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Accounting Methodology Centre (AMC) is pleased to have the opportunity to comment on the IFRS Standards Exposure Draft ED/2019/7 "General Presentation and Disclosures". AMC is responsible for the development of Russian Accounting Standards and for issuance of interpretations and guidance for Russian companies.

Comments on IFRS Standards Exposure Draft ED/2019/7 General Presentation and Disclosures

General impression

The scope of the proposed changes in IAS 1 does not justify replacing the entire standard with a new one. The changes relate only to local insignificant issues. Meanwhile, significant issues remain unaffected. The existing IAS 1 is full of provisions that were invented in the 90s and included in the first edition of IAS 1 in 1997. They have changed since in detail, but not in the main content. Those provisions require revision urgently because they are built on the assumption that financial statements are prepared, presented and used on paper media, not on a computer.

This is the main reason why most common format of financial reporting is PDF or similar formats that mimic paper documents. Due to the inadequate "paper-format" provisions of the standard, the only task of electronic reporting is the tagging of statement lines (BC301 – BC303 of the ED), while the lines themselves remain a vestige of the paper past. Instead of a data-based taxonomy, we have to deal with standard-based or statement-based taxonomies, neither of which can serve for anything more than simulating paper documents on a computer screen.

Today's financial reporting user is not able to access any of the vast armory of information visualization tools that the digital era has created. In all other information areas users actively use these facilities, but they are practically forbidden for financial reporting information. Over the past 20 years, the computer has dramatically changed the image of all types of information in all areas, with the exception of financial reporting information. For example, geographical information. A paper map or atlas are incomparable with modern navigation software in their informational usefulness. However, you hardly find any noticeable difference between financial reporting which you see on your screen and which you see on paper. Image on the screen and a hard copy look identical.

Even XBRL does not help. Although XBRL reporting is not PDF, it has very few differences with PDF. The only advantage is that you can transfer reporting data from multiple companies and collect it in a single pool. However, when you look at the reports themselves, you do not feel any additional comfort compared to if you were flipping through paper pages. You are still dealing with a bunch of statements and notes instead of an integral system. Such reporting is not essentially electronic. This is still a paper reporting, just displayed on a screen.

The reason is not that XBRL is a bad language. The reason is the inadequate requirements of IFRS, especially of IAS 1. The ED seriously tackles such issues as aggregation and disaggregation. For what, if not for paper reporting? For what purpose does the standard require financial reporting to be divided into separate statements and notes, if not for paper reporting? There are no such issues with regard to electronic reporting. The most primitive electronic tools, such as unfolding windows and hyperlinks, alone allow you to close such issues completely, remove them from the agenda and forget them forever, not to mention the more modern means of reproducing information.

However, the requirements of the IAS 1 and other IFRS actually prohibit the use of modern information visualization tools in accounting software. As a result financial statements are gradually turning from a source of useful information to formal legal documents. Regulators and courts are becoming their main users, while investors are losing interest in this "official" reporting due to the inconvenience of using it for making economic decisions.

The level of issues covered by the ED is worthy, at most, of annual IFRS improvements, but is not worthy to replace the existing IAS 1 with a new standard. To issue a new standard, we definitely need to change the agenda. The primary issue that needs to be urgently addressed is the transformation of the IFRS requirements to electronic forms of financial information presentation. First of all, it is necessary to conceptually change approaches to solving such issues as aggregation and disaggregation, stop dividing financial reporting into separate statements and notes, reorient the IFRS requirements from the form to the substance of the information provided. The concept of "primary financial statements" is an extremely harmful concept, the use of which will lead to nothing other than the eternal stuck of IFRS in paper formats of the 20th century. If we want to see the beneficiaries of IFRS not only regulators and courts, then IFRS should at least stop blocking the use of modern tools for presenting financial data.

Question 1 — operating profit or loss

Paragraph 60(a) of the Exposure Draft proposes that all entities present in the statement of profit or loss a subtotal for operating profit or loss.

Paragraph BC53 of the Basis for Conclusions describes the Board's reasons for this proposal.

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

Partially agree.

Agree with the idea of allocating operating profit or loss as part of entity's profit or loss but disagree with the way this idea is implemented in the ED.

According to par.13 of the ED the statement of profit or loss is the first part of statement of financial performance. The second part is "other comprehensive income". Nothing more. The financial performance in the ID is strangely limited to only these two categories, although they are a small part of the actual financial performance.

