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EFRAG
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Our ref: RJ-EFRAG 598A
Date: Amsterdam, 28 September 2020
Re: Comments on EFRAG draft comment letter in response to ED/2019/7 'General Presentation and Disclosures'

Dear members of the EFRAG Technical Expert Group,

The Dutch Accounting Standards Board (DASB) appreciates the opportunity to offer its views on your draft comment letter dated 24 February 2020 in response to the Exposure Draft 'General Presentation and Disclosures' (ED).

We generally agree with EFRAG's response to the ED, except as set out below (in the same order as the ED):

- We have some reservations about EFRAG's view, as currently expressed in response to Question 3, on the interaction of IFRS and existing regulatory frameworks.
- We support the IASB's proposal to classify in the financing category (i) income and expenses from cash and cash equivalents and (ii) interest income and expenses on liabilities that do not arise from financing activities, and thus do not see a need to explore alternative approaches. However, we do believe that the IASB should (more clearly) require separate presentation (or disclosure) of the main financing category items.
- While we see merit in requiring the use of a single method of operating expense analysis, some DASB members note that a mixture of both methods could also be beneficial in certain circumstances. Further comments are provided in the appendix.
- We do not consider the proposed definition of unusual income and expenses too narrow given the disclosure's intended purpose. However, we do not agree with the IASB's proposal to remove the contents of paragraph 97 of IAS 1. In our view, 'unusual items' and 'material items' are different concepts and we believe that both should be disclosed.
- We understand the IASB's rationale for not defining EBITDA and EBIT, and agree with not describing some of the newly defined subtotals as such. Accordingly, we believe that EFRAG's implied suggestion that the IASB should have defined EBITDA and EBIT can be omitted.
- We do not share your concerns about the list of measures not considered to be MPMs being rule-based. In our view, no underlying principle needs to be included.

- With regard to interim financial statements, we believe that MPM reconciliations (including the income tax effect and effect on NCI for reconciling items) should be required and believe that the benefits outweigh the costs.

Our further feedback, including some additional comments raised in our comment letter to the IASB, is provided in the appendix.

Please feel free to contact us if you wish to discuss the contents of this letter.

Yours sincerely,

prof. dr. Peter Sampers
Chairman Dutch Accounting Standards Board

Appendix – Views on EFRAG Draft Comment Letter

ED Question 1—operating profit or loss

The DASB agrees with EFRAG's response to the ED.

ED Question 2—the operating category

The DASB generally agrees with EFRAG's response to the ED.

Additional comments DASB:

- It is not clear to us why the wording in paragraphs 48 and 51 of the ED is different (i.e., "in the course of its main business activities" and "as a main business activity" respectively). We recommend that the IASB clarifies the difference if it is intentional, including the use of the plural or singular form. If not, then we recommend using consistent wording.
- In our view, the IASB should clarify the interplay between the notion of "an entity's main business activities" (in the ED) and the notion of "an entity's ordinary activities" used to distinguish revenue from other forms of income (e.g., in IFRS 15).

ED Question 3—the operating category: income and expenses from investments made in the course of an entity's main business activities

The DASB generally agrees with EFRAG's response to the ED. However, we have some reservations about EFRAG's view, as currently expressed, on the interaction with existing regulatory frameworks. We believe that the IASB should continue to focus on financial information that is relevant to primary users and that provides a faithful representation, rather than focus on avoiding differences with such frameworks. While liaising with constituents like regulators might help to ensure that IFRS Standards result in useful information (e.g., by learning about common industry practices), other frameworks might have different objectives and, therefore, should not predominate the IASB's decisions.

EFRAG – Questions to constituents

32 For those in a regulated industry, would the IASB proposals in paragraph 48, for entities that invest in the course of the entity's main business activities, result in significant changes in practice that would be in conflict with regulation in your industry? Do you expect any additional challenges or significant costs?

