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Dear Kil-Woo

Exposure Draft ED 8 Operating Segments

Thank you for the opportunity to comment on the Exposure Draft ED 8 *Operating Segments*.

Our comments have been prepared in consultation with members through our Asia-Pacific Financial Reporting Advisory Group (APFRAG) which is a Board Committee representing a regional perspective from South-East Asia, Oceania and Australasia and our Financial Reporting and Governance Centre of Excellence.

The Introduction to the ED notes that the [draft] International Financial Reporting Standard (IFRS) arises from the International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB) joint short-term project with the objective of reducing differences between IFRSs and US Generally Accepted Accounting Principles (US GAAP) that are capable of resolution in a relatively short time and can be addressed outside major projects.

CPA Australia is not convinced that the [draft] IFRS is necessary to achieve convergence between IFRSs and US GAAP, for the reasons that:

- we understand that the current requirements do not prevent an entity from preparing one set of segment information that complies with both the requirements of IAS 14 *Segment Reporting* and SFAS 131 *Disclosures about Segments of an Enterprise and Related Information*;¹ and
- segment reporting is a disclosure standard and therefore does not affect the reconciliation of IFRS amounts to US GAAP.

¹ The Background information basis for conclusions of the FASB on SFAS 131 paragraph 55 states "The [International Accounting Standards Committee] IASC expects to issue a standard on segment reporting later in 1997. Although there will likely be differences between the IASC's requirements for segment reporting and those of this Statement, the boards expect that it will be possible to prepare one set of segment information that complies with both the IASC requirements and those of this Statement."

However, should the IASB intend to proceed with the proposals, we consider that this opportunity should be utilised to undertake a joint short-term project to improve SFAS 131 – in the absence of a significant improvement in the quality of segment reporting, CPA Australia is not able to support a change from the existing IAS 14.

Our detailed comments to the specific matters identified in the ED are attached to this letter.

Should you have any queries on our comments, please contact Dr Mark Shying, CPA Australia's Financial Reporting and Governance Senior Policy Adviser at mark.shying@cpaaustralia.com.au.

Yours sincerely

A handwritten signature in black ink, appearing to read 'GR', with a small dot above the 'i'.

Geoff Rankin FCPA
Chief Executive Officer

cc: D Boymal
M Shying

**CPA Australia comments on
Exposure Draft ED 8 Operating Segments**

CPA Australia is not convinced of the need for the [draft] International Financial Reporting Standard (IFRS). However, should the International Accounting Standards Board (IASB) intend to proceed with the proposals, we consider that the opportunity should be utilised to undertake a joint short-term project of improve SFAS 131 *Disclosures about Segments of an Enterprise and Related Information*. Our comments to the questions are made with that purpose in mind.

1. Adoption of the management approach in SFAS 131

Is this approach to segment reporting appropriate? If not, why not? What, if any alternative approach would you propose?

To not support an approach to segment reporting that is based on information about the components of the entity that management uses to make decisions about operating matters is difficult. Nevertheless, we are concerned that the segments based on the structure of an entity's internal organisation may not be comparable between entities that engage in similar activities (as opposed to the possible increased comparability within an entity across time). Accordingly, we are strongly of the view that retaining as a "safety net" the current approach in IAS 14 to identifying primary and secondary operating segments serves a useful purpose – increased comparability between entities.

We note the adoption of the management approach in SFAS 131 does not require that an entity report all of the information that is reviewed by the entity's chief operating officer to make decisions about resource allocations and to assess the performance of the entity. Rather, the approach to segment reporting is a modified management approach that includes both aggregation criteria and quantitative thresholds for determining reportable operating segments. Should the IASB proceed with the [draft] IFRS, we consider that the Introduction and Basis for Conclusions should carry that statement.

2. Divergence from SFAS 131

Do you think the draft IFRS should depart from the management approach in SFAS 131 by setting requirements for:

- a. the measurement of specified items; or
- b. the disclosure of specified amounts that might otherwise not be given?

