facilitate referencing but will be removed when the tentative agenda decision is published in IFRIC *Update*.

Management-defined Performance Measures—Gross profit measures (IFRS 18 *Presentation and Disclosure in Financial Statements*)

A1. The Committee received requests about whether a particular subtotal of income and expenses is similar to gross profit as described in IFRS 18 *Presentation and Disclosure in Financial Statements* and is consequently not a management-defined performance measure.

Fact pattern

A2. The requests described a subtotal of income and expenses—total revenues—that an entity (a bank) uses in public communications outside financial statements to communicate management's view of an aspect of the financial performance of the entity as a whole.

A3. The requests explained that total revenues depicts revenues from the bank's main business activities and directly related expenses. Total revenues consists of three components:

(a) net interest income;

(b) net fee and commission income; and

(c) net income on financial instruments measured at fair value through profit or loss.

A4. The requests noted that total revenues would otherwise meet the definition of a management-defined performance measure but asked whether total revenues is similar to gross profit. If a subtotal of income and expenses is similar to gross profit it is not a management-defined performance measure.

Applicable requirements

A5. Paragraph 117(c) of IFRS 18 explains that a subtotal of income and expenses is not a management-defined performance measure if it is listed in paragraph 118 of IFRS 18 or specifically required to be presented or disclosed by IFRS Accounting Standards.

A6. Paragraph 118 says that 'Subtotals of income and expenses that are not management-defined performance measures are: (a) gross profit or loss (revenue minus cost of sales) and similar subtotals (see paragraph B123)…'

A7. Paragraph B123 says that 'a subtotal is similar to gross profit when it depicts 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…'

Applying the requirements in IFRS 18

A8. The Committee observed that an entity assesses each subtotal of income and expenses used in public communications outside financial statements separately. Therefore, the analysis of whether a subtotal of income and expenses meets the criteria in paragraph 117 of IFRS 18 is done for each subtotal, regardless of the components of that subtotal.

A9. In assessing whether a subtotal is similar to gross profit, an entity assesses whether that subtotal 'depicts the difference between a type of revenue and directly related expenses incurred in generating that revenue' (paragraph B123 of IFRS 18). The Committee observed that the examples in paragraph B123 are not an exhaustive list of subtotals that are similar to gross profit.

A10. The Committee noted that a subtotal that depicts the difference between revenue from an entity's main business activities—an example of a type of revenue—and directly related expenses incurred in generating that revenue is a subtotal similar to gross profit and therefore not a management-defined performance measure.

Conclusion

A11. The Committee concluded that the principles and requirements in IFRS 18 provide an adequate basis for an entity to determine whether a subtotal is similar to gross profit. Consequently, the Committee [decided] that a standard-setting project is not needed to address the request.

Appendix B—Submissions

B1. We have reproduced the submissions below.

Submission A

Management-defined Performance Measures (MPMs): interpretation under IFRS 18, *Presentation and Disclosure in Financial Statements*

Dear Mr Mackenzie,

We appreciate the opportunity to submit a potential agenda item to the IFRS Interpretations Committee (the IFRS IC) regarding certain interpretations of the requirements in IFRS 18, *Presentation and Disclosure in Financial Statements* (IFRS 18) and the potential impact on financial reporting of banks when they prepare their financial statements under IFRS Accounting Standards.

The issue

Our specific concern relates to the inclusion of certain line items, notably "Net income on financial instruments measured at fair value through profit or loss"[3] within subtotals presented in the income statements of banks and whether that inclusion should result in those subtotals being treated as management defined-performance measures (MPMs).

For illustration purposes, we refer to "Total revenues", a commonly presented subtotal in the income statements of many banks (although naming may differ), irrespective of whether they report under IFRS Accounting Standards. "Total revenues" depicts revenues from a bank's main business activities, alongside directly related expenses, including interest from lending and borrowing, fees from advisory work and fair value gains and losses from trading and managing positions on a fair value basis. Generally, the composition of this subtotal is as illustrated below.