33 Do you consider that separating returns from investments made in the course of an entity's main business activities from those that are not will be difficult to make in practice? Please explain.

The DASB is not aware of significant issues that, as a result of the IASB proposals, would arise for entities that invest in the course of their main business activities. Neither do we anticipate that separating returns from investments made in the course of an entity's main business activities from those that are not, would be too difficult or costly. When relevant, we would typically expect that such distinction is already made for management purposes.

ED Question 4—the operating category: an entity that provides financing to customers as a main business activity

The DASB agrees with EFRAG's response to the ED.

EFRAG – Question to constituents:

42 Do you consider that it is difficult or costly to allocate income and expenses from financing activities and from cash and cash equivalents to those that do or do not relate to the provision of financing to customers? Please explain.

43 For those that provide financing to customers as a main business activity and are in a regulated industry, would the IASB's proposals in paragraph 51 of the ED be in conflict with regulation in your industry? Do you expect any additional challenges or significant costs?

The DASB has no clear indications that it would be too difficult or costly to allocate income and expenses from financing activities and from cash and cash equivalents to those that do relate to the provision of financing to customers and those that do not. We are also not aware of significant issues that, as a result of the IASB proposals, would arise for entities that provide financing to customers as a main business activity.

ED Question 5—the investing category

The DASB generally agrees with EFRAG's response to the ED. However, while we support EFRAG's call on the IASB to better explain the interaction between paragraphs 45 and 60 of the ED on the one hand (requiring the use of predefined categories and subtotals in the statement of profit or loss) and paragraph 24 of the ED on the other (referring to the notion of materiality), we do not consider the phrase "subject to materiality considerations" necessary. We suggest to remove this phrase in EFRAG's final comment letter as the same would arguably apply to any other (proposed) requirement.

<u>Additional comments DASB:</u>

- We encourage the IASB to further clarify the meaning of "incremental". This notion also exists in other IFRS Standards (e.g., IFRS 9, IFRS 15, IFRS 16) but, in our experience, is applied differently across entities in practice. While paragraph BC50 of the ED explains that incremental expenses do not include an allocation of labour costs if some employees are engaged in both operating and investing activities, it remains unclear whether labour costs of employees engaging only in investing activities are incremental. In addition, different interpretations exist as to whether, for example, legal and advisory fees for activities including due diligence, negotiating terms, preparing legal documents, etc. are incremental, considering that often (part of) these fees would still have been due even if the transaction had not been closed.

EFRAG – Question to constituents:

57 Do you consider income and expenses from cash and cash equivalents (i.e. short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value) as part of the entity's financing (paragraph 54 above) or investing activities (paragraph 55 above)? Please explain.

63 How costly would it be to track whether exchange differences relate to the entity's main business activities, investing activities or financing activities? Please explain.

The DASB considers income and expenses from cash and cash equivalents as part of the entity's financing activities (with some exceptions, i.e., when an entity provides financing to customers as a main business activity). Taking the requirements in IAS 7 (e.g., paragraph 7) and the widespread use of "net debt" measures into account, we consider that cash and cash equivalents are linked more closely to the financing category than the investing category. Hence, in our view, there is no need to explore an alternative approach as set out in your draft comment letter.

We have no clear indications that tracking whether exchange differences relate to operating, investing or financing activities, would be too difficult or costly.

ED Question 6—profit or loss before financing and income tax and the financing category

The DASB generally agrees with EFRAG's response to the ED, but does not see a need to reconsider the proposed classification of (i) income and expenses from cash and cash equivalents and (ii) interest income and expenses on liabilities that do not arise from financing activities. We support the IASB's proposal to classify these items in the financing category. That being said, we consider it appropriate to separately present (or disclose) the amounts for each item specified in paragraph 49 of the ED. This would enable users with different views to adjust the classification for their own analyses. Therefore, in our view, the IASB should (more clearly) require separate presentation (or disclosure) of these three items.

