IASB's Disclosure Initiative: Project Update

Tentative decisions made by the IASB – October & November 2013

1 At its October 2013 meeting the IASB considered proposed narrow-scope amendments to IAS 1 *Presentation of Financial Statements* addressing net debt and totals and subtotals and continued discussing the current/non-current classification of liabilities. The proposed amendments are intended to address some of the concerns raised at the IASB's Discussion Forum (summarised in the *Discussion Forum: Financial Reporting Disclosure* Feedback Statement) as well as proposals arising from submissions to the IFRS Interpretations Committee.

2 An overview of the IASB tentative decisions is provided below.

IAS 1 Amendments

(A) Proposed amendments to IAS 1 – Net Debt

3 At the October IASB meeting the IASB discussed the topic of net debt disclosure and whether the IASB should include net debt disclosure as part of the short-term amendments to IAS 1 Disclosure Initiative Project.

4 IASB staff recommended including net debt as part of the medium term project on the basis that:

(a) any amendments made about net debt are outside the scope of the short-term project, which concerns clarifying the requirements in IAS 1; and

(b) the project would require more extensive outreach to better understand the issues and provide a full analysis on the topic.

5 One IASB member expressed serious concern about doing a project on net debt on its own, questioning why key performance indicators (KPI) as opposed to all other KPIs. The member noted their support for a project that looks into what disclosures might be necessary around cash and liabilities so that someone could do a net debt reconciliation if required – however, there are other indicators used in the market, more widely, more globally than net debt.

6 It was acknowledged, consistent with the IASB staff recommendation, that the IASB needs to learn more about the analysts and users of net debt and determine if the IASB needs to describe rather than define net debt.

7 Staff and IASB members noted that the Capital Markets Advisory Committee (CMAC) members think it is a very important disclosure and support the IASB pursuing the topic. From a review of the Summary of the CMAC discussions held on

17 October 2013, CMAC members generally agreed that 'net debt' is an important issue that should be considered and indicated that net debt information, including reconciliations between the beginning and the end of the year, is important for investors and analysts and helps them to understand many items about a company's operations.

8 The IASB agreed that 'net debt' disclosures should not be part of the Amendments to IAS 1 short-term project and decided that requiring disclosures related to 'net debt' should be considered within another part of the Disclosure Initiative. The IASB requested that the staff prepare a paper that outlines the potential scope of a shorter-term project on 'net debt'.

<u>(B) Proposed amendments to IAS 1 – Totals and subtotals</u>

9 In response to feedback received at the Discussion Forum, IASB staff looked into whether subtotals of IFRS numbers, such as EBIT and EBITDA, should be acknowledged in IAS 1, addressing a view that certain subtotals or totals are not permitted to be presented or disclosed.

10 IASB staff noted that there are provisions in IAS 1, paragraphs 55 and 85, which already enable an entity to use judgement in disclosing totals and subtotals when they provide relevant information. In addition, paragraph 112(c) requires that the notes shall provide information that is not presented elsewhere in the financial statements, but is relevant to an understanding of any of them. Furthermore, paragraphs 15 and 17 of IAS 1 would require the presentation or disclosure of a subtotal/total to be a fair presentation of the amounts included in that subtotal/total.

11 However, IASB staff also noted concerns raised by constituents that:

(a) there may be confusion regarding how the totals and subtotals are presented;

(b) some subtotals and totals may be misleading or confusing; and

(c) some preparers are being discouraged by their auditors from presenting some subtotals/totals of IFRS recognised amounts on the face of their primary financial statements

The staff therefore recommended that additional wording be added to IAS 1 that relates to the notion of the presentation of totals and subtotals.

12 IASB staff noted a further possible reason why entities are discouraged from presenting or disclosing a subtotal/total is that there is a misconception that commonly used measures, such as EBIT and EBITDA calculated using IFRS recognised

amounts, cannot be presented or disclosed in the financial statements because they are not specifically permitted by IFRS and are therefore 'non-GAAP financial measures'.

13 After noting that they believe paragraphs 55, 85 and 112(c) permit subtotals/totals of IFRS recognised amounts, IASB staff noted another approach to address the issue would be to amend IAS 1 to clarify what factors an entity should consider when aggregating IFRS recognised amounts into subtotals and totals.