[3] It is noted that the naming among banks may differ, but essentially "Net income on financial instruments measured at fair value through profit or loss" represents a line item in the income statements that includes gains and losses on financial instruments measured at fair value through profit or loss, which are required to be presented or disclosed by IFRS 7, *Financial Instruments: Disclosures* (IFRS 7.20(a)(i)).

Income statement
Interest income from financial instruments measured at amortized cost and fair value through other comprehensive income
Interest expense from financial instruments measured at amortized cost
Net interest income from financial instruments measured at fair value through profit or loss and other
Net interest income
Fee and commission income
Fee and commission expense
Net fee and commission income
Net income on financial instruments measured at fair value through profit or loss
Other income[4]
Total revenues

As the adoption date of IFRS 18 approaches, we have become increasingly concerned by recent discussions among certain regulators and accounting firms that emphasize a strict reading of IFRS 18.117 and IFRS 18.B123 when determining whether a subtotal of income and expenses should be considered as an MPM and when it is deemed similar to gross profit. More specifically, we understand that certain regulators and accounting firms interpret IFRS 18.117, IFRS 18.118 and IFRS 18.B123 as requiring that a bank's "Total revenues", as detailed above, be considered an MPM.

Our understanding is that it would generally be considered acceptable and within a reasonable interpretation of the accounting requirements to aggregate measures already included in IFRS 18.B123 (i.e. "Net interest income" and "Net fee and commission income") and consider the resulting subtotal as not being an MPM. However, we understand, as part of the aforementioned discussions, that challenges are being raised as to whether it would be possible to reach the same conclusion if, in addition to "Net interest income" and "Net fee and commission income", the subtotal also included "Net income on financial instruments measured at fair value through profit or loss", which includes fair value gains and losses from measuring financial instruments that are both mandatorily at fair value and designated at fair value. It is important to note that although the initial determination of why an instrument is fair valued through profit or loss may differ depending on the product and its characteristics (e.g. considering the business model, whether the cash flows are solely payments of principal

[4] Other income is assumed to be immaterial for the purposes of this analysis and is therefore not considered further.

and interest, etc.), once the instrument is subject to fair value measurement, the nature of the revenue generated from those products is consistent, representing fair value gains and losses from measuring the products at fair value in line with principles in IFRS 13, *Fair Value Measurement*.

The challenge stems from several arguments that have been raised during those discussions, particularly the fact that "Net income on financial instruments measured at fair value through profit or loss" is not similar to gross profit, as it is not listed as an example in IFRS 18.B123, is not considered to represent a difference between a type of revenue and directly related expenses incurred in generating that revenue, and represents a line item rather than a subtotal. This is despite the fact that fair value gains and losses from measuring financial instruments at fair value reflect a core activity of the banking industry and are a required disclosure under IFRS 7.20.

We therefore seek clarifications from the IFRS IC on the questions set out in the section *Questions and views* below. Those questions are raised on the assumption that "Total revenues" is used in communications outside of the financial statements to communicate management's view of an aspect of the performance of the entity as a whole to users.

Questions and views

Question 1: Is *"Net income on financial instruments measured at fair value through profit or loss"* similar to gross profit as referred to in IFRS 18.B123?

View 1

Yes – "Net income on financial instruments measured at fair value through profit or loss" is similar to gross profit.

Proponents of View 1 would note the following.

- IFRS 18.B123 refers to "Net interest income" and "Net fee and commission income" as examples of subtotals that are similar to gross profit and therefore not MPMs. The list is non-exhaustive and therefore can include "Net income on financial instruments measured at fair value through profit or loss".

- ''Net income on financial instruments measured at fair value through profit or loss'' is a simple aggregation of revenue and expenses arising from a specific category of financial instruments that are fair valued through the profit or loss, either mandatorily or through designation.