EFRAG – Question to constituents:

76 Do you consider income and expenses that reflect the effect of the time value of money on liabilities that do not arise from financing activities (as in paragraph B47 of the ED) as part of the entity's financing or operating activities? Please explain.

The DASB could see arguments for either view. Based on feedback from users of financial statements, as noted above, we support the IASB's proposal to classify interest income and expenses on liabilities that do not arise from financing activities within the financing category. Separate presentation or disclosure of the three items mentioned in paragraph 49 of the ED would be appropriate in our view and should resolve most concerns.

ED Question 7—integral and non-integral associates and joint ventures

The DASB generally agrees with EFRAG's response to the ED. In particular, we echo your comment that the proposed definitions need to be tested in practice, considering that some preparers signalled that, in their situation, the current proposals result in outcomes that are difficult to reconcile to their understanding of the business.

<u>Additional comments DASB:</u>

- With regard to the proposed definition of integral associates and joint ventures (in IFRS 12 Appendix A), we believe that the wording "and hence do not generate a return individually and largely independently of the other assets of the entity" is not necessary and could potentially restrict the scope (e.g., arguably, a joint investment by a real estate company in a separate entity holding commercial property might not meet the definition). Therefore, we recommend that the IASB removes this wording from the definition of integral associates and joint ventures.

EFRAG – Questions to constituents:

93 Do you consider that the IASB needs to expand the new paragraph 20D of IFRS 12, for example to include additional indicators, to reduce the level of judgement involved when making a distinction between integral and non-integral entities? Please explain.

94 Considering that the IASB is proposing the subtotal 'profit before financing and income tax', which includes the result of associates and joint-ventures on a net basis, do you consider that it would be useful to separately present or disclose the income tax related to associates and joint-ventures accounted for under the equity method?

The DASB does not consider additional indicators necessary to expand the new paragraph 20D of IFRS 12. No list of indicators will be exhaustive and judgement will likely be required anyway. We believe that the requirement to disclose information about significant judgements is sufficient.

We are sympathetic to EFRAG's proposal to require separate presentation or disclosure of the income tax related to equity-accounted associates and joint ventures.

ED Question 8—roles of the primary financial statements and the notes, aggregation and disaggregation

The DASB agrees with EFRAG's response to the ED.

ED Question 9—analysis of operating expenses

While the DASB sees merit in requiring the use of a single method to present in the statement of profit or loss an analysis of operating expenses, some members note that a mixture of both methods could also be beneficial. In our view, there is a trade-off between standardisation and reflecting how an entity is run. On the one hand, the use of a single method (whether by nature or function) enhances comparability and seems more aligned with the role of the primary financial statements to provide a 'structured and comparable summary' (paragraph 20 of the ED). On the other hand, some members argue that in certain circumstances a mixture of both methods could potentially provide the most useful information to users of financial statements. This is because a mixture provides flexibility to management to explain financial performance in a manner consistent with how it manages the company.

Those who believe that a mixture of both methods could also be beneficial, note that, in practice, there is particularly a need to present gross margin information when an entity uses the nature of expense method. As a compromise between requiring the use of a single method and allowing mixtures of both methods, the IASB could therefore consider to allow the presentation of cost of sales in a statement of profit or loss based on the nature of expense method, provided that a breakdown of this functional line item is provided on the face of the same primary financial statement. As a consequence, users might need to add together two lines to determine, for example, total employee benefit expenses. However, such presentation is transparent and all required information would be readily available.

All DASB members agreed that a 'clean' analysis of expenses using the nature of expense method should *always* be provided, either in the statement of profit or loss or in a single note. This is in line with the proposed requirement in paragraph 72 of the ED. We note however that an entity that presents its primary analysis of expenses using the function of expense method (i.e., in the statement of profit or loss), would likely arrange its notes accordingly, which might be less helpful to users focusing on the nature of expenses.

