IFRS® Accounting

April 2024

Effects Analysis

IFRS® Accounting Standards

IFRS 18 *Presentation and Disclosure in Financial Statements*

This Effects Analysis accompanies, but is not part of, IFRS 18 *Presentation and Disclosure in Financial Statements*.

What is the purpose of this Effects Analysis?

This Effects Analysis describes the likely costs and benefits of IFRS 18. The International Accounting Standards Board (IASB) gains insights into the likely effects of new or revised IFRS Accounting Standards through its exposure of proposals, consultation with stakeholders and research and analysis. This document describes the IASB's consideration of the effects of IFRS 18.

Background

IFRS 18 will be effective from 1 January 2027, replacing IAS 1 *Presentation of Financial Statements*. A company is permitted to apply IFRS 18 before that date.[1]

IFRS 18 completes the IASB's Primary Financial Statements project to improve how companies communicate information in their financial statements, with a focus on information about financial performance in the statement of profit or loss.

1 In this document, the term 'company' refers to a company that prepares financial statements using IFRS Accounting Standards and is used interchangeably with 'preparer'.

Executive summary

What is IFRS 18?

IFRS 18 is a new IFRS Accounting Standard aimed at improving how companies communicate in their financial statements. IFRS 18 responds to investor demands for better information about companies' financial performance.

Why develop IFRS 18?

IFRS Accounting Standards do not have detailed requirements on:

- where to classify income and expenses in the statement of profit or loss (also referred to as the 'income statement');
- what subtotals to present above 'profit or loss' in the statement of profit or loss; or
- how to group the information to be presented in the primary financial statements or disclosed in the notes.[2]

This lack of detailed requirements leads to diversity in practice. Companies define their own subtotals and performance measures (often referred to as 'alternative performance measures', 'APMs' or 'non-GAAP measures') and group items in their own ways. Investors said that this diversity makes it difficult to analyse and compare companies' performance.

Research background of IFRS 18

The Primary Financial Statements project was added to the IASB's research agenda in July 2014 in response to strong stakeholder demand for the IASB to improve the reporting of financial performance. Feedback on the IASB's 2015 Agenda Consultation confirmed that the Primary Financial Statements project would be a high priority for the IASB.

Feedback during the research phase	Response in IFRS 18
Statements of profit or loss vary in content and structure between companies.	IFRS 18 requires new defined subtotals in the statement of profit or loss.
Investors find measures defined by management useful in analysing performance and making forecasts about future performance but they are concerned about the lack of transparency of how these measures are calculated.	IFRS 18 requires companies to disclose information about management-defined performance measures (MPMs).
Some companies don't provide enough detailed information and important information is often obscured.	IFRS 18 provides companies with principles for grouping information. It also defines the roles of the primary financial statements and the notes.

2 'Primary financial statements' comprise the statement(s) of financial performance, the statement of financial position (also referred to as the 'balance sheet'), the statement of changes in equity and the statement of cash flows.

Who will have to apply IFRS 18 and when does it have to be applied?

All companies that prepare financial statements that comply with IFRS Accounting Standards are required to apply IFRS 18 retrospectively from 1 January 2027. They are permitted to apply it earlier.

What are the main changes for companies?

IFRS 18 means companies will:

- **in the statement of profit or loss—report two new defined subtotals** including operating profit, based on a new set of requirements for classifying income and expenses in categories;
- **in the notes—disclose information about some performance measures defined by management**, which IFRS 18 identify as 'management-defined performance measures' (MPMs); and
- **in both the primary financial statements and the notes—group items applying enhanced requirements for aggregation and disaggregation of information**.

IFRS 18 also introduces limited changes to the statement of cash flows.

What are the likely benefits?

IFRS 18 will improve the quality of financial reporting by:

- providing investors with **additional useful information** about financial performance;
- improving investors' ability to **compare performance** between companies and between reporting periods for the same company; and
- improving **transparency** to help investors understand how management defines the company's performance measures and how those performance measures compare with measures defined by IFRS Accounting Standards.

The IASB expects these improvements will enable investors to make more informed decisions leading to better allocations of capital that will contribute to long-term financial stability.

Table 1 shows the main changes to the financial statements and the relationship between each main change and its likely benefits.

Table 1—Main changes and likely benefits of those changes

Part of the financial statements	Main changes introduced by IFRS 18	Likely benefits of those changes			
		Providing investors with **additional useful information** about financial performance	Improving investors' ability to **compare performance**		Improving **transparency** to help investors understand how companies measure their own performance
			between companies	between reporting periods for the same company	
Statement of profit or loss	• Classification of income and expenses in three new defined categories to provide a consistent structure for the statement of profit or loss —operating, investing and financing • Two new required subtotals to improve analysis —operating profit and profit before financing and income taxes	✓	✓		
Notes to the financial statements	• Disclosure of management-defined performance measures (MPMs) in a single note, including: o a statement that the MPM reflects management's view o an explanation of why the MPM is reported and how it is calculated o a reconciliation to the most directly comparable subtotal listed in IFRS 18 or total or subtotal required by IFRS Accounting Standards o an explanation of any changes to MPMs	✓		✓	✓
	• Disclosure of specified expenses by nature included in each line item in the operating category	✓			
Both the primary financial statements and the notes	• Enhanced requirements for grouping of information (aggregation and disaggregation) • Guidance on whether information should be in the primary financial statements or in the notes • Disclosures about items labelled 'other'	✓	✓	✓	

What are the likely costs?

Costs for companies

The IASB expects that all companies will incur some costs in implementing IFRS 18.

Most costs are likely to relate to changes in internal processes and systems to make the company's financial statements comply with IFRS 18. These costs will vary depending on the company's current systems and reporting practices.

Some companies will have lower implementation costs than others. Companies are likely to have lower costs if:

- their current reporting practices are similar to the requirements in IFRS 18; or
- most of the information required to apply IFRS 18 is available through their current systems.

Some requirements will result in ongoing costs. The IASB has introduced simplifications and reliefs to reduce these costs, summarised in Table 2.

Table 2—Requirements likely to be costly for companies and cost mitigations

Part of the financial statements	Potentially costly requirements	Cost mitigations for companies
Statement of profit or loss	Companies will classify income and expenses in the operating, investing and financing categories in the statement of profit or loss.	IFRS 18 provides relief from some classification requirements if those requirements would result in undue cost or effort. IFRS 18 provides an accounting policy choice for some companies in classifying specific types of income and expenses in the statement of profit or loss.
Notes to the financial statements	Companies will identify the income tax effect and effect on non-controlling interests for each reconciling item in the reconciliation between an MPM and the most directly comparable subtotal listed in IFRS 18 or total or subtotal required by IFRS Accounting Standards.	IFRS 18 allows simplified approaches to calculating the income tax effect for each reconciling item.
	Companies that present operating expenses by function in the statement of profit or loss will disclose some specified expenses by nature included in each line item in the operating category.	IFRS 18 limits the disclosure to five expenses: depreciation, amortisation, employee benefits, impairment losses and write-downs of inventories. The amounts disclosed can include amounts that have been recognised as part of the carrying amount of an asset in the period.

Costs for investors and other stakeholders

The IASB also expects that investors will incur some costs from the implementation of IFRS 18. These costs will mostly arise from adjusting models and analyses to reflect the new structure of the statement of profit or loss.

The IASB expects the implementation of IFRS 18 to ultimately lower costs for investors. Investors are expected to spend less time obtaining the information they need for their analyses.

Other stakeholders, in particular regulators and auditors, are also likely to incur some costs from the implementation of IFRS 18. For regulators, these costs will mostly arise from revising regulatory templates and developing procedures to enforce the new requirements. For auditors, these costs will mostly arise from developing audit procedures for new disclosure requirements.

Regulators and auditors will also incur some ongoing costs to evaluate the judgements that companies make in applying IFRS 18.

Are there any other likely effects?

The IASB expects that IFRS 18 will improve the quality of digital reporting and improve consistency in digital tagging of information.

Some companies have contracts, agreements and compensation policies based on measures in the statement of profit or loss. Companies may need to assess whether to change these contracts, agreements and policies because of changes to the statement of profit or loss required by IFRS 18.

Overall assessment—do the benefits outweigh the costs?

IFRS 18 is expected to improve the quality of financial reporting by defining categories and subtotals in the statement of profit or loss, requiring the disclosure of MPMs, and introducing enhanced requirements for grouping of information in the primary financial statements and the notes.

Companies will incur some costs to implement and apply the requirements in IFRS 18. The IASB has included reliefs in IFRS 18 to reduce costs for companies while still providing investors with better information for better decisions.

The IASB has concluded that the benefits to financial reporting from applying IFRS 18 outweigh the likely costs of implementing and applying it.

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1—Introduction

1—Introduction

What is an effects analysis?

Before the IASB issues an IFRS Accounting Standard, it assesses the likely costs and benefits (collectively referred to as ‘effects’) of the new requirements, including the effects for companies that prepare financial statements and for users of financial statements (referred to as ‘investors’ in this document). This assessment is based on research, analysis, consultations with stakeholders, and fieldwork and feedback on the Exposure Draft.

The IASB also considers the fact that preparers can often develop information that investors need more accurately and at lower cost than investors can do themselves. One of the main objectives of developing a single set of high-quality global accounting standards is to improve the allocation of capital. The IASB therefore considers the benefits of better economic decision-making that result from improved financial reporting.

When it issues a major Standard, the IASB publishes a separate report that summarises the likely effects and how the IASB made its assessment (this Effects Analysis).

Consultation process

Consultations with stakeholders are central to the IASB’s analysis of the effects of new or revised IFRS Accounting Standards. These consultations take place both before and after the publication of an exposure draft.

The IASB published the Exposure Draft *General Presentation and Disclosures* in December 2019. Public consultations on the Exposure Draft included hundreds of meetings, roundtables and other outreach activities.

The consultations involved extensive discussions with preparers, investors, regulators, standard-setters, large accounting networks and academics. The IASB held further outreach meetings in 2022 on some changes that it made to the proposals in the Exposure Draft during its redeliberations.

The IASB also undertook fieldwork. Fifty companies recast their statements of profit or loss and cash flows according to the proposed requirements and discussed the expected changes to their financial statements and expected costs of implementation.

Consultation process for IFRS 18

- Agenda Consultation (2015)
- Exposure Draft *General Presentation and Disclosures* (2019)—216 comment letters received and analysed
- 57 meetings with the advisory bodies and consultative groups throughout the project
- Fieldwork with 50 participants
- Outreach meetings, including:
  - 117 outreach meetings before the Exposure Draft was published;
  - 139 outreach events during the consultation period in 2020; and
  - additional outreach meetings during redeliberations, including 37 targeted outreach meetings in 2022.

Methodology used for this Effects Analysis

This report is mainly a qualitative rather than quantitative evaluation of the expected effects of IFRS 18. The reason is that quantifying costs and, particularly, benefits is a subjective and difficult process. There are no well-established and reliable techniques for the quantification of either costs or benefits in this type of analysis.

The analysis covers the likely effects of the new accounting requirements rather than the actual effects, because the actual effects cannot be known until after companies apply the new requirements. The actual effects will be evaluated during the IASB's Post-implementation Review.

In evaluating the likely effects of IFRS 18, the IASB has considered how IFRS 18 will affect:

- reporting of activities in the financial statements of companies applying IFRS Accounting Standards;
- comparability of financial information, both between reporting periods for the same company and between companies for the same reporting period;
- investors' ability to assess the amount, timing and uncertainty of a company's future cash flows, as well as the company's financial position and performance;
- economic decision-making—specifically, whether better decision-making will be possible because of improved financial reporting;
- compliance costs for companies, both for initial application and on an ongoing basis; and
- costs of analysis for investors.

Analysis of current practice

In addition to the information on current practice obtained from academic literature and other external research, the IASB obtained information on current practice from its own analysis using data collated from 2021–2022 financial statements prepared applying IFRS Accounting Standards, together with related reports and public communications.