- ''Net income on financial instruments measured at fair value through profit or loss'' is also similar to gross profit as it depicts the difference between *a type of revenue* and *directly related expenses* incurred in generating that revenue' (*emphasis added*) as set out in IFRS 18. B123, with revenue including all fair value gains and losses arising from measuring fair value (on initial recognition and during the holding period) in line with the consistent fair value principles set out in IFRS 9 and IFRS 13, which are equally applicable to all financial instruments that are mandatorily measured at fair value or designated at fair value, alongside directly associated transaction costs, irrespective of the underlying products and the driver behind the fair value determination (e.g. business model, product characteristics, etc.).

They also note that judgement is required when interpreting the notion of "a type of revenue", with revenue not confined to a single product but can be applicable to revenues generated from a specific category of financial instruments that are consistently measured at fair value through profit or loss and therefore the nature of the revenues is the same. They highlight other examples in IFRS 18 that are deemed similar to gross profit yet appear to combine revenues of a different nature as further support for this view, e.g. "net financial result (investment income minus insurance finance income and expenses)" in IFRS 18.B123(d), further discussed in IFRS 18.E12, that includes "Investment income", "Credit impairment losses" and "Insurance finance expenses".

Furthermore, in assessing whether expenses included in "Net income on financial instruments measured at fair value through profit or loss" are 'directly related expenses', it is important to note that IFRS 18 already allows a range of revenues and expenses to be combined, with the subtotal nonetheless still listed as an example of a measure similar to gross profit in IFRS 18.B123, e.g. interest expense on financial liabilities may not be related to interest income when the funding from the liability is used to acquire equity instruments. Proponents of View 1 would also highlight that transactions costs included within ''Net income on financial instruments measured at fair value through profit or loss'' are required by IFRS 9 to be directly attributable to the acquisition, issue or disposal of the associated financial instruments.

In addition, the presentation of "Net income on financial instruments measured at fair value through profit or loss" as a single line item is not inconsistent with the conclusion that it is similar to gross profit. Neither IFRS 18 nor any other IFRS Accounting Standard define the term "subtotal". Although a subtotal may result from an explicit presentation of its components, the presentation of separate components on the face of the income statement does not affect the nature of the subtotal, nor is it required by IFRS. Proponents of View 1 would argue that in fact presentation within a single line is required by the net presentation requirements in IFRS 18.B28.

View 1 sees "Net income on financial instruments measured at fair value through profit or loss" as a subtotal "commonly used … and understood by users of financial statements…" (IFRS 18.BC362). In turn, concluding that "Net interest income" and "Net fee and commission income" are similar to gross profit and "Net income on financial instruments measured at fair value through profit or loss" as not similar to gross profit would produce an artificial and misleading split for banks, considering the inherent linkage between the measures, e.g. a loan measured at fair value through profit or loss may generate fees and interest (it is noted that some banks voluntarily present interest from financial instruments measured at fair value through profit or loss separately from fair value gains and losses within "Net interest income") in addition to fair value gains and losses. Consequently, on similar grounds, "Net income on financial instruments measured at fair value through profit or loss" can also be considered as similar to gross profit.

View 2

No – "Net income on financial instruments measured at fair value through profit" is not similar to gross profit.

IFRS 18.B123 includes only "Net interest income" and "Net fee and commission income" as examples of subtotals that are similar to gross profit but does not include "Net income on financial instruments measured at fair value through profit". Proponents of this view interpret the exclusion of "Net income on financial instruments measured at fair value through profit or loss" from the list of examples in IFRS 18.B123 as confirmatory of the IASB's view that it is not similar to gross profit. They believe that contrary to the description of "similar to gross profit" in IFRS 18.B123 as "…the difference between *a type of revenue* and *directly related expenses*…" (*emphasis added*), "Net income on financial instruments measured at fair value through profit" is just an aggregate of gains and losses. Furthermore, they believe that "Net income on financial instruments measured at fair value through profit" is not a subtotal as it is commonly understood, but a presentation line resulting from the application of offsetting requirements in IFRS 18.B28 and therefore cannot be described as similar to gross profit.

