IFRS Accounting

# Meeting summary

## Capital Markets Advisory Committee

Date **9 March 2023**

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This document summarises a meeting of the Capital Markets Advisory Committee (CMAC), a group of nominated members with extensive practical experience in analysing financial information and who are established commentators on accounting matters in their own right or through the representative bodies with which they are involved. The CMAC supports the IFRS Foundation and the International Accounting Standards Board (IASB) in their objectives, and contributes towards the development, in the public interest, of high-quality, understandable, enforceable and globally accepted IFRS Accounting Standards.

### CMAC members who attended the meeting

| Region | Members |
|---|---|
| Asia-Oceania<br>(including one at large) | Ge Xiaobo[a]<br>Koei Otaki[a] |
| Europe<br>(including one at large) | Anthony Silverman<br>Deirdre O'Leary<br>Jacques de Greling[a]<br>James Hyde<br>Jeremy Stuber<br>Joao Toniato[a]<br>Kenneth Lee<br>Matthias Meitner<br>Oliver Gottlieb<br>Philip Robinson<br>Selim Gogus<br>Sunil Singhania [a]<br>Terence Fisher |
| The Americas | Enitan Adebonojo<br>Paulo Cesar Aragão<br>Anthony Scilipoti<br>Rosemary Zigrossi |

[a] Remote participation via videoconference.

## IASB Update

1. Members received an update on the work plan of the IASB, including the amendments to IFRS 7 on supplier finance (publication expected in the second quarter), and the Exposure Draft *International Tax Reform—Pillar Two Model Rules*, which was published in January.
2. IASB staff gave a detailed overview of the proposals in the Exposure Draft *International Tax Reform-Pillar Two Model Rules (*proposed amendments to IAS 12).
3. Members asked questions about, and shared views on, the proposals in the Exposure Draft.
4. Staff set out the expected timetable for redeliberations and issuance of amendments to IAS 12 (subject to feedback on the Exposure Draft).

## ISSB Update

5. The session aimed to provide CMAC members with an update on the recent activities of the International Sustainability Standards Board (ISSB), including:
    (a) The current status of the development of the prospective Standards IFRS S1 *General Requirements for Disclosure of Sustainability-related Financial Information* and IFRS S2 *Climate-related Disclosures*, expected to be published in the first half;
    (b) the digital taxonomy, training materials and capacity building efforts related to the prospective Standards; and
    (c) the ISSB's next steps.

## Primary Financial Statements

6. The purpose of this session was to update the CMAC members on the Primary Financial Statements project and to seek members' views on:
    (a) the factors that the IASB should consider in determining the transition period and effective date of the forthcoming IFRS Accounting Standard *General Presentation and Disclosures*; and

(b) the expected benefits and costs for users of the forthcoming IFRS Accounting Standard to help develop the Effects Analysis that will be published with the Accounting Standard.

**Update on the project**

7. The staff explained the status of the Primary Financial Statements project, including an overview of the feedback received from targeted outreach conducted in 2022.
8. Most members are supportive of the IASB's overall direction taken in the redeliberations. Some members are supportive of the IASB's tentative decisions to withdraw the proposals related to integral and non-integral associates and joint ventures and the disclosure of unusual income and expenses. One member added that the disclosure of management performance measures and the general requirements for disaggregation would mitigate the concerns about the withdrawal of the proposal to disclose unusual income and expenses.
9. One member asked the staff how entities that provide financing to customers as a main business activity, such as automobile manufacturers, would classify the expected credit losses arising from providing financing to customers. The staff responded that they would be classified in the operating category.
10. One member asked whether the illustration of the statement of profit or loss should also include profit attributable to holders of claims against the parent classified as equity and non-controlling interests. An IASB member said that they would be included and that further work on profit attributable to ordinary shareholders and other shareholders is being considered in the Financial Instruments with the Characteristics of Equity project.
11. One member asked where in the financial statements an entity would include management performance measures. The staff responded that if a management performance measure fits within the structure of the statement of profit or loss, the entity can present the measure in the statement of profit or loss but all disclosures for management performance measures are required to be included in the notes.
12. Some members asked about education of users. The staff said that education sessions for users are planned for after the IASB has completed its redeliberations and issued the Accounting Standard and closer to the effective date of the Accounting Standard.

## Benefits and costs to users

13. Staff asked CMAC members for input on:
    (a) the expected overall benefits and costs to users of the proposals;
    (b) the expected benefits to users from the proposals for subtotals, management performance measures, and disaggregation; and
    (c) the expected benefits and additional benefits being developed for digital reporting.
14. CMAC members did not specifically comment on the expected benefits for digital reporting.

