

Primary Financial Statements Income and expenses of limited recurrence (unusual income and expenses)

Joint CMAC-GPF meeting
Agenda Paper 3
June 2022

Purpose of this session

- The purpose of this session is to obtain feedback from CMAC/GPF members to help the IASB's future discussions on income and expenses with limited recurrence (unusual income and expenses):
 1. The population of income and expenses captured by the definition; and
 2. The period to be considered in making the assessments required by the definition (the assessment period)

Agenda

Background (see slides 4-7)

Working definition of income and expenses with limited recurrence
(see slides 8-9)

The assessment period (see slides 10-11)

Examples to be considered in the breakout groups (see slides 12-24)

What was proposed in the ED—unusual income and expenses

Definition



Income and expenses with **limited predictive value**.

Income and expenses have limited predictive value when it is reasonable to expect that income or expenses that are similar in **type and amount** will not arise for several future annual reporting periods.

Income and expenses from the recurring remeasurement of items measured at a current value would not normally be classified as unusual.

Disclosures

Amount & narrative description

Amount disaggregated by:

- line items presented in statement of profit or loss; and
- line items disclosed in analysis of operating expenses by nature, if the entity analyses expenses by function in the statement of profit or loss

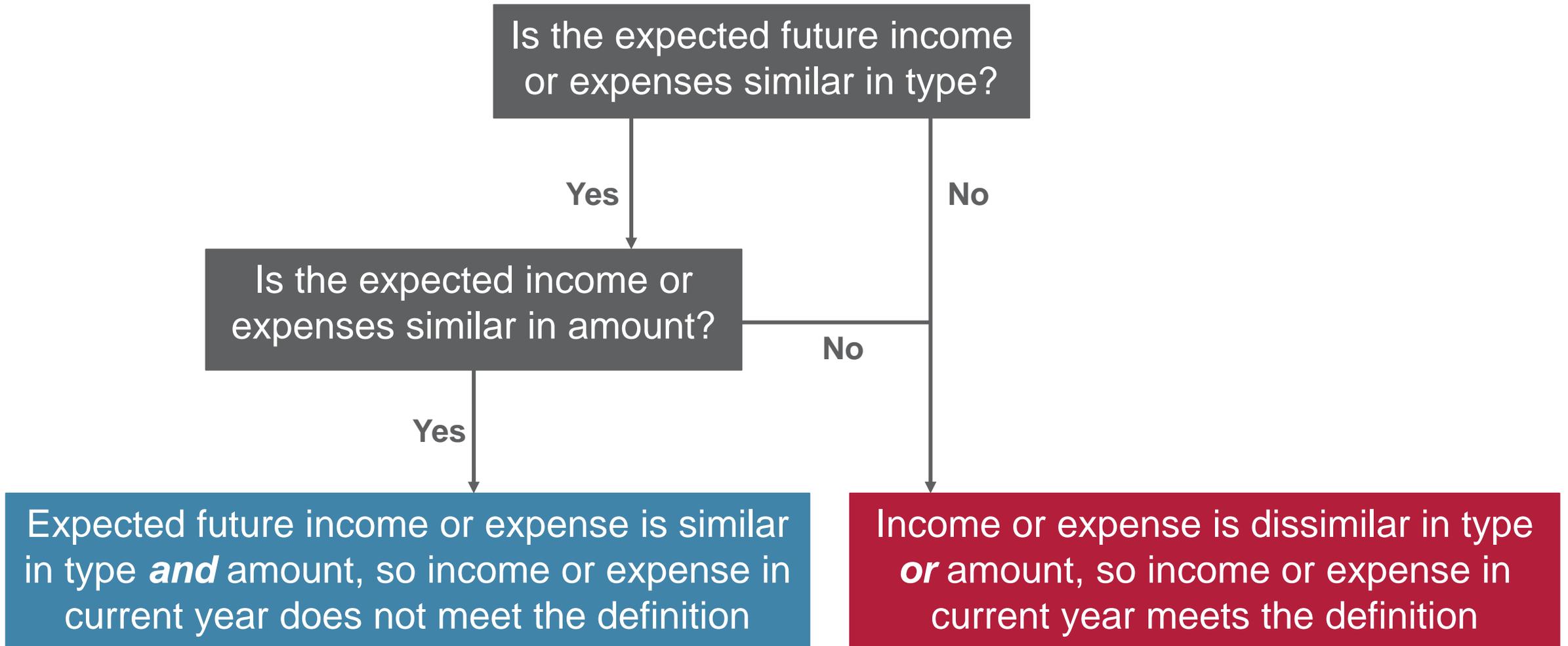
Overview of feedback

- Many respondents, including almost all users, agreed the IASB should define unusual items
 - users want to identify recurring or normalised earnings but currently have to rely on voluntary disclosures by an entity to do so
 - definition would provide discipline and reduce opportunistic classification of items as unusual
- Most, mainly preparers, but also some users, did not agree with the proposed definition. Concerns over
 - the scope of the items captured in the proposed definition, for example
 - comparison with the past as well as the future
 - items that are expected to arise in more than one reporting period
 - the subjectivity inherent in the proposed definition
 - more guidance needed

IASB redeliberations to date—December 2021 and May 2022 meetings

- Tentatively decided to explore how to proceed with a definition of unusual items
 - acknowledged that a ‘perfect’ answer may not be possible
- Identified two main questions to address first
 - Topic 1: whether an item must be ‘unusual’ compared to income and expenses in the past to meet the definition
 - Topic 2: how to deal with items that arise in a few reporting periods, not just a single reporting period
- Feedback from limited outreach with users
 - Mostly supportive of a definition that captures a broad range of items