Question 2: If the answer to Question 1 is 'Yes', is the aggregation of several measures similar to gross profit, namely "Net interest income", "Net fee and commission income" and "Net income on financial instruments measured at fair value through profit or loss", also considered to be similar to gross profit and therefore, not an MPM?

View 1

Yes – Although IFRS 18 does not explicitly address the sum of measures that are each similar to gross profit, the aggregation of ''Net interest income'', ''Net fee and commission income''

and ''Net income on financial instruments measured at fair value through profit or loss'' should be considered similar to gross profit and therefore not an MPM. The sum merely combines gross-profit-type subtotals without introducing adjustments. The aggregation does not change the nature of the underlying measures. Instead, it remains a subtotal that reflects revenue and directly related expenses arising from an entity's core activities. Accordingly, treating the individual measures as similar to gross profit, while treating their simple aggregation as not similar to gross profit, and therefore an MPM, would lead to an inconsistent outcome that is difficult to reconcile with the rationale underlying IFRS 18.118 and B123.

IFRS 18.117 defines an MPM as "… a subtotal of income and expenses that…(a) an entity uses in public communications *outside the financial statements…and* (c) is not listed in paragraph 118" (*emphasis added*). Furthermore, IFRS 18.118 and IFRS 18.BC362 acknowledge that some subtotals are commonly used and well understood, including gross profit and similar subtotals, and therefore should not be considered MPMs. IFRS 18.121 explicitly states that the objective behind the disclosure for MPMs is to provide information to help a user compare the MPM to measures defined by IFRS Accounting Standards and to provide further information on measures that are not necessarily comparable with other entities.

The primary purpose of "Total revenues", as used by many banks in their income statements, is to provide a subtotal that combines several components, each of which are considered similar to gross profit and therefore not MPMs. It is a simple aggregation of reported amounts that depicts revenue from main business activities (without adjustments) and directly related expenses, which is then also consistently reported in management commentary and investor presentations. Transparency and comparability are not in question.

It would be contradictory to these objectives to conclude that "Total revenues" is an MPM, considering that the individual components are not MPMs.

View 2

No – An aggregate of three measures, namely "Net interest income", "Net fee and commission income" and "Net income on financial instruments measured at fair value through profit or loss", each of which is considered similar to gross profit, is not similar to gross profit and, therefore, is an MPM.

IFRS 18.B123 refers to measures such as "Net interest income" and "Net fee and commission income" as examples of subtotals similar to gross profit. The standard does not extend that concept to a subtotal that aggregates several different gross-profit-type measures.

The fact that each component qualifies individually does not automatically mean that any combination of them also qualifies as a gross-profit-type measure. The proponents of this view believe that although each component may individually depict the difference between "a type

of revenue and directly related expenses" (as set out in IFRS 18.B123), their aggregation does not. The resulting subtotal reflects multiple revenue streams and multiple sets of related expenses and therefore lacks the defining characteristic of a gross-profit-type measure.

Question 3: If the answer to Question 1 is 'No', is the aggregation of several measures similar to gross profit, namely "Net interest income" and "Net fee and commission income" and "Net income on financial instruments measured at fair value through profit or loss" which is a required IFRS disclosure under IFRS 7.20, not an MPM?

View 1

Yes – An aggregation of gross-profit-type measures, namely ''Net interest income'' and ''Net fee and commission income'' and "Net income on financial instruments measured at fair value through profit or loss" that must be disclosed under IFRS 7.20, should not be considered an MPM. Although "Net income on financial instruments measured at fair value through profit or loss" may not be regarded as similar to gross profit, given that it is a required IFRS disclosure, the inclusion of that measure with others that are gross-profit-type measures does not convert the resulting subtotal into an MPM.