The financial statements came from a cross-industry sample of 100 listed companies with large market capitalisations in 26 jurisdictions. Data and analysis from this study are reported and reproduced in tables and figures throughout this Effects Analysis.

Figure 1 and Figure 2 show the industries and regions covered in the sample.

This selection of companies and industries may not be enough to reliably predict the effect of IFRS 18 globally. However, the IASB expects the analysis will help stakeholders assess what changes they can expect from IFRS 18.

Figure 1—Industries covered by the analysis

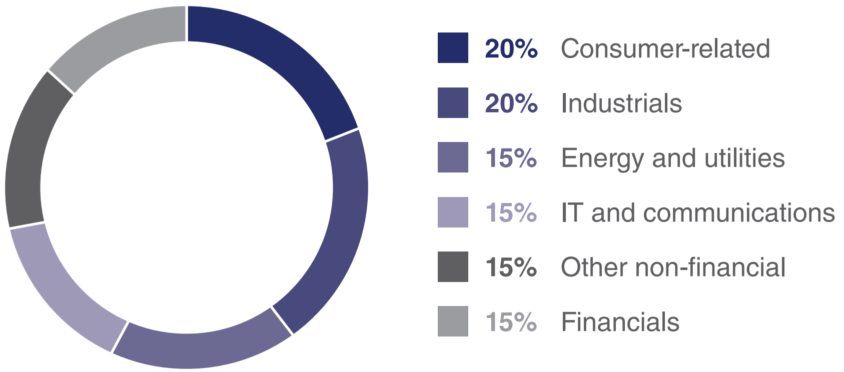
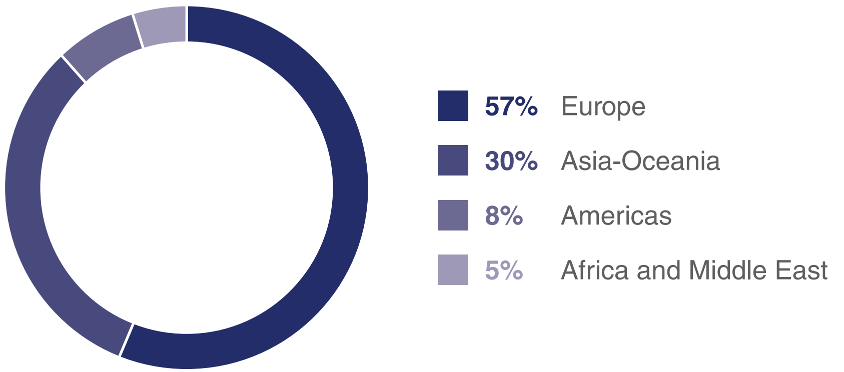


Figure 2—Regions covered by the analysis



Section 2 of this document describes the changes to the financial statements introduced by IFRS 18. Sections 3 to 5 describe the effects that are likely to result from these changes.

2—Changes to accounting requirements

2.1—Overview of changes introduced by IFRS 18

IFRS 18 introduces new requirements for information presented in the primary financial statements and disclosed in the notes. The new requirements are focused on the statement of profit or loss.

IFRS 18 is expected to affect all companies that apply IFRS Accounting Standards. The effects of IFRS 18 will vary depending on the presentation and disclosure practices used by a company and the type and range of its business activities.

The effect is likely to be more significant for a company if:

- its current classification of income and expenses differs from the new classification requirements for income and expenses; or
- it is no longer permitted to present a subtotal in the statement of profit or loss but continues to use such a subtotal in its communications with investors.

After considering the needs of companies and investors, the IASB set the effective date for IFRS 18 from 1 January 2027.

This section focuses on the changes to presentation and disclosure in financial statements introduced by IFRS 18 and how the changes relate to the objectives of the project.

Main changes in IFRS 18

The main changes introduced by IFRS 18 relate to three areas:

1. **Presentation of new defined subtotals in the statement of profit or loss**—operating profit and profit before financing and income taxes—and **consistent classification of income and expenses in categories** to provide useful information and improve comparability (see Section 2.2).

2. **Disclosure of information about management-defined performance measures (MPMs)** to promote transparency and discipline (see Section 2.3).

3. **Enhanced requirements for grouping (aggregation and disaggregation) of information** to help a company provide useful information (see Section 2.4).

IFRS 18 is accompanied by limited changes to the statement of cash flows to improve comparability (see Section 2.5).

This project did not include:

- **changes to the statement of cash flows** (other than the limited changes explained in Section 2.5)—the IASB added a research project on the statement of cash flows and related matters to its work plan for 2022–2026.
- **other comprehensive income**—the IASB decided not to reconsider its work on when to include income or expenses in other comprehensive income and when to reclassify such items to the statement of profit or loss. The IASB considered other comprehensive income as part of the *Conceptual Framework for Financial Reporting*.
- **segment reporting and discontinued operations**—the IASB decided not to consider these areas because doing so would widen the scope of the project.

2.2—Subtotals and categories

Main points

- Presentation of two new defined subtotals—**operating profit** and **profit before financing and income taxes**
- Five categories for classifying income and expenses in the statement of profit or loss—**operating, investing, financing, income taxes** and **discontinued operations**
- Additional requirements for classification of income and expenses by **companies with specified main business activities**

An illustration of a statement of profit or loss for a company applying IFRS 18 is shown in Figure 3. The appendix contains a case study that illustrates some of the changes that might arise on implementing IFRS 18.

All companies will follow the same classification requirements, with some modifications for companies that invest in assets as a main business activity (such as investment entities, investment property companies and insurers) and companies that provide financing to customers as a main business activity (such as banks). See page 18 for the requirements for companies with such specified main business activities.

What are the required totals and subtotals?

A company is required to present:

- operating profit (or loss);
- profit (or loss) before financing and income taxes;[3] and
- profit (or loss).

Can additional subtotals be presented?

In addition to presenting required totals and subtotals, a company is required to present additional subtotals in the statement of profit or loss when such presentations are necessary to provide a useful structured summary of the company's income and expenses (see Section 2.4).

3 This subtotal is not presented by some companies that provide financing to customers as a main business activity.

Figure 3—Statement of profit or loss (extract from the Illustrative Examples on IFRS 18)[4]

Statement of profit or loss	20X2	20X1	Categories[5]
Revenue	367,000	353,100	Operating
Cost of sales	(241,600)	(224,100)	Operating
Gross profit	125,400	129,000	Operating
Other operating income	12,200	4,100	Operating
Selling expenses	(28,900)	(27,400)	Operating
Research and development expenses	(25,100)	(25,900)	Operating
General and administrative expenses	(20,900)	(22,400)	Operating
Goodwill impairment loss	(4,500)	–	Operating
Other operating expenses	(1,200)	(5,600)	Operating
Operating profit	**57,000**	**51,800**	
Share of profit and gains on disposal of associates and joint ventures	5,300	7,300	Investing
Profit before financing and income taxes	**62,300**	**59,100**	
Interest expenses on borrowings and lease liabilities	(13,000)	(13,200)	Financing
Interest expenses on pension liabilities and provisions	(6,500)	(6,000)	Financing
Profit before income taxes	**42,800**	**39,900**	
Income tax expense	(10,700)	(9,975)	Income taxes
Profit from continuing operations	**32,100**	**29,925**	
Loss from discontinued operations	–	(5,500)	Discontinued operations
Profit	**32,100**	**24,425**	

What is classified in the operating category?

The operating category includes all income and expenses in the statement of profit or loss that are not classified in the investing, financing, income taxes or discontinued operations categories.

The operating category is the default category that:

- **comprises all income and expenses arising from a company's operations, regardless of whether they are volatile or unusual in some way.** Operating profit is not a measure of 'persistent' or 'recurring' operating performance. It provides a complete picture of the results from a company's operations for the period.
- **includes, but is not limited to, income and expenses from a company's main business activities.** Income and expenses from other business activities, such as income and expenses from additional activities, are also classified in the operating category if those income and expenses do not meet the requirements to be classified in any of the other categories.

4 Subtotals highlighted in blue in this statement of profit or loss are required subtotals and those highlighted in grey are additional subtotals. Line items illustrate what is included in each category and do not denote line items that any particular company would present. Presentation of profit or loss attributable to owners of the parent and non-controlling interests and references to items that would be disclosed in the notes are not shown for simplicity.

5 The 'Categories' column is presented to illustrate the structure of the statement of profit or loss. Category labels are not required to be presented in the statement of profit or loss.

What is classified in the investing category?

The investing category comprises income and expenses from:[6]

- investments in associates, joint ventures and unconsolidated subsidiaries;
- cash and cash equivalents; and
- other assets that generate a return individually and largely independently of the company's other resources.

Examples of the income and expenses that will be classified in the investing category are:

- the share of profit of associates and joint ventures accounted for using the equity method;
- interest revenue from debt investments;
- dividends from equity investments; and
- rental income and fair value gains or losses from investment properties.

What is classified in the financing category?

The financing category comprises:

- income and expenses from liabilities arising from transactions that involve only the raising of finance;[7] and
- interest income and expenses and the effects of changes in interest rates from liabilities arising from transactions that do not involve only the raising of finance.

Liabilities that arise from transactions that involve only the raising of finance include debt instruments settled in cash such as debentures, loans, notes, bonds and mortgages.

Liabilities arising from transactions that do not involve only the raising of finance include:

- payables for goods or services;
- lease liabilities; and
- defined benefit pension liabilities.

What is classified in the other categories?

Income taxes category

The income taxes category comprises:

- tax expense or tax income included in the statement of profit or loss applying IAS 12 *Income Taxes*; and
- any related foreign exchange differences.

Discontinued operations category

The discontinued operations category comprises income and expenses from discontinued operations required by IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*.

6 'Income and expenses' classified in the investing category comprises income generated by the assets, income and expenses that arise from the initial and subsequent measurement of the assets, including on derecognition of the assets, and incremental expenses directly attributable to the acquisition and disposal of the assets, for example transaction costs and costs to sell the assets.

7 'Income and expenses' classified in the financing category comprises income and expenses that arise from the initial and subsequent measurement of the liabilities, including on derecognition of the liabilities, and incremental expenses directly attributable to the issue and extinguishment of the liabilities, for example transaction costs.

Companies with specified main business activities

Operating profit is an important measure of operating performance. IFRS 18 requires a company with specified main business activities to classify in the operating category some income and expenses that would otherwise be classified in the investing category or the financing category.

IFRS 18 requires a company to assess whether it:

- invests in assets as a main business activity; or
- provides financing to customers as a main business activity.

Some companies, for example investment and retail banks, may both invest in assets and provide financing to customers as main business activities.

Companies that invest in assets as a main business activity

Some companies invest in assets as a main business activity, for example investment entities, investment property companies and insurers. Such companies will classify in the operating category the income and expenses that arise from those assets that would otherwise be classified in the investing category.

There are two exceptions to this principle:

- income and expenses from investments in associates, joint ventures and unconsolidated subsidiaries accounted for using the equity method are always classified in the investing category.
- cash and cash equivalents are excluded from the assessment. The classification of income and expenses from cash and cash equivalents depends on whether a company has specified main business activities and, if so, the type of specified main business activity.[8]

Companies that provide financing to customers as a main business activity

Some companies provide financing to customers as a main business activity, for example banks or automotive finance companies.

Such companies will:

- classify in the operating category income and expenses from liabilities that arise from transactions that involve only the raising of finance related to the provision of financing to customers; and
- make an accounting policy choice to classify in the operating category or financing category income and expenses from liabilities that arise from transactions that involve only the raising of finance not related to the provision of financing to customers.

Such companies are still required to classify interest income and expenses (and the effect of changes in interest rates) from liabilities that arise from transactions that *do not* involve only the raising of finance in the financing category.

8 If a company invests in financial assets as a main business activity it will classify all income and expenses from cash and cash equivalents in the operating category. If a company does not invest in financial assets as a main business activity but provides financing to customers as a main business activity, it will apply an accounting policy choice to classify all income and expenses from cash or cash equivalents or the portion related to providing financing to customers in the operating category.

