IFRS Accounting

# Meeting summary

## CMAC Meeting

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This document summarises the discussions at the November 2024meeting of the Capital Markets Advisory Committee (CMAC). (The CMAC is a group of nominated members with extensive practical experience in analysing financial information. The group's members are also 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 | CMAC members |
|---|---|
| Asia-Oceania | Koei Otaki*<br>Ge Xiaobo |
| Europe | Diego S Barerro*<br>Megan Clark<br>Larissa van Deventer<br>Oliver Gottlieb*<br>Jacques de Greling*<br>Kenneth Lee<br>Matthias Meitner<br>Deirdre O'Leary<br>Philip Robinson<br>Tony Silverman<br>Jeremy Stuber<br>Joao Toniato |
| The Americas | Enitan Adebonojo<br>Paulo Cezar Aragão<br>Anthony Scilipoti<br>Michael Thom |

* This member participated remotely.

## Climate-related and Other Uncertainties in the Financial Statements

1. The IASB staff:

   (a) provided an update on the project; and

   (b) asked CMAC members for feedback on the proposed illustrative examples included in the Exposure Draft *Climate-related and Other Uncertainties in the Financial Statements*.

2. CMAC members generally supported providing examples to help improve the reporting of the effects of climate-related and other uncertainties in the financial statements. However, some CMAC members said that IFRS Accounting Standards already require entities to disclose these effects in their financial statements. A few CMAC members said that the examples worked well as a package and that providing illustrative examples was an effective way of helping to improve the reporting of the effects of climate-related and other uncertainties in the financial statements.

3. Some CMAC members expressed concern that Example 1 ('Materiality judgements leading to additional disclosures (IAS 1/IFRS 18)') could result in entities providing disclosures about a wide variety of uncertainties, leading to boilerplate disclosures. In addition, a few CMAC members said that it was unclear what 'other uncertainties' mean. However, some other CMAC members said that entities are only required to provide information when that information is material in the context of their financial statements. Most CMAC members said the examples should make that clear. One CMAC member said that material information that does not affect an entity's financial position or financial performance for the current period should be included in other general purpose financial reports, such as an entity's sustainability or risk report.

4. Some CMAC members said that providing a sensitivity analysis together with the assumptions about uncertainties is helpful to users of financial statements. One CMAC member said that an entity might provide information, including scenario analyses, outside its financial statements when it does not affect the entity's financial position for the current period.

5. CMAC members also shared their views on some of the other illustrative examples proposed in the Exposure Draft:

(a) *Example 3 ('Disclosure of assumptions: specific requirements (IAS 36)')*—one CMAC member said that disclosures about the assumptions made when testing an asset for impairment—for example, assumptions about carbon prices—would provide useful information to users of financial statements.

(b) *Example 6 ('Disclosure about credit risk (IFRS 7)')*—one CMAC member observed that entities already consider climate-related uncertainties in their expected credit loss models.

(c) *Example 7 ('Disclosure about decommissioning and restoration provisions (IAS 37)')*—one CMAC member said that, although the effects of climate-related uncertainties on an entity's financial performance might be immaterial, information about some of the assumptions made about future events might be material information to users of financial statements.

(d) *Example 8 ('Disclosure of disaggregated information (IFRS 18)')*—a few CMAC members said that disaggregated information about climate-related and other uncertainties would allow for better connections to information provided outside an entity's financial statements. They also said that that kind of disaggregated information would be helpful to users of financial statements.

6. A few CMAC members said that it would be helpful if entities provided the time period(s) associated with the assumptions disclosed in their financial statements.

## Next step

7. The IASB will consider the feedback from CMAC members together with other feedback on the Exposure Draft when it reviews stakeholder feedback at a future IASB meeting.

## Post-implementation Review of IFRS 16 *Leases*

1. The purpose of the session was to provide CMAC members with an overview of the project plan for the post-implementation review of IFRS 16 *Leases*, and to seek members' views on the implementation and application of the Standard.

2. IASB technical staff asked CMAC members to share their experience of using information that is provided in accordance with IFRS 16, including whether in their view IFRS 16 has improved:
   (a) the quality of financial information; and
   (b) the comparability of financial information.
3. IASB technical staff also asked CMAC members about the transition to IFRS 16, in particular:
   (a) whether entities provided sufficient information in their first financial statements prepared in accordance with IFRS 16; and
   (b) what, if anything, CMAC members would recommend the IASB do differently in its future standard-setting.

