STAFF PAPER

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IASB Meeting

Project	**Improvements to IFRS 8 *Operating Segments* arising from the post-implementation review**
Paper topic	Proposed amendment to the aggregation criteria for segments

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Objective

1. The objective of this paper is to discuss the proposal in Exposure Draft *Improvements to IFRS 8 Operating Segments* (Proposed amendments to IFRS 8 and IAS 34) (Exposure Draft) that aimed to help apply the aggregation criteria.

2. IFRS 8 permits an entity to aggregate operating segments for disclosure purposes where the segments exhibit similar economic characteristics. The proposed amendments aimed to assist entities in applying the aggregation criteria by providing clarity on the meaning of similar economic characteristics.

3. In this paper we are asking the Board two questions:

   (a) Do you agree with the staff recommendation not to proceed, at this time, with the proposed amendment to clarify the meaning of similar economic characteristics?

   (b) Do you agree with the staff recommendation to monitor the US Financial Accounting Standards Board (FASB) project it is undertaking, specifically its work on the aggregation criteria?

Structure of the paper

4. This paper is structured as follows:

   (a) review of proposal and comments received on the Exposure Draft (paragraphs 5-10);

   (b) additional outreach (paragraphs 11-15); and

   (c) staff analysis and recommendations (paragraph 16-23).

   Appendix A – Overview of the US Financial Accounting Standards Board's (FASB) project – Segment Reporting

Review of proposal and comments received on the Exposure Draft

5. As part of the Post-implementation Review (PIR), we asked stakeholders questions relating to the implementation of the aggregation criteria requirements in IFRS 8. The key findings of the PIR[1] related to the aggregation criteria were:

   (a) there is too much aggregation of operating segments; and

   (b) there are practical difficulties in determining when operating segments may be aggregated.

6. Investors, in particular, expressed a view that the current aggregation basis does not assist them in developing valuation models because there is too much aggregation. Whereas preparers and auditors raised the concern about practical difficulties in determining when operating segments may be aggregated.

7. The proposed amendments aimed to assist entities in applying the aggregation criteria. The Exposure Draft inserted two examples of similar economic characteristics; similar long-term revenue growth, and similar long-term return on assets. IFRS 8 contains only one example and respondents to the PIR noted this was not sufficient for assessing whether two segments exhibit similar long-term performance. It was anticipated that providing further examples would reduce aggregation and thereby respond to investors' concerns.

[1] Findings extracted from page 23 of the July 2013 Report and Feedback Statement published by the Board.

8. The feedback to the Exposure Draft received some support for the proposed amendments; however, a number of questions[2] on how to apply the proposed amendments were raised. Overall respondents were still seeking clarity on the assessment of similar economic characteristics. For example, one respondent[3] stated:

> … it is not sufficiently clear the extent to which economic characteristics need to be similar in order to aggregate operating segments. We recommend that the Board provides additional guidance around similar economic characteristics.

9. Other respondents indicated that they were not sure if the amendments would result in any change in practice. The Canadian Accounting Standards Board[4] stated:

> We do not have any specific concerns with regards to Question 2(b), the proposed amendment to include further examples to the aggregation criteria in paragraph 12A of IFRS 8. However, we think that when applied in Canada, this amendment will not result in a change in the identification of any entity's reportable segments.

10. In summary although there were no strong objections to the proposed amendments, many respondents to the Exposure Draft thought that the amendments did not provide additional clarity and would not improve the application of the IFRS 8 requirements.

Additional outreach

11. Since November 2017, when we presented the feedback summary on the Exposure Draft to the Board, the staff have conducted further review of the feedback received on the Exposure Draft and undertaken additional outreach.

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[2] This paper does not contain a comprehensive analysis of all of the feedback received but rather is intended to provide a recap on the status of this amendment and actions taken since the November Board meeting.

[3] Comment letter from KPMG dated 31 July 2017.

[4] Comment letter from the Canadian Accounting Standards Board dated July 31, 2017.

12. The staff identified alternative approaches to clarifying application of the aggregation criteria to those proposed in the Exposure Draft. These alternatives were discussed at the Accounting Standards Advisory Forum (ASAF) meeting in December 2017. The alternative approaches discussed with ASAF were:

    (a) remove all of the aggregation criteria (but include a practical upper limit) in IFRS 8;

    (b) remove the aggregation criteria but retain the quantitative thresholds in IFRS 8; and

    (c) provide a more detailed list of factors to consider helping entities identify similar economic characteristics.

13. Approaches (a) and (b) are being considered by the FASB as part of its project on segment reporting. The FASB have not released any due process documents at this time. Extended preparer outreach is planned to take place later in 2018. The Appendix to this agenda paper provides an overview of the FASB project.

14. A number of ASAF members support approach (c), although one ASAF representative said that, in his view, whatever approach was adopted, there would not be a clear consensus from constituents.