Classification of specific income and expenses

Foreign exchange differences

Foreign exchange differences are classified in the same category as the income and expenses from the items that gave rise to those differences. For example, foreign exchange differences on a foreign-currency denominated receivable for a sale of goods are classified in the operating category (the same category as the sale of goods). IFRS 18 provides undue cost or effort relief for the classification of foreign exchange differences, as discussed in Section 4.2.

Fair value gains and losses on derivatives

The classification of fair value gains and losses on derivatives depends on whether the derivatives are used to manage exposure to identified risks and whether they are designated as hedging instruments.

IFRS 18 provides undue cost or effort relief for the classification of gains or losses on derivatives used to manage identified risks but not designated as hedging instruments, as discussed in Section 4.2.

Income and expenses from hybrid contracts

The classification of income and expenses from hybrid contracts comprising host liabilities and embedded derivatives depends on whether the embedded derivative is separated from the host liability and the nature of the hybrid contract.

Changes to the financial statements—subtotals and categories in the statement of profit or loss	
Presentation of operating profit All companies will present operating profit in the statement of profit or loss, regardless of whether they currently present such a subtotal. Companies that currently present a subtotal labelled operating profit are likely to change the items included in operating profit to align with the definition in IFRS 18, which is designed to be comparable between companies. IAS 1 does not require or define an operating profit subtotal. Therefore, current practice varies with each company having its own definition of operating profit. For example, some companies include in operating profit income and expenses from associates and joint ventures accounted for using the equity method, but others do not (see Section 3.2).	**Presentation of profit before financing and income taxes** Many companies will present the new subtotal of profit before financing and income taxes. Some companies currently present a subtotal labelled ‘earnings before interest and tax (EBIT)’. However, EBIT is not defined in IAS 1. The IASB’s definition of ‘profit before financing and income taxes’ is likely to differ from the definition companies use for EBIT. **Presentation of a company’s own subtotals in the statement of profit or loss** Some companies currently present their own subtotals in the statement of profit or loss. The requirements for the classification of income and expenses into categories may prevent companies from presenting some of these subtotals because they will not fit into the new structure of the statement of profit or loss.

2.3—Management-defined performance measures

Main points

Identifying **management-defined performance measures**

Disclosure of information about management-defined performance measures in the notes to the financial statements

What are management-defined performance measures (MPMs)?

An MPM is a subtotal of income and expenses that:

- is used in public communications outside financial statements;
- is used to communicate to investors management's view of an aspect of the financial performance of the company as a whole; and
- is not listed in IFRS 18 or specifically required by IFRS Accounting Standards.

Companies often use their own measures to track performance, including subtotals of income and expenses that they communicate in connection with financial performance.

However, not all of these measures are MPMs. Figure 4 provides examples of MPMs and other performance measures. Figure 5 explains how to identify an MPM.

Figure 4—MPMs and other performance measures

Performance measures		
Subtotals of income and expenses		Other performance measures
MPMs	IFRS-Specified	
• Adjusted profit • Adjusted operating profit • Adjusted earnings before interest, tax, depreciation and amortisation	• Operating profit • Operating profit before depreciation, amortisation and impairments within the scope of IAS 36 *Impairment of Assets*	• Free cash flow • Return on equity • Net debt • Number of customers • Customer satisfaction

Criteria for MPMs

Subtotals of income and expenses

MPMs are subtotals of income and expenses. Other measures, such as free cash flow, are not MPMs.

Used in public communications outside financial statements

Public communications include management commentary, press releases and investor presentations. For the purpose of identifying MPMs, public communications do not include oral communications, written transcripts of oral communications or social media posts (see Section 4.2).

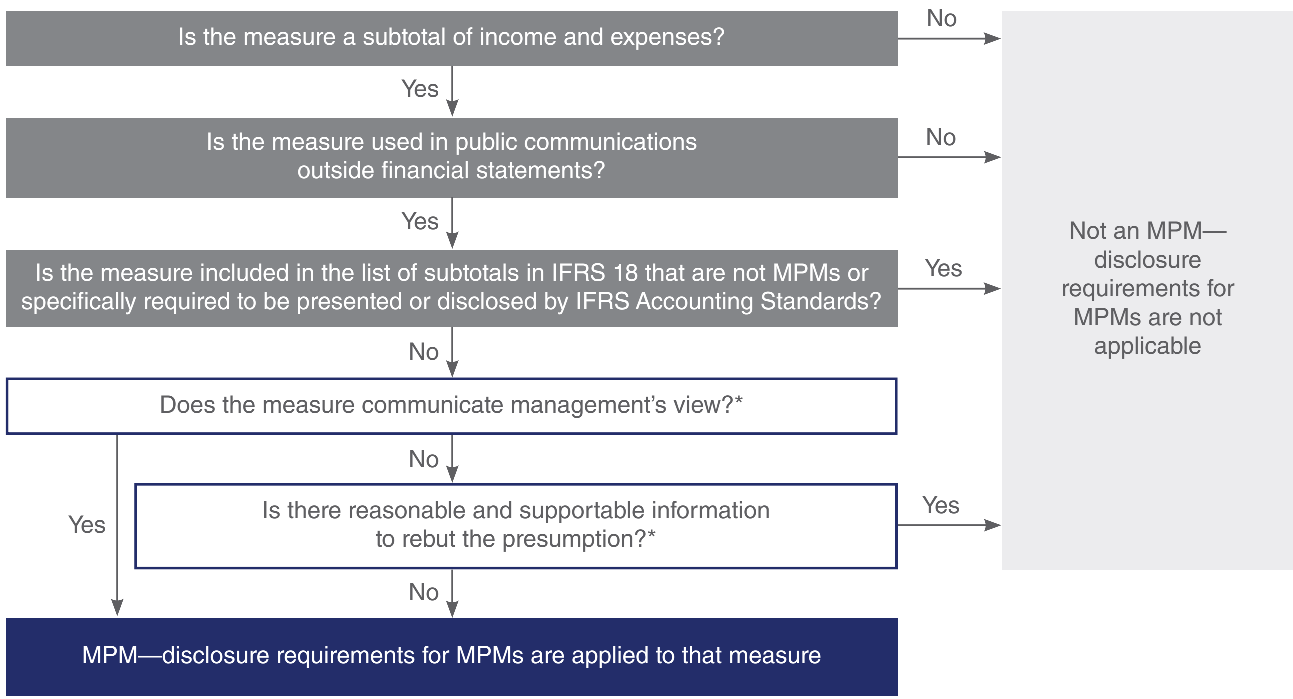
Subtotals not listed in IFRS 18 or specifically required by IFRS Accounting Standards

Examples of subtotals that are not MPMs are gross profit and profit before income taxes.

Communicate management's view of financial performance

IFRS 18 presumes that a subtotal of income and expenses used in public communications outside financial statements represents management's view of financial performance. A company is permitted to rebut this presumption if it has reasonable and supportable information demonstrating that such a subtotal does not communicate management's view. This rebuttable presumption is discussed in Section 4.2.

Figure 5—Identifying an MPM



* It is presumed that a subtotal of income and expenses used in public communications communicates management's view; a company is not required to consider whether to rebut the presumption.

What disclosures does IFRS 18 require for MPMs?

A company will disclose information about its MPMs in a single note to the financial statements. The note will include a statement that the MPMs provide management's view of an aspect of the financial performance of the company as a whole and are not necessarily comparable with measures sharing similar labels or descriptions provided by other companies.

The note will also include for each MPM:

- **a description of the aspect of financial performance that it communicates**, including why management believes the MPM provides useful information about the company's financial performance;
- **a description of how the MPM is calculated**;
- **a reconciliation between the MPM and the most directly comparable subtotal listed in IFRS 18 or total or subtotal required by IFRS Accounting Standards**, including the income tax effect and the effect on non-controlling interests for each item disclosed in the reconciliation (see Figure 6); and
- **a description of how the company determined the income tax effect**.

Figure 6—Illustrative example of an MPM reconciliation (extract from the Illustrative Examples on IFRS 18)[9]

		Adjusting items			
	IFRS	Impairment losses	Restructuring expenses	Gains on disposal of property, plant and equipment	**MPM**
Other operating income		–	–	(1,800)	
Research and development expenses		1,600	–	–	
General and administrative expenses		–	3,800	–	
Goodwill impairment loss		4,500	–	–	
Operating profit / Adjusted operating profit	**57,000**	6,100	3,800	(1,800)	**65,100**
Income tax expense		–	(589)	297	
Profit from continuing operations / Adjusted profit from continuing operations	**32,100**	6,100	3,211	(1,503)	**39,908**
Profit attributable to non-controlling interests		305	161	–	

9 Comparative information and narrative disclosures are not shown for simplicity.

If a company changes the calculation of an MPM, introduces a new MPM, or ceases to use a previously disclosed MPM, it will disclose:

- an explanation of the change, addition or cessation and its effects;
- the reasons for the change, addition or cessation; and
- restated comparative information to reflect the change, addition or cessation unless it is impracticable to do so.

What about EBITDA?

IFRS 18 does not define EBITDA (earnings before interest, tax, depreciation and amortisation). Instead, IFRS 18 specifies that 'operating profit or loss before depreciation, amortisation and impairments within the scope of IAS 36' (OPDAI) is not an MPM.

The IASB considered introducing a defined subtotal for EBITDA. However, the IASB's research showed that there is no consensus among investors about what EBITDA represents.

If a company provides an EBITDA subtotal in its public communications that is not calculated in the same way as OPDAI, that subtotal would be an MPM, so the company will need to provide disclosures about it.

Changes to the financial statements—alternative performance measures (APMs)

Use of APMs

The introduction of newly defined subtotals in IFRS 18 could reduce the use of some performance measures companies define themselves (referred to hereafter as APMs). For example, some companies may decide to explain operating performance in public communications using operating profit as defined in IFRS 18.

Disclosure

Companies that currently use APMs, without providing detailed information about them inside or outside the financial statements, will need to provide the MPM disclosures in the financial statements for those APMs that meet the definition of MPMs in IFRS 18.

Companies that already disclose information about APMs in the financial statements may need to change the contents of the disclosure to comply with IFRS 18 if the APMs meet the definition of MPMs. For example, a company may need to change the reconciliation that it currently provides as a result of applying the guidance in IFRS 18 on which totals or subtotals can be used for MPM reconciliations and the requirement to disclose for each item in the reconciliation the amounts related to each line item in the statement of profit or loss.

For many companies, disclosure of the income tax effect and the effect on non-controlling interests of each reconciling item will be new. Companies that currently provide aggregated information about those effects for all reconciling items will need to disaggregate this information.

2.4—Grouping of information

Main points

- Primary financial statements provide **useful structured summaries**—notes provide other material information
- Grouping and labelling of items follows **consistent principles**
- Some companies will be required to disclose **specified expenses by nature** in the notes

Roles of the primary financial statements and the notes

The objective of financial statements is to provide financial information about the company's recognised assets, liabilities, equity, income and expenses that is useful to investors in assessing the prospects for future net cash inflows to the company and in assessing management's stewardship of the company's economic resources.

To achieve the objective of financial statements, the primary financial statements and the notes have distinct and complementary roles in providing financial information, shown in Table 3.

Table 3—Roles of the primary financial statements and the notes

Primary financial statements	Notes
Provide **structured summaries** of a company's recognised assets, liabilities, equity, income, expenses and cash flows, that are **useful** for: • **obtaining an understandable overview** of the company's recognised assets, liabilities, equity, income, expenses and cash flows; • **making comparisons** between companies, and between reporting periods for the same company; and • **identifying items or areas** about which users of financial statements may wish to seek additional information in the notes.	Provide **material information** necessary: • to **enable investors to understand the items in the primary financial statements**; and • to **supplement the primary financial statements** with additional information to achieve the objective of the financial statements.