IFRS 18.B123 acknowledges that certain subtotals, including "Net interest income" and "Net fee and commission income", are similar to gross profit and therefore are not MPMs. These measures represent core revenue-generating activities of banks and are widely understood by users of financial statements. An aggregate that combines those measures with "Net income on financial instruments measured at fair value through profit or loss", which is specifically required to be presented or disclosed by IFRS Accounting Standards, continues to provide information about the gross profit generated from an entity's principal business activities. That is to say, "Net income on financial instruments measured at fair value through profit or loss" is not a management-defined adjustment.

Furthermore, IFRS 18.118 and IFRS 18.BC362 acknowledge that some subtotals are commonly used and well understood, including gross profit and similar subtotals, and therefore should not be considered MPMs. IFRS 18.121 explicitly states that the objective behind the disclosure for MPMs is to provide information to help a user compare the MPM to measures defined by IFRS and to provide further information on measures that are not necessarily comparable with other entities. It would be contradictory to this objective to conclude that "Total revenues" is an MPM, considering that the individual components of "Total revenues" are either similar to gross profit or required IFRS disclosure items. Furthermore, "Total Revenues" reflects a subtotal that is already used by many banks and clearly presented on the face of the income statement; therefore comparability is not in question.

Accordingly, where

- "Net interest income" is similar to gross profit,
- "Net fee and commission income" is similar to gross profit, and
- "Net income on financial instruments measured at fair value through profit or loss" is a measure specifically required to be presented or disclosed by IFRS Accounting Standards,

the simple aggregation of such measures into a subtotal such as "Total revenues" should not be viewed as an MPM. The subtotal does not reflect management adjustments, is derived entirely from IFRS-required information and provides a transparent depiction of the revenues generated from an entity's main business activities and directly related expenses.

View 2

No – "Total revenues", consisting of "Net interest income", "Net fee and commission income", and "Net income on financial instruments measured at fair value through profit or loss", is not automatically considered to be a non-MPM measure merely because two components are similar to gross profit and the third is specifically required to be disclosed by IFRS. Therefore, the aggregate could meet the definition of an MPM if the other conditions in IFRS 18.117 are met.

IFRS 18.117 (c) identifies measures that are not MPMs, which include measures similar to gross profit (such as "Net interest income" and "Net fee and commission income"). However, the standard does not explicitly extend that concept to a subtotal that aggregates several different qualifying non-MPMs.

The fact that each component qualifies individually does not automatically mean that any combination of them also qualifies as a non-MPM. The proponents of this view believe that although each component may individually depict the difference between "a type of revenue and directly related expenses" (as set out in IFRS 18.B123), their aggregation does not. The resulting subtotal reflects multiple revenue streams and multiple sets of related expenses and therefore lacks the defining characteristic of a gross-profit-type measure.

Reasons for the IFRS IC to address this issue

There is limited time remaining until IFRS 18 is effective. We therefore request the IFRS IC to urgently consider these interpretation questions given the widespread effects they will have.

- "Total revenues" referred to in this submission and similar subtotals are widely reported by the vast majority of banks in their income statements, irrespective of whether those are prepared under IFRS Accounting Standards.

- IFRS 18 does not explicitly address how an entity assesses whether a subtotal meets the definition of an MPM if it represents an aggregate of measures that are similar to gross profit and/or measures required to be disclosed under IFRS. This lack of guidance will result in inconsistent application and reduced comparability. As we approach the effective date of IFRS 18, many preparers are still in discussions with their auditors to try and determine the treatment envisaged by the IASB when drafting IFRS 18.