 - Strong support for including items that arise in a few reporting periods, not just a single reporting period

Not similar in type *and* amount = dissimilar in type *or* amount



Working definition

Income and expenses have limited recurrence when it is reasonable to expect that income or expenses that are similar in type and amount will cease, and once ceased will not arise again, before the end of the assessment period

- Similar income and expenses can have arisen in the past, consistent with the proposal in the Exposure Draft
- Similar income and expenses can be expected to arise within the assessment periods, as long as they cease by the end of the assessment period, a change from the Exposure Draft
- Income and expenses will be captured by the definition if they are dissimilar in type or amount to expected ongoing income or expenses, consistent with the proposal in the Exposure Draft
- Broad definition that captures many items of income and expenses with limited recurrence
 - Responds to feedback from those that wanted information about a broad range of items
 - IASB also exploring splitting the note that provides the information to allow users of financial statements to identify easily items with different recurrence characteristics

Is the working definition too broad?

- Discussion at the May IASB meeting about the required disclosures indicated some potential concerns about some items that would meet the definition
 - For example, revenue lower than expected in the future because of an expected future acquisition
- Indicates we may need to consider possible constraints on the definition, for example one or more of:
 - Requiring a comparison with past income and expenses
 - Limiting the definition to income and expenses that are dissimilar to future expected income or expenses *in type*, ie do not include income and expenses that are only dissimilar *in amount*
 - Requiring the comparison to future income and expenses to be based on future events for which there is sufficient objective evidence, consistent with the requirements in IAS 37 on when future events should be reflected in a provision
- See examples for discussion in breakout groups (slides 13-22)

The assessment period

- The future period in which the entity needs to make an assessment of whether similar income or expenses are expected to arise
 - Too short a period would:
 - exclude items even though they are expected to arise over only a few annual periods (because they do not cease soon enough), ie be too restrictive and
 - capture items that are expected to arise in the future but not immediately (because they do not arise again soon enough), ie be too broad
 - Too long a period would:
 - capture items that are expected to arise for many periods, ie be too broad and
 - exclude items that are not expected to arise again for many years, ie be too restrictive