Principles for grouping (aggregation and disaggregation) of information

IFRS 18 requires companies to aggregate or disaggregate information about individual transactions and other events into the information presented in the primary financial statements and disclosed in the notes.

The requirements are based on principles for grouping (aggregation and disaggregation) of information. IFRS 18 requires companies to ensure that:

- items are aggregated based on shared characteristics and disaggregated based on characteristics that are not shared;
- items are aggregated or disaggregated such that the primary financial statements and the notes fulfil their roles; and
- the aggregation and disaggregation of items does not obscure material information.

Companies will be specifically required to disaggregate information whenever the resulting information is material. If a company does not present such information in the primary financial statements, it will disclose the information in the notes.

To help companies apply the principles, IFRS 18 provides application guidance on grouping items and labelling aggregated items, including which characteristics to consider when assessing whether items have similar or dissimilar characteristics.

Changes to the financial statements—roles of the primary financial statements and the notes and principles for grouping of information

Roles of the primary financial statements and the notes

To ensure that the primary financial statements and the notes fulfil their roles, a company will need to consider whether to:

- present the line items listed in IFRS 18 for the statement of profit or loss and the statement of financial position if doing so is necessary for the statements to provide useful structured summaries of the company's income, expenses, assets, liabilities and equity;
- present additional subtotals and line items in the primary financial statements if necessary to provide useful structured summaries of the company's income, expenses, assets, liabilities and equity; and
- disclose items that are not presented in the primary financial statements in the notes if the information is material.

Principles for grouping of information

The new requirements for aggregation and disaggregation will result in some companies:

- changing the way they aggregate and disaggregate items in order to fulfil the roles of the primary financial statements and the notes;
- changing the way they describe items presented or disclosed so that the description faithfully represents the characteristics of each item;
- changing the labels that they use for aggregated amounts, such as 'other', to more informative labels; and
- explaining how amounts disclosed in the notes relate to the amounts in a primary financial statement, including the line item in which the amount is included.

Presentation of operating expenses

IFRS 18 requires companies to classify and present operating expenses in a way that provides the most useful structured summary of its expenses using the characteristics of:

- the nature of the expense (for example, raw material expenses and employee benefit expenses); or
- the function of the expenses within the company (for example, cost of sales).

A company will classify some operating expenses by function and others by nature if doing so would provide the most useful structured summary of its expenses.

In deciding how to present operating expenses, a company will consider factors such as what line items provide the most useful information about the main components or drivers of the company's profitability and industry practice.

Disclosure of expenses by nature

A company that presents one or more line items for operating expenses classified by function is required to disclose the amounts for five specified expenses by nature related to each line item in the operating category of the statement of profit or loss.[10]

The expenses required to be disclosed are:

- depreciation;
- amortisation;
- employee benefits;
- impairment losses and reversals of impairment losses; and
- write-downs and reversals of write-downs of inventories.

Changes to the financial statements—presentation and disclosure of operating expenses

Presentation of operating expenses

The requirement in IFRS 18 to assess whether to present operating expenses by nature or function will result in some companies being required to change the line items presented in the statement of profit or loss.

IAS 1 requires companies to present an analysis of expenses based on either their nature or their function within the company—whichever provides information that is reliable and more relevant. However, IAS 1 contains limited guidance on how to apply this requirement.

Disclosure of expenses by nature

Companies that currently do not disclose information about expenses by nature included in each line item in the operating category will be required to do so.

As a result, more companies will provide detailed information about their operating expenses than they currently provide.

10 The amounts to be disclosed need not be the amounts recognised as an expense in the reporting period. The disclosed amounts can include amounts that have been recognised as part of the carrying amount of an asset in the period (see Section 4.2).

2.5—Other changes to financial reporting

Statement of cash flows

The IASB amended IAS 7 *Statement of Cash Flows*:

- to require all companies to use the operating profit subtotal as the starting point for the indirect method of reporting cash flows from operating activities; and
- to remove the presentation alternatives for cash flows related to interest and dividends paid and received as shown in Table 4.

Do the categories have the same meaning in the statement of profit or loss and the statement of cash flows?

No, they have different meanings. In developing IFRS 18, the IASB prioritised the objectives of each primary financial statement and did not seek alignment between the operating, investing and financing categories in the statement of profit or loss and the statement of cash flows.

The IASB added a research project on the statement of cash flows and related matters to the research project pipeline in its Third Agenda Consultation completed in July 2022.

Table 4—Classification of interest and dividends paid and received in the statement of cash flows

Cash flow item	Classification **before** amendments to IAS 7	Classification **after** amendments to IAS 7	
		Companies with no specified main business activities	Companies with specified main business activities
Interest received	Operating or investing	Investing	A single category for each item—operating, investing or financing
Interest paid	Operating or financing	Financing	
Dividends received	Operating or investing	Investing	
Dividends paid	Operating or financing	Financing	Financing

Changes to the financial statements—statement of cash flows

Starting point for the indirect method

All companies presenting a statement of cash flows using the indirect method will use the same starting point—operating profit—to report cash flows from operating activities, resulting in a change to the starting point for many companies.

Changing the starting point will simplify the presentation of cash flows from operating activities. For example, it will remove some reconciling items that companies might currently present, such as the share of profit of associates and joint ventures accounted for using the equity method.

Classification of interest and dividend cash flows

Some companies that classify interest received, interest paid and dividends received as cash flows from operating activities will need to change their classification to improve the comparability of the statement of cash flows.

Earnings per share

In addition to reporting basic and diluted earnings per share, companies are permitted by IAS 33 *Earnings per Share* to disclose additional earnings per share calculated based on any component of the statement of comprehensive income.

The amendments to IAS 33 permit a company to disclose these additional earnings per share only if the numerator is either a total or subtotal identified in IFRS 18 or is an MPM.

A company cannot present additional earnings per share in the primary financial statements. It can only disclose additional earnings per share in the notes.

Can a company disclose adjusted earnings per share required by local law or regulation applying the amendments to IAS 33?

Yes, if a company concludes that the numerator used in an earnings per share measure required by local law or regulation meets the definition of an MPM. The company will provide the disclosures for MPMs for that numerator (see Section 2.3).

3—Benefits

3.1—Useful information about financial performance

The IASB expects that application of IFRS 18 will result in companies providing investors with additional useful information about:[11]

- **operating performance**, through the operating profit subtotal;
- **performance before the effect of financing**, through the profit before financing and income taxes subtotal; and
- income, expenses, assets, liabilities, equity and cash flows, through **improved aggregation and disaggregation**, including the disaggregation of specified expenses and better labelling of items.

Subtotals and categories in the statement of profit or loss

What investors said:

'Structure and content of the statement of profit or loss varies between different companies, making it difficult to compare companies' performance.'

Investors are expected to benefit from companies presenting the new defined subtotals required by IFRS 18 in the statement of profit or loss.

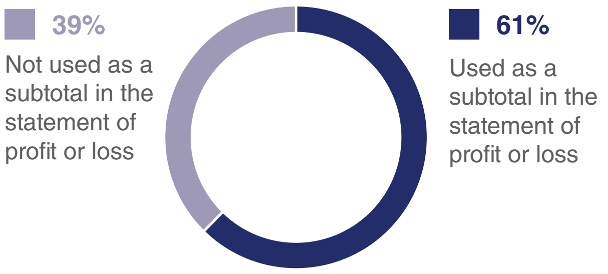
The majority of investors who responded to a survey by the CFA Institute wanted standard-setters to define key subtotals for companies to present in the primary financial statements, such as operating profit or loss.[12]

Operating profit

The requirement in IFRS 18 for all companies to present a consistently defined operating profit subtotal will provide useful information about financial performance and give investors a consistent starting point for their analyses.

Operating profit is one of the most commonly presented subtotals in financial statements. In the IASB's sample of 100 companies, 61 companies presented in the statement of profit or loss a measure labelled operating profit (or similarly labelled subtotal, such as profit from operations), using at least nine different definitions.

Figure 7—Use of operating profit and similarly labelled subtotals



11 Feedback from investors suggests that alternative performance measures companies currently use to communicate with investors can provide useful information about financial performance. The benefits of management-defined performance measures are discussed separately in section 3.3.

12 V Papa, S J Peters, and K Schacht, *Bridging the Gap: Ensuring Effective Non-GAAP and Performance Reporting*, CFA Institute, 2016.

Research on line items and subtotals presented by companies from 46 countries showed that 'value relevance' is highest for measures in the middle of the statement of profit or loss, for example, in the operating profit subtotal.[13]

Profit before financing and income taxes

The requirement in IFRS 18 for companies to present the subtotal of profit before financing and income taxes is expected to provide useful information to investors about company performance before the effect of its financing.

Profit before financing and income taxes serves a similar purpose to a subtotal for earnings before interest and tax (EBIT), which investors use to compare the financial performance of companies with varied financing structures. EBIT is commonly used for screening and ratio analysis, and as a starting point for forecasting cash flows. EBIT is sometimes used interchangeably with operating profit. Companies who use EBIT also vary in their presentation and disclosure of it.

A survey by the CFA Institute in 2016 found that 46% of 431 respondents (mostly buy-side analysts) use EBIT in their analysis.[14]

IFRS 18 defines profit before financing and income taxes rather than EBIT and requires most companies to present this subtotal in the statement of profit or loss. The IASB expects investors will use this subtotal in the way they currently use subtotals such as EBIT that seek to represent the performance of companies before financing and income taxes.

The IASB's research found that presentation and disclosure of EBIT varies by company (see Table 5). Some companies presented EBIT in the statement of profit or loss or disclosed it in the notes, and others disclosed it outside the financial statements.

Table 5—Use of subtotals labelled EBIT or profit before financing by non-banking and non-insurance companies[15]

	Number of companies
Provided in the financial statements	21
of which only presented as a subtotal in the statement of profit or loss	*6*
of which only disclosed in the note about segment information	*7*
of which presented in the statement of profit or loss and disclosed in the note about segment information	*8*
Provided only in sections of the annual report other than the financial statements	4
Not provided	60
Total	85

13 J Barton, T B Hansen, G Pownall, 'Which Performance Measures Do Investors Around the World Value the Most—and Why?', *The Accounting Review*, vol 85, no 3, 2010, pages 753–789. In this study, 'value relevance' of a measure is explained as 'its ability to explain variation in contemporaneous stock returns'.

14 V Papa, S J Peters, and K Schacht, *Bridging the Gap: Ensuring Effective Non-GAAP and Performance Reporting*, CFA Institute, 2016.

15 None of the companies in the banking and insurance industries in the IASB's sample of 100 companies presents or discloses a subtotal labelled EBIT or profit before financing.

Grouping of information in the financial statements[16]

What investors said:

'Information is sometimes aggregated to the extent that useful information is omitted.'

The new requirements for grouping information in the financial statements are expected to increase the amount of useful information available to investors. The requirements include guidance on grouping and labelling information and presentation and disclosure of operating expenses.

Grouping and labelling information

The new guidance for grouping of items in the financial statements is introduced to help companies determine where to present or disclose information in the financial statements and the level of detail required.

A company will aggregate or disaggregate line items to fulfil the role of the primary financial statements to provide useful structured summaries and aggregate or disaggregate items to provide material financial information in the notes that supplement those summaries.

Once a company has grouped items for presentation and disclosure, it will apply the new guidance on labelling of information to determine an informative label.

The IASB further expects that the new guidance on the use of the label 'other' in the financial statements will lead to companies using more informative labels and providing more explanation of what is captured within a line item labelled 'other'.

Presentation of operating expenses

The IASB expects that the guidance on the presentation of operating expenses will help companies provide the most useful structured summary of their expenses. This information will be helpful to investors in analysing returns on a company's operations and making decisions about future investments.

Companies currently present operating expenses using a classification based on either the nature of the expenses or their function within the company—whichever provides information that is 'reliable and more relevant', as required by IAS 1. Some companies present expenses in the statement of profit or loss classified both by nature and by function (mixed presentation).

