

21 September 2020

Mr Hans Hoogervorst
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Submitted to: www.ifrs.org

Dear Hans

ED/2019/7 *General Presentation and Disclosures*

Thank you for the opportunity to comment on ED/2019/7 *General Presentation and Disclosures*. The ED has been exposed for comment in New Zealand and some New Zealand constituents may comment directly to you.

We are very supportive of the IASB's projects to help make financial information more useful and improve the way financial information is communicated to users of the financial statements.

Overall comments

We support the proposals to provide more structure to the statement of profit or loss by introducing defined and required subtotals. We acknowledge there can be tension between increasing comparability and allowing sufficient flexibility for an entity to communicate its performance story. The proposals in the ED allow an entity to communicate management's view of performance by disclosing information about management performance measures in the notes to the financial statements. We are of the view that the package of proposals can increase comparability between entities without adversely affecting the ability of individual entities to communicate their story to the users of their financial statements.

Materiality

We are of the view that the concept of materiality and materiality judgements plays a critical role in the presentation and disclosure of information in financial statements. Because an entity makes materiality judgements when making decisions about recognition and measurement, as well as presentation and disclosure, we can understand the IASB's rationale for proposing to move the definition of material and associated guidance to IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* as the concept of materiality is pervasive in the preparation of financial

statements. However, we believe the IASB has missed an opportunity to embed the concept of materiality into a general presentation and disclosure standard.

With presentation and disclosure – and particularly disclosure – there are good reasons why a general presentation and disclosure standard should include specific guidance on applying materiality. By including such guidance in a general presentation and disclosure standard, that guidance could then be applied (via cross-reference) to all other standards containing disclosure requirements.

Please refer to our response to question 8(b) for a detailed discussion on materiality.

The proposals

While we support many of the proposals in the ED, there are some areas where we disagree or recommend improvements. We have highlighted these areas below (see our response to the questions for our detailed recommendations and responses).

The investing category (Question 5)

In relation to the proposed new categories of ‘operating’, ‘investing’ and ‘financing’ in the statement of profit or loss, we strongly recommend that the IASB considers using different terms or more descriptive terms than those used in the statement of cash flows. Using the same terms as the statement of cash flows, but with a different meaning will be very confusing for users of financial statements.

Integral and non-integral associates and joint ventures (Question 7)

We do agree that separately presenting operating profit or loss and income and expenses from associates and JVs provides useful information to users of financial statements. However, we do not agree with the proposal to classify associates and joint ventures accounted for using the equity method as integral or non-integral. The classification would require significant judgement to be applied, would result in lack of comparability and would be difficult to audit. Furthermore, IFRS 12 *Disclosure of Interests in Other Entities* already requires entities to disclose information about the nature, extent and financial effects of their interests in associates and JVs.

Analysis of operating expenses (Question 9)

We do not agree with the proposal that an entity shall present in the operating category of the statement of profit or loss an analysis of expenses using a classification based on either the nature or function of the expense. Our view is that companies should be allowed the flexibility to determine the most appropriate analysis of expenses, even if that results in a mixed analysis.

Unusual income and expenses (Question 10)

We do not agree with the IASB proposals to define and require disclosure by all entities of unusual income and expenses. We have concerns that the proposals as currently drafted will not be operable.

Management Performance Measures (Question 11)

While we agree that MPMs provide useful information and should be included in the financial statements (as this will bring more transparency and discipline to the reporting of these financial performance measures), we have concerns with the proposals as they are currently drafted.

Going concern

The economic impact of the COVID-19 pandemic is expected to increase the level of uncertainty over the ability of many entities to continue as a going concern for financial reporting purposes. As a result, the NZASB recently issued domestic narrow-scope amendments to FRS-44 *New Zealand Additional Disclosures*¹ to improve going concern disclosures to provide better information to users of financial statements during this period of exceptional circumstances.

The issue of New Zealand specific disclosures is a short-term measure to deal with the most pressing need for improved disclosures. We strongly recommend that the IASB add a project to its agenda to look at going concern issues more comprehensively. The major economic disruption from COVID-19 has highlighted this matter as an area where improvements are needed.

Questions for respondents

Our detailed recommendations and responses to the specific questions for respondents are provided in the Appendix to this letter.

New Zealand outreach

We would like to take the opportunity to thank IASB staff member Aida Vatrenjak for her assistance with an outreach event we held on the proposals with institutional investors in New Zealand.

If you have any queries or require clarification of any matters in this letter, please contact Lisa Kelsey (Lisa.Kelsey@xrb.govt.nz) or me.

Yours sincerely



Michael Bradbury

Acting Chair – New Zealand Accounting Standards Board

¹ *Going Concern Disclosures* (Amendments to FRS-44)

Appendix to General Presentation and Disclosures

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| <p>Question 1—operating profit or loss</p> <p>Paragraph 60(a) of the Exposure Draft proposes that all entities present in the statement of profit or loss a subtotal for operating profit or loss.</p> <p>Paragraph BC53 of the Basis for Conclusions describes the Board’s reasons for this proposal.</p> <p>Do you agree with the proposal? Why or why not? If not, what alternative approach would you suggest and why?</p> |
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Response to question 1

1. We agree with the proposal that all entities present in the statement of profit or loss a subtotal for operating profit or loss.
2. Like the IASB, we have also seen diversity in practice, in terms of (a) entities that present an operating profit subtotal and others that do not; and (b) for those entities that do present an operating profit subtotal, what the subtotal comprises.
3. We believe that having a consistent view of the income and expenses that are included in a subtotal for operating profit or loss will reduce diversity in practice and improve comparability between entities.

