

EFRAG FR TEG-CFSS
15 March 2022
Paper 07-03
EFRAG Secretariat: PFS team

PRIMARY FINANCIAL STATEMENTS

EXPECTED COSTS AND BENEFITS AND EFFECTIVE DATE

15 MARCH 2023



DISCLAIMER

This paper has been prepared by the EFRAG Secretariat for discussion at a public meeting of EFRAG FR TEG-CFSS. The paper forms part of an early stage of the development of a potential EFRAG position. Consequently, the paper does not represent the official views of EFRAG or any individual member of the EFRAG Board or EFRAG FR TEG-CFSS. The paper is made available to enable the public to follow the discussions in the meeting. Tentative decisions are made in public and reported in the EFRAG Update. EFRAG positions, as approved by the EFRAG Board, are published as comment letters, discussion or position papers, or in any other form considered appropriate in the circumstances.

TRANSITION AND EFFECTIVE DATE

PROPOSAL IN THE IASB EXPOSURE DRAFT

- An entity would have to apply the draft Standard for **annual reporting periods beginning on or after 18–24 months from the date of publication**
- An entity would have to **apply the draft Standard retrospectively** in accordance with IAS 8
- **Earlier application would be permitted** - if an entity applied the draft Standard for an earlier period, it should disclose that fact in the notes
- In the first year of application an entity would have to present each of the headings and subtotals required by the draft Standard (including operating profit or loss) in **condensed financial statements provided in interim financial reports**, despite the requirements in paragraph 10 of IAS 34
- The requirements in paragraph 10 of IAS 34 for condensed financial statements would only be applied after the preparation of the first set of annual financial statements prepared in accordance with the draft Standard

TRANSITION AND EFFECTIVE DATE

EFRAG COMMENT LETTER

- EFRAG recommended that consideration is given to the practicalities and timescales of implementation of IFRS 17 together with any new standards or amendments arising from this project
- EFRAG considered that the proposed time of 18 to 24 months for a retrospective first-time application may not be sufficient, particularly if the IASB decides to proceed with all its proposals, particularly disclosures by nature when presenting by function

EFRAG SUMMARY REPORT AND RECOMMENDATIONS

- A few participants cautioned the IASB deciding on the effective date of the future IFRS Accounting Standard given the practicability and timescales of implementation of IFRS 17 and Sustainability Standards in Europe
- In addition, some preparers that are currently listed in the U.S. and/or present operating expenses by function noted that they would need longer for implementing the new requirements

TRANSITION AND EFFECTIVE DATE

EFRAG SECRETARIAT ANALYSIS

- The EFRAG Secretariat considers that the proposed time horizon of 18 to 24 months for retrospective first-time application is likely to be sufficient, when considering the IASB's redeliberations on disclosures by nature when presenting by function and introduction of the undue cost or effort relief for foreign exchange differences and gains or losses on derivatives not designated as hedging instruments
- Nonetheless, the EFRAG Secretariat considers that consideration should be given to the practicalities and timescales of implementation of the new requirements arising from this project, together with the sustainability standards in Europe, which apply to corporates in general, and IFRS 17 for insurers (which is already being implemented and impacting presentation)
- The time needed to implement maybe longer depending on how the IASB deals with the cases where it is not possible to determine the exact amount of specific costs by nature that were capitalised and expensed later (e.g. sale of inventory). In addition, this project will also impact other departments that rely on financial information
- Thus, the EFRAG Secretariat would prefer that the IASB would provide preparers 24 months for implementation. Still, the EFRAG Secretariat needs to see the outcome of the IASB's redeliberations to be able to make a full assessment

OVERVIEW OF THE EFFECTS ANALYSIS

OVERVIEW OF THE EFFECTS ANALYSIS BY THE IASB

- The IASB typically publishes a separate effects analysis report when a major new IFRS Accounting Standard is issued, including the likely costs of implementing the new requirements and the likely ongoing associated costs and benefits

Most benefits would relate to:

- Additional required subtotals that will provide greater comparability of financial performance across entities and between periods for an entity
- Transparency of reporting of management defined performance measures to facilitate communication between preparers and users of financial statements
- Aggregation and disaggregation principles that will provide relevant information and facilitate communication between preparers and users of financial statements

Most implementation costs would relate to:

- the process changes and possible system changes required to implement the new requirements; and
- training of staff and communicating changes to reported information to external parties

Some of the proposed requirements may also result in ongoing cost (statement of profit or loss mainly)

For users, mostly initial implementation costs would be related to adjusting models and analysis methods to the new structure of the financial statements and additional information provided

OVERVIEW OF THE EFFECTS ANALYSIS

LOCAL LAWS OR REGULATIONS

- Some jurisdictions have local laws for presentation and disclosure in financial statements (e.g. requirements to disclose some or all operating expenses by nature when presenting by function). Such laws may make the proposed requirements easier to apply and result in lower implementation costs

Benefits for digital reporting

Some proposals are likely to provide similar benefits to paper-based and digital users (thus reducing the cost of obtaining information for digital users), for example:

- comparability of defined subtotals (such as operating profit or loss)
- disclosures on management performance measures (included in financial statements, thus more likely to be tagged)

Other proposals are not likely to provide similar benefits to paper-based and digital users without further development. For example, proposals that will improve how information is communicated – focusing in particular on providing users with a better understanding of ‘relationships’:

- relationships between items presented in primary financial statements; and
- relationships between items presented in primary financial statements and items disclosed in notes