- An interpretation that "Total revenues" is an MPM will result in a requirement to present reconciliation disclosures set out in IFRS 18.123, **including the calculation of income tax and non-controlling interest effects for "Net income on financial instruments measured at fair value through profit or loss"**; this would be extremely onerous considering the nature of the net income stream and not help a user's understanding of a bank's financial performance. We believe this was neither the intention of the IASB and nor was it requested by any user. Consequently, we question whether costs associated with the application of such an interpretation would be justified by the benefits of reporting, as set out in paragraph 2.39 of the *Conceptual Framework of Financial Reporting*.

Submission B

Re: IFRS 18 "Presentation and Disclosure in Financial Statements" Interpretation Issue

Dear Mr. Mackenzie,

We are writing to request that the IFRS Interpretations Committee (IFRS IC) respond to an important matter in relation to the requirements in IFRS 18 Presentation and Disclosure in Financial Statements (IFRS 18). Specifically, the question of whether "Total Revenues"[5], which is a commonly presented subtotal in the income statements of many banks, although naming may differ across firms, should be considered a management defined performance measure (MPM) that requires additional disclosures.

We acknowledge that presentation practices, business models and banking subtotals differ across institutions and jurisdictions. Consequently, the fact pattern described in this letter should not be understood as the only relevant circumstance under IFRS 18, but rather as an illustration of a broader interpretative issue affecting revenues and directly related expenses from main business activities.

We would like to make the IASB and the IFRS IC aware that, based on discussions with accounting experts at large banks around the world, there is not a clear understanding in the financial services sector, the accounting/audit community and the regulatory community as to how to interpret IFRS 18.117, IFRS 18.118 and IFRS 18.B123 as applied to "Total Revenues". Some are interpreting the current IFRS 18 text as requiring that "Total Revenues" is treated as an MPM. However, accounting experts do not believe that this is an appropriate interpretation or that it reflects the IASB's original intention in drafting IFRS 18. More generally, we observe that requiring MPM disclosures for subtotals that represent

[5] For the purposes of this letter, "Total revenues" generally refers to the subtotal that may also be described as "Total Banking Income", "Total Operating Income" or a similar term. It comprises "Net interest income", "Net fee and commission income", "Net gains or losses on financial instruments measured at fair value through profit or loss", "Net gains or losses on debt instruments measured at fair value through other comprehensive income (FVOCI)" and, where applicable, a residual or balancing "Other income" line item. Depending on the entity's business model, "Total Revenues" may also include insurance-related results, particularly for financial conglomerates with significant insurance activities.

aggregations of revenue arising from an entity's main business activities and directly related expenses may offer limited additional value to users of financial statements. We outline the rationale for this view below.

Given the prevailing and widespread lack of clarity about this important provision at a late stage in the IFRS 18 implementation process, with different interpretations being considered by market participants and other relevant stakeholders across multiple jurisdictions, we **urge the IFRS IC to take up these questions at the next opportunity and provide clarity on the intended application of the requirements**. As explained below, **our accounting experts are of the view that "Total Revenues" should not be treated as an MPM because it depicts a subtotal similar to gross profit**. However, there is no general consensus between banks and audit firms resulting in interpretative uncertainty at this late stage of implementation. This creates a material risk of divergent application across jurisdictions and, consequently, inconsistent and potentially meaningless disclosures by financial institutions.

Timely clarification by the IFRS IC is therefore essential to secure consistent global implementation of IFRS 18, safeguard comparability across jurisdictions, and ensure that disclosures provide decision-useful information to users of financial statements.

Recommendations on the IFRS 18 treatment of "Total Revenues"

Primary position of our accounting experts: "Total Revenues" should not be considered an MPM. Paragraph 118(a) of IFRS 18 excludes gross profit and similar subtotals from the definition of an MPM, while paragraph B123 explains that a subtotal is similar to gross profit when it depicts the difference between a type of revenue and the directly related expenses incurred in generating that revenue, expressly identifying "Net interest income" and "Net fee and commission income" as examples.