Other comments

4. We note that the IASB is proposing to bring forward paragraph 8 (shown below) from IAS 1 *Presentation of Financial Statements* into the proposed new IFRS Standard (as paragraph 12). Paragraph 8 of IAS 1 has been amended to include a reference to subtotals. Paragraph 12 of the proposed IFRS X *General Presentation and Disclosures* allows entities to use another label when presenting the new operating profit or loss subtotal. In fact, entities may be able to use different labels for all the proposed new subtotals. As the main objective of the proposals to add defined subtotals to the statement of profit or loss is to increase comparability between entities, we believe that these new required subtotals should be labelled consistently across entities. We recommend that the IASB amend paragraph IFRS X.12 to exclude the subtotals required by paragraph 60 of IFRS X. This will also remove the risk that entities may label the new subtotals with existing labels which may confuse users.

| A comparison of proposals with requirements in IAS 1 <i>Presentation of Financial Statements</i> | | |
|---|---|-------------------|
| IAS 1 para # | Revised text (new text underlined, deleted text struck through) | New para # |
| IAS 1.8 | Although this <u>[draft] Standard</u> uses the terms <u>such as</u> ‘other comprehensive income’, ‘profit or loss’ and ‘total comprehensive income’, an entity may use other terms to describe the totals, <u>subtotals and line items required by this [draft] Standard</u> as long as the meaning is clear. For example, an entity may use the term ‘net income’ to describe profit or loss. | IFRS X.12 |

Question 2—the operating category

Paragraph 46 of the Exposure Draft proposes that entities classify in the operating category all income and expenses not classified in the other categories, such as the investing category or the financing category.

Paragraphs BC54–BC57 of the Basis for Conclusions describe the Board’s reasons for this proposal.

Do you agree with this proposal? Why or why not? If not, what alternative approach would you suggest and why?

Response to question 2

5. We agree with the proposal that entities classify in the operating category all income and expenses not classified in the other categories, such as the investing category or the financing category.
6. We acknowledge the challenges the IASB faced trying to define operating profit or loss. We agree that, because entities have various business activities, it is difficult to arrive at a direct definition of operating profit or loss that could be applied consistently, even between entities in the same industry. Therefore, for practical reasons we support the operating category being a default or residual category.
7. We agree that the operating category should include all income and expenses from an entity’s main business activities. We have discussed main business activities in more detail under question 3.
8. We have heard concerns that the proposal not to define operating profit or loss directly may mean that some income and expenses not arising from an entity’s core operations may be classified as operating by virtue of the fact that those income and expenses do not meet the definitions to be classified in the other categories. However, in considering this concern, we are satisfied that the disaggregation proposals should provide the users of the financial statements with enough information to enable adjustments to be made where appropriate.

Question 3—the operating category: income and expenses from investments made in the course of an entity’s main business activities

Paragraph 48 of the Exposure Draft proposes that an entity classifies in the operating category income and expenses from investments made in the course of the entity’s main business activities.

Paragraphs BC58–BC61 of the Basis for Conclusions describe the Board’s reasons for this proposal.

Do you agree with the proposal? Why or why not? If not, what alternative approach would you suggest and why?

Response to question 3

9. We agree with the proposal that an entity classifies in the operating category income and expenses from investments made in the course of the entity’s main business activities.
10. The ability for an entity to classify income and expenses from investments as operating rather than investing rests on the application of judgement as to what is “generated in the course of its main business activities”. For some entities, for example, global conglomerates with multiple business activities, significant judgement may be involved in determining the entity’s main business activities. In our response to Question 2 we have agreed with the IASB’s proposals not to define operating profit or loss and agreed that, because entities have various business activities, it is difficult to arrive at a direct definition of operating profit or loss that could be applied consistently, even between entities in the same industry. We believe the IASB would have the same difficulty if we requested a definition or further guidance on what is meant by ‘main business activities’.
11. We note that the IASB is proposing to bring across paragraph 138 of IAS 1 into the new IFRS X as paragraph 99. This will require an entity to disclose in the notes (if not disclosed elsewhere) a description of the entity’s main business activities. It is this description of main business activities that will drive the classification of income and expenses into each of the categories.
12. We also note that an entity may disclose information on the significant judgements involved in determining an entity’s main business activities under paragraph 122 of IAS 1, which is moving to IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* as paragraph 27E.
13. We are of view that the above disclosures should give users of the financial statements enough information about an entity’s main business activities and how this has affected the classification of income and expenses in the statement of profit or loss. Any information provided on main business activities and subsequent classification of income and expenses should also be consistent with any business model information that may be provided by an entity in its annual report, for example, in its management commentary.

Other comments

14. Investors have told us they would support proposals that are applicable to as many company types as possible. They agree with the proposals for banks but would not like to see other exceptions or modifications being made for other types of business.

Question 4—the operating category: an entity that provides financing to customers as a main business activity

Paragraph 51 of the Exposure Draft proposes that an entity that provides financing to customers as a main business activity classify in the operating category either:

- income and expenses from financing activities, and from cash and cash equivalents, that relate to the provision of financing to customers; or
- all income and expenses from financing activities and all income and expenses from cash and cash equivalents.

Paragraphs BC62–BC69 of the Basis for Conclusions describe the Board’s reasons for the proposals.

Do you agree with the proposal? Why or why not? If not, what alternative approach would you suggest and why?

Response to question 4

15. We agree with the proposal in paragraph 51 of the ED that an entity that provides financing to customers as a main business activity classify in the operating category either:
 - (a) income and expenses from financing activities, and from cash and cash equivalents, that relate to the provision of financing to customers; or
 - (b) all income and expenses from financing activities and all income and expenses from cash and cash equivalents.
16. We agree that when an entity provides financing to customers as a main business activity, the difference between the interest revenue from that activity and the related interest expense (a cost of earning that income) is an important indicator of operating performance. The IASB’s proposals would enable entities such as banks to continue presenting a net interest income subtotal.
17. We initially had reservations about allowing alternative accounting policy choices because they can lead to a loss of comparability between entities. In addition, if an entity chooses to allocate all income and expenses from cash and cash equivalents and financing activities to the operating category, this could result in a loss of relevant information for users. For example, a car manufacturer that provides financing to customers as one of its main business activities may elect to allocate all income and expenses from cash and cash equivalents and financing activities to the operating category. In this case, the car manufacturer would not present a subtotal for profit or loss before financing and income tax and, effectively, the income statement would not have a separate category for financing. The user of the financial statements would therefore not have access to information about the financing activities undertaken by the car manufacturer that are unrelated to the provision of financing to customers.
18. However, we have received feedback from some New Zealand banks (the entities most likely to make use of the proposed accounting policy choice) that any methodologies to split (i) income and expenses from financing activities, and from cash and cash equivalents, that

relate to the provision of financing to customers from (ii) income and expenses from financing activities and from cash and cash equivalents that are unrelated to the provision of financing to customers would be arbitrary at best.