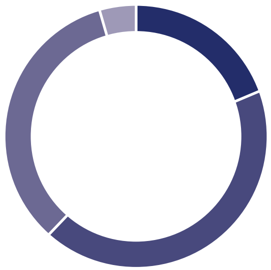
A study of financial statements of 197 European companies applying IFRS Accounting Standards showed that whether they present expenses by nature or function was influenced mainly by their country or industry and to some degree by their audit firm.[17]

16 Requirements related to grouping of information apply not only to income and expenses but also to assets, liabilities, equity and cash flows.

17 V Cole, J Branson, D Breesch, 'Determinants influencing the IFRS accounting policy choices of European listed companies', conference paper, International Accounting and Auditing Conference, Vrije Universiteit Brussel, 20–21 July 2013.

The IASB's analysis of 100 companies also showed that the presentation of operating expenses in current practice varies by company (see Figure 8).

Figure 8—Presentation of expenses in the statement of profit or loss



19% By nature

42% By function

35% Mixed presentation

4% No analysis of expenses presented in the statement of profit or loss

Disclosure of specified expenses by nature

The disclosure of five specified expenses by nature[18] is expected to provide investors with additional useful information needed for their analyses. It will enable investors to better understand:

- what is included in line items in the statement of profit or loss (which is useful, for example, when performing margin analysis);
- how information presented in the primary financial statements relates to information disclosed in the notes; and
- how line items in the statement of profit or loss relate to the statement of cash flows.

Investors have told the IASB that they find information about expenses by nature useful to forecast future operating expenses, but nature information is sometimes missing or incomplete. In the sample of 100 companies, the companies generally provided some analysis of expenses by nature in the notes, but the range of information disclosed varied widely across the sample.

Limiting the list of disclosures to five specified expenses by nature balances the information needs of investors with the costs to companies to provide the disclosures (see Section 4.1).

Where will investors find information about unusual income and expenses?

IFRS 18 includes no specific requirements on unusual income and expenses. Nonetheless, the IASB expects that investors will obtain material information about such income and expenses through:

- the disaggregation of items with dissimilar characteristics—for example, if an item of income or expenses lacks persistence, a company will need to consider whether information about it is material and should be disclosed;
- the description of items using labels that faithfully represent the characteristics of those items—for example, if a company discloses an item because it lacks persistence, or is identified as unusual, the company will label the item as such; and
- the disclosure of information about MPMs—in some cases, unusual income and expenses might appear as adjusting items when a company calculates its MPMs.

18 Depreciation, amortisation, employee benefits, impairment losses and reversals of impairment losses and write-downs and reversals of write-downs of inventories (see Section 2.4).

3.2—Comparability of financial information

The IASB expects that IFRS 18 will improve comparability of financial information through:

- the principles for and guidance on **grouping and labelling information**—which will improve comparability between companies and between reporting periods for the same company;
- the requirements for **subtotals and categories in the statement of profit or loss**, along with the **amendments to IAS 7 for the statement of cash flows**—which will improve comparability between companies; and
- the requirements to disclose **information about MPMs**—which will improve comparability between reporting periods for the same company.

Grouping and labelling information

What investors said:

‘Companies often disclose items of large amounts labelled as “other” with no information provided about what is included in the amount, which reduces comparability of information.’

The requirements for grouping and labelling information, including the requirements for the label ‘other’, are expected to improve comparability.

IAS 1 requires companies to present separately each material class of similar items but does not provide detailed guidance on how to do so. The items disclosed in the notes vary considerably by company, impeding comparability.

Academic research shows that imprecision in requirements for the disaggregation of financial information affects the content of financial statements and the comparability of information between companies operating in different jurisdictions.[19]

19 R Libby, S A Emett, ‘Earnings Presentation Effects on Manager Reporting Choices and Investor Decisions’, *Accounting and Business Research*, vol 44, no 4, May 2014, pages 410–438.

Statement of profit or loss

What investors said:

'The structure and content of the statement of profit or loss vary even between companies operating in the same industry.'

'Inconsistencies in classification of income and expenses can reduce comparability.'

'We need comparable subtotals as a starting point for analysis, including screening and ratio analysis.'

Required subtotals

By defining and requiring the two most common performance subtotals, IFRS 18 provides a consistent starting point for analysis and will enable investors to more easily compare aspects of performance between companies, as summarised in Table 6.

Companies have followed their own definitions for the subtotals they present in the statement of profit or loss, such as operating profit and EBIT, because IAS 1 has no specific requirements for these.

Investors observed that these subtotals are difficult to compare between companies because companies present different subtotals or calculate similarly labelled subtotals differently (see Section 3.1).

Investors expend considerable effort in comparing companies' performance using their own methods for defining 'operating profit', and they cannot always be sure the outcome is accurate.

Table 6—Expected improvements in comparability from required subtotals

Subtotal	What the subtotal enables investors to compare
Operating profit or loss	Results from operating activities for companies in the same industry and for companies in different industries
Profit or loss before financing and income taxes	Performance of companies before the effects of their financing

Consistent classification of income and expenses

IFRS 18 is expected to improve comparability by introducing requirements for consistent classification of income and expenses. Consistent classification will also help investors to adjust amounts presented if the required classification of particular income or expenses in IFRS 18 differs from their needs.

IAS 1 does not have requirements for where to classify income and expenses in the statement of profit or loss, which has led to diversity in classification of income and expenses.

The IASB's analysis of 100 companies showed that some classify net interest expense on a net defined benefit liability in operating profit whereas others include that expense in finance costs (see Table 7). Diversity in practice also exists for classification of foreign exchange differences (see Table 8) and income and expenses from associates and joint ventures accounted for using the equity method (see Figure 9).

Table 7—Classification of net interest expense on net defined benefit liabilities

	Number of companies
Classified above an operating profit (or EBIT/EBITDA) subtotal	9
Classified in finance costs, below an operating profit (or EBIT/EBITDA) subtotal	33
Classification unclear	19
Did not present a subtotal labelled operating profit (or EBIT/EBITDA), nor present or disclose net interest expense on net defined benefit liabilities	39
Total	100

Table 8—Classification of foreign exchange differences

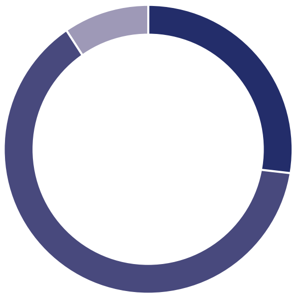
	Number of companies
Classified above an operating profit (or EBIT/EBITDA) subtotal	12
Classified below an operating profit (or EBIT/EBITDA) subtotal	33
Classified both above and below an operating profit (or EBIT/EBITDA) subtotal	16
Classification unclear	13
Did not present a subtotal labelled operating profit (or EBIT/EBITDA)	26
Total	100

How does the classification of income from associates and joint ventures in IFRS 18 help comparability?

Companies present the share of profit of associates and joint ventures accounted for using the equity method as a separate line item, as required by IAS 1. However, IAS 1 does not specify where this line item should appear in the statement of profit or loss.

The IASB has observed wide diversity in practice in the presentation of this item, as shown in Figure 9.

Figure 9—Classification of the share of profit of associates and joint ventures accounted for using the equity method[20]



- **26%** Above an operating profit (or EBIT/EBITDA) subtotal
- **62%** Between an operating profit (or EBIT/EBITDA) subtotal and profit before tax
- **12%** Below profit before tax

One factor for the diversity is that some associates and joint ventures are more closely related to a company's operating activities than others.

Feedback from investors

Investors expressed concerns that this diversity reduces comparability of the subtotals in the statement of profit or loss, making their analysis more difficult and time consuming. Investors also said when analysing the performance of a company and determining a valuation for it, they generally analyse investments in associates and joint ventures accounted for using the equity method separately from the company's consolidated operations.

Requirements in IFRS 18

IFRS 18 requires a company to classify income and expenses from all associates and joint ventures accounted for using the equity method in the investing category. The IASB expects that the requirement will:

- reduce diversity in practice and improve comparability; and
- enhance the usefulness of the operating profit subtotal and provide a consistent anchor for investors.

20 This analysis is based on the companies that present a share of profit of associates and joint ventures accounted for using the equity method and operating profit (or EBIT/EBITDA) subtotal.

Statement of cash flows

What investors said:

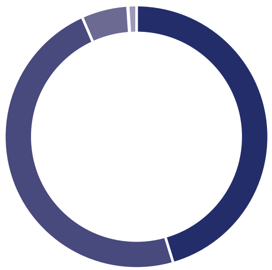
'Classification and presentation options make it difficult to compare companies' cash flows.'

Starting point for reporting operating cash flows

The IASB expects that requiring companies to use the operating profit subtotal as a consistent starting point will make the statement of cash flows more consistent and help investors analyse and compare companies' operating cash flows.

The IASB's research found that companies use varied starting points for the indirect method of reporting cash flows from operating activities in the statement of cash flows (see Figure 10).

Figure 10—Starting points for operating cash flows[21]



- **47%** Profit or loss
- **45%** Profit before tax
- **7%** Operating profit
- **1%** EBITDA

Classifying interest and dividend cash flows

The IASB expects that removing the presentation alternatives for cash flows related to interest and dividends paid or received will make the statement of cash flows more consistent and comparable.

Investors said they wanted to spend less time and incur fewer cost searching for information about interest and dividends in the statement of cash flows and would like the IASB to make such information more comparable. The IASB, therefore, decided to require a consistent classification for interest and dividends paid or received in the statement of cash flows (see Section 2.5).

These requirements will be simpler for companies to apply because they will no longer be required to make choices about how and where to classify these items. Classification in a consistent place will also reduce the costs to investors when searching for these items.[22]

21 Four companies in the sample of 100 companies are excluded from this table because they present operating cash flows using the direct method.

22 Companies with specified main business activities are required to classify interest received, interest paid and dividends received in a single category in the statement of cash flows (see Section 2.5).

Academic research shows that the classification options in IAS 7 lead to diversity in the presentation of cash flows from interest and dividends. A study of 798 companies from 13 European countries found that in cash flows from operating activities, 76% of the sample included interest paid, 60% included interest received and 57% included dividends received in these cash flows. The study concluded that this kind of diversity in presentation hinders the comparability of reported cash flows from operating activities.[23]

The IASB has also observed diversity in the presentation of cash flows arising from interest and dividends (see Table 9).

Table 9—Classification of interest and dividends in the statement of cash flows

	Number of companies			
	Interest received	Interest paid	Dividends received	Dividends paid
Classified in operating cash flows	46	48	35	1
Classified in investing cash flows	31	0	37	0
Classified in financing cash flows	1	39	0	92
Classified in multiple categories	0	3	2	0
Classification unclear	22	10	26	7
Total	100	100	100	100

MPMs

What investors said:

'It is not always clear how and why the calculation of APMs has changed since a previous reporting period.'

IFRS 18 requires companies to explain how their MPMs are calculated, as well as to disclose changes to MPMs. Companies are also required to restate comparative information when they change the calculation of their MPMs or introduce new MPMs, except when doing so would be impracticable.

These requirements will improve the comparability of information between reporting periods for the same company.

23 E A Gordon, E Henry, B N Jorgensen, C L Linthicum, 'Flexibility in cash-flow classification under IFRS: determinants and consequences', *Review of Accounting Studies*, vol 22, no 2, March 2017, pages 839–872.

3.3—Transparency of alternative performance measures

The IASB expects that requirements in IFRS 18 to provide information about APMs that meet the definition of MPMs will make those measures more transparent.

The CFA institute survey result said that investors found APMs useful as a valuation input, indicator of accounting quality and starting point for analysis.[24]

Investors said that APMs often provide useful information about a company's financial performance. The IASB therefore included requirements in IFRS 18 that will improve the transparency of some APMs, enabling investors to better assess the relevance of individual measures.