Thus, the first Chapter of the IFRS Conceptual Framework for Financial Reporting states that financial performance is reflected in the financial statements by two types of indicators. There is financial performance reflected by accrual accounting and financial performance reflected by past cash flows. Paragraphs 1.17 – 1.19 of the CF speak of the financial performance reflected by accrual

accounting. Paragraph 1.20 of the CF speaks of the financial performance reflected by past cash flows. The ED contradicts the CF in this matter. The question of which of the two conflicting approaches is correct would be answered no doubt in favor of the approach of the CF. The ED should be brought into line with the CF, and not vice versa.

So, cash flows should be undoubtedly reported as part of the financial performance. And not only cash flows. The issue of allocating operating profit or loss cannot be considered in isolation from other structural elements of the entity's profit or loss. Paragraph 45 of the ED proposes to classify income and expenses included in profit or loss into operating, investing and financing categories. They are the same as cash flow categories. Indeed, investors are interested in both sides of the entity's operating, investment and financing activities – monetary and non-monetary. They cannot see the full picture of the entity's financial performance by looking only at cash flows. The reflection of any fact in the financial reporting always has two sides – debit and credit. Knowing information about one side, you still have no idea about the other one. In this sense, it is really a good idea to show these two sides of the entity's operating, investment and financing activities in their relationship. Due to this idea, reporting users would get a comprehensive picture of the entity's financial performance for the period.

But income and expenses are not able to show the entire non-monetary side of the entity's financial performance, but only a small part of it. They cover only activities that affect equity. As for operating activities, income and expenses do represent most of their non-monetary side. But this cannot be said about investment and financing activities. Most of them do not affect equity at all. Therefore, it is pointless to distinguish operating, investing and financing categories only as part of income and expenses without presenting other non-monetary results of the entity's financial performance. You will get a strange incomplete fragment of something larger, hidden from the reporting user. To get a comprehensive picture the financial performance information should also include information about changes in assets (other than cash) and in liabilities.

Income and expenses does not inform us of changes in assets and liabilities. They tell us only about changes in the difference between them, that is, changes in equity. A change in an asset or liability may result in a change in equity or in cash, or both, or neither. In any case, we are talking about different sides of the same fact. Changes in assets and liabilities have an independent informational value for the reporting users, regardless of how much they are informed about the other side – about changes in cash or in equity.

IFRS do require the data of changes in assets and liabilities be presented in financial statements. Here are some examples from the standards:

IAS 16 “Property, Plant and Equipment”. Paragraph 73 (e);
IAS 38 “Intangible Assets”. Paragraph 118 (e);
IAS 2 “Inventories”. Paragraph 37 (d), (e), (f);
IAS 37 “Provisions, Contingent Liabilities and Contingent Assets”. Paragraph 84 (b) – (e);
etc.

Such requirements are dispersed by different standards like scattered pieces. There are no consistency, no framework, no principles, and no intelligible approaches for them. Otherwise as the word “mess” it can't be called. A suitable place in the financial reporting for representing changes in assets and liabilities has not yet been found. They were lost somewhere between the primary statements and the notes.

So-called primary financial statements cover changes only in cash and in equity, but do not cover changes in assets and liabilities. The concept of “notes” in the meaning that the ED puts in it, also does not cover changes in assets and liabilities. We cannot call the table that reveals the movement of PPE for the period, a “note” to the line “PPE” in the balance sheet, because these are fundamentally different types of information. They have different dimensions and correspond to the well-known concept of stocks and flows, which are tagged in the IFRS Taxonomy with terms “instant” and “duration”.

We cannot refer to duration data as a “note” to corresponding instant data. Otherwise, we would have to call income and expenses a “note” to the line “retained earnings”. This idea is unlikely to please anyone. In the ED in paragraph 10, the statement of financial performance has now taken the first place among the primary financial statements, shifting the statement of financial position from it. But it is pointless to rank financial statements by importance. They are all important to users. Here we need to pay attention to something else.

The statement of financial position, no matter what place it is assigned in paragraph 10 of the ED, is better than other primary statements in the sense of its completeness. The name “balance sheet” speaks for itself. This is not just data about the financial position. This is also a RECONCILIATION between all instant indicators. Thanks to this valuable feature, this statement can only exist if it reflects absolutely all stocks, covers absolutely all instant data. We can only detail this data in the notes, but we cannot add anything to it or exclude anything from it.