***Overall benefits and costs***

15. The overall benefits of the project mentioned by members included:
    (a) improving transparency in how entities create economic value which will help users to understand how management allocate capital and to make better judgements about an entity's value;
    (b) providing clarity about where information is included in the financial statements which will allow users to make their own adjustments when using the information in their analysis;
    (c) improving the efficiency in model construction by analysts due to the additional links between information presented in the primary financial statements and information disclosed in the notes;
    (d) enhancing comparability of information between entities; and
    (e) increasing the level of trust in the numbers provided in the financial statements due to enhanced disclosures about amounts included in line items presented in the primary financial statements and management performance measures.
16. Most members said that users are likely to benefit from the project without significant cost. One member added that the IASB's proposal would likely reduce the costs for users and improve efficiency in analysing financial statements.

***Benefits and costs related to subtotals***

17. Most members said that the proposed structure of the statement of profit or loss would benefit users because income and expenses will be classified in categories consistently by all entities.
18. Some members commented on the proposal to classify interest revenue from cash and cash equivalents in the investing category and interest expenses in the financing category. These members said that it would be beneficial to users if these income and expenses are classified in the same category because some entities manage interest revenue and interest expenses on a net debt basis. An IASB member said that classifying these income and expenses in a consistent location by all entities is expected to be beneficial to users because it would provide users with information to make their own adjustments.
19. One member commented that cash flows from interest received and interest paid would be classified in different categories in the statement of cash flows. The member thinks that an approach that requires an entity to classify these cash flows as operating cash flows is more beneficial to users because it is consistent with US GAAP. An IASB member said that the IASB tentatively decided not to delay the proposed amendments to the cash flow statement until the cash flow statement project because the amendments are expected to bring incremental benefits to users.
20. One member supported the IASB's tentative decision for classifying income and expenses from associates and joint ventures accounted for using the equity method in the investing category because it would make it easier to analyse operating profit. However, another member noted that for certain industries in the member's jurisdiction, income and expenses from associates and joint ventures accounted for using the equity method could be relatively large compared to the reporting entity's total revenue. Users in that jurisdiction analyse the income and expenses from these associates and joint ventures as part of the entity's operating profit or loss because they are part of the main business activities of the entity.

***Benefits and costs related to management performance measures***

21. Most members said that the proposals for management performance measures would benefit users. The expected benefits include:
    (a) assurance of management performance measures as management performance measures will be included in the audit scope;

(b) improving the transparency of management performance measures which over time is expected to make such measures more consistent and reliable and help to build trust between users and preparers;

(c) providing useful information to understand the diversity in how management performance measures are calculated within sectors; and

(d) providing useful information about the adjustments an entity has made to management performance measures, such as items that an entity considers as unusual or one-time.

22. Some members said the disclosure of tax and non-controlling interests for reconciling items would be useful for their analysis, especially to make forecasts.
23. One member said that the disclosure requirements for management performance measures might be less relevant for entities in Europe because they already have the ESMA framework for alternative performance measures. An IASB member said that the ESMA framework is guidance instead of a requirement and the disclosure of the tax effect and non-controlling interests for each reconciling item are not included in that guidance.

***Benefits and costs related to disaggregation***

24. Some members said that the IASB's proposals on disaggregation would be beneficial because users can obtain incremental information about the entity.
25. One member asked about expanding the scope of the disclosure of operating expenses by nature. The staff said the IASB will discuss whether impairments and write-downs of inventory should be included in the disclosure requirement in a future meeting. Some members said that disclosure of impairments in each line item would be important for users' analysis.
26. One member said that the disclosure of depreciation, amortisation and employee benefits would not provide the complete picture of an entity's operating expenses and, therefore, the member said that requiring an entity to disclose all operating expenses by nature would be beneficial to users. An IASB member said that the revised proposal on the disclosure of operating expense would provide users with incremental information on the amount of each operating expense included in each line item by function. The IASB member also said that if the IASB were to retain the proposal in the

Exposure Draft, entities might need another two or three years to develop a system to provide the information required.

**Transition period and effective date**

27. The staff asked CMAC members for input on proposals for which users would need comparative information in the first year of application in order to obtain the full benefits from the proposal.
28. Some members said that comparative information for at least one year would be needed for all proposals in the first year of application. One member said that comparative information for three years would be helpful for trend analysis.

**Next steps**

29. The IASB will consider the feedback from the members on transition and effective date in a future meeting. Illustrative examples for this project are planned to be discussed at the joint Global Preparers Forum (GPF) and CMAC meeting in June 2023.