19. We therefore agree with the IASB that an allocation should not be required but should be permitted.

Question 5—the investing category

Paragraphs 47–48 of the Exposure Draft propose that an entity classifies in the investing category income and expenses (including related incremental expenses) from assets that generate a return individually and largely independently of other resources held by the entity, unless they are investments made in the course of the entity’s main business activities.

Paragraphs BC48–BC52 of the Basis for Conclusions describe the Board’s reasons for the proposal.

Do you agree with the proposal? Why or why not? If not, what alternative approach would you suggest and why?

Response to question 5

20. We agree that an investing category will provide users with useful information about the returns from investments that are not part of the entity’s main business activities, particularly for non-financial institutions.
21. We have concerns that users will not understand the difference in the definition of the proposed investing category in the statement of profit or loss and the existing ‘investing activities’ in the statement of cash flows. Although both are labelled as investing, the definitions are not aligned. For example, cash proceeds from the disposal of property, plant and equipment would be classified as investing activities in the statement of cash flows, but the disposal gain/loss would be classified in the operating category in the statement of profit or loss. This is because property, plant and equipment are used in combination with other resources of an entity in its main business activities and do not “generate a return individually and largely independently of other resources held by an entity”.
22. One of the main criticisms levelled at financial statements is that many users do not understand them, and they are becoming more and more complicated. If the IASB then introduces the same terms, but with different meanings for the statement of profit or loss and the statement of cash flows, this will be very confusing for users of financial statements.
23. We strongly recommend that the IASB considers using different terms or more descriptive terms in each of the statements. For example, the definition for income and expenses from investments in the statement of profit or loss seems to focus on ‘distinct’ or ‘separable’ investing activities (which generate returns independently of other assets), whereas the IAS 7 definition seems to focus on ‘long-term’ investing activities. We suggest the IASB considers using a more descriptive label, based on the key underlying principle that drives the classification in each statement. We believe this would at least make it clearer that they are not the same thing.

Question 6—profit or loss before financing and income tax and the financing category

- (a) Paragraphs 60(c) and 64 of the Exposure Draft propose that all entities, except for some specified entities (see paragraph 64 of the Exposure Draft), present a profit or loss before financing and income tax subtotal in the statement of profit or loss.
- (b) Paragraph 49 of the Exposure Draft proposes which income and expenses an entity classifies in the financing category.

Paragraphs BC33–BC45 of the Basis for Conclusions describe the Board’s reasons for the proposals.

Do you agree with the proposals? Why or why not? If not, what alternative approach would you suggest and why?

Response to question 6

24. We support the proposal for entities to present a profit or loss before financing and income tax subtotal in the statement of profit or loss, other than some specific entities (i.e. entities that provide financing to customers as a main business activity (e.g. banks) and classify all income and expenses from financing activities and all income and expenses from cash and cash equivalents in the operating category).
25. We support the proposals for entities to classify in the financing category:
- (a) income and expenses on liabilities arising from financing activities;
 - (b) income and expenses from cash and cash equivalents; and
 - (c) interest income and expenses on liabilities that do not arise from financing activities.
26. We acknowledge that some users have different views on the appropriate classification of income and expenses from cash and cash equivalents (e.g. as investing, financing, or operating). However, we support the inclusion of income and expenses from cash and cash equivalents in the financing category (with the proposed exceptions for some specific entities) for reasons similar to including interest income and expenses on liabilities that do not arise from financing activities in the financing category (i.e. a consistent location for the presentation of information). This consistent location would enable users to reclassify income and expenses from cash and cash equivalents to other categories if they wish to do so.
27. The ED stipulates that entities would classify in the investing category incremental expenses incurred to generate income and expenses from investments. However, the ED is silent on incremental expenses related to the financing category. We recommend that the IASB includes guidance on whether incremental expenses related to financing activities should also be in the financing category as this would be useful.

Other comments

28. The proposals define financing activities as follows:

financing activities: Activities involving the receipt or use of a resource from a provider of finance with the expectation that:

- (a) the resource will be returned to the provider of finance; and
- (b) the provider of finance will be compensated through the payment of a finance charge that is dependent on both the amount of the credit and its duration.

29. We suggest the IASB clarifies the following.

- (a) How the proposed definition interacts with interest recognised on interest free or low interest loans recognised initially at fair value? (The definition implies the lender is expected to be compensated for extending credit, which is not the case for interest free or low interest loans).
- (b) Whether the 'payment of a finance charge' would include notional interest calculated for accounting purposes, rather than a contractual interest charge.

Question 7—integral and non-integral associates and joint ventures

- (a) The proposed new paragraphs 20A–20D of IFRS 12 would define ‘integral associates and joint ventures’ and ‘non-integral associates and joint ventures’; and require an entity to identify them.
- (b) Paragraph 60(b) of the Exposure Draft proposes to require that an entity present in the statement of profit or loss a subtotal for operating profit or loss and income and expenses from integral associates and joint ventures.
- (c) Paragraphs 53, 75(a) and 82(g)–82(h) of the Exposure Draft, the proposed new paragraph 38A of IAS 7 and the proposed new paragraph 20E of IFRS 12 would require an entity to provide information about integral associates and joint ventures separately from non-integral associates and joint ventures.

Paragraphs BC77–BC89 and BC205–BC213 of the Basis for Conclusions describe the Board’s reasons for these proposals and discuss approaches that were considered but rejected by the Board.

Do you agree with the proposals? Why or why not? If not, what alternative approach would you suggest and why?

Response to question 7

- 30. We do not agree with the proposal to classify associates and joint ventures (JVs) accounted for using the equity method as integral or non-integral. Our reasons are as follows.
 - (a) Our outreach with investors does not suggest there is a demand for this information.
 - (b) IFRS 12 *Disclosure of Interests in Other Entities* already requires entities to disclose information about the nature, extent, and financial effects of their interests in associates and JVs.
 - (c) Preparers have suggested it would be more beneficial for the IASB to reconsider whether equity accounting for associates and JVs is appropriate or whether another method should be considered.
 - (d) Any definition of ‘integral’ and ‘non-integral’ would require significant judgement to be applied, would result in lack of comparability, and would be difficult to audit.
- 31. However, we have heard from investors that it would be useful to have an entity’s share of profit or loss of associates and JVs accounted for using the equity method presented separately from operating profit or loss.
- 32. Although we do not agree with classifying associates and JVs as integral or non-integral, we do agree that separately presenting operating profit or loss and income and expenses from associates and JVs provides useful information to users of financial statements.
- 33. We suggest, for simplicity, that the IASB considers requiring the separate presentation of associates and JVs immediately below operating profit (so effectively part of the investing

category but as a separate line item). We recommend requiring the presentation of two line items to differentiate between

- (a) share of profit or loss from associates and JVs (for equity-accounted associates and JVs); and
- (b) FV movements for other associates and JVs measured at fair value (given the feedback from users).