Other comments include:

- The DASB believes that in order to enable a meaningful comparison between different entities using the function of expense method, further guidance would be necessary. The allocation of operating expenses to activities is often judgemental and, currently, significant diversity exists in practice. The ED does not contain specific requirements on the application of the function of expense method.
- There seems to be an internal inconsistency between some of the proposed requirements in the ED. We interpret the reference to paragraph 71 in paragraph 65(a)(vii) to imply that the requirement to present cost of sales as a minimum line item in the statement of profit or loss is only applicable if the function of expense method is used. However, paragraph B47 states that the line items required by paragraph 65 must be presented regardless of the method of analysis of operating expenses used.
- The requirements in paragraphs 65 and B47 of the ED, to present certain line items regardless of the method of analysis of operating expenses used, create an exception to the principle that entities should use a single method (e.g., separate presentation of IFRS 9 impairment losses conflicts with a 'clean' by function analysis). It is unclear to us why this exception is needed, because the IASB could also require disclosure in the notes in case separate presentation on the face of the statement of profit or loss would conflict with the method of analysis of operating expenses used. In fact, such disclosure might already be provided based on paragraph 72 of the ED.
- It follows that the DASB does not support EFRAG's proposal to include a reference to paragraph B15 in paragraph B47 of the ED, as this would represent yet another exception to the principle. We also note that paragraph B15 already mentions disclosure in the notes as an alternative to separate presentation in the statement of profit or loss (i.e., there is no need for such change).

EFRAG – Questions to constituents:

121 Do you consider that it is useful to have disclosures by nature in single note when an entity presents its expenses within operating profit or loss by function (i.e. when an entity assesses that presentation by function provides the most useful information)? Do you anticipate that such information will be costly to provide? Please explain.

122 Do you consider that it is useful to have in the statement of profit or loss:

(a) a strict presentation either by nature or by function (no mix);

(b) a general presentation by nature or by function together with limited additional requirements as suggested in the ED by the IASB; or

(c) a mix presentation basis (no restrictions). Please specify why.

The DASB notes that users in particular seem to prefer disclosures by nature. As explained above, we did not reach consensus on whether the use of a single method should be required or a mixture of both methods allowed and it is unclear to us why the IASB created an exception to its general principle.

ED Question 10—unusual income and expenses

(a) Paragraph 100 of the Exposure Draft introduces a definition of 'unusual income and expenses'.

(b) Paragraph 101 of the Exposure Draft proposes to require all entities to disclose unusual income and expenses in a single note.

(c) Paragraphs B67–B75 of the Exposure Draft propose application guidance to help an entity to identify its unusual income and expenses.

(d) Paragraphs 101(a)–101(d) of the Exposure Draft propose what information should be disclosed relating to unusual income and expenses.

Paragraphs BC122–BC144 of the Basis for Conclusions describe the Board's reasons for the proposals and discuss approaches that were considered but rejected by the Board.

Do you agree with the proposals? Why or why not? If not, what alternative approach would you suggest and why?

The DASB generally agrees with EFRAG's response to the ED, except that it does not consider the proposed definition of unusual income and expenses too narrow given the disclosure's intended purpose (i.e., assist users in predicting future cash flows). That being said, we do not agree with the IASB's proposal to remove the contents of paragraph 97 of IAS 1, even more so because the related examples are brought forward from IAS 1 into paragraph B15 of the ED. In our view, 'unusual items' and 'material items' are two different concepts. Although the latter might not have predicative value, separate disclosure could still be important to provide relevant information to users. Therefore, we believe that all entities should be required to disclose both material items and unusual items. We would not support a mere replacement of the existing requirement to disclose material items by a new requirement to disclose unusual items.

<u>Additional comments DASB:</u>

- We believe that the requirement to identify *all* unusual income and expenses could be an onerous task, especially for large multinational groups. Therefore, we recommend that the IASB changes the wording in paragraph 101 of the ED to "… that includes all <u>significant</u> unusual income and expenses …".