## Business Combinations—Disclosures, Goodwill and Impairment

30. The purpose of this session was to seek members' views on some suggestions from respondents to the Discussion Paper *Business Combinations—Disclosures, Goodwill and Impairment* for changes to the impairment test of cash-generating units containing goodwill (impairment test). Staff asked about:
    (a) the criteria used to select suggestions to be explored further (paragraphs 31–32);
    (b) suggested changes to improve the application of the impairment test by reducing management over-optimism (paragraphs 33–54);
    (c) suggested changes to improve the application of the impairment test by reducing shielding (paragraphs 55–61); and
    (d) suggested ways to reduce the cost and complexity of the impairment test (paragraphs 62–63).

### Criteria for considering suggestions

31. In identifying suggested changes to the impairment test for further exploration within this project, staff considered whether the suggestion:

    (a) improves the effectiveness of the impairment test by mitigating, at a reasonable cost, either management over-optimism or shielding; or

    (b) reduces cost and complexity of the impairment test, without significantly reducing its effectiveness.

32. Staff asked whether there were any comments on the criteria. Members had no comments.

### Possible changes to reduce management over-optimism

***Comparison with past forecasts***

33. Members discussed a suggested requirement for entities to disclose a comparison of cash flow forecasts used in impairment tests performed in prior years with actual cash flows. In the view of respondents to the Discussion Paper this requirement could enable users of financial statements (users) to assess the accuracy of those past forecasts. Members commented on:

    (a) The usefulness of information that would be disclosed applying this suggestion (paragraphs 34–44); and

    (b) Time horizon for disclosing cash flow forecasts and cash flows (paragraphs 45–47).

***Usefulness***

34. Members generally agreed that such a comparison, together with the amounts of past cash flows, would be useful information. They said this disclosure would help show whether entities were meeting their forecasts, and would give insight into whether management historically behaved over-optimistically.
35. One member suggested the disclosure could improve accountability of corporate boards and that it is management’s job to make decisions in highly uncertain environments and there needs to be a due process and this information would help them assess that due process. One member said the suggested disclosure would

provide a chance to ask management about cases where they chose not to record impairments.

36. One member suggested adding a requirement for commentary from management on any difference between forecast and actual cash flows, with the aim of identifying factors inside and outside management's control.
37. One member said the suggested disclosure would be useful and help reduce over-optimism, but users would also use the information for other purposes, so it would have a second-order effect and that could have unintended consequences—it could utilise a lot of management's time.
38. However, some members were sceptical of its usefulness. One member said IAS 36 *Impairment of Assets* requires an entity to disclose the assumptions used in the impairment test and that should be sufficient. One member said that the suggested disclosure meant more information would be reported about business combinations than about the rest of the entity, and questioned whether the suggested disclosure was a good use of resources.
39. Members also raised specific concerns or asked for clarifications. Some members said the information could give rise to litigation, although one member questioned what the basis of that litigation would be because the information would be about past forecasts.
40. One member said that forecasts might change for reasons other than management over-optimism, for example subsequent business combinations or disposals, and asked how such changes in scope would be dealt with.
41. One member asked how disaggregated the information would be and whether the comparison would be provided for all impairment tests.
42. One member, although supportive of the suggestion, questioned whether it would result in more timely impairment losses because most of the value in a forecast is not in the first three years but in the terminal value. However, one member had a different view and said the first five years of the forecast is a 'black box' and having information on that period together with the long-term assumptions would be useful.
43. Members asked staff about the response to the suggested disclosure from preparers, questioning how costly providing this information could be. Staff said that preparers had mainly questioned the usefulness of the disclosure since actual cash flow amounts

always differ from forecasts but had raised questions about the cost of providing this information when an entity may perform many impairment tests.

44. One member said they did not expect the forecast and actual cash flows to match, but the differences should be ‘normally' or systematically distributed and the comparison would identify if management are always too optimistic.

***Time horizon for disclosing cash flow forecasts and cash flows***

45. Members generally agreed that requiring more years to be disclosed would provide more useful information. Some members suggested three years as a baseline for the disclosure of cash flow forecasts and cash flows associated with impairment testing.
46. One member said three to five years would be reasonable—two years would be too short because too many things can affect the forecast in that period, and ten years would be too long.
47. One member said the number of years that would be useful might vary by sector. For example, three years’ worth of cash flow information might be sufficient for a noncyclical industry such as consumer goods or healthcare, but in cyclical industries such as mining, a longer period would be better.