Investors' concerns about APMs

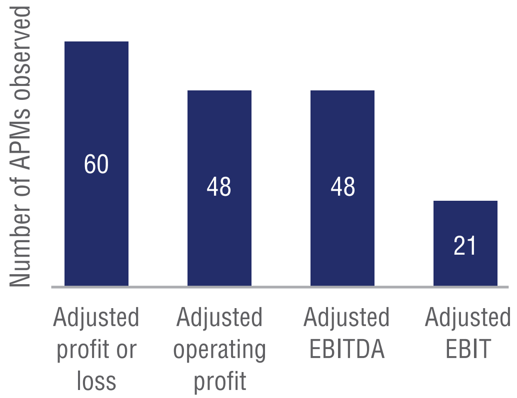
What investors said:

'The disclosure of APMs sometimes lack transparency into the calculation and reasons for providing those measures.'

'Even when companies do provide information about APMs in public communications, it is often difficult to find.'

Figure 11 shows the diversity in companies' selection of APMs. Companies do not always explain how they calculate their APMs or why they are providing such measures.

Figure 11—Common APMs other than those labelled operating profit, EBIT, profit before financing or EBITDA[25]



24 V Papa, S J Peters, K Schacht, *Investor Uses, Expectations and Concerns on Non-GAAP Financial Measures*, CFA Institute, 2016. In the context of accounting quality, the CFA Institute said that alternative performance measures (APMs) are used 'to help assess earnings quality' and 'to identify management misreporting incentives and choices'.

25 The IASB's study of APMs was generally based on measures included in the annual report or financial statements of each company in the sample of 100 companies. Additional measures might have been identified if other documents, such as earnings releases or presentation materials, had also been analysed. Some companies used more than one APM, and therefore the total is greater than the sample size of 100.

Table 10 and Table 11 show that companies disclose information about APMs in a variety of locations. Table 11 shows that EBITDA is frequently provided outside financial statements.[26]

Table 10—Location of information about APMs[27]

	% of APMs observed
Provided in the financial statements	41%
Provided *only* outside the financial statements	59%

Table 11—Use of measures labelled EBITDA by non-banking and non-insurance companies[28]

	Number of companies
Provided in the financial statements	26
of which presented as a subtotal in the income statement and disclosed in the notes	*1*
of which only disclosed in the notes	*25*
Provided only in sections of the annual report other than the financial statements	32
Not provided	27
Total	85

What investors said:

'The quality of the disclosures provided about APMs varies between jurisdictions and depends on whether the measures are subject to regulation, the type of regulation and how strictly the regulations are enforced.'

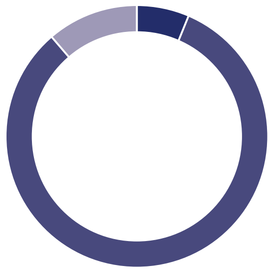
'We don't have enough information to make adjustments when we disagree with items adjusted for in these measures.'

The information companies provide about APMs does not always show how these measures relate to measures defined in IFRS Accounting Standards.

The IASB's analysis shows that (see Figure 12):

- not all companies provide a reconciliation between APMs and totals or subtotals presented in the statement of profit or loss; and
- only a limited number of companies provide detailed information related to the income tax effect on adjusting items.

Figure 12—Reconciliation of APMs[29]



7% Reconciliation provided with detailed information on tax effects

79% Reconciliation provided with limited or no information on tax effects

14% No reconciliation provided

Even if a company provides a reconciliation for APMs, in some jurisdictions that information is not subject to audit when provided outside of financial statements.

26 The analysis of measures labelled profit before financing or EBIT is covered in Section 3.1.
27 The sample only includes measures other than those labelled operating profit, EBIT, profit before financing or EBITDA.
28 No companies in the banking or insurance industries in the IASB's sample of 100 companies presented or disclosed a subtotal labelled EBITDA.
29 The sample only includes measures other than those labelled operating profit, EBIT, profit before financing or EBITDA.

In the IASB's analysis of the reconciliation between APMs and totals or subtotals presented in the statement of profit or loss, items frequently included in the reconciliation were:

- restructuring costs;
- gains or losses on disposal of property, plant or equipment, intangible assets or investments;
- impairment losses on property, plant or equipment;
- impairment and amortisation of intangible assets, including amortisation of intangible assets recognised in business combinations;
- fair value remeasurements on financial instruments;
- acquisition-related costs; and
- legal expenses.

Improvements to transparency of some APMs

Disclosure in financial statements

The IASB expects the disclosure of information about MPMs to help companies communicate their performance to investors and to help investors better understand the company's performance.

IFRS 18 defines MPMs and requires a company to disclose information about those measures in the financial statements (see Section 2.3). If an APM meets the definition of an MPM, it is subject to the disclosure requirements in IFRS 18. Although not all performance measures defined by management meet the definition of MPMs in IFRS 18, the IASB expects that the disclosure requirements will improve discipline and transparency in the use of measures that meet the definition of MPMs.

In particular, IFRS 18 requires disclosure of information about MPMs in a single location in the notes to the financial statements, making it easier for investors to access complete information about such measures.

This single note will include a reconciliation to the most directly comparable subtotal listed in IFRS 18 or total or subtotal required by IFRS Accounting Standards. A company will be required to apply the principles of aggregation and disaggregation (see Section 2.4) when grouping items in the reconciliation.

A company will also be required to disclose the income tax effect and the effect on non-controlling interests for each reconciling item.

The reconciliation will improve investors' understanding of the relationship between MPMs and the totals or subtotals in the statement of profit or loss. The information about the income tax effect and the effect on non-controlling interests will enable investors to calculate an adjusted version of the MPM if they disagree with an adjustment that the company has used in its calculation.

Disclosure in interim financial statements

The IASB expects that requiring the same disclosures in both annual and interim financial statements, especially the reconciliation of MPMs, will make those measures more transparent to investors.

The IASB's analysis of its sample of companies shows that at least 75% of APMs (other than those labelled operating profit, EBIT, profit before financing or EBITDA) that were included inside or outside annual financial statements were also disclosed for interim periods. However, the analysis also showed variation in the location in which those APMs were disclosed among the companies, similar to the disclosure of APMs in annual reporting. Some companies included information on APMs in interim financial statements while others provided it in the management discussion and analysis (MD&A) section in interim reports or earnings releases for the interim period.

When a company issues condensed financial statements or a complete set of financial statements for an interim period and uses measures that meet the definition of MPMs in its public communications for the interim period, the company is required to provide the MPM disclosures relating to those measure in the notes to those financial statements.

Improvement to transparency through audit

The disclosures required for MPMs will be included in the financial statements and therefore, in many jurisdictions, these disclosures will generally be subject to audit. The IASB expects that assurance by auditors will help improve transparency and discipline in the reporting of these measures.

4—Costs

4.1—Costs for companies

The IASB expects that all companies will incur some implementation costs, and possibly some ongoing costs, in applying IFRS 18 and the accompanying amendments to IAS 7.

Implementation costs will vary depending on the company's current systems and reporting practices.

Some companies will incur lower costs than others in implementing IFRS 18. For example, a company is likely to incur lower costs if:

- the current reporting practices are similar to the requirements in IFRS 18; or
- most of the information required to apply IFRS 18 is available through its current systems.

Implementation costs

The likely implementation costs identified by the IASB relate to changes in internal processes for preparing the financial statements, changes to information systems, training for staff and management and communicating changes to reported information to internal and external parties.

Implementation costs are likely to arise from the requirements to:

- classify income and expenses into categories in the statement of profit or loss;
- identify and provide disclosures for MPMs, including disclosure of the income tax effect and effect on non-controlling interests for adjustments made in calculating those measures;
- group information applying the principles of aggregation and disaggregation;
- disclose specified expenses by nature; and
- implement changes to the statement of cash flows.

Operating, investing and financing categories

Some companies will need to change their internal processes and adapt their accounting systems to comply with the requirements to classify income and expenses into categories in the statement of profit or loss.

Management of foreign exchange and derivatives

The costs of applying IFRS 18 are likely to be higher for companies with large volumes of derivatives and foreign currency-denominated items that are managed centrally.

Such companies might incur additional costs to classify foreign exchange differences and derivatives in the relevant categories of the statement of profit or loss. For example, a company might decide to set up a system to track the underlying items giving rise to foreign exchange differences.

> In the fieldwork the IASB conducted after publishing the Exposure Draft, about 40% of participating companies indicated they might need to change their systems or internal processes to apply the proposed requirements for the classification of foreign exchange differences.[30]

30 The IASB did not propose an undue cost or effort relief for the classification of foreign exchange differences in the Exposure Draft. The IASB introduced the relief in response to feedback on the proposal in the Exposure Draft to require companies to classify foreign exchange differences in each category in the statement of profit or loss.

Some companies have limited transactions denominated in a foreign currency or use derivatives only in limited circumstances. For example, a company might recognise foreign exchange differences only from trade receivables denominated in foreign currencies and use derivatives only to hedge the foreign currency risk on those trade receivables.

In such cases, the company is required to classify all foreign exchange differences and gains and losses on derivatives in the operating category. Such companies are likely to incur limited costs to classify such income and expenses into categories in the statement of profit or loss.

> IFRS 18 includes cost mitigations for the classification of foreign exchange differences and gains and losses on derivatives (see Section 4.2).

Other costs relating to categories

The costs of classifying income and expenses into categories are likely to vary depending on the granularity of income and expense accounts in a company's current accounting systems. If a company has a detailed chart of accounts, the cost may be limited to remapping each account to the categories in the statement of profit or loss.

However, if a company records some types of income or expense in aggregated accounts with labels such as 'other income' or 'other expenses' and does not have a method to capture more detailed information, the costs are likely to be higher. The company will need to investigate the details of the income and expenses in those accounts, assess the classification of them, create new accounts and change its processes to classify income and expenses in the appropriate categories. Companies that have many subsidiaries using varied accounting systems may incur additional costs.

Changes in the classification of income and expenses in the statement of profit or loss may affect the company's key performance indicators (KPIs), budgets or forecasts. If the company needs to revise these indicators when it applies IFRS 18, it is likely to incur additional costs.

The requirements to present new subtotals and line items mean that companies that digitally report their financial statements will need to retag their financial statements for these subtotals and line items. Retagging is likely to involve some one-time costs (see Section 5.1).

The IASB expects that once a company has developed processes for classifying income and expenses into the categories in the statement of profit or loss, it is not likely to incur ongoing incremental costs to implement the requirements for subtotals and categories.

When should a company begin its assessment of classification of income and expenses?

A company is required to apply IFRS 18 retrospectively, which means restating comparative information when it first applies IFRS 18.

For some companies it will be difficult to change the classification of income and expenses retrospectively because their systems did not previously capture the required information. Those companies are likely to need to start the work sooner in order to complete their assessment of classification of income and expenses before the beginning of the comparative period(s)—1 January 2026 if the company applies IFRS 18 on its effective date of 1 January 2027 and presents one year of comparative information.

Companies that prepare interim financial reports in the first year of applying IFRS 18 are required to present each subtotal required by IFRS 18 in their condensed financial statements—including information for the comparative period(s). Therefore, such companies should also allow time and budget for preparing interim financial report(s) in the first year of applying IFRS 18.

Disclosures for MPMs

The costs for implementing the disclosure requirements related to MPMs are expected to vary by company.

Companies that already communicate using measures that are MPMs will incur some costs to implement IFRS 18 if they do not currently provide all the required disclosures and continue to use those measures in public communications after applying IFRS 18.

In some jurisdictions that already have regulatory guidance or requirements for APMs, such as the European Union, the United Kingdom, Canada and Australia, companies may already have some of the information required for the disclosure of MPMs.

Companies that do not communicate using measures that are MPMs will not incur costs related to the requirements for MPMs.

Reconciliation of MPMs

Companies that communicate using measures that are MPMs are likely to incur costs in providing a reconciliation between those measures and the most directly comparable subtotal listed in IFRS 18 or total or subtotal required by IFRS Accounting Standards, and in providing the other disclosures required for MPMs (see Section 2.3).