14 The IASB tentatively decided that guidance should be added to paragraphs 55 and 85 of IAS 1 to clarify the factors an entity should consider when aggregating IFRS recognised amounts into subtotals and totals. Those factors are outlined below[1]:

The totals and subtotals should:

(a) be made up of items recognised or otherwise disclosed in compliance with IFRS;

(b) reference line items and/or other amounts disclosed in the financial statements so that what constitutes the total or subtotal is understandable;

(c) should be calculated on a consistent basis from period to period;

(d) be labelled to reflect how they have been calculated; and

(e) not be displayed with more prominence than the specific subtotals referred to in this Standard.

15 In addition, IASB staff noted that the Feedback Statement raised the issue of whether examples of subtotals/totals such as EBIT or EBITDA should be specifically acknowledged in IAS 1. Staff noted that singling out particular subtotals or totals may be interpreted as giving these examples more significance than others and therefore recommended to the IASB that IAS 1 should not be amended to include specific examples of commonly reported totals or subtotals.

16 The IASB tentatively decided that specific examples of commonly reported totals or subtotals should not be included in IAS 1.

<u>(C) Presentation order of notes in the financial statements</u>

17 At the meeting in November the IASB staff presented to the IASB proposed amendments to paragraph 114 of IAS 1 to allow entity's greater flexibility to present

1 The wording proposed in Agenda Paper 8B to be included in a new IAS 1 paragraph 31B.

notes to the financial statements in a varied order. In addition, IASB staff proposed amendments to paragraph 113 to reflect the greater emphasis on understandability and comparability on the basis that[2]:

(a) related disclosures can be presented together therefore increasing the connectivity and linking in the financial statements, for example, financial instrument accounting policy and financial instrument note presented together;

(b) more prominence can be given to the main transactions and events affecting an entity; and

(c) users of the financial statements are provided with an insight into what management view as important to the reporting entity.

18 The IASB tentatively decided to include a proposal in the forthcoming amendment to IAS 1 Exposure Draft to allow entities more flexibility when ordering the notes to the financial statements[3].

IAS 1 Current/non-current classification of liabilities

19 At the September meeting the IASB requested staff to further develop a general approach to addressing the issue of classification of liabilities as current or non-current. At the October meeting staff sort the IASB's direction regarding:

(a) the classification principle; and

(b) the effect that breaches of conditions and events after the reporting period should have on classification.

20 There was general agreement from IASB members that:

(a) classification of a liability as non-current depends on whether there is a contractual arrangement in existence at the reporting date whereby the entity will not be required to settle the liability within the next 12 months;

(b) 'unconditional' should be deleted from paragraphs 69(d) and 74; and

(c) 'discretion' should be replaced with 'right' in paragraph 73.

21 In relation to the settlement of liabilities, there was general agreement with the proposed wording of 'by the transfer of cash or other assets'. However, one IASB

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2 IASB Agenda Paper 8A, November 2013

3 Based on a report in IASB Daily Staff Update, 20 November 2013

member commented that staff should consider in their paper the items that are classified as liabilities but would be settled in equity (e.g. a variable number of shares) and within 12 months.

22 The IASB then discussed, in the context of IASB's staff proposal to reaffirm the inclusion of 'with the same lender' in paragraph 73 of IAS 1 and clarifying the distinction between existing loans and loans from a new lender, and the issue of rolling over loans to the same lender on different terms.

23 A member noted situations in which a company may have the right to refinance its loan but the terms are determined by the lender who can thereby effectively deny the company the finance by increasing interest rates sufficiently that the company would not want to refinance. In response, it was agreed to include something along the lines of 'on same or similar terms' and that such loans would be classified as non-current. A member also raised the point of what the classification of a loan would be if a company were refinancing with the same lender on materially different terms. There was general agreement that such a loan would be classified as current.

24 The IASB discussed the issue of conditionality and the effect on the classification of a loan if the loan with a bank had a material adverse covenant that was outside the control of the entity (an example discussed by the IASB was where the main shareholder of a company holds 30% of the shares and the right to refinance is conditional on that shareholder's share), questioning whether this should be classified as conditional. The IASB generally agreed that this would involve management's judgement and should be considered within the scope of IAS 10 *Events After the Reporting Period.*

25 The IASB discussed whether to insert 'at the reporting date' into paragraph 69(d) and there was general agreement that post balance sheet events need to be considered, although IAS 1 should only go as far as provide a link to IAS 10. In relation to this, the IASB considered the effect of conditionality on the classification of liabilities and, in particular, whether breach of those conditions at the reporting date should affect classification as at the reporting date. The IASB requested that staff prepare a further analysis of the conditionality of rights including how changes in those conditions and management's expectations about the outcome of those changes would affect the classification of liabilities at the reporting date.