ED Question 11—management performance measures

(a) Paragraph 103 of the Exposure Draft proposes a definition of 'management performance measures'.

(b) Paragraph 106 of the Exposure Draft proposes requiring an entity to disclose in a single note information about its management performance measures.

(c) Paragraphs 106(a)–106(d) of the Exposure Draft propose what information an entity would be required to disclose about its management performance measures.

Paragraphs BC145–BC180 of the Basis for Conclusions describe the Board's reasons for the proposals and discuss approaches that were considered but rejected by the Board.

Do you agree that information about management performance measures as defined by the Board should be included in the financial statements? Why or why not?

Do you agree with the proposed disclosure requirements for management performance measures? Why or why not? If not, what alternative disclosures would you suggest and why?

The DASB generally agrees with EFRAG's response to the ED, but does not share the concern about paragraph 104 of the ED arguably being rule-based (as noted under Question 12 below).

EFRAG – Questions to constituents:

185 What is your assessment of the overall costs and benefits of the IASB's proposal on the calculation of the income tax effect and the effect on non-controlling interests for each item disclosed in the reconciliation as required by paragraph 106(b)?

186 What is your assessment on number of MPMs that will need to be disclosed by entities under the IASB's proposals? Please indicate which MPMs you have identified.

187 What is your assessment on the relevance of the MPMs identified (is it too much? too little? which additional ones?)

188 Do you agree with the scope of the IASB's proposals? If not, which alternative (Alternative 1 or Alternative 2 above) would you prefer so that financial statements remain relevant?

189 Do you agree with EFRAG's suggestion to apply the MPM requirements also to the non-GAAP performance measures, presented within financial statements, that may not satisfy the proposed criteria of MPMs (e.g. adjusted revenues and ratios)?

190 The ED is introducing more structure in the presentation requirements, including a requirement to present on the face of the income statement a new subtotal named "operating profit or loss", which will become an IFRS defined measure. Entities that currently use a performing measure labelled "operating profit or loss" on the face or in the notes will be forced to either (i) change the label for their performing measure and continue to use both the old measure and the new IFRS defined "operating profit", or to (ii) discontinue the pre-existing performance measure, replacing its use with the new IFRS defined "operating profit or loss".

In the context described above, do you believe that the IASB's proposals on the structure and content of the statement of profit or loss will lead to an increased number of MPMs?

The DASB agrees with the information that entities would be required to disclose (i.e., paragraph 106(a)-(d) of the ED) and supports the proposal to require disclosure of all information on MPMs in a single note. However, we have concerns about the proposed definition of MPMs and disagree with the scope of the IASB's proposals on MPMs.

In line with EFRAG, the DASB considers the proposed definition too narrow, as it restricts MPMs to subtotals of income and expenses. It is unclear to us why other common non-IFRS measures such as adjusted revenue, net debt and ratios are excluded from the proposed definition. Also, having specific requirements for some non-IFRS measures, but not for all, would be confusing.

The DASB considers the proposed scope of the MPM requirements too broad. Although we appreciate the arguments stated in paragraph BC156 of the ED, this proposal raises questions on the role of the IASB. In our view, the IASB should not set mandatory requirements relating to information outside the financial statements, which is regulated by different bodies. Accordingly, in line with Alternative 1 in your draft comment letter, we believe that the scope of the MPM requirements in IFRS X should be limited to MPMs presented or disclosed within the financial statements. In addition, we propose to include similar guidance on MPMs in IFRS Practice Statement 1 'Management Commentary'. Competent authorities could then decide whether or not entities in their jurisdiction need to comply, as far as MPMs outside the financial statements are concerned.

We have no clear expectations as to whether, overall, the proposals in the ED will increase or decrease the number of MPMs being presented within and outside financial statements across different industries and entities. However, we do support the IASB's efforts to improve the comparability of primary financial statements.

ED Question 12—EBITDA

Paragraphs BC172–BC173 of the Basis for Conclusions explain why the Board has not proposed requirements relating to EBITDA.