***Reasonable and supportable assumptions***

48. Members discussed a suggestion to clarify the interaction between the requirements in paragraph 33 of IAS 36 to base cash flow projections on (a) reasonable and supportable assumptions; and (b) the most recent financial budgets or forecasts approved by management.
49. Members raised no concerns about this suggestion.

***Segments to which goodwill is allocated***

50. Members discussed a suggestion to supplement the disclosure of goodwill allocated to cash-generating units with information about the reportable segments to which the goodwill is allocated.
51. Respondents to the Discussion Paper had said this information might help users better assess the reasonableness of assumptions used in impairment tests by improving the ability of users to compare the assumptions to information disclosed about reportable segments.

52. Members generally agreed that the suggestion is a good idea. One member said this disclosure might also help users learn more about how goodwill might be shielded by entities in the impairment test to avoid recognising an impairment of goodwill.

***Indicators of impairment***

53. Members discussed a suggestion to improve the list of indicators of impairment in paragraph 12 of IAS 36.
54. Some members saw no reason to amend the list of indicators of impairment, and observed that the list was not intended to be exhaustive. One member spoke in favour of improving the indicators of impairment, particularly if the IASB decides to remove the requirement to perform a quantitative impairment test annually.

## Possible changes to reduce shielding

***Allocating goodwill to cash-generating units***

55. Members discussed suggestions to reduce shielding by means of providing additional guidance on allocating goodwill to cash-generating units.
56. In particular, staff asked whether and how to:
    (a) clarify that the requirement in paragraph 80(b) of IAS 36 that the group of cash-generating units to which goodwill is allocated is not larger than an 'operating segment' is intended as a safeguard to prevent goodwill being tested at too high a level (for example at an entity level), rather than a default level;
    (b) clarify the meaning of the expression 'goodwill is monitored for internal management purposes' used in paragraph 80(a) of IAS 36 or alternatively replace it with 'the business associated with the goodwill is monitored'; and
    (c) link the level at which goodwill is tested for impairment with the level at which the business combination is monitored for the purpose of the proposed disclosures about the subsequent performance of business combinations (tentatively decided on in September 2022).
57. Members had no comments on these suggestions.

***Impairment testing on reorganisation***

58. Members discussed a suggestion to require an entity to perform an impairment test based on its previous reporting structure before reallocating goodwill to different cash-generating units following, for example, a reorganisation of its reporting structure. A few respondents to the Discussion Paper had said entities may decide to reallocate goodwill opportunistically to avoid impairments of goodwill.
59. There were mixed views on this suggestion. One member questioned how frequently entities reorganise to avoid recognising an impairment loss. They said that if this was a material issue the suggestion would be sensible. One member said they would be surprised if it was a material issue, whereas another member said they were aware of this happening but they were not sure how prevalent an issue this was.
60. One member said they observe this behaviour and the suggestion would be an effective solution for the delayed recognition of impairment losses. One member said if more than six months had elapsed between the last reporting day and the restructuring of a cash-generating unit including goodwill, an impairment test using the previous reporting structure would be useful.
61. One member suggested an entity should be required to disclose if there has been a material change in the allocation of goodwill for impairment testing purposes.

**Possible changes to reduce cost and complexity**

62. Members discussed the application of paragraph 99 of IAS 36. Paragraph 99 offers relief to help reduce the costs of performing an impairment test annually, without compromising its integrity. Feedback from the Discussion Paper suggested the relief might not be working as intended and is used infrequently because of the perceived lack of clarity on some of the criteria. Some respondents to the Discussion Paper had said making the relief easier to apply could reduce cost and complexity and could be an alternative to removing the requirement for an annual quantitative impairment test.
63. One member said it is not clear what difficulties entities have with the current requirement but that there was no problem in clarifying the wording. However, some members raised concerns about the suggestion. One member said there needs to be clear and strong pre-conditions and another member was concerned about weakening the impairment test, given the IASB's previous decision to retain the impairment-only model.

**Next steps**

64. The IASB will decide whether to further explore any of these suggestions at a future IASB meeting. In reaching its decisions, the IASB will consider feedback from members, its other consultative groups and the IFRS Interpretations Committee.

## Equity Method

65. This session asked CMAC members' for their views on application questions in the scope of the Equity Method project.
66. Members' views were requested on a specific aspect of the project, on whether gains and losses from transactions between an investor and its associate should be restricted.
67. Views were also sought on some of the tentative decisions made by the IASB, including:
    (a) Purchase of an additional interest while retaining control; and
    (b) Other changes in net assets that change an investor's ownership interest.