For companies that already provide such a reconciliation and make these disclosures, the incremental costs of including these disclosures in the financial statements are likely to be limited.

The reconciliation is expected to be subject to audit (see Section 3.3). Some companies will need to develop or revise the internal processes they use for preparing the reconciliation and will incur costs in having the reconciliation audited.

The requirement to disclose the income tax effect and the effect on non-controlling interests for each adjusting item in the MPM reconciliation will result in costs for many companies. Determining the income tax effect could be more challenging if a company adjusts for items that arise in different tax jurisdictions.

IFRS 18 includes cost mitigations for the identification of MPMs and a simplified approach to calculating the income tax effect (see Section 4.2).

Are there likely costs for a company that continues to communicate with investors using the same subtotal of income and expenses it used before applying IFRS 18?

The subtotal would meet the definition of an MPM unless:

- it is listed in IFRS 18 or specifically required by IFRS Accounting Standards; or
- the company rebuts the presumption that a subtotal of income and expenses used in public communications communicates management's view (see Section 2.3).

Companies will provide disclosures for MPMs for these subtotals, which may result in additional costs for such companies.

For example, assume that before applying IFRS 18, a company:

- disclosed adjusted EBIT (EBIT adjusted for non-recurring items determined by the company) in its public communications;
- provided no information related to the adjusted EBIT other than a reconciliation between adjusted EBIT and profit before income taxes, which was disclosed outside the financial statements; and
- did not disclose the income tax effect and effect on non-controlling interests.

In this case, if the company continues to disclose adjusted EBIT after applying IFRS 18, the company will:

- consider which total or subtotal is the most directly comparable with adjusted EBIT. This may require the company to change the total or subtotal to which adjusted EBIT is reconciled.
- disclose information about adjusted EBIT such as qualitative information about why the measure provides useful information about the company's financial performance and how the measure is calculated, including how the company determined the adjusting items. This may require the company to provide additional information on how the reconciling items relate to the statement of profit or loss.
- disclose the income tax effect and effect on non-controlling interests for each reconciling item. This may require the company to gather additional information.

Grouping of information

Application of the principles for grouping of information

Applying the principles of aggregation and disaggregation is likely to result in incremental costs for most companies.

Some companies will incur costs in implementing an internal process to ensure compliance with the aggregation and disaggregation requirements in IFRS 18.

Some companies may also incur costs in applying the requirements to disaggregate some items that they currently aggregate under the label 'other'.

Presentation of expenses classified in the operating category

Companies are likely to incur implementation costs for assessing how to present expenses in the operating category using the new guidance on classification by nature or function (see Section 2.4).

If a company determines that it is required to change the way it presents expenses in the operating category as a result of that assessment, it will incur additional costs to implement the change. For example, if a company determines that it needs to change from classification of expenses by nature to classification of some or all operating expenses by function, it will need to change its systems and internal processes accordingly.

Disclosure of specified expenses by nature

Companies that will be required to disclose the five specified expenses by nature—depreciation, amortisation, employee benefits, impairment losses and write-downs of inventories—will incur costs if they currently disclose only limited information about some of these expenses.

For example, if a company is currently disclosing only the total amounts of depreciation, amortisation and employee benefits, it will need to gather additional information to disclose the amount of each of the five specified expenses included in each line item in the operating category of the statement of profit or loss.

The IASB introduced some cost mitigations in IFRS 18 related to disclosing information about expenses by nature (see Section 4.2).

Why did the IASB identify these five items for the disclosure requirement?

IFRS 18 requires a company to disclose the amounts for these five items because:

- limiting the requirement to five items results in useful information for investors without causing undue costs for preparers.
- depreciation, amortisation and employee benefits will likely be included in more than one function line item in the statement of profit or loss. Disaggregated information about them is generally useful for understanding a company's business, regardless of its industry.
- some stakeholders view impairment losses as similar to depreciation or amortisation (because of their non-cash nature).
- impairment losses and write-downs of inventories are sometimes included in more than one line item in the statement of profit or loss. Even if they are included in only one line item, disclosure in a single note together with other nature expenses would make such information more accessible for investors.

Statement of cash flows

The IASB expects that the requirement to use operating profit as the starting point for the indirect method of reporting cash flows from operating activities may result in costs for some companies to adapt their systems. Costs will depend on the company's current starting point for reporting cash flows from operating activities, and the extent to which they prepare the statement of cash flows automatically from data in their accounting systems.

The removal of alternatives in the classification of interest and dividend cash flows required by the amendments to IAS 7 is not expected to be costly to implement because companies typically already have the necessary information to implement the change. However, some companies may incur costs to adapt their systems to reflect those changes.

Costs for education and communication

The IASB expects that companies will also incur costs for internal education and external communications when they first apply IFRS 18.

Costs for internal education

The IASB expects that companies will incur costs for educating staff on the requirements in IFRS 18. Staff will need to be trained, for example, in understanding the classification of income and expenses into categories in the statement of profit or loss.

Applying IFRS 18 may lead to changes in formulas for calculating the remuneration of management and other employees (discussed in Section 5.2), or in the company's KPIs. If this is the case, companies may incur additional costs for educating all employees and executives on the requirements in IFRS 18 that will affect remuneration and the company's KPIs.

Costs for external communications

The IASB expects that companies will incur costs in communicating with external parties, such as investors and lenders, about the changes in its reported information, including:

- variations in the structure of the statement of profit or loss and the content and amount of operating profit if the company presented an operating profit subtotal before applying IFRS 18 (see Section 2.2);
- which APMs are MPMs and therefore which information will be disclosed in the financial statements (see Section 2.3); and
- any changes made in the presentation and disclosure of items in the financial statements as a result of applying the principles of aggregation and disaggregation (see Section 2.4).

Ongoing costs

The IASB expects that most costs related to the requirements in IFRS 18 will be one-time implementation costs. However, companies might incur some ongoing costs in applying parts of IFRS 18 when there are changes in a company's business, how it operates or how it communicates performance.

For example, when there is a significant change to a company such as a business combination or a restructuring, the company may be required:

- to exercise judgement on whether the change affects the assessment of the company's main business activities, which would lead to changes in the classification of income and expenses in the statement of profit or loss (see Section 2.2);
- to consider whether the change leads to an addition, change or cessation of MPMs, which would require new information to be disclosed because of the change in its business (see Section 2.3); and
- to consider whether to change the line items, totals and subtotals the company presents in the primary financial statements and discloses in the notes to achieve their roles (see Section 2.4).

Even if there are no significant changes to a company's business, requirements in IFRS 18 may result in ongoing costs when, for example:

- a company's processes require the collection of data manually; or
- a company has items labelled as 'other' that need to be disaggregated into items to be separately presented in the primary financial statements or disclosed in the notes, because the composition of 'other' changes from period to period.

However, such ongoing costs are expected to decrease gradually or be eliminated as new systems are implemented and processes and procedures become embedded in the company's ordinary routines.

4.2—Cost mitigations for companies

The IASB introduced the cost mitigations summarised in Table 12 to ensure that, in providing useful information to investors about their performance, companies will not incur undue costs.

Table 12—Overview of cost mitigations in IFRS 18

	Cost mitigations
Subtotals and categories	• Reliefs for undue cost or effort for classification in the statement of profit or loss of: o gains or losses on derivatives not designated as hedging instruments applying IFRS 9 *Financial Instruments*; and o foreign exchange differences • Accounting policy choice for companies that provide financing to customers as a main business activity • Grouping of assets with shared characteristics for purposes of assessing whether investments are made as a main business activity
MPMs	• Exclusion of some communications from public communications • Rebuttable presumption in the definition of MPMs • Simplified approach to calculating income tax effects for each reconciling item disclosed in MPM reconciliations
Grouping of information	• Limiting the requirement to disclose specified expenses by nature to five • Amounts disclosed for nature expenses may be the cost incurred for the period

Simplifications and reliefs for subtotals and categories

Undue cost or effort reliefs for the classification of income and expenses

The IASB acknowledged that some of the classification requirements could impose substantial implementation costs on some companies. Therefore, IFRS 18 includes reliefs for classification in the statement of profit or loss for two items summarised in Table 13.

Table 13—Undue cost or effort reliefs for classification of income and expenses

Item	Details of undue cost or effort relief
Derivatives used to manage identified risks but not designated as hedging instruments applying IFRS 9	A company will classify all gains and losses on those derivatives in the operating category if classifying gains and losses in the category of the statement of profit or loss affected by the risk managed would involve undue cost or effort.
Foreign exchange differences	A company will classify foreign exchange differences in the operating category if classifying them in the same category as the income and expenses from the items that gave rise to them would involve undue cost or effort.

Accounting policy choice for companies that provide financing to customers as a main business activity

If a company provides financing to customers as a main business activity, IFRS 18 permits it to choose to classify income and expenses from liabilities in the operating category or in the financing category if those liabilities (see Section 2.2):

- arise from transactions that involve only the raising of finance; and
- do not relate to the provision of financing to customers.

If a company chooses to classify income and expenses from these liabilities in the operating category, income and expenses from all liabilities that arise from transactions that involve only the raising of finance will be classified in the operating category. Such a company is therefore not required to separate those liabilities into liabilities that relate—and do not relate—to the provision of financing to customers.

IFRS 18 also introduces a similar accounting policy choice to classify in the operating category or in the investing category income and expenses from cash and cash equivalents that do not relate to providing financing to customers. This accounting policy choice is for companies that do not invest in financial assets as a main business activity but provide financing to customers as a main business activity.

Grouping of assets to assess whether investments are made as a main business activity

IFRS 18 permits a company to assess whether it invests in assets as a main business activity by assessing groups of assets with shared characteristics. For example, a company may invest in only a single type of asset, such as investment properties, for which the outcome of the assessment will be the same for each property. Permitting companies to conduct the assessment for groups of assets is expected to reduce the cost of the assessment.

Simplifications and reliefs for MPMs

Scope of public communications

For the purpose of defining MPMs, IFRS 18 excludes the following from public communications (see Section 2.3):

- oral communications;
- written transcripts of oral communications; and
- social media posts.

The IASB expects these media channels to contain information already included in other forms of communication, so the risk of excluding measures that would otherwise meet the definition of an MPM is low.

Some stakeholders said that these types of communications are the most challenging to monitor. Removing these types of communication is expected to reduce the costs of applying the definition of MPMs by eliminating the need for companies and auditors to search them.

Rebuttable presumption in the definition of MPMs

Companies need not make the required disclosures about a subtotal used in public communications if there is reasonable and supportable information demonstrating that:

- the subtotal does not communicate management's view of an aspect of the company's financial performance; and
- the company has a reason for using the subtotal in its public communications other than communicating management's view of an aspect of the company's financial performance.

IFRS 18 includes application guidance on what is considered reasonable and supportable information. For example, the fact that a subtotal is required to be included in a public communication by law or regulation would be reasonable and supportable information demonstrating that a company has a reason for using a subtotal in its public communications other than to communicate management's view of an aspect of the company's financial performance.

If the company rebuts the presumption, the subtotal will not be an MPM.

The IASB expects that excluding such subtotals from their MPM disclosures will reduce costs for companies without affecting the objectives of disclosing information about MPMs.

Simplified approach for calculating the income tax effect for items disclosed in the reconciliation

In determining the income tax effect for each item disclosed in a reconciliation between an MPM and the most directly comparable subtotal listed in IFRS 18 or total or subtotal required by IFRS Accounting Standards, IFRS 18 gives companies the option of calculating the income tax effects using:

- the statutory tax rates applicable to the transactions in the tax jurisdictions concerned;
- a reasonable pro rata allocation of the current and deferred tax of the company in the tax jurisdictions concerned; or
- another method that achieves a more appropriate allocation in the circumstances.

The IASB expects that providing these options will reduce the costs of calculating the income tax effect for each item in the MPM reconciliation.