## Quality of information

4. Most CMAC members said that IFRS 16 enhances transparency and provides useful information that helps them better to assess the capital employed by, and the financial leverage of, lessees, in particular in industries that use leases extensively (such as retail, airlines and telecommunications). Some CMAC members said that they no longer need to adjust lessees' statements of financial position by estimating an amount of debt arising from lease commitments (either by calculating the present value of lease commitments or by applying a multiple to the lease expense recognised in a reporting period). They said that the information provided in accordance with IFRS 16 is more accurate than the estimates they previously made.

5. A few CMAC members raised concerns about the quality of information that is provided in accordance with IFRS 16. Their comments included:
   (a) EBITDA is no longer useful as a proxy for cash flow, because it does not include lease expense. As a result, some entities (for example, in the telecommunications industry) introduced a new alternative performance measure: 'EBITDA after leases'.
   (b) lease liabilities are not viewed as debt by all users of financial statements and many entities still need to comply with loan covenants that are based on pre-IFRS

16 information (that is, information that would have been reported if IAS 17 *Leases* still applied). In addition, and contrary to how some users view leases, IFRS 16 changed entities' risk profile from 'operational' to 'financial'.

(c) there seem to be opportunities to structure what might otherwise have been a lease as a service contract—to avoid lease accounting and thereby achieve a preferable reporting outcome.

(d) in some industries short-term leases have become more prevalent than in pre-IFRS 16 times. In the view of some users of financial statements, entities might enter into short-term contracts to apply the exemption in IFRS 16 (which permits an entity to account for a lease of 12 months or less as a service contract) or to recognise a lower lease liability.

(e) in some industries (for example, retail or telecommunications) users of financial statements need to adjust their models because, in their view, the classification of leases in the statement of cash flows of such an entity does not faithfully represent the underlying economics of leases.

## Comparability

6. Many CMAC members said that IFRS 16 improved the comparability of an entity's financial statements with those of its previous periods, and with the financial statements of other similar entities.
7. But some CMAC members raised concerns about comparability. In their view, there are several aspects that hinder it. For example:

(a) diversity in the application of judgement to determine discount rates.

(b) diversity in the application of judgement to determine a lease term and inconsistency with the expectations of users of financial statements based on:

i. past practice;

ii. entities' business models;

iii. lease terms determined by peer entities; or

iv. assumptions in the impairment test.

(c) the non-comparability of information about leases with variable payments (that are not included in the measurement of lease liability) with information about leases with fixed payments (or in-substance fixed payments).

(d) diversity in the accounting for economically similar contracts when, for example, some entities sell their assets and enter with the buyer into a service agreement that might otherwise have been structured as a lease.

(e) differences in the lessee accounting models and the sale and leaseback requirements in IFRS 16 and in US GAAP.

(f) differences in the cash flows reported by entities that borrow to buy assets and those that lease assets (because non-cash movements related to the initial recognition of leases are not presented in the statement of cash flows).

## Disclosures

8. All CMAC members who commented said that IFRS 16 significantly improved the quality of disclosures.
9. CMAC members' suggestions for additional information included:

(a) disclosure of discount rates and lease terms and how they were determined, including better disclosure of options to terminate or extend a lease;

(b) disaggregation of lease payments into interest and principal amounts, preferably in the statement of cash flows instead of in the notes;

(c) information about the useful life of leased assets—because some users of financial statements recalculate lease liabilities based on the lease payments over the life of the asset instead of the lease term estimated by the entity—or, alternatively, more detailed information about the nature of leased assets that would enable users of financial statements to estimate the relevant useful lives.

## Transition

10. All CMAC members who commented said that the disclosures made in the first year of an entity's application of the new requirements were sufficient to help them understand the impact of IFRS 16 on its financial statements. In particular, users of financial statements found that the following requirement provided useful information:

(a) requiring an entity to reconcile its lease liabilities recognised in accordance with IFRS 16 with its lease commitments disclosed in prior year financial statements in accordance with IAS 17.