We have shown what our suggestion would look like in Figure 1 below.

Figure 1—Summary of a statement of profit or loss

| | | |
|--|----------|-----------|
| Revenue | X | Operating |
| Operating expenses | (X) | |
| Operating profit or loss | X | |
| Share of profit or loss from associates and JVs | X | Investing |
| FV movements for other associates and JVs measured at fair value | X | |
| Income from investments | X | |
| Profit or loss before financing and income tax | X | |
| Interest revenue from cash and cash equivalents | X | Financing |
| Expenses from financing activities | (X) | |
| Unwinding of discount on pension liabilities and provisions | (X) | |
| Profit or loss before tax | X | |

Question 8—roles of the primary financial statements and the notes, aggregation and disaggregation

(a) Paragraphs 20–21 of the Exposure Draft set out the proposed description of the roles of the primary financial statements and the notes.

(b) Paragraphs 25–28 and B5–B15 of the Exposure Draft set out proposals for principles and general requirements on the aggregation and disaggregation of information.

Paragraphs BC19–BC27 of the Basis for Conclusions describe the Board’s reasons for these proposals.

Do you agree with the proposals? Why or why not? If not, what alternative approach would you suggest and why?

Response to question 8(a)

34. We agree that clarifying the role of the primary financial statements and the notes would:

- (a) help entities decide what information to disclose in the notes to explain and supplement the primary financial statements; and
- (b) assist the IASB in deciding what information it should require to be presented in the primary financial statements or permit disclosure in the notes instead.

35. We agree with the proposed description of the roles of the primary financial statements and the notes.

36. In our view, the notes form an integral part of the financial statements. It is the combination of the primary financial statements and the notes that meets the objective of financial statements. We would like the IASB to acknowledge in IFRS X that while the primary financial statements and the notes do have separate roles to play, they are both equally important in meeting the objective of financial statements.

Response to question 8(b)

37. We are supportive of the IASB providing principles and guidance on aggregation and disaggregation. We have received feedback from users of financial statements that financial statements do not always include information that is appropriately aggregated or disaggregated. Aggregating items that have shared characteristics makes large volumes of information understandable and avoids obscuring relevant information. Similarly, disaggregating items with dissimilar characteristics provides users of financial statements with relevant information and avoids obscuring material information.

38. While we generally agree with the principles and guidance for aggregation and disaggregation included in the ED, we have identified below some areas for further consideration by the IASB.

Materiality

39. We are of the view that the concept of materiality and materiality judgements plays a critical role in the presentation and disclosure of information in financial statements. Because an entity makes materiality judgements when making decisions about recognition and

measurement, as well as presentation and disclosure, we can understand the IASB's rationale for proposing to move the definition of material and associated guidance to IAS 8 as the concept of materiality is pervasive in the preparation of financial statements. However, we believe the IASB has missed an opportunity to embed the concept of materiality into a general presentation and disclosure standard.

40. We consider that materiality is well established as a concept in relation to recognition and measurement but is less so in relation to presentation and disclosure. In general, the application of recognition and measurement requirements results in quantitative information. Because recognition and measurement requirements result in quantitative information, materiality judgements are typically judgements about the magnitude of the amounts concerned, i.e. a quantitative assessment. Therefore, when applying materiality to recognition and measurement, it is often judgements about whether, and the extent to which, it is necessary to comply with the recognition and measurement requirements in standards.
41. In contrast, when applying materiality to presentation and disclosure, the following judgements are needed.
 - (a) Information might be qualitative rather than quantitative, especially information disclosed in the notes.
 - (b) Whether information is material might depend on the nature of the item, instead of (or in addition to) its magnitude (for example, the definition of unusual items considers not just the magnitude of the item but also its nature), so it is not simply a quantitative assessment.
 - (c) Materiality judgements do not merely relate to whether, and the extent to which, it is necessary to comply with the requirements of the standard. They also relate to how to apply those requirements, so are a key driver in determining what information is disclosed (as is acknowledged in the guidance on aggregation and disaggregation in paragraph B9 "In the notes, it is the concept of materiality that drives aggregation and disaggregation. To achieve the objective of financial statements, items that have dissimilar characteristics shall be disaggregated into component parts when the resulting information is material").
42. All the above points mean that materiality is not only a very important concept for presentation and disclosure, but also that it is much harder to apply in practice. The reality is that it is easier for preparers and auditors to make materiality judgements when dealing with quantitative information, so it is an easier concept to apply to recognition and measurement requirements. Therefore, it is sufficient to have materiality guidance in IAS 8 when dealing with recognition and measurement requirements. But with presentation and disclosure – and particularly disclosure – there are good reasons why a general presentation and disclosure standard should include specific guidance on applying materiality. And by including such guidance in a general presentation and disclosure standard, that guidance could then be applied (via cross-reference) to all other standards containing disclosure requirements.

43. Section 8 of the IASB's DP/2017/1 *Disclosure Initiative—Principles of Disclosure* (POD DP) included the New Zealand Accounting Standards Board staff's proposed approach to drafting disclosure requirements in IFRS® Standards. One of the main features of this proposed approach was placing greater emphasis on the need to exercise judgement when deciding how and what to disclose to meet the disclosure objectives.
44. Below is an extract from section 8 of the POD DP. A lot of the guidance in the section below has been picked up by the IASB in the new guidance on aggregation and disaggregation, but not all – for example, the guidance on considering the extent and mix of quantitative and qualitative information. We have included this as it may be of some help when considering what specific guidance on materiality judgements to include in a general presentation and disclosure standard.

NZASB staff example 1—Guidance on the use of judgement

This is an example of clarifying paragraphs emphasising the need to use judgement and could be placed in each Standard that contains disclosure requirements or could be placed in a general disclosure standard, such as in IAS 1.