Simplifications and reliefs for grouping of information

Amount disclosed for specified expenses by nature

When companies make their required disclosures of the five specified expenses by nature (depreciation, amortisation, employee benefits, impairment losses and write-downs of inventories), the amounts disclosed need not be the amounts recognised as an expense in the statement of profit or loss in the reporting period.

For example, a company could include amounts in the disclosure that have been recognised as part of the carrying amounts of assets.

Some companies said that, for the five specified expenses by nature, it could be too costly to determine the amounts recognised as an expense during a reporting period. They were concerned that companies might incur undue costs to track amounts not immediately recognised as an expense in the statement of profit or loss but instead included in the carrying amount of assets—for example, inventories.

Investors said that their information needs could be met by a reasonable approximation of the amounts of specified operating expenses by nature in each line item. The IASB concluded that information about the costs incurred would meet those needs.

Exemptions from general disaggregation requirements

IFRS 18 specifically requires companies to disaggregate information if any of the resulting information is material. If required to apply this requirement to operating expenses reported in function line items, companies would be required to disclose information about each operating expense by nature in the notes, if it were material.

Such a requirement could have involved costs for companies that outweigh the benefits of providing that information to investors. A company that reports operating expenses by function would incur additional costs to identify material information about operating expenses by nature, including costs to identify whether such information would be material. The IASB therefore decided to limit the disclosure requirements for such companies by including exemptions to the requirement in IFRS 18 to disaggregate material information in relation to operating expenses by nature.

4.3—Costs for investors and other stakeholders

Costs for investors

The IASB expects that the costs for investors will arise mostly from adjusting their models and methods of analysis to the new structure of the statement of profit or loss and the additional information provided. Such costs will be incurred when IFRS 18 is first implemented.

Investors might incur further costs from assessing long-term trend information. Investors will bear these costs because they consider trends over longer periods such as five years whereas most companies present comparative information for just one or two years in the financial statements. The costs to investors of assessing trend information is likely to relate to estimating the effects of IFRS 18 on the statement of profit or loss for prior comparative periods—which IFRS 18 does not require companies to do.

However, the IASB expects that IFRS 18 will ultimately save costs for investors by requiring companies to provide them with more information that they need for their analyses.

Costs for regulators and auditors

The IASB expects that regulators will incur some costs relating to the requirements in IFRS 18—for example, a regulator may incur costs to revise regulatory templates and to develop procedures to regulate the new requirements. The costs incurred by regulators are expected to vary by jurisdiction because regulations are specific to each jurisdiction.

In some jurisdictions, some amounts reported applying IFRS Accounting Standards fulfil regulatory and prudential requirements. Therefore, changes to presentation and disclosure requirements introduced by IFRS 18 might affect regulatory reporting.

If a regulator requires companies to disclose information about APMs outside the financial statements, the regulator may need to consider the relationship of such regulatory requirements and the requirement in IFRS 18 to disclose information about MPMs.

A regulator is also likely to incur ongoing costs to enforce the new requirements for MPMs and the grouping of information.

The IASB expects that auditors will incur implementation and ongoing costs for auditing the disclosures related to MPMs—which will be included in the financial statements—because they will be subject to audit in many jurisdictions.

Likely costs for auditors include:

- costs of auditing a company's internal controls and procedures relating to disclosures of MPMs; and
- costs of expanding the audit scope to assess whether a company discloses information required by IFRS 18 in the financial statements for all measures that are MPMs.

In addition, auditors are expected to incur ongoing costs in evaluating the judgements made by companies in applying IFRS 18, such as the judgements a company makes on presentation of line items in the primary financial statements and disclosure of items in the notes.

5—Other effects

5.1—Effects on digital reporting

IFRS Accounting Taxonomy

In some jurisdictions, companies are required to provide both paper-based and digital financial statements.

The IFRS Accounting Taxonomy reflects the presentation and disclosure requirements of IFRS Accounting Standards and includes elements from the accompanying materials such as Implementation Guidance and Illustrative Examples.

The IASB is developing an IFRS Accounting Taxonomy Update incorporating the requirements of IFRS 18. The IASB expects the update to be available 9–12 months after IFRS 18 is issued.

Digital reporting for investors

Investors require digital information that:

- is comparable between companies and periods;
- communicates company-specific information;
- is in an easily usable format;
- is consistently available; and
- is free from errors.

However, digital information that comes directly from companies does not always meet these requirements. As a result, many investors instead rely on paid services from information intermediaries, such as data aggregators, who can supply data that has been standardised and is comparable.

The IASB expects that IFRS 18 will contribute to improving the quality of digital reporting (for example, through the presentation of defined subtotals in the statement of profit or loss and the disclosure of information related to MPMs). Table 14 analyses the likely effects of the IFRS 18 requirements on digital reporting.

Table 14—Likely effects of IFRS 18 on digital reporting

Investor needs	Current practice	Likely effects of IFRS 18
Comparable between companies and periods	Diversity in reporting practices results in companies tagging: • comparable data in various ways; and • non-comparable data in the same way. Investors often assume information tagged using the same IFRS Accounting Taxonomy element is comparable, but that is not always the case.	The new structure for the statement of profit or loss will reduce diversity in reporting practices, which will reduce diversity in tagging. The subtotals defined in IFRS 18 will be comparable between companies and will give investors an anchor point, which they can use to develop a 'mental map' of the statement of profit or loss when they extract data points.
Communicate company-specific information	Company-specific information, such as APMs are: • tagged using extensions; or • not tagged at all—some APMs are not required to be tagged by some regulators. Therefore, such information is difficult to extract and analyse.	Disclosures of information about MPMs (including reconciliations to the most directly comparable subtotal listed in IFRS 18 or total or subtotal required by IFRS Accounting Standards) are included in a single note to the financial statements, making them more likely to be tagged. New IFRS Accounting Taxonomy elements resulting from the new disclosure requirements will reduce the need for companies to create their own extensions.
Available in an easily usable format	Investors either use information intermediaries or need to invest time in understanding XBRL (eXtensible Business Reporting Language) calculations and make manual adjustments to normalise subtotals and otherwise make data comparable.	The cost of using digital data will be reduced through: • enhanced comparability of subtotals between companies; and • required disclosure of MPMs in a single note, which will make such measures easier to extract.
Consistently available	The IFRS Accounting Taxonomy contains elements for commonly reported line items and subtotals such as operating profit. However, not all companies report such line items and subtotals, making it difficult to compare large samples of companies.	Required subtotals in IFRS 18 of operating profit and profit before financing and income taxes will be consistently available. A company would be expected to tag two subtotals required by IFRS 18 even if the two subtotals are equal and presented as a single amount with a label that represents both subtotals.
Free from errors	Tagged information in digital financial statements is not free from errors.	There is no evidence that IFRS 18 will have a significant effect on the number of errors.

5.2—Effects on contracts, agreements and compensation

Contracts and agreements

IFRS 18 affects the presentation and disclosure of information in the financial statements. IFRS 18 does not change the way companies recognise and measure items in the financial statements and therefore does not affect companies' overall financial performance and financial position. However, the IASB observed that when information reported in financial statements is used to monitor compliance with contracts and agreements, the new requirements might affect those contracts and agreements.

For example, covenants in banking and loan agreements might impose minimum requirements for measures such as the operating profit subtotal presented in a borrower's financial statements. Many companies that present such subtotals might need to change what they include in the subtotals to align with the requirements in IFRS 18 (see Section 2.2).

In such cases, the parties to the contract or agreement will need to consider how the changes introduced by IFRS 18 could affect the contract or agreement. In contrast, the changes introduced by IFRS 18 will have no effect on loan covenants that specify the calculation of such requirements without reference to amounts in financial statements.

Compensation

Many companies have remuneration policies for management based on particular measures in the statement of profit or loss. In the IASB's sample of 100 companies, performance measures commonly linked to management remuneration included operating profit, EBIT, EBITDA, profit or loss (net income) and other APMs, such as adjusted operating profit and adjusted net income.

IFRS 18 defines operating profit (see Section 2.2) and requires a company to disclose information about MPMs (see Section 2.3). Companies with management remuneration policies based on particular measures in the statement of profit or loss will need to consider whether to change their policies to reflect changes to those measures when applying IFRS 18.

For example, if a company's operating profit presented after applying IFRS 18 is different from the company's operating profit as reported prior to applying IFRS 18, the company might consider whether to change the measure in the remuneration policy to operating profit as defined in IFRS 18.

In addition, if measures linked to management remuneration meet the definition of MPMs, a company will provide the MPM disclosures for such measures.

Appendix—Case study: Statement of profit or loss

Case study: Statement of profit or loss

This case study illustrates changes in the classification of six items of income and expenses for a manufacturer that does not have any specified main business activities.

Statement of profit or loss applying IAS 1		
Revenue	350,000	
Cost of sales	(200,000)	
Gross profit	150,000	
Other operating income	15,000	1
Selling expenses	(30,000)	
General and administrative expenses	(45,000)	2
Research and development expenses	(20,000)	
Share of profit from associates and joint ventures	3,500	3
Other operating expenses	(6,000)	
Operating profit	67,500	
Finance income	500	4
Finance costs	(7,500)	5, 6
Profit before income taxes	60,500	
Income tax expense	(15,500)	
Profit	**45,000**	

	Statement of profit or loss applying IFRS 18[31]		
	Revenue	350,000	Operating
	Cost of sales	(200,000)	Operating
	Gross profit	150,000	Operating
	Other operating income	10,500	Operating
	Selling expenses	(30,000)	Operating
	General and administrative expenses	(44,000)	Operating
	Research and development expenses	(20,000)	Operating
5	Other operating expenses	(7,500)	Operating
	Operating profit	**59,000**	
3	Share of profit from associates and joint ventures	3,500	Investing
1, 4	Other investment income	5,000	Investing
	Profit before financing and income taxes	**67,500**	
6	Income and expenses on borrowings	(6,000)	Financing
2	Interest expense on lease and pension liabilities	(1,000)	Financing
	Profit before income taxes	60,500	
	Income tax expense	(15,500)	
	Profit	**45,000**	

Change in the classification of income and expenses after applying IFRS 18	
1	Fair value gains and rental income from investment properties will be classified in the investing category (included in other operating income before IFRS 18)
2	Net interest expense on net defined benefit liabilities will be classified in the financing category (included in general and administrative expenses before IFRS 18)
3	Income and expenses from associates and joint ventures accounted for using the equity method will be classified in the investing category (included in operating profit before IFRS 18)
4	Interest income on cash and cash equivalents will be classified in the investing category (included in finance income before IFRS 18)
5	Foreign exchange differences arising from trade receivables will be classified in the operating category (included in finance costs before IFRS 18)
6	Foreign exchange differences arising from borrowings will be classified in the financing category (included in finance costs before IFRS 18)

31 The line items illustrate what is included in each category and do not denote line items that any particular company would present. Gross profit and profit before income taxes are presented as additional subtotals because they are necessary for the statement of profit or loss to provide a useful structured summary of income and expenses.

Important information

This Effects Analysis accompanies, but is not part of, IFRS 18 *Presentation and Disclosure in Financial Statements*.

Other relevant documents

IFRS 18 *Presentation and Disclosure in Financial Statements*—specifies requirements for the presentation and disclosure of information in general purpose financial statements.

Basis for Conclusions on IFRS 18—summarises the IASB's considerations in developing the requirements in IFRS 18.

Illustrative Examples on IFRS 18—illustrates aspects of IFRS 18 without interpretative guidance.

Supporting Materials—includes flowcharts of key requirements in IFRS 18.

Project Summary on IFRS 18—provides an overview of the project to develop IFRS 18.

Feedback Statement on IFRS 18—summarises feedback on the proposals that preceded IFRS 18 and the IASB's response.

Reference Materials—includes a table of concordance and a comparison of the requirements in IAS 1 and IFRS 18.

IFRS 18 on one page.

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