Examples of the effect of the assessment period

- Period too short, for example just one year in the future
 - Would exclude expenses from a one-off restructuring that starts shortly before the end of the current period and is expected to last for only 18 months
 - Would capture an expense that regularly occurs every other year
- Period too long, for example six years in the future
 - Would capture expenses from a restructuring that starts at the beginning of the current period and is expected to last five years
 - Would exclude a one-off expense that arose this year and then is not expected to arise again for at least 4 years, but is expected to arise at some point before the end of six years
- See questions for breakout groups (slides 23-24)

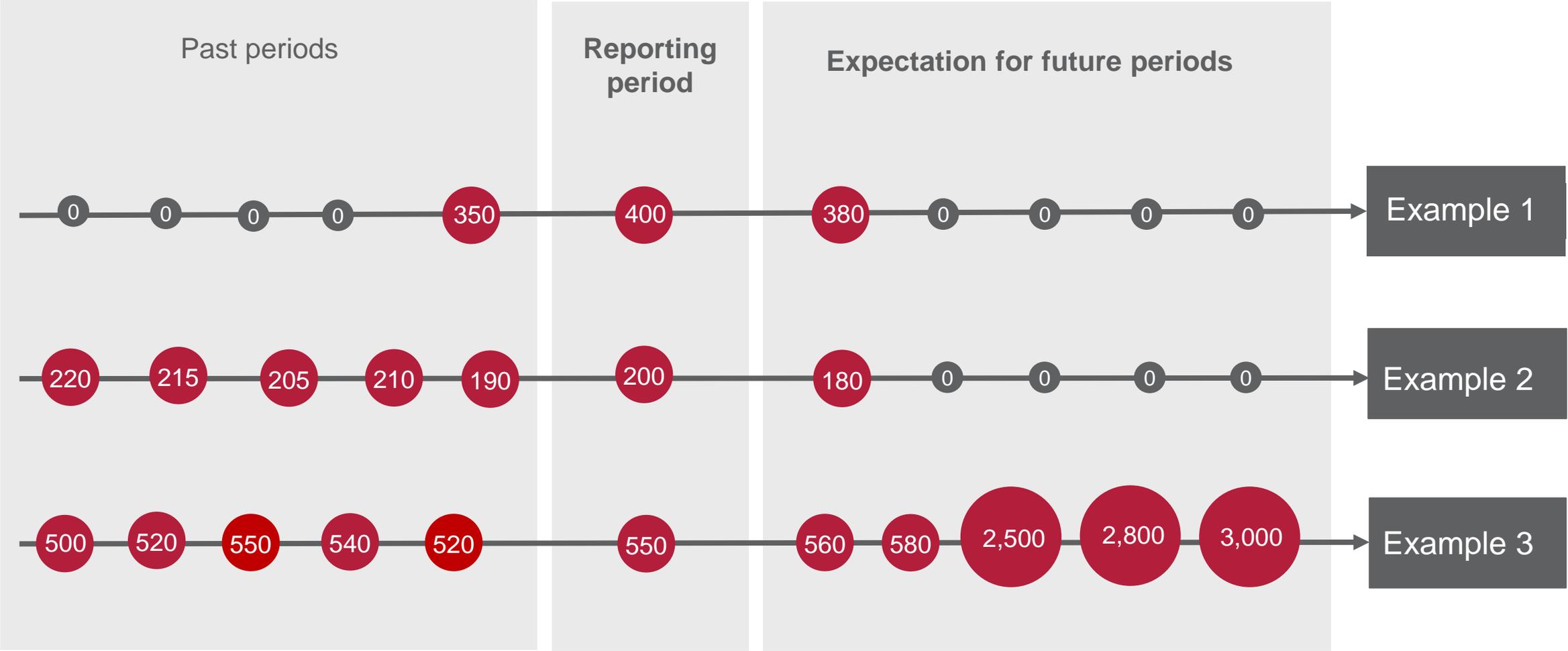
Topics for discussion in breakout groups