11. The main difficulty that users of financial statements encountered in relation to an entity's transition to IFRS 16 was that the new Standard made the entity's historical trends harder to analyse. In particular, in order to present such information on a comparable basis, users of financial statements were required to adjust their models. Moreover, such analyses were further complicated because, under IFRS 16, entities were allowed to use different transition options and practical expedients.
12. One CMAC member said that some entities disclosed expected changes early, which was very helpful. The same member said it would also be helpful in the future standard setting, if the IASB reinforced the requirement for an entity to disclose known or reasonably estimable information relevant to assessing the possible impact that application of a new IFRS Accounting Standard will have on the entity's financial statements in the period of initial application.

## Next step

13. The IASB will consider the feedback from CMAC members when it decides what matters to include in the request for information. The request for information is expected to be published in the first half of 2025.

## Equity Method

1. The purpose of this session was to seek CMAC members' views on the proposals in the Exposure Draft *Equity Method of Accounting—IAS 28* Investments in Associates and Joint Ventures *(revised 202x)*.

***Changes in an investor's ownership interest while retaining significant influence***

2. CMAC members commented on the proposal to recognise in profit or loss the gains or losses from other changes in an investor's ownership interest, such as dilutions. Two CMAC members supported the proposal because, in their view, the economic substance of a dilution is similar to a disposal of an ownership interest and the gain or loss should therefore, they said, be presented in the same manner. However, two

other CMAC members said the gain or loss should be presented in equity and not in profit or loss as part of the investor's performance, because these gains do not arise from a transaction that involves the investor.

3. A CMAC member asked if the IASB will specify where in its statement of profit or loss an investor should present gains or losses from other changes in the investor's ownership interest. The staff explained that the investor would apply IFRS 18 *Presentation and Disclosure in Financial Statements*. Other CMAC members said it is important that these amounts are separately presented or disclosed.

### *Transactions with associates and joint ventures*

4. A CMAC member asked about the IASB's rationale for its proposal to recognise in full the gains and losses resulting from all transactions with an entity's associates or joint ventures. The staff explained the rationale and noted that the IASB's decision followed the advice given by CMAC members in previous discussions.

### *Investments in subsidiaries to which the equity method is applied in separate financial statements*

5. A CMAC member noted that the proposal for an investor to recognise in full gains or losses resulting from all transactions with investments accounted for under the equity method could affect dividend distribution and taxable income. This is because in some jurisdictions these amounts are based on the entity's separate financial statements. Furthermore, some jurisdictions require investments in subsidiaries to be accounted for in separate financial statements using the equity method.

### *Disclosure requirements*

6. CMAC members expressed support for the disclosure requirements proposed in the Exposure Draft, noting that they will provide:

(a) useful information, if appropriately disaggregated; and

(b) greater insight into investments accounted for using the equity method.

7. One CMAC member said that strategic information, including forward-looking information, would be useful to users of financial statements.

### *Supplementary comments*

8. The staff asked CMAC members for their views on accounting for transaction costs: should they be considered as part of the cost of an investment, or should they be expensed as incurred in profit and loss? The staff explained that the IASB has not addressed this question in the Exposure Draft. A CMAC member said that the IASB should address the question when redeliberating the proposals.

9. A CMAC member asked the IASB to clarify the unit of account for an entity's investment in an associate or joint venture. The staff acknowledged that IAS 28 *Investments in Associates and Joint Ventures* uses different units of account, whereas the proposals in the Exposure Draft use the same units of account. The staff explained that the project approach was to answer application questions. The IASB did not therefore define a single unit of account for the equity method, because doing so would be beyond the project's scope.

## Next step

10. The Exposure Draft is open for comment until 20 January 2025. After the consultation period ends, the IASB will analyse the feedback and redeliberate the project proposals. The feedback from CMAC members will be included in the analysis and will be considered by the IASB when redeliberating the project proposals.

## Statement of Cash Flows and Related Matters

1. The purpose of the session was to better understand the nature and the prevalence of the issues with the statement of cash flows and related information discussed in the June 2024 joint CMAC-GPF meeting. The staff asked CMAC members to share their experiences with each of the issues identified in that meeting.

2. Most CMAC members said that some improvements to IAS 7 *Statement of Cash Flows* would provide them with more transparent information. In particular:
   (a) requiring more disaggregated information about cash flows;
   (b) requiring additional information about 'free cash flows'; and
   (c) requiring additional information on the effects of non-cash transactions.