15. Another ASAF representative said that if the Board were to continue with approach (c) it might be useful to add ‘a state of an entity’s maturity’ as one of the factors to be considered in assessing similar economic characteristics.

Staff analysis and recommendations

16. The proposed amendments to the aggregation criteria were proposed in order to respond to the PIR findings that clarification of the aggregation criteria was required. However, the responses to the Exposure Draft indicate that the proposed amendments have not provided the clarification intended and, as such, will not necessarily improve financial reporting.

17. As is described in the *Due Process Handbook*, a PIR is an opportunity to assess the effect of the new requirements of a new Standard, on investors, preparers and auditors. The *Due Process Handbook* also notes that there is no presumption that a PIR will lead to changes to a Standard.

18. In performing our staff analysis and arriving at a recommendation for the Board, we have considered the following questions:

    (a) Does the feedback indicate that the outcome of the proposed amendment(s) will achieve the objective set out in the Exposure Draft and address the finding(s) identified in the PIR?

    (b) Does the feedback indicate that there are further actions that should be taken with respect to the matter addressed in the proposed amendment(s)?

19. In response to the first question:

    (a) The findings identified in the PIR was that too much aggregation of operating segments takes place and preparers found it difficult to apply the aggregation criteria.

    (b) The objective of the Exposure Draft was to provide additional clarity to help address the practical difficulties in determining when operating segments may be aggregated.

    (c) The feedback to the Exposure Draft indicates that the proposed amendments will not result in additional clarity; in fact additional questions have been raised on how to apply the aggregation criteria.

20. In view of the above, the staff so not think the proposed amendments will significantly change practice. Consequently, the staff recommend the Board does not proceed with the proposed amendment as set out in the Exposure Draft.

21. In response to the second question:

    (a) The feedback indicates that there are still challenges encountered in applying the aggregation criteria to operating segments.

    (b) The FASB have added a project to its technical agenda on segments, which includes the aggregation criteria.

22. Although we are not recommending that the Board proceeds with the proposed amendments we are recommending that the Board continues to monitor the work that is being undertaken by the FASB. This recommendation takes into consideration:

    (a) practical challenges are still encountered in apply the aggregation criteria; and

    (b) the fact that IFRS 8 and Topic 280 are converged.

23. The staff are not, at this time, recommending that the Board itself develops further the proposals presented to the ASAF because we believe it would be more effective to monitor the work of the FASB. We recommend the Board decides on an appropriate direction for this proposed amendment based on the progress of the FASB project.

Questions for Board members

Questions
1. Do you agree with the staff recommendation not to proceed, at this time, with the proposed amendment to clarify the meaning of similar economic characteristics?
2. Do you agree with the staff recommendation to monitor the US Financial Accounting Standards Board (FASB) project it is undertaking specifically on the aggregation criteria?

Appendix A

Overview of US Financial Accounting Standards Board (FASB) project – Segment Reporting:[5]

A1. In September 2017 the FASB added a project to its Work Plan on:

(a) the aggregation criteria for operating segments; and

(b) segment disclosure requirements.

Aggregation criteria for operating segments

A2. The FASB is considering the following two approaches to the aggregation of operating segments:

(a) move the quantitative thresholds for determining a reportable segment as a number one step in the aggregation criteria, ie develop a bright line threshold for aggregation;[6] and

(b) remove the aggregation criteria altogether, but retain the practicable limit guidance (for example, a practical upper limit of 10 reportable segments).

A3. The FASB is considering potential changes to the quantitative thresholds (of revenue, profit or loss, and assets) that require separate disclosure about operating segments that meet those thresholds. Currently the FASB are establishing the parameters of the extended preparer outreach that the FASB and the FASB staff intend to undertake later this year.

Segment disclosure requirements

A4. For segment disclosure requirements, the FASB is considering three alternatives:

(a) add individual line items of segment information to the list of disclosure requirements (for example, gross margin, operating cash flows and working capital balances if this information is regularly reviewed by the CODM);

[5] http://www.fasb.org/jsp/FASB/FASBContent_C/ProjectUpdatePage&cid=1176169383606#decisions @ 14/02/2018

[6] Currently, the quantitative thresholds are a second step (ie it follows the assessment of the qualitative thresholds) in the aggregation criteria.

(b) require the disclosures in Topic 280, *Segment Reporting*, to be reported in a table; and

(c) require a table of regularly reviewed information based on how it relates to the line items in the financial statements. The next paragraph describes this alternative in more detail.

A5. Alternative (c) would require a table that:

(a) presents segment information by segment (ie one segment in one column);

(b) adds up the above information (in a separate column);

(c) has a column for reconciling items;

(d) which will ultimately lead to the numbers reported in an entity's financial statements. The novelty of the approach is that this final column will have all line items from an entity’s financial statements. In other words, if the entity reports, for example, only two pieces of segment information then there will be many blank fields within the table.