### Should gains and losses from transactions between an investor and its associate should be restricted?

***CMAC members approach to the valuation of an equity-accounted investment***

68. Members were asked about their approach to analysis and valuation of investors' financial statements with equity-accounted investments. They were asked whether they evaluate these investments separately and what is their main source of information for the valuation.
69. One member said each associate, if it is material, is evaluated separately to the investor entity. If the associate is quoted and not considered to be material, the market valuation is used; if it is material, it is valued as a separate entity. Sources used for valuation include the carrying amount on the reporting entity's balance sheet, income attributed to the associate, other information sources, and comparison with peers.
70. Another member said if a joint venture or associate operations is effectively part of the reporting entity's operating business they are valued together. An associate that is not part of the operating business is evaluated to see if it makes a material difference to the investment case, and if it is, then further analysis may be carried out using

multiples of earnings and industry comparatives. The member noted that information on debt is important to the analysis, but it may not be disclosed for such investments.

71. An IASB member said IFRS Accounting Standards require disclosures on individually material joint ventures and associates; the IASB member asked if these disclosures are used in the valuation. CMAC members said the disclosures are sometimes provided, but not consistently, perhaps owing to differences of opinion on whether an associate or joint venture is material.
72. One member asked how it is assessed whether an associate is material. An IASB member responded that there were no specific criteria and preparers were required to use the general notion (information that could reasonably be expected to influence investor decisions).
73. One member said that when entities disclose the required information for material joint ventures and associates, liabilities may only be split between current and non-current, while users are interested in financial liabilities and leverage. One member suggested that where debt is disclosed in the statement of financial position of an associate, there should be a requirement to say whether or not it is non-recourse.
74. One member reported using a range of approaches in evaluating a joint venture or associate that is not material, including multiple of net earnings, value of equity, flow of dividends, and implicit valuation. The member concurred on the importance of disclosing financial liabilities to assess leverage.

***Recognition of gains or losses from transactions between an investor and its associate***

75. One member stated a preference for not restricting gains or losses from transactions between an investor and an associate.
76. One member said if gains or losses from the equity method are a material component of consolidated profit, then it is preferable to account in a way consistent with a one-line consolidation approach. If additional information was provided in the notes, investors could derive the unrestricted gain or loss from the restricted gain or loss. However, if the user is expected to adjust restricted gain or loss based on the note, it would be more efficient for the user to use the adjusted financial information. If the amount is small or the contribution to the consolidated profit is not material, then it may be better not to restrict the gain or loss from a cost perspective.

77. Two members said amortising the restricted portion of the gain over time added unnecessary complexity to financial reporting. They said recognising the gain and adequate disclosure would be sufficient for financial users.
78. One member said there is no reason to restrict the gain. The associate has purchased the asset at its current value. Adjusting the gain assumes that the associate has purchased the asset at its book value, or an amount other than its current value. The disclosures on related party transactions should provide the necessary information.
79. One member asked whether the elimination method (restricting the gain) is also applied to exchange of services. Staff responded that there is a separate application question on transfer of services, that the IASB's will discuss this application at a future meeting. The member said the gains or losses should not be restricted.
80. Two members said they would prefer to restrict the gains because part of the transfer is related to the interest owned by the investor. That portion of the gain is not a 'real' profit. Not restricting the gain, in their view opens up the possibility to abuse. The member said he was not sure what a better alternative was.

***Need for other information***

81. Many members suggested further disaggregation of information about individual associates and joint ventures would be useful:
    (a) One member said it would help to see the individual contributions of associates and joint ventures that were not individually material but were material in aggregate. In these cases, the total is required to be disclosed but the individual contributions are not. Another member said this disaggregation could be important in sectors such as real estate, utilities and telecommunications.
    (b) One member suggested that the entity's share of the profit or loss from associates, disclosed applying IFRS 12, could be disaggregated into the share of net income for each associate.
    (c) One member said many adjustments are required to calculate the return on investor capital for individual joint ventures. Although the needed information could be obtained directly from the reporting entity, there is a cost to obtaining information in that way, the member said.
    (d) One member asked whether the proposed additional disclosure would only apply to individually material transactions. The member said it would be undesirable if

there was no disclosure on gains that are material in aggregate but not material individually.

### Other changes in net assets

82. One member asked why the IASB decided to recognise dilution gains or losses in profit or loss. Staff explained that the IASB considered that all changes in an investor's ownership interest are economically similar, if they do not give rise to a change in control.

### Purchase of an additional interest while retaining significant influence

83. Members had no comments on the tentative decision on a purchase of an additional interest.

### Next steps

84. The IASB will continue its discussions on the application questions within the scope of the project.