If so, identify the requirements you would add and indicate what you see as the relative costs and benefits of any such requirements.

Yes. CPA Australia considers the requirement of paragraph 25 inappropriate and recommend its deletion. We are concerned that the entity's capacity to provide information about the components of the entity that management uses to make decisions about operating matters is hindered by the requirement that the principles most consistent with those used in the reported measures of the segment's profit or loss and assets are required to be used if the chief operating decision maker uses more than one measure (paragraph 25). For example, we note that some commentators assert that IFRS profit is artificially made more volatile as a consequence of adjustments for impairment losses, fair value movements in derivatives and share based payments with changes in estimates of forfeitures. Should the chief operating decision maker use two measures of the segment's profit or loss – one that includes IFRS volatile items and another that is the pre-IFRS adjustments figure, paragraph 25 requires the disclosure of the reported measures of the segment profit or loss and assets, notwithstanding that it is but one input used by management for the purpose of internal decision-making (and possibly not the most significant input).

3. Scope of the standard

Do you agree with the scope of the draft IFRS? If not, why not?

No. We note the scope of the [draft] IFRS extends to all entities that hold assets in a fiduciary capacity for a broad range of outsiders, such as a bank, insurance company, securities broker/dealer, pensions fund, mutual fund or investment banking entity. Paragraph BC16 infers that the decision to extend the scope is consistent with the still under-decision concept of "public accountability". CPA Australia recommends that the scope not be extended prior to the finalisation of that concept. Further, we do not consider it appropriate to extend the scope beyond that of SFAS 131. We suggest that when the IASB concludes on the concept of public accountability it should then use its best endeavours to get the Financial Accounting Standards Board to extend the scope of SFAS 131 to accommodate that concept.

Level of reconciliation

Do you agree with the level of reconciliation required in the draft IFRS? If not, indicate what you see as the relative costs and benefits of any other level of reconciliation.

We agree with the level of reconciliation required in the [draft] IFRS.

4. Geographical information about assets

Do you agree with the requirement to disclose geographical information about non-current assets excluding specified items? If not, for which assets would you require geographical information to be given?

No. We note that the [draft] IFRS requires disclosures by individual countries (paragraph 32). We do not support this requirement. In our opinion, separate disclosures for each individual country in Europe seems excessive, when it is likely the operations in each country (assuming same or similar product) are basically the same. We consider that aggregation should be permitted based on the aggregation criteria under IAS 14.

5. Consequential amendments to IAS 34 *Interim Financial Reporting*

Do you agree with the consequential amendments made to IAS 34? If not, why not?

We agree with the consequential amendment to IAS 34 to require an entity to report selected information about its operating segments in interim financial reports.

OTHER CONCERNS

Paragraph 32. Balance between benefit and cost: If operating segments are not based on differences in geographical areas of operation, then disclosures by geographic area are required (unless the necessary information is not available and the costs to develop it would be excessive). CPA Australia considers that the "balance between benefit and cost" is a decision for the IASB when making the standard, and not the entity - if the information has the qualitative characteristics that makes it useful to users, the entity should not be able to avoid the requirement of the Standard. We recommend the withdrawal of the balance between benefit and cost from paragraph 32 (and paragraph 31) and its replacement with the "impracticable" requirement.

Implementation Guidance paragraph IG4.

- We are not sure how you can have goodwill not allocated to a reportable segment, at least for such a large amount, as goodwill under IFRS 3 *Business Combinations* must be allocated to a cash-generating unit no larger than a segment.
- The expression "capital asset" is not defined in the Glossary of Terms. Accordingly, we do not know its meaning.

Implementation Guidance paragraph IG7. Flowchart appears incorrect. We would have placed the arrow that comes from the box "aggregate segments if desired" before the diamond "do identified reportable segments account for 75% etc.".

Implementation Guidance paragraph IGA1. Should the reference to reportable segments be to operating segments? Operating segments is the internal segments, and reportable segments are the ones required to be reported, which can be after aggregation.