Unfortunately, only the statement of financial position is so perfect. All other primary financial statements, which reflect flows for the reporting period, are defective. Despite the fact that there are three of them (clauses (a), (c), (d) of the paragraph 10 of the ED) they do not cover all duration data. They lack changes in assets and liabilities mentioned above. Because of this, the reporting user cannot get proper information about the operating, investment and financing activities of an entity for the reporting period.

These activities affect changes in all entity’s resources, including both cash and assets, and in all claims, including both equity and liabilities. But the statement of changes in equity together with the statement of profit or loss and other comprehensive income reflects only changes in equity for the reporting period, but does not reflect changes in liabilities. Similarly, the statement of cash flows reflects only changes in cash for the reporting period, but does not reflect changes in assets.

Such fragments are not able to provide any reconciliation between duration indicators. They could be reconciled with each other in their entirety, but they cannot be reconciled when we only take the changes in cash and equity and ignore the changes in assets and liabilities. This is the reason why existing attempts to reconcile flows take on such ridiculous clumsy forms as the indirect method of reporting cash flows from operating activities or placing among expenses inappropriate items like “Changes in inventories of finished goods and work in progress”.

In order to provide the reporting user with a complete picture of financial performance, financial statements must reflect all the results of the entity's operating, investment and financing activities. These results are expressed as duration indicators of changes in money, assets, equity, and liabilities. Taken together, they can be presented as a system of interconnected financial performance data that is as complete and perfect as the existing financial position data system.

In summary, the question of the subtotal for operating profit or loss cannot be considered separately. Differentiation of financial performance indicators in the context of operating, investment and financing activities makes sense only in the complex of all flows for the period, when the perimeter of these indicators covers, along with comprehensive income and cash flows, also transactions with owners, changes in assets and changes in liabilities.

Question 2 — the operating category

Paragraph 46 of the Exposure Draft proposes that entities classify in the operating category all income and expenses not classified in the other categories, such as the investing category or the financing category.

Paragraphs BC54–BC57 of the Basis for Conclusions describe the Board’s reasons for this proposal.

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

Partially agree.

Agree with the idea of classifying the operating category on a residual basis – as everything that is not included in the investing and financing categories. However, disagree with the implementation of this idea solely within the scope of profit and loss.

Most investment and financing activities do not affect profit or loss. The non-monetary side of investing activities is characterized mainly not by income and expenses, but by indicators of changes in non-current assets. Similarly, the non-monetary side of financing activities is characterized mainly not by income and expenses, but by indicators of changes in non-current liabilities, as well as changes in equity from transactions with shareholders. As for operating activities, some of them also do not affect equity, but are characterized by indicators of changes in current assets and current liabilities.

The definition of an operating category as results of activities that are not included in the investing and financing categories makes sense only if the financial statements present all the results of operating, investment and financing activities together in their relationship to each other and in relation to the corresponding cash flows. As noted in the comments on the question 1, this means presenting information about the entity's financial performance in the form of reconciliation of interrelated indicators of all changes in money, assets, equity and liabilities. Fragmentary allocation of these categories only within the scope of profit and loss is meaningless and will not provide useful information for users of financial reporting.

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

Paragraph 48 of the Exposure Draft proposes that an entity classifies in the operating category income and expenses from investments made in the course of the entity's main business activities.

Paragraphs BC58–BC61 of the Basis for Conclusions describe the Board's reasons for this proposal.

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

Partially agree (see the comments on the questions 1 and 2).

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

Paragraph 51 of the Exposure Draft proposes that an entity that provides financing to customers as a main business activity classify in the operating category either:

- income and expenses from financing activities, and from cash and cash equivalents, that relate to the provision of financing to customers; or
- all income and expenses from financing activities and all income and expenses from cash and cash equivalents.

Paragraphs BC62–BC69 of the Basis for Conclusions describe the Board's reasons for the proposals.

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

Partially agree (see the comments on the questions 1 and 2).

Question 5 — the investing category

Paragraphs 47–48 of the Exposure Draft propose that an entity classifies in the investing category income and expenses (including related incremental expenses) from assets that generate a return

individually and largely independently of other resources held by the entity, unless they are investments made in the course of the entity's main business activities.

Paragraphs BC48–BC52 of the Basis for Conclusions describe the Board's reasons for the proposal.

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

Disagree.