- X1.1 To achieve the [overall] disclosure objective in a Standard, an entity shall use its judgement to determine the extent and appropriate mix of quantitative and qualitative information to disclose, including the extent of aggregation or disaggregation of that information. Assessments about the amount of information to disclose depend on the relative importance of an item or transaction to the entity (taking into account the nature and/or size of that item or transaction) and the amount of judgement involved in accounting for that item or transaction. Therefore, assessments need to take into account the extent to which the entity's financial position, financial performance or cash flows are affected by:
- (a) the item or transaction; and
 - (b) risks and uncertainties associated with the item or transaction.
- X1.2 When using judgement to determine the information to be disclosed in accordance with a Standard, an entity considers:
- (a) how much emphasis to place on particular disclosures;
 - (b) the level of detail needed (taking into account the expectation that users of financial statements should have a reasonable knowledge of business and economic activities);
 - (c) how much aggregation or disaggregation to undertake; and
 - (d) whether users of the financial statements need additional information to meet the disclosure objective.
- X1.3 An entity aggregates or disaggregates disclosures in accordance with this Standard or another IFRS Standard so that useful information is not obscured by either the inclusion of a large amount of insignificant detail or the aggregation of items that have different characteristics.

Materiality – other comments

45. The IASB is not proposing to carry forward paragraph 97 from IAS 1 which states “when items of income and expense are material, an entity shall disclose their nature and amount separately”. We believe that the IASB should include this paragraph in a new general presentation and disclosures standard.

The label ‘other’

46. We have heard concerns from investors that some companies use the label ‘other’ when describing expenses, without providing information to help them understand what those items comprise.

47. We are in complete agreement that disaggregation of material items of income and expenses provides useful information to users. However, we would caution the IASB against requiring an entity to disaggregate an 'other expenses' line made up of immaterial items where the entity has made every effort to apply the principles set out in paragraphs 25 to 28 in the ED, and the resulting amount in the line item 'other expenses' is immaterial. We recommend amending paragraph 28 to clarify this. We also suggest including this scenario in the illustrative examples.
48. In support of our comments in the paragraph above, we have received feedback that too much emphasis on disaggregation is counterinitative with the focus in recent years on decluttering financial statements. The concern is that the proposals in the ED may cause the pendulum to swing too far in the other direction and have the effect of cluttering the financial statements.

Question 9—analysis of operating expenses

Paragraphs 68 and B45 of the Exposure Draft propose requirements and application guidance to help an entity to decide whether to present its operating expenses using the nature of expense method or the function of expense method of analysis. Paragraph 72 of the Exposure Draft proposes requiring an entity that provides an analysis of its operating expenses by function in the statement of profit or loss to provide an analysis using the nature of expense method in the notes.

Paragraphs BC109–BC114 of the Basis for Conclusions describe the Board’s reasons for the proposals.

Do you agree with the proposals? Why or why not? If not, what alternative approach would you suggest and why?

Response to question 9

49. We do not agree with the proposal that an entity shall present in the operating category of the statement of profit or loss an analysis of expenses using a classification based on either their nature or function. Our reasons are as follows.
- (a) In practice, we observe that it is common for companies to provide a mixed method of analysis based on the type of analysis that companies regard as providing the most useful information to users of their financial statements. Our view is that companies should be allowed the flexibility to determine the most appropriate analysis of expenses, even if that results in a mixed analysis.
 - (b) We have received feedback that companies report an analysis of expenses that reflects the way they track and manage the expenses internally. Requiring companies to then report in a different manner in our view will add to the costs for little benefit.
 - (c) Our outreach has shown that there is not a good understanding of what is meant by an analysis of expenses by nature or function.
 - (d) Additionally, we note that despite paragraph B46, which states that an entity shall not use a mixture of the nature of expense method and the function of expense method, paragraph B47 states that an entity shall present the line items required by paragraph 65 (which are by nature). Therefore, in practice, paragraph B47 is requiring a mixture of methods for an entity analysing operating expenses by function.
50. We acknowledge that our comments above may be seen as inconsistent with views expressed earlier in our comment letter, where we agreed with increased structure in the statement of profit or loss (by way of categories and subtotals) to aid comparability. In our view standardisation of the structure of the statement of profit or loss—including the key subtotals—is sufficient to improve comparability, without the need to take that standardisation a step further by being overly prescriptive in how expense line items are presented.

51. We do not agree with the proposal that an entity presenting an analysis of expenses using the function of expense method shall also disclose in a single note an analysis of its total operating expenses using the nature of expense method. Our reasons are as follows.
- (a) Some may argue that the above is already required under the existing requirement in IAS 1, but in our experience the existing requirement is not interpreted as requiring a comprehensive analysis in the notes. Rather, selected additional information is provided, for example, depreciation, amortisation, and employee benefit expense (possibly because these items are individually listed in paragraph 104 of IAS 1).
 - (b) We have concerns with the practical application of the requirement. Some entities may not have the ability to be able to analyse operating expenses by more than one method in their accounting/reporting systems. Therefore, these entities would need to incur additional costs to track operating expenses using another method outside of their current systems.
 - (c) As well as the practical application problem above, there is also a conceptual problem with requiring 'cost of goods sold' to be reanalysed. Conceptually, if this line item is just made up of inventory, then it is not actually a functional line item. Rather, it is the cost of an asset (inventory) that is expensed at the point that it is sold to another party. For a manufacturing entity, the analysis required under the proposals (and existing IAS 1, if you follow the illustrative example) involves a decapitalisation process, to break down the cost of this asset into the original inputs (for example, raw materials, employee costs, etc) that were then capitalised into inventory under IAS 2 *Inventories*. Then, to balance the total cost of inputs purchased back to the COGS expense, there is an adjusting line item for the movement in inventory. Therefore, these input costs included in the analysis are not "expenses" as defined in the conceptual framework.
52. The IASB has acknowledged in the Basis for Conclusions that it did think about the costs to preparers when it developed this proposal. However, the IASB went ahead with the proposal due to the strong demand from users for this information to forecast future operating expenses. We do understand the driver for the proposal, but we suggest that the IASB considers alternatives. For example, given that users seem to be looking for information that is based on cash flows rather than accrual accounting, an alternative is to consider the presentation and disclosure requirements in IAS 7.