- Examples of income and expenses captured by the definition (slides 13-22)
- How to set the assessment period (slides 23-24)

Examples of items captured by the definition

- Examples for discussion:
 - Example 1: Restructuring expenses
 - Example 2: Revenue and expenses higher than expected in the future because of the expected end of existing activities
 - Example 3: Revenue and expenses lower than expected in the future because of the expected start of new activities in the future
- Examples explore:
 - The effect of the entity's circumstances
 - Income and expenses expected in the future are not similar if they have sufficient dissimilar characteristics that information about the limited recurrence of the income or expenses in the current period is material (ie could affect investors' decisions)
 - The effect of three possible constraints on the definition (slide 9)
 - Requiring a comparison with past income and expenses
 - Limiting the definition to income and expenses that are dissimilar to future expected income or expenses *in type*
 - Requiring the comparison to future income and expenses to be based on future events for which there is sufficient objective evidence

Overview of the examples



Example 1 – restructuring expenses

- **Fact pattern**

- An entity is restructuring its activities in jurisdiction X, to align them with its activities in other jurisdictions. The restructuring started 1 year ago and is expected to continue for a further 6 months after the end of the current reporting period. (Assume the assessment period is at least three years.)

- **Effect of entity-specific circumstances**

- Are similar restructurings expected to occur in the future (ie any expected future restructurings do not have sufficient dissimilar characteristics that information about the limited recurrence of the income or expenses in the current period is material)?

- If not, the expenses have limited recurrence
- If so, the expenses do not have limited recurrence

Example 1 – possible changes to (or constraints on) the definition

- **Comparison with the past**
 - Have similar restructurings (in type and amount) occurred in the past?
 - If no, the expenses could have limited recurrence if similar expenses are expected to cease and then not recur in the assessment period
 - If yes, the expenses do not have limited recurrence
- **Limited recurrence by type only, not amount**
 - Are similar restructuring expenses by type expected to recur in the assessment period, after having ceased?
 - If yes, the restructuring expenses this year would not meet the amended definition, even if the amounts are dissimilar to those expected in the future
 - If no, restructuring expenses this year would meet the amended definition
- **Only compare this year's restructuring expenses with future restructuring expenses for which there is sufficient objective evidence**
 - We assume there is sufficient objective evidence that the current restructuring will cease before the end of the assessment period
 - If there is insufficient objective evidence that similar restructurings will occur in the future, the definition would be met
 - In this case, such an amendment to the definition could in fact expand the scope because similar restructurings might be expected to recur in the assessment period, but no objective evidence for the future expected restructurings is available

Example 2 - Revenue and expenses higher than expected in the future because of the expected end of existing activities

- **Fact pattern**

- An entity is planning to discontinue a product in the next few years, resulting in expected reduced revenue and expenses.

- **Effect of entity-specific circumstances**

- Is the entity expecting to replace the product with a similar type of product?

- If no, the revenue and expenses have limited recurrence

- If so, are the future revenue and expenses from the similar type of product expected to be similar amounts to the amounts in the current year?

- If no, the revenue and expenses have limited recurrence

- If yes, the revenue and expenses do not have limited recurrence

Example 2 – possible changes to (or constraints on) the definition

- **Comparison with the past**
 - Assume revenue and expenses similar in type have occurred in the past
 - Have revenue and expenses similar in amount occurred in the past?
 - If yes, the revenue and expenses this year would not meet the amended definition
 - If no, the revenue and expenses this year would meet the amended definition (assuming they already met the working definition)
- **Limited recurrence by type only, not amount**
 - Is similar revenue and expenses by type expected not to recur in the assessment period, after having ceased?
 - If yes, the revenue and expenses this year would not meet the amended definition, even if the amounts are dissimilar to those expected in the future
 - If no, the revenue and expenses this year would meet the amended definition
- **Only compare this year's revenue and expenses with future revenue and expenses for which there is sufficient objective evidence**
 - Is there sufficient objective evidence that the product will be discontinued?
 - If yes, consider whether a similar product will replace it.
 - If no, the existing revenue and expenses would be regarded as continuing and the definition would not be met
 - Is there sufficient objective evidence that the product will be replaced by a similar product?
 - If no, amended definition will be met
 - If yes, consider whether the amounts of revenue and expenses will be similar.
 - If amounts not similar, amended definition will be met
 - If amounts similar, amended definition will not be met