The results of an entity's investing activities rarely affect its equity and therefore data about them is not shown in income and expenses. The indicators referred to in paragraphs 47–48 of the ED are a tiny part of the of the entity's investment performance. Their separate presentation outside the context of the main part of investment performance is meaningless and will not provide any useful information to the reporting user.

Data on investing activity is mainly presented by indicators on changes in non-current assets. Examples of IFRS requirements to present such changes have already been provided in the comments to question 1 above (IAS 16, Par. 73 (e); IAS 38 Par. 118 (e)). Typically, such changes are presented in tabular form. And such a table can also be called a statement, for example, a "statement of changes in property, plant and equipment" (similar to the statement of changes in equity). If we add in that table changes in investment properties and intangibles it could be called a "statement of changes in non-financial long-term assets" or something like that.

Of course, the question is not what to call such a statement. As already noted, the issue of dividing into statements is irrelevant for electronic reporting. The main thing is that information about changes in assets should be positioned in the reporting as information about the entity's financial performance along with and in relation to information about income and expenses. In particular, information about the entity's investment performance should be presented primarily by indicators of changes in non-current assets. In this case, the income and expenses classified in the investing category would naturally complement the overall picture of the company's investing activities.

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

(a) Paragraphs 60(c) and 64 of the Exposure Draft propose that all entities, except for some specified entities (see paragraph 64 of the Exposure Draft), present a profit or loss before financing and income tax subtotal in the statement of profit or loss.

(b) Paragraph 49 of the Exposure Draft proposes which income and expenses an entity classifies in the financing category.

Paragraphs BC33–BC45 of the Basis for Conclusions describe the Board's reasons for the proposals.

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

Disagree.

The issue of allocating a financing category is similar to the issue of allocating an investing category (see comments on the question 5). Income and expenses do not characterize the non-monetary side of the entity's financing activities because financing activities rarely affect profits and losses. Financing activities are characterized mainly by changes in non-current liabilities, as well as by changes in equity from transactions with shareholders.

For example, an IPO is one of the most important performances that an entity's management performs. The attention of reporting users is focused on the results of the IPO much more than on profits for the period. But according to the ED, the IPO result should not be positioned as financial performance in financial reporting, as it is the result of raising funds from shareholders.

The same applies to changes in long-term liabilities. These changes are a much more informative indicators of the company's financial performance in the context of financing activities than the pathetic income and expenses that the ED puts in the financing category.

If such "financing" income and expenses were to complement changes in liabilities and transactions with owners in relation to financial cash flows, then the reporting user would see a comprehensive picture of the entity's financing activities. However, it makes no sense to separate financial income and expenses only within the scope of profit and loss.

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

(a) The proposed new paragraphs 20A–20D of IFRS 12 would define "integral associates and joint ventures" and "non-integral associates and joint ventures"; and require an entity to identify them.

(b) Paragraph 60(b) of the Exposure Draft proposes to require that an entity present in the statement of profit or loss a subtotal for operating profit or loss and income and expenses from integral associates and joint ventures.

(c) Paragraphs 53, 75(a) and 82(g)–82(h) of the Exposure Draft, the proposed new paragraph 38A of IAS 7 and the proposed new paragraph 20E of IFRS 12 would require an entity to provide information about integral associates and joint ventures separately from non-integral associates and joint ventures.

Paragraphs BC77–BC89 and BC205–BC213 of the Basis for Conclusions describe the Board's reasons for these 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?

Partially agree (see the comments on the questions 1, 2 and 5).

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

(a) Paragraphs 20–21 of the Exposure Draft set out the proposed description of the roles of the primary financial statements and the notes.

(b) Paragraphs 25–28 and B5–B15 of the Exposure Draft set out proposals for principles and general requirements on the aggregation and disaggregation of information.

Paragraphs BC19–BC27 of the Basis for Conclusions describe the Board's reasons for these proposals.

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

Strongly disagree.

Such issues as dividing reporting into separate statements and notes, aggregation and disaggregation of information and its distribution between primary statements and notes are relevant only for paper formats of reporting. Such issues do not exist in electronic forms of transmitting and visualizing financial information.

The provisions of IFRS on dividing reporting into separate statements and notes, as well as on aggregation and disaggregation of information, were born WHEN the statements were prepared on paper and BECAUSE they were prepared on paper. Since then, the situation has changed dramatically. Today, financial reporting is prepared in electronic form, presented in electronic form and, most importantly, used in electronic form. But the provisions of IFRS have not changed in this regard.