"Total Revenues" commonly comprises "Net interest income", "Net fee and commission income" and "Net gains or losses on financial instruments measured at fair value through profit or loss (FVTPL)". It may also include "Net gains or losses recognized on derecognition of debt instruments measured at fair value through other

comprehensive income (FVOCI)", "Net gains or losses recognized on debt instruments measured at amortized cost" and, where applicable, a residual or balancing "Other income" line item, which may, amongst other things, aggregate some of these former items if they are not individually material.

"Net fee and commission income" and "Net interest income" are explicitly not MPMs per paragraph B123 of IFRS 18[6]. We consider that "Net income on financial instruments measured at fair value through profit or loss (FVTPL)"[7], commonly referred to as "Net trading income", should be viewed on the same basis: it plays an analogous role to gross profit as the only meaningful measure of performance for financial instruments measured at fair value through profit or loss, and is therefore similar to gross profit. We also consider that "Net gains or losses recognized on derecognition of financial instruments measured at FVOCI or amortized cost" are similar to gross profit because the sale proceeds are similar to revenue and amortized cost is similar to cost of sales.

The information relating to gains and losses on FVTPL instruments may be presented or disaggregated in different ways, including through separate line items for trading and non trading instruments, while related interest income and expense may be presented within this measure or elsewhere in the statement of profit and loss within "Total Revenues". Accordingly, where "Total Revenues" aggregates some or all of "Net interest income", "Net fee and commission income", "Net gains and losses on FVTPL instruments", "Net gains and losses on derecognition of financial instruments measured at FVOCI", and "Net gains and losses on financial instruments measured at amortized cost" without introducing management adjustments that would alter the nature or key characteristics of the subtotal as a measure of "Total Revenues", the resulting subtotal represents an aggregation of subtotals similar to gross profit, and should itself be treated as similar to gross profit because the

[6] We note that a firm may be part of a financial conglomerate and as such, "Total Revenues" may also include insurance services results. For simplicity and ease of articulation, this component of "Total Revenues" is not referred to throughout the rest of the document, but arguments presented equally apply to insurance service results which, similarly to "Net interest income" and "Net fee and commission income", is identified by IFRS 18.B123 as a subtotal similar to gross profit.

[7] The terminology used for this line item may differ among banks. In this letter, "Net income on financial instruments measured at fair value through profit or loss" refers to the line item in the income statement comprising gains and losses on financial instruments measured at fair value through profit or loss, which is required to be presented or disclosed under paragraph 20 (a)(i) of IFRS 7 *Financial Instruments: Disclosures*.

aggregation does not alter the character of its underlying components. The composition of “Total Revenues” therefore represents the revenue from the main business activities of the banks and its directly related expenses. Differences in the presentation or disaggregation of those amounts should not change the nature of the underlying measures and, therefore, that aggregation should not cause the resulting subtotal to become an MPM.

Similarly, where “Other income” is included in “Total Revenues” as an immaterial residual or balancing amount, its inclusion should not alter the nature of the subtotal or convert an otherwise gross-profit-like subtotal into an MPM. On that basis, “Other income” does not represent a separate management adjustment or an alternative view of performance but merely captures residual items arising in the ordinary course of the entity’s activities. Treating the inclusion of an immaterial residual amount as determinative of whether “Total Revenues” is an MPM would place undue weight on the presentation of a minor component rather than on the substance of the subtotal as a whole. Accordingly, the inclusion of “Other income” should not prevent “Total Revenues” from being regarded as a subtotal similar to gross profit under paragraph B123.

Furthermore, the IASB was clear, as set out in BC362 of the Basis of Conclusions of IFRS 18, that providing the MPM disclosures for subtotals similar to gross profit (as set out in paragraph B123 of IFRS 18), which are commonly used in financial statements and well understood by users of financial statements, would not provide useful information because their purpose and relationship to totals or subtotals defined by IFRS accounting standards are well understood or would usually be apparent from their presentation in the statement of financial performance.