Example 3 - Revenue and expenses lower than expected in the future because of the expected start of new activities

- **Fact patterns**

- **A:** the existing revenue-generating activities are expected to continue but the entity is planning to introduce a new product in the next few years, resulting in increased revenue and expenses.
- **B:** the existing revenue-generating activities are expected to continue but the entity is expecting higher revenue and expenses in the future because of an expected acquisition

- **Effect of entity-specific circumstances**

- **A:** is the new product similar in type to existing products?
 - If no, the current revenue and expenses will not have limited recurrence because they are expected to continue
 - If yes, the revenue and expenses could have limited recurrence if their amount is expected to be dissimilar in the future
- **B:** Will the expected acquisition result in new products that are similar to existing products?
 - Outcomes the same as for A

Example 3 – possible changes to (or constraints on) the definition

- **Comparison with the past**
 - Assume revenue and expenses similar in type have occurred in the past
 - Have revenue and expenses similar in amount occurred in the past?
 - If yes, the revenue and expenses this year would not meet the amended definition
 - If no, the revenue and expenses this year would meet the amended definition, if they met the working definition
- **Limited recurrence by type only, not amount**
 - the revenue and expenses this year would be excluded from the note, because the existing type of revenue and expenses are expected to continue
- **Only compare this year's revenue and expenses with future revenue and expenses for which there is sufficient objective evidence**
 - Assume there is sufficient objective evidence that the existing product will continue to generate similar revenue and expenses
 - Accordingly, this year's revenue and expenses would meet the amended definition only if there were sufficient objective evidence of future changes resulting in revenue and expenses similar in type but dissimilar in amount

Possible and likely effects of possible constraints

	Require comparison with the past	Include only items that are dissimilar in type	Require future income and expenses to be based on events with sufficient objective evidence
Example 1- restructuring expenses	Often the same outcome, but could be narrower	Often the same outcome, but could be narrower	Could be the same, but might be broader
Example 2 – existing product line expected to be discontinued	Could be the same, but often would be narrower	Could be the same, but often would be narrower	Same or broader or narrower (outcome depends on stage in process)
Example 3 – existing revenue-generating activity continuing, new product/acquisition expected in near future	Could be the same, but often would be narrower	Excluded from definition	Could be the same, but often would be narrower

* Same – refers to same as outcome as the working definition without constraints

Definition – questions for breakout groups

- **Q1** In what entity-specific circumstances would you find it useful to have information about income/expenses in a single note about items with limited recurrence?
 - Example 1: restructuring expenses
 - Example 2: existing product line expected to be discontinued
 - Example 3: existing revenue-generating activity continuing, new product/acquisition expected in near future
- **Q2** Which, if any, of the possible constraints of the working definition would help achieve your answers to Q1?

Period of assessment

- Possible ways of setting the period:
 - Link to period of budgets and forecasts
 - Period or range specified by the IASB (very initial thinking—2-4 years)
 - Period decided by entity

Period of assessment

- Questions for breakout group
 - How important is it for entities to use the same period?
 - What periods are budgets and forecasts available for?
 - Is that a sufficiently long period for the assessments?
 - If not, what information would be used for an assessment if the period extends beyond the period of budgets and forecasts?
 - If you, as a preparer of financial statements, had to set the period, how would you decide what period to use?
 - Are there any other factors the IASB should consider?
 - Given your view on the questions above, which of the possible ways of setting the period do you favour?