As a result, today these paper-format-based provisions of IFRS do not contribute to, but rather hinder the development of high quality financial reporting, preventing the use of modern electronic

tools in the field of information about the entity’s financial position and financial performance. That is why users of financial reporting today are deprived of all the advantages of digitalization that users of other types of information have.

For example, thirty years ago, the makers of geographic maps tackled questions such as how many pages of an atlas to devote to maps of a country, maps of regions, maps of cities, what scale of each map would be most convenient for users, where place data on geographic objects – in the corners of map pages or make a separate section with statistical information and indices at the end of the atlas, and the like. Who deals with such issues today? Only the one who is going to print maps on paper. The makers of electronic maps have forgotten about such problems.

In order to select the appropriate scale of a map, the user simply zooms in or out at his discretion, as it is convenient for him. He uses the same technique to switch from a country map to a city or region map in one motion. In order to see hotels, shops, gas stations, hospitals, schools, the user of electronic maps turns on or off the corresponding layers with one click. In order to find out the data about a geographic object, the user simply hovers the mouse over it and does not even have to click, the data window opens automatically.

What would happen if, in the last quarter of the 20th century, some sort of “international geographic map standards” were created, which would contain requirements for the aggregation and disaggregation of geographic information, its distribution among primary geographic maps and notes? It is unlikely that in such conditions the modern navigation systems to which we are accustomed today would appear. This is exactly the kind of misfortune that happened to financial reporting. Today, no one even tries to create some kind of navigation system for the entity's financial position and financial performance. Because any way of presenting information other than in paper-based forms will be considered non-compliance with the IFRS.

Happy is the user of an electronic map, which is not burdened with the paper-format-based requirements of International Geographic Map Standards. Unhappy is the user of electronic financial reporting, which must comply with the paper-format-based requirements of International Financial Reporting Standards.

Often, information that is useful in principle for the reporting user looks unreadable in the reporting due to its form, which IFRS require to fit into paper formats. Paragraphs 101 and 106 of the ED, which are referred to in questions 10 and 11, are good examples of such indigestible forms of presentation. Only an expert in fraud investigation would deal with such inconveniently visualized data. There is hardly a user who is willing and able to make economic decisions based on it.

In order not to aggravate the situation, all requirements for the formats of information presented in financial reporting should be urgently removed from IFRS. Classification, recognition and measurement of entity’s resources, claims and changes in them, the content and scope of information provided – these are the issues that can and should be the subject of IFRS provisions. However, the standards should not say anything about what information in financial reporting should look like, and certainly should not require that this information should look like a folio lump of paper pages.

IAS 1 or any new standard may set requirements for the scope and content of information about the entity's financial position to be included in its financial reporting. However, the standard should not set requirements for LINES in the STATEMENT of financial position. The standard may set requirements for the scope and content of information about the changes in financial position and refer to them as financial performance but should not require to present this information in that poor clumsy form of several statements mentioned in the clauses (a), (c), (d) of the paragraph 10 of the ED. The standard may specify which disclosures should be included in the reporting, but should not require those disclosures to be presented in the form of NOTES, which are numbered in a column of a “primary” statement.

The standard may set the minimum required level of detail for data to be included in financial statements, but it should not say anything about aggregation and disaggregation of this data. Electronic tools can provide the user with the ability to choose any desired aggregation level in any part of the reporting and shift this level at their own discretion.

Question 9 — analysis of operating expenses

Paragraphs 68 and B45 of the Exposure Draft propose requirements and application guidance to help an entity to decide whether to present its operating expenses using the nature of expense method or the function of expense method of analysis. Paragraph 72 of the Exposure Draft proposes requiring an entity that provides an analysis of its operating expenses by function in the statement of profit or loss to provide an analysis using the nature of expense method in the notes.

Paragraphs BC109–BC114 of the Basis for Conclusions describe the Board's reasons for the proposals.

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

Disagree.

If we look closely, we realize that these two analyses correspond to two sides of the accounting double entry – debit and credit. A more accurate name for the analysis by function is the analysis of the debit side. And the analysis by nature is actually the analysis of the credit side. The first one talks about where the entity's resources are spent. And the second one speaks about what resources are spent.

Clearly, users of financial statements require both types of information. It is very foolish to ask which analysis is more useful and which is less. This is the same as allowing entities to present only one side of the balance sheet, something like presenting an analysis of financial position "by resources" or "by claims", whichever provides the most useful information. Obviously, it does not make sense to ask what is more important in accounting – debit or credit.