Do you agree? Why or why not? If not, what alternative approach would you suggest and why?

The DASB understands the IASB's rationale for not defining EBITDA and EBIT, mainly given the lack of consensus on what these measures represent. We also agree with not describing operating profit or loss before depreciation and amortisation as EBITDA (as well as with not describing profit or loss before financing and tax as EBIT, as noted under Question 6 above) because such label might not match its content.

Accordingly, we believe that EFRAG's implied suggestion that the IASB should have defined EBITDA and EBIT can be omitted. We do however agree with your comment that EBITDA and EBIT should be included in the scope of the IASB's proposals regarding MPM disclosures.

The DASB does not believe that there is a need to include a principle underlying the list of measures not considered to be MPMs in paragraph 104 of the ED. A clear and unambiguous list helps to prevent possible discussions about the scope of the MPM requirements.

<u>Additional comments DASB:</u>

- In our view, the IASB should clarify whether operating profit or loss before depreciation and amortisation includes or excludes impairments (and reversals thereof). We observe that different views exist in this respect.

ED Question 13—statement of cash flows

(a) The proposed amendment to paragraph 18(b) of IAS 7 would require operating profit or loss to be the starting point for the indirect method of reporting cash flows from operating activities.

(b) The proposed new paragraphs 33A and 34A–34D of IAS 7 would specify the classification of interest and dividend cash flows.

Paragraphs BC185–BC208 of the Basis for Conclusions describe the Board's reasons for the proposals and discusses approaches that were considered but rejected by the Board.

Do you agree with the proposals? Why or why not? If not, what alternative approach would you suggest and why?

The DASB generally agrees with EFRAG's response to the ED. In particular, we support your suggestion to start a separate project on IAS 7 to comprehensively review the challenges that arise in practice (e.g., for financial entities) and to improve consistency with the newly proposed content and structure of the statement of profit or loss.

Like EFRAG, the DASB would welcome further guidance on the presentation and disclosure of supply chain financing arrangements. However, we note that this topic is currently being addressed by the IFRS Interpretations Committee.[1]

Additional comments DASB:

- We find the proposed approach for "financial" entities to classify interest and dividend cash flows rather technical (i.e., complex to read) and are not convinced by the argument in paragraph BC199 of the ED that it may be costly to split dividends received and interest paid and received between different categories.

ED Question 14—other comments

Do you have any other comments on the proposals in the Exposure Draft, including the analysis of the effects (paragraphs BC232–BC312 of the Basis for Conclusions, including Appendix) and Illustrative Examples accompanying the Exposure Draft?

The DASB generally agrees with EFRAG's other comments, except with those in paragraphs 240-241 of your draft comment letter regarding the proposed amendment to IAS 34 in respect of MPMs.

In our view, entities should not be required to always provide all disclosures about MPMs in their interim financial statements. If MPMs were already described in an entity's most recent annual financial statements and are not changed, then there would be no need to repeat such disclosures (i.e., those in paragraph 106(a) of the ED) in the interim financial statements. However, the DASB believes that the disclosures in paragraph 106(b)-106(d) should be required for transparency purposes and to provide users with the information needed to make their own adjustments. We believe that the benefits of providing MPM reconciliations (including the income tax effect and effect on NCI for reconciling items) in interim financial statements outweigh the costs.

EFRAG – Question to Constituents

250 Do you agree that the IASB should consider providing more guidance for the presentation of revenues and costs when they are allocated to different business activities on the face of the statement of profit or loss, including consistency with IFRS 8 and disclosure on judgement applied in the allocation process?

The DASB has no objections to EFRAG asking for further guidance on this topic.

[1] In June 2020, the IFRS Interpretations Committee issued a tentative agenda decision on reverse factoring arrangements and discussed a possible narrow-scope standard-setting project: https://www.ifrs.org/news-and-events/updates/ifric-updates/june-2020/#1.