Other comments

53. We would like the IASB to consider the removal of paragraph 65 in the ED. This paragraph requires the presentation in the statement of profit or loss of minimum line items. We would like to challenge the status quo here – why do we need to continue to have minimum line items in a general presentation and disclosure standard? The IASB has worked hard to develop new proposals, including principles and general requirements on the aggregation and disaggregation of information. The application of the IASB's proposals plus our recommendation in question 8 above to give greater emphasis to the concept of materiality should be sufficient for preparers to determine what information is presented and disclosed in the statement of profit or loss.

54. Further to the above, the requirements in paragraph 65 are an ad hoc collection of line items that have accumulated over the years, with no coherent rationale for singling out particular income or expense items.
55. As an alternative to paragraph 65, we would be supportive of the IASB retaining requirements for entities to disclose particular types of income or expenses in the notes to the financial statements, if necessary to meet user information needs, as opposed to requiring the disclosure of these line items on the face of the statement of profit or loss.

Question 10—unusual income and expenses

- (a) Paragraph 100 of the Exposure Draft introduces a definition of ‘unusual income and expenses’.
- (b) Paragraph 101 of the Exposure Draft proposes to require all entities to disclose unusual income and expenses in a single note.
- (c) Paragraphs B67–B75 of the Exposure Draft propose application guidance to help an entity to identify its unusual income and expenses.
- (d) Paragraphs 101(a)–101(d) of the Exposure Draft propose what information should be disclosed relating to unusual income and expenses.

Paragraphs BC122–BC144 of the Basis for Conclusions describe the Board’s reasons for the proposals and discuss approaches that were considered but rejected by the Board.

Do you agree with the proposals? Why or why not? If not, what alternative approach would you suggest and why?

Response to question 10

- 56. We do not agree with the IASB’s proposals to define and require disclosure by all entities of unusual income and expenses.
- 57. IAS 1 already includes a requirement to separately disclose the nature and amount of material income and expenses (paragraph 97). Paragraph 98 of IAS 1 includes examples of circumstances that would give rise to the separate disclosure of income and expenses.

Information to be presented in the statement(s) of profit or loss and other comprehensive income or in the notes

- 97 When items of income or expense are material, an entity shall disclose their nature and amount separately.**
- 98 Circumstances that would give rise to the separate disclosure of items of income and expense include:
- (a) write-downs of inventories to net realisable value or of property, plant and equipment to recoverable amount, as well as reversals of such write-downs;
 - (b) restructurings of the activities of an entity and reversals of any provisions for the costs of restructuring;
 - (c) disposals of items of property, plant and equipment;
 - (d) disposals of investments;
 - (e) discontinued operations;
 - (f) litigation settlements; and
 - (g) other reversals of provisions.

- 58. The IASB has not carried forward paragraph 97. Paragraph 98 is carried forward into the application guidance as paragraph B15 (with minor amendments). In question 8 we commented that in our view the IASB has missed an opportunity to embed the concept of materiality into a general presentation and disclosure standard. An alternative to trying to refine the definition of unusual income and expenses is to focus on the existing requirements in IAS 1 (paragraph 97 and 98) and strengthen these requirements to ensure users receive information about material income and expenses to enable them to assess prospects for future cash flows.

59. As we acknowledged in our comment letter to the IASB on the POD DP “information on unusual or infrequently occurring items is useful to users of financial statements, because it helps them to assess the recurring/sustainable performance and make assessments about the future, provided the items are genuinely unusual or infrequently occurring”.
60. In our comment letter to the IASB on the POD DP, we did not support the development of definitions of, and requirements for, the presentation of unusual or infrequently occurring items. We suggested instead that the IASB develop principles for the fair presentation of these items.
61. Our suggestion is that the IASB relies on the existing requirements in IAS 1 (existing paragraphs 97 and 98) for the disclosure of material items, adds “occurrence of other unusual or infrequently occurring items” to the list of circumstances that would give rise to the separate disclosure of items of income and expense, and adds requirements for the fair presentation of these unusual or other infrequently occurring items.

Question 11—management performance measures

- (a) Paragraph 103 of the Exposure Draft proposes a definition of ‘management performance measures’.
- (b) Paragraph 106 of the Exposure Draft proposes requiring an entity to disclose in a single note information about its management performance measures.
- (c) Paragraphs 106(a)–106(d) of the Exposure Draft propose what information an entity would be required to disclose about its management performance measures.

Paragraphs BC145–BC180 of the Basis for Conclusions describe the Board’s reasons for the proposals and discuss approaches that were considered but rejected by the Board.

Do you agree that information about management performance measures as defined by the Board should be included in the financial statements? Why or why not?

Do you agree with the proposed disclosure requirements for management performance measures? Why or why not? If not, what alternative disclosures would you suggest and why?

*Response to question 11**Overall*

62. We agree:

- (a) That MPMs can provide useful information to users of financial statements.
- (b) There is a demand from users for information about MPMs.
- (c) That information about MPMs should be included in the financial statements and be subject to audit.
- (d) That the proposals will bring more transparency and discipline to the reporting of these financial performance measures.

63. There is currently an audit expectation gap as users think that information about non-GAAP measures included in an entity’s annual report has been audited. Disclosing MPMs in the financial statements will make it clear these measures have been subject to audit.

64. We acknowledge that in the case of some MPMs (such as measures based on tailor-made accounting policies), the audit work may be restricted to checking that the measure has been calculated in accordance with the entity’s definition of the measure and that the entity has complied with the disclosure requirements for MPMs. However, we do not think that this should prevent these measures from being included in the audited financial statements.

MPM definition – subtotals of income and expenses

65. The IASB is proposing to limit MPMs to financial performance measures that are subtotals of income and expenses. This is in line with the IASB’s focus on improving the reporting of financial performance in the statement of profit or loss. Paragraph BC154 is the key paragraph that explains why the IASB is limiting MPMs.