It is also pointless to discuss which analysis should be presented in the primary financial statement and which should be presented in the notes. A debit cannot be a note to a credit, just as a credit cannot be a note to a debit. These are types of information of the same level of importance.

Two analyses characterize two different sides of the entity's financial performance. The so-called "analysis by function" characterizes financial performance in terms of changes in the entity's equity. The so-called "analysis by nature" characterizes financial performance in terms of changes in the entity's assets and liabilities.

If we are talking about expenses, they are recorded on the debit side. Therefore, there can be only one way to analyze expenses – based on what an entity spends resources on – what is now called "analysis by function". And as for the analysis by nature, it is undoubtedly very useful information. However, it is not an analysis of expenses at all. Because it is not about changes in equity. It is about changes in assets and liabilities.

Amortization and depreciation are changes in fixed assets for a period. There is no such phenomenon as depreciation *expense* in accounting as well as employee benefits *expense*. We could call them costs or expenditures, but not expenses.

There is an important difference between the terms "expenditures" and "expenses". It is clearly visible in the definition of expenses (Conceptual Framework for Financial Reporting, par. 4.69). Expenses are decreases in assets, or increases in liabilities, that result in decreases in equity … The first part of the definition is about the credit side – about expenditures. Decreases in property, plant and equipment or increases in employee benefits liability. The second part of the definition is about the debit side – what do those changes result in, how they should be recognized. Sometimes those changes are indeed recognized as expenses. However, only sometimes. More often, they are recognized as cost

of assets. In operating activities, this is the cost of inventories. In investing activities, this is the cost of fixed assets.

Look at this item “Changes in inventories of finished goods and work in progress” (Illustrative Examples of the ED, Note 1 – Analysis of operating expenses by nature). It is neither income, nor expense. This item is not related to the statement of profit or loss. Clearly, it is a random guest, which does not belong here.

Nor do the following items. What is “Raw material used” in terms of accounting? It is just a conversion of one type of inventory to another type. Raw materials are converted into work in progress. Even the asset class hasn't changed. There were inventories and there are inventories in the same amount. Definitely, it is not expense. A similar story with such items as “Employee benefits”, “Depreciation”, “Amortization”. They will be recognized as expenses only when revenue from the sale of finished goods is recognized. Until this happens, these are changes in assets and liabilities that do not result in changes in equity.

The time interval between these accruals and the sale of the finished goods depends on the length of the entity's operating cycle. In some industries, it can last for several years. But even with shorter operating cycles, the current analysis “by nature” often does not correspond to the current profit and loss, since it refers to future profits that have not yet been earned.

The above does not detract from the value of information about the entity's cost structure. This information is undoubtedly necessary for the reporting user and should be presented in it. The question is how this information should be positioned in the financial reporting. The accountant should not deceive the user by saying that the cost structure is allegedly an analysis of expenses. It is not an expense analysis. It is an analysis of changes in assets and liabilities.

When an accountant pushes this cost analysis inside the P&L statement to make it look like an expense analysis, his enemy is math. Math prevents the accountant from solving this preposterous task. But he persists in his efforts to deceive reporting users and defeats math with the help of such misplaced items like “Changes in inventories of finished goods and work in progress”.

But these tricks are still not enough to beat math. The expenditures may be included in the cost of PPE or Intangible asset. Trying to reconcile such amounts we have to include here “Changes in fixed assets” as well. This will take us very far from what is considered a profit or loss.

Besides, there is no reason to limit the “analysis by nature” to operating activities only. If we have decided to allocate an investing category in income and expenses, why hide the investment part of the cost analysis from the reporting user?

The analysis of cost “by nature” is necessary for financial reporting users to understand how much the labor costs compared to how much the means of labor and objects of labor cost. The users want to see this expenditure structure as a comprehensive picture in all its aspects. This picture can't be presented as an expense analysis because most of the expenditures are included in the cost of current or non-current assets and only a small part is recognized immediately as expenses.

Thus, the need to choose one of the two analyses of operating expenses is far-fetched, because only one of them is related to expenses – the one we call “by function”. The cost structure analysis, which we call “by nature”, is information about changes in assets and liabilities.