Alternative approach: If “Total Revenues” is nevertheless considered an MPM, we consider that further clarification is required regarding the identification of the most directly comparable IFRS subtotal and the resulting reconciliation requirements. We strongly believe that “Net gains and losses on FVTPL instruments” should not be presented as a reconciling item for the purposes of IFRS 18.123(c). IFRS 18.123(c) requires that an entity discloses a reconciliation between an MPM and the most directly comparable subtotal listed in IFRS 18.118 or total or subtotal specifically

required to be presented or disclosed by IFRS Accounting Standards. “Net gains and losses on FVTPL instruments” is a total specifically required to be presented or disclosed under IFRS 7.20(a)(i). Similarly, “Net gains or losses recognized on derecognition of a financial instruments measured at FVOCI” is a total specifically required to be presented or disclosed under IFRS 7.20(a)(viii) and “Net gains or losses recognized on financial instruments measured at amortized cost” is a total specifically required to be presented or disclosed under IFRS 7.20(a)(v),(vi) and IFRS 7.20A. Because these totals are specifically required by IFRS they should not be reconciling items in the MPM disclosure.

Impact and request for clarification: If “Total Revenues” were considered an MPM and line items presenting net gains or losses on financial instruments were not totals or subtotals specifically required by IFRS Accounting Standards for the purposes of IFRS 18.123(c), IFRS 18.123 would require a reconciliation to the most directly comparable IFRS total or subtotal and disclosure of the income tax effect and the effect on non-controlling interests (NCI) for each reconciling item.

We question the usefulness of providing such a reconciliation as “Total Revenues” is a non adjusted subtotal of line items presented on the face of the income statement – line items that are either explicitly required by IFRS 18 or line items presented as disaggregation of income or expenses following the requirement of paragraph 41 of IFRS 18. The reconciling items are then directly and still readable on the face of the income statement. In this case, providing a reconciliation in the notes to financial statements does not improve the comparability with other banks. Furthermore, we would like to understand how the disclosure of income tax effect and NCI effects on each of these line items of the income statement, which are included in the sub-total “Total Revenues” and which should be used as reconciling items, would meet the objective set out in BC 385.[8]

For example, assuming the most directly comparable IFRS subtotal is the aggregate of the “Net interest income” and “Net fee and commission income” and therefore

[8] BC 385 stated that: “The IASB decided to require this disclosure for each reconciling item because it gives users of financial statements information needed to calculate an adjusted earnings per share measure based on only the adjustments they want to consider in their analysis.”

applying the reconciliation requirements to “Net gains and losses on FVTPL instruments” would create significant implementation complexity as banks would need to determine the relevant tax and NCI effects associated with a net income stream comprising gains and losses on financial instruments measured at fair value through profit or loss. The tax calculation would require consideration of the underlying transactions and the applicable tax jurisdictions, including the methods permitted under IFRS 18.B141.We do not believe that it was the intention of the IASB to require such additional disclosures. Nor do they reflect an informational gap for users of financial statements today as investors, bank analysts and other users of financial statements have not been requesting such information from banks in any jurisdiction. Banks have been required for many years to disclose under IFRS 7.20(a)(i) net gains or net losses equivalent to those included in “Net gains and losses on FVTPL instruments”, yet we are not aware of users having requested information about the related tax and/or NCI effects. In the absence of demonstrated user demand, the significant implementation costs associated with providing this information would clearly and substantially outweigh any potential benefits. To provide this additional breakdown when it does not appear to provide useful information could in fact obscure the understanding of an important line item in the financial statements. We therefore question how the presentation of the tax effect and NCI effects on the identified reconciling item will respond the objective set out in BC 385.

Given these implications, the widespread presentation of “Total Revenues” in banks’ income statements and the limited time remaining before IFRS 18 becomes effective, we would greatly welcome timely clarification from the IFRS IC to support consistent and proportionate implementation of the requirements.

We thank the IFRS Interpretations Committee for its consideration of this time-sensitive issue.