The IASB is exploring modelling approaches to IFRS Accounting Taxonomy that could facilitate digital users in consuming information (specifically with regard to ‘relationship information’)

EFFECTS ANALYSIS

EFRAG SECRETARIAT ANALYSIS

In its draft comment letter, EFRAG presented an early-stage analysis in order to help its constituents understand current practices on presentation and how the IASB's tentative decisions will impact current practices on presentation. Some of the key messages include:

- The IASB's proposals would lead to a significant change to current practice on presentation of financial statements, both for financial institutions and corporates (mainly for the statement of profit or loss)
- **Subtotals:** the IASB's proposals would require the presentation of subtotals that are already widely used in practice, such as operating profit. However, many entities may need to change the labelling and their calculation. Entities may continue to use previous subtotals but then as an MPM (e.g. core profit)
- **Operating profit:** In most cases the IASB's proposals are likely to affect how the financial institutions define their subtotal 'operating profit or loss' (e.g. unwinding of discount of leases)
- **Investing category:** the IASB's proposals are likely to change current practice as currently companies either present a single category for financing and investing or do not present an investing category at all

EFFECTS ANALYSIS

EFRAG SECRETARIAT ANALYSIS

- **Investing category:** currently entities do not need to separate returns from investments made in the course of their main business activities from those that are not. Therefore, this would be a change to current practice as companies would be required to make such split under the IASB's proposals
- **Financing category:** the IASB proposals are likely to impact entities that currently include all income and expenses related to financing and investing together above profit before tax and those that have a single category for financing and investments (e.g. those that currently present 'finance results' may need to change its labelling and how this subtotal is calculated)
- **Financing category:** currently entities do not need to make an accounting policy for the presentation of income and expenses from financing activities and from cash and cash equivalents. Therefore, this may impact current practice
- **Associates and joint ventures:** entities that present their share of the profit or loss in associates and joint ventures as part of operating profit are likely to have to revise their current subtotals and line items
- **Disaggregation:** the IASB proposals on aggregation and disaggregation are likely to affect many entities which will need to revise their current presentation of line items in order to meet the new requirements - many non-financial entities will need to provide a higher level of disaggregation

EFFECTS ANALYSIS

EFRAG SECRETARIAT ANALYSIS

- **MPMs:** the IASB's proposals would on the one hand provide more clarity to the disclosed performance measures and would require this information to be audited. On the other hand, it would bring a significant number of non-IFRS measure disclosures into the IFRS financial statements related to the statement of financial performance (it would exclude other APMs related to the statement of financial position and statement of cash flows)
- **Statement of cash flows:** the IASB's proposals are likely to change significantly current practice when using the indirect reconciliation of cash flows from operating activities. Thus, most non-financial and financial entities will have to revise their statement of cash flows to start with an operating profit subtotal. Non-financial entities will have to revise the presentation of interest received, interest paid, and dividends received in the statement of cash flows. No significant impact is expected for the presentation of dividends paid which are presented within the financing activities section.
- With regard to financial entities, presentation of interest paid and received, and dividends received, will impact the statement of cash flows depending on how these entities will classify related income and expenses in the statement of profit or loss. It is likely that many financial entities will present most, or all, of their interest income, interest expenses and/ or dividend income in the operating section of the statement of profit or loss. EFRAG assessed that in such cases there would not be a significant change in practice

EFFECTS ANALYSIS

EFRAG SECRETARIAT ANALYSIS

- The EFRAG Secretariat will need to update its early-stage analysis as soon as the IASB's redeliberations draw to a close
- In general, the EFRAG Secretariat agrees with the IASB Staff's preliminary effects analysis. In particular, the EFRAG Secretariat highlights that the IASB has made a number of tentative decisions that will reduce implementation costs, such as those related to disclosures by nature when presenting by function and introduction of undue cost or efforts reliefs and a simplified approach for calculating the tax effect as part of the required reconciliation of MPMs
- Nonetheless, the EFRAG Secretariat will need to see the outcome of the IASB's redeliberations to be able to make an assessment of the potential costs and benefits. In particular, the IASB's decisions on disclosures by nature when presenting by function in cases where it is not possible to determine the exact amount of specific costs by nature that were capitalized in one year but expensed later, including those expensed on the following years (e.g. sale of inventory), and the presentation of associates and joint ventures

QUESTIONS FOR EFRAG FR TEG-CFSS MEMBERS

- For entities in your jurisdiction, what information that is needed to apply the requirements in the new IFRS Accounting Standard would be readily available? (ASAF question)
- For entities in your jurisdiction, what new information will they need to gather to apply the requirements in the new IFRS Accounting Standard? Please explain (ASA F question):
 - which new information is likely to be easily obtainable, for example, because of similar requirements in local laws or regulations (see slide 19 of Agenda Paper 07-04); and
 - which new information is likely to require changes in systems and processes to gather and what is the extent of changes that are likely to be required.
- Are there any entities in your jurisdiction that are planning to apply early the new IFRS Accounting Standard? (ASAF question)
- How much time between finalisation and effective date is needed, assuming no relief from providing comparative information? (EFRAG Secretariat question)
- Do you have any comments on the expected costs and benefits to preparers and users in your jurisdiction shown on slides 14–18? (Agenda Paper 07-04 – ASAF question)
- Do you have any comments on the expected benefits and additional benefits that the IASB is developing for digital reporting on slide 20? (Agenda Paper 07-04 – ASAF question)



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THANK YOU



EFRAG
Aisbl - ivzw
35 Square de Meeüs
B-1000 Brussel
Tel. +32 (0)2 210 44 00
www.efrag.org