- BC154 Feedback from users of financial statements led the Board to focus on improvements to the reporting of financial performance in the statement(s) of financial performance and the related notes. Therefore, the Board's proposed definition for management performance measures is limited to subtotals of income and expenses. Thus, other financial measures (such as currency adjusted revenue or return on capital employed) and non-financial measures (such as customer retention rate) are not management performance measures and would not be included in the proposed disclosure.
66. Limiting MPMs to financial performance measures that are subtotals of income and expenses will mean in some cases only a subset of the non-GAAP financial measures used by management in its public communications will be MPMs. The remainder of the non-GAAP financial measures used by management will continue to be reported outside the financial statements, for example, in management commentary.
 67. We recommend that the definition of MPMs is widened to include non-GAAP financial measures that are derived from an IFRS amount in the financial statements. The first part of the MPM definition could be replaced with: "a numerical/financial measure of historical financial performance, financial position, or cash flows..... (insert rest of definition)".
 68. Internationally, this would be consistent with the approach taken in the ESMA's *Guidelines on Alternative Performance Measures*, IOSCO's *Statement on Non-GAAP Financial Measures* (IOSCO's statement) and US SEC *Conditions for Use of Non-GAAP Financial Measures*.
 69. In New Zealand, this would align with the FMA guidance on *Disclosing non-GAAP financial information* (which is broadly aligned with the IOSCO statement). The FMA guidance sets out guidelines for FMC reporting entities to follow when they disclose non-GAAP financial information outside the financial statements. We are of the view that analysts and investors would welcome the inclusion in the financial statements of other key financial measures that are used by management.

Definition of an MPM – scope of public communications

70. We believe that the IASB needs to provide guidance to clarify the intended scope of 'public communications outside the financial statements' used in the definition of MPMs for the following reasons.
 - (a) The proposed guidance (see paragraph B79) provides examples of public communications (management commentary, press releases and investor presentations). However, the guidance does not limit public communications to these forms of communication.
 - (b) Some constituents have questioned whether public communications outside the financial statements would include posts on social media made by the company.
 - (c) Other constituents have raised concerns from an audit perspective, noting the challenges of having to review all an entity's public communications for possible MPMs.
 - (d) We also have concerns that the IASB has not provided guidance on the timeframe regarding public communications. It is not clear from the proposed definition of an MPM or associated guidance, whether an entity would need to consider all public communications during the year (such as quarterly investor communications) or only those communications relating to the interim/annual reporting period.

- (e) Do financial statements meet the definition of public communications – if a measure is only in the financial statements does it meet the MPM definition?
- (f) It is not clear whether an entity must make the required MPM disclosures when it publicly communicates adjusted profit measures for different branches/business activities. For example, an entity publicly communicates, via investor presentations, different adjusted profit measures regarding its activities in two different cities. Is the entity then required to make the disclosures proposed in the ED for both of these adjusted profit measures?

Definition of an MPM – complement totals or subtotals specified by IFRS Standards

71. We have received feedback that the purpose of subparagraph 103(b) of the proposed definition of MPMs is not clear. This subparagraph states that MPMs are subtotals of income and expenses that “complement totals or subtotals specified by IFRS Standards”. We believe that the requirement in subparagraph 103(b) is needed in order for an MPM to be reconciled back to an IFRS specified subtotal in the statement of profit or loss. But we also question whether the IASB intended this subparagraph to restrict MPMs to those that are subtotals of income and expenses that cover the same reporting period as the financial statements (see previous comment on the scope of ‘public communications’). We recommend that the IASB considers adding an explanation for the purpose of this requirement in the application guidance.

Faithful representation

72. We have concerns with paragraph 105(a) of proposed IFRS X which specifically restricts the disclosure of MPMs in the financial statements to those MPMs that “faithfully represent aspects of the financial performance of the entity to users of the financial statements”.
- (a) We acknowledge there is a general requirement in IFRS Standards that financial statements shall present fairly the financial position, financial performance, and cash flows of an entity. Fair presentation requires the faithful representation of information.
 - (b) Paragraph 2.13 of the *Conceptual Framework for Financial Reporting* states “To be a perfectly faithful representation, a depiction would have three characteristics. It would be complete, neutral, and free from error. Of course, perfection is seldom, if ever, achievable. The Board’s objective is to maximise those qualities to the extent possible.”
 - (c) We note that IFRS 8 *Operating Segments* does not place a similar explicit restriction on the disclosure of segment information which reflects the views of management (see paragraph BC160).
 - (d) The restriction in paragraph 105(a) does not prevent entities from using such MPMs outside of the financial statements.
 - (e) In our view, there can be tension between:
 - (i) communicating to users of financial statements management’s view of an aspect of an entity’s financial performance; and

- (ii) the restriction that MPMs must faithfully represent an aspect of an entity's financial performance.
 - (f) We believe that where entities are reporting such MPMs outside the financial statements, information about these MPMs is still useful to users of the financial statements and should be disclosed in the financial statements and be subject to audit.
 - (g) Additionally, we have heard concerns from auditors and preparers about how to interpret 'faithfully represents' in the context of MPMs and subsequently how this will be audited.
73. Therefore, we recommend that the IASB removes this restriction. We consider that paragraph 105(b) of proposed IFRS X, which requires MPMs to be described in a clear and understandable manner that does not mislead users, will be sufficient.
74. We acknowledge that removing paragraph 105(a) will allow MPMs that might not faithfully represent an aspect of an entity's financial performance to be included in the financial statements. However, we believe that such MPMs should not be restricted from being included in the financial statements. Information about such MPMs could provide useful information to users, for example, why the MPM presents management's view of performance and a reconciliation back to a comparable total or subtotal specified by IFRS Standards.
75. If the IASB retains the restriction in paragraph 105(a), then we believe that further guidance is needed to clarify when an MPM faithfully represents aspects of the financial performance of the entity to users of the financial statements.

Proposed disclosures

76. Generally, we agree with the proposed disclosure requirements.
77. We have received feedback that some companies do not adequately explain why a non-GAAP measure provides useful information to users (regardless of whether this non-GAAP information is inside or outside the financial statements). In most cases companies are providing very generic explanations. We have also received feedback that the illustrative example in the ED is too generic and is not very helpful.
78. We have heard concerns that the reconciling items between the MPM and the IFRS number may not be described in a useful manner. We note that paragraph B85 requires that reconciling items meet the requirements in paragraphs 25 to 28, which includes a requirement that the description of the items in the financial statements shall faithfully represent the characteristics of those items. We recommend the IASB considers whether it should add to paragraph 106(b) that reconciling items must be described in a clear and understandable manner.

Question 12—EBITDA

Paragraphs BC172–BC173 of the Basis for Conclusions explain why the Board has not proposed requirements relating to EBITDA.