3. Most CMAC members said that segmental cash flow information is not often disclosed. These members said that segmental cash flow information would be useful for a better understanding of individual segment performance, particularly in diversified entities. However, some CMAC members said that without specific guidance on how to allocate cash flows to segments there could be diversity in practice. Some CMAC members also said that they would prefer a more comprehensive review of segment reporting in a separate project instead of considering segmental cash flow information in isolation.

4. Most CMAC members commented that disaggregating information on capital expenditure between growth and maintenance would be useful. These members said that such disaggregated information would be a useful aid to understanding the cash generated by an entity from its operations, how its cash resources are allocated in its business and for evaluating management stewardship. Some CMAC members said that it would be difficult to develop commonly agreed definitions of 'capital expenditure for growth' and 'capital expenditure for maintenance'. These members said that without such agreed definitions it would be harder to compare entities. Some CMAC members also said that requiring additional disclosures on how an entity's management views the disaggregation of such information would provide users of financial statements with useful insights.

5. Many CMAC members said that requiring more disaggregated information on changes in an entity's working capital, either in the statement of cash flows or as additional disclosures, would help users of the entity's financial statements better to understand information about its cash flows. For example, additional information about the impact of an entity's business acquisitions and foreign exchange would help users of financial statements to understand a change in its working capital.

6. Some CMAC members said that there is diversity in the classification of cash flows from discontinued operations in entities' statement of cash flows. Some members also said that discontinued operations are not always presented consistently in the statement of profit or loss and the statement of cash flows.

7. Most CMAC members said that having additional information about 'free cash flows' is important. They said that the definitions of 'free cash flows' they use are diverse. Some members have a standard definition, others have definitions that vary by industry and some use the definition proposed by the individual entity being analysed. Some members said that much of the diversity in definitions relates to adjustments for non-cash transactions, such as share-based compensation. Some CMAC members also said that devising a universally applicable definition of 'free cash flows' would be challenging.

8. Some CMAC members said that it is not always clear how an entity's reported free cash flow relates to its statement of cash flows, and sometimes entities change the calculation without explanation. Some members said that requiring companies to reconcile free cash flow to a consistent starting point would help users of financial statements to understand the various definitions and would increase the information's transparency.

9. Many CMAC members said that information regarding the non-cash effects of some transactions is important. They said that there are different uses for such information. For example, some members adjust free cash flow for non-cash effects to calculate what they consider to be a more sustainable operating cash flow, some use information about non-cash effects to understand their impact on changes in working

capital, and some compare the non-cash effects of some transactions to economically similar cash transactions.

10. Some CMAC members said that they would prefer that information about non-cash effects was provided in the notes to an entity's financial statements instead of an entity including notional cash flows in its statement of cash flows. However, some members said that information about non-cash effects is often difficult to find, with no indication in the statement of cash flows that such information is available elsewhere. These members said that including a link in the statement of cash flows to this information, or including all related information in a single note, would be useful.

11. Some CMAC members said that an entity's statement of cash flows has limited use for financial institutions because it does not effectively distinguish between the cash available to the entity's shareholders and the cash that belongs to its customers; and that regulatory disclosure requirements provide more useful information about an entity's cash and liquidity management. However, other CMAC members said that the statement of cash flows can provide some useful cash flow information, such as regarding dividend payments. Some members also said that the statement of cash flows can provide inputs for valuations of financial institutions, but the information will be analysed in a different way than for entities that are not financial institutions. For example, for valuing a financial institution information about earnings might be adjusted to include those items that impact an entity's capital and by removing those items that do not.

12. Other comments made by CMAC members:

(a) most said that they adjust the classification of various items in the statement of cash flows in their analyses. For example, leases, research and development expenses, factoring receivables and supplier finance arrangements.[1]

(b) a few said that information to understand the changes in an entity's net debt is important.

(c) a few said that both direct and indirect methods provide useful information in reporting cash flows from operating activities.

(d) a few said that information about cash flows attributable to a non-controlling interest is useful.

(e) a few said that the statement of cash flows is the most important statement for credit analysts, but it appears that preparers often pay little attention to it.

## Next step

The IASB will consider the feedback from CMAC members in deciding what topics to explore further in the project.

[1] In May 2023 the IASB introduced new disclosure requirements for supplier finance arrangements: an entity is required to disclose information so that users of its financial statements can assess the effects of those arrangements on the entity's liabilities and cash flows, and on the entity's exposure to liquidity risk. These requirements were effective from 1 January 2024.