Do you agree? Why or why not? If not, what alternative approach would you suggest and why?

Response to question 12

79. We agree with not proposing requirements relating to EBITDA. In our view, the calculation of EBITDA is diverse in practice. It would be difficult for the IASB to come up with a globally accepted definition of EBITDA.
80. However, as EBITDA is an almost universal measure of performance (not just in financial statements), we would suggest that the IASB provides guidance to clarify when EBITDA would be able to be presented on the face of the statement of profit or loss. We suggest it would also be helpful to clarify that EBITDA can be presented in the notes to the financial statements as an MPM. In paragraph 85 below we recommend that the IASB considers including the content of paragraph BC165 in the ED, as this explains when the IASB would expect that an MPM such as EBITDA would meet the requirements for presentation on the face of the statement of profit or loss.
81. We consider paragraph BC165 (shown below) is helpful and should be included in the ED.
- BC165 However, the Board expects that few management performance measures would meet the requirements for presentation as a subtotal in the statement(s) of financial performance. To meet the requirements, such subtotals must:
- (a) fit into the structure of the proposed categories (see paragraph BC28);
 - (b) not disrupt the presentation of an analysis of expenses in the operating category using either the function of expense or nature of expense method (see paragraph BC109); and
 - (c) comprise amounts recognised and measured applying IFRS Standards.
82. We support the IASB’s proposal to include operating profit before depreciation and amortisation in the list of IFRS specified subtotals.

Question 13—statement of cash flows

- (a) The proposed amendment to paragraph 18(b) of IAS 7 would require operating profit or loss to be the starting point for the indirect method of reporting cash flows from operating activities.
- (b) The proposed new paragraphs 33A and 34A–34D of IAS 7 would specify the classification of interest and dividend cash flows.

Paragraphs BC185–BC208 of the Basis for Conclusions describe the Board’s reasons for the proposals and discusses approaches that were considered but rejected by the Board.

Do you agree with the proposals? Why or why not? If not, what alternative approach would you suggest and why?

Response to question 13(a)

83. The indirect method of reporting cash flows from operating activities is not prevalent in New Zealand. Therefore, we have not commented on this question.

Response to question 13(b)

84. We agree with the feedback received by the IASB that diversity in how companies classify interest and dividend cash flows reduces comparability between companies, making analysis by investors/users difficult. Therefore, we support the proposal to remove the classification choice for interest and dividend cash flows for most entities.

Other comments

85. As highlighted in our response to question 5 above, the use of similar labels to describe the categories in the statement of profit or loss and the classifications in the statement of cash flows will create substantial confusion in practice. Therefore, we strongly recommend that the IASB explores further the use of different labels between the two statements before finalising the proposals.
86. In line with our response to question 7 above, we do not agree with the proposal to separate cash flows from investments into those from integral and non-integral associates and JVs.

Question 14—other comments

Do you have any other comments on the proposals in the Exposure Draft, including the analysis of the effects (paragraphs BC232–BC312 of the Basis for Conclusions, including Appendix) and Illustrative Examples accompanying the Exposure Draft?

Response to question 14

Going concern

- 87. The economic impact of the COVID-19 pandemic is expected to increase the level of uncertainty over the ability of many entities to continue as a going concern for financial reporting purposes. As a result, the NZASB recently issued domestic narrow-scope amendments to FRS-44 *New Zealand Additional Disclosures*² to improve going concern disclosures to provide better information to users of financial statements during this period of exceptional circumstances.
- 88. The issue of New Zealand specific disclosures is a short-term measure to deal with the most pressing need for improved disclosures. We strongly recommend that the IASB adds a project to its agenda to look at going concern issues more comprehensively. The major economic disruption from COVID-19 has highlighted this matter as an area where improvements are needed.

Statement presenting comprehensive income

- 89. IAS 1 requires income and expenses included in other comprehensive income (OCI) to be categorised into income and expenses that may be reclassified (recycled) to profit or loss in subsequent periods and items that are permanently reported outside profit or loss and will not be reclassified. This creates two categories of income and expenses included in other comprehensive income.
- 90. To increase the understandability of amounts included in other comprehensive income, the IASB proposes to create more descriptive labels for these two categories of other comprehensive income.

| Categories of income and expenses included in other comprehensive income | |
|---|---|
| Current labels | Proposed labels |
| will not be reclassified subsequently to profit or loss. | remeasurements permanently reported outside profit or loss. |
| will be reclassified to subsequently to profit and loss when specific conditions are met. | income and expenses to be included in profit or loss in the future when specific conditions are met |

- 91. We support the proposed new labels for the categories of income and expenses included in other comprehensive income. The new labels use plain English and are easier to understand.

² *Going Concern Disclosures* (Amendments to FRS-44)

92. We would encourage the IASB to undertake a specific project on OCI. We have received feedback that users do not understand the distinction between profit or loss and OCI and the role of recycling.

Negative interest rates

93. During discussions on the ED, an issue was raised regarding the presentation of income and expenses in a negative interest rate environment. We are aware of the January 2015 IFRS Interpretations Committee agenda decision *Income and expenses arising on financial instruments with a negative yield—presentation in the statement of comprehensive income (IAS 39 Financial Instruments: Recognition and Measurement and IAS 1 Presentation of Financial Statements)—January 2015*. While this agenda decision clarified that you cannot present negative interest as a revenue line item, it did not clarify how the resulting expense should be presented. We have received feedback that clarification of presentation would be helpful to ensure consistent reporting and remove potential diversity in practice.

Illustrative Examples

94. We recommend the IASB provides examples that are entity specific and avoids boiler plate examples. For example, we have received feedback that note 2 to part 1 of the illustrative examples does not contain entity specific information on how the three MPMs provide useful information about the entity's performance (proposed required disclosure under paragraph 106(a) of IFRS X).
95. We have received feedback that the IASB should provide an example regarding the classification of the fair value movements for biological assets (are the movements in fair value operating or investing in nature?) There is currently diversity in practice so clarity would be helpful.
96. We note that the illustrative statement of profit and loss in Part I (analysis of expenses by function) includes a line item 'impairment losses on trade receivables'. We also note that impairment losses on trade receivables is listed separately in note 1, which is an analysis of operating expenses by nature. We question how the same item can be by nature and by function.