Obviously, both analyses characterize the company's financial performance: the “function” analysis – in terms of changes in equity, the “nature” analysis – in terms of changes in assets and liabilities. If financial performance is not narrowed down to profit and loss alone, but is presented as interrelated changes in money, assets, equity, and liabilities, then each of the analyses will take its proper place, and accountants will not have to deceive reporting users by calling expenses what are not expenses.

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?

Partially agree.

Agree with the idea of allocating unusual results and how this "unusual" is defined but disagree with the feasibility of implementing this idea only in terms of income and expenses.

The paragraphs BC122–BC144 of the Basis for Conclusions do not explain why data on unusual items should be disclosed only in terms of impact on equity. Data on unusual income and expenses will be useless to the reporting user if he does not see other aspects of unusual financial performance results. Definitely, unusual cash flows should be disclosed too for the same reasons as well as unusual changes in assets and unusual changes in liabilities.

As explained above in the answers to questions 1, 2, 5, 6, 9 the entity's financial performance should be presented in the financial reporting as a reconciliation of all changes in money, assets, equity, and liabilities, where income and expenses represent only a fraction of the changes in equity. Unusual items should be highlighted in the same way in all four specified types of changes. Only then would this information be useful to the reporting user, and its presentation in the financial reporting would be justified.

In view of our response to question 8, we strongly disagree with the requirements of paragraph 101 of the ED regarding HOW information of unusual items should be presented. No user of financial reporting will want to deal with data presented in such an inconvenient form.

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?

Partially agree.

Agree that information about management performance measures should be included in financial reporting but disagree with how it is defined in the ED and how it should be reported.

Paragraph 103 of the ED defines management performance measures as subtotals of income and expenses. This definition is based on the presumption that management performance is assessed solely in terms of the impact on the entity's equity, since income and expenses are defined as what affects the equity (CF, 4.69). This presumption has little to do with reality. In practice, most of the differences between MPM and items presented in the P&L statement are not that income and expenses are grouped in a different way than in the statement, but that amounts that are not essentially income or expenses, i.e. amounts that do not affect equity, are added to or deducted from profit and loss.

For example, it is common practice to deduct depreciation and amortization from profit or loss when assessing management performance. Depreciation and amortization are not changes in equity but changes in assets. These changes are more often included in the cost of inventories than are recognized in profit or loss. If the depreciable asset is used to create other non-current assets, then the depreciation is included in the cost of the asset being created.

In addition, the management performance is not only in operating activities, but also in investing and financing activities. Investing and financing activities mostly do not affect equity. Therefore, in practice, to assess financial performance in terms of investing and financing activities indicators are used, which are mostly not income or expenses.

Thus, the MPM cannot be defined as subtotals of income and expenses. They should be defined as subtotals of changes in money, in assets, in equity, and in liabilities that: (a)…, (b)…, (c)… (ED, 103). As explained above in the comments to questions 1, 2, 5, 6, 9, 10 the entity's financial performance should be presented in the financial reporting as a reconciliation of all changes in money, assets, equity, and liabilities. With this way of presentation, any MPM can be designated as the selected set of elements of this reconciliation. Then there would be no need for a separate note referred to in paragraph 106 of the ED. As for the way of presenting data on MPM required by the paragraph 106, this way does not stand up to any criticism. No user of financial reporting will want to deal with data presented in such an inconvenient form.

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?

Agree taking into account the comments to question 11.

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.

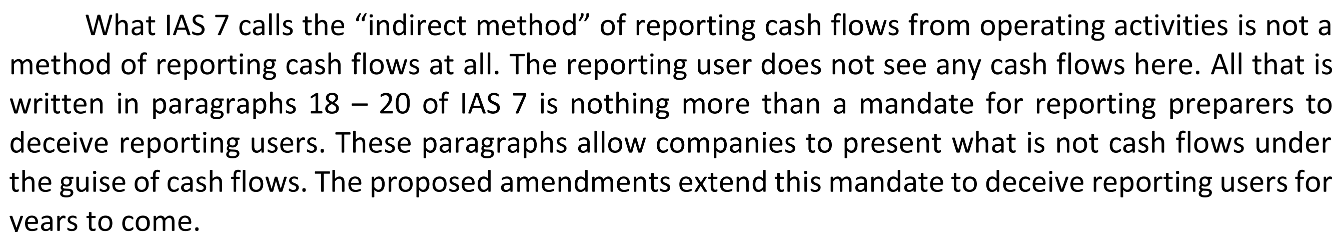
(b) The proposed new paragraphs 33A and 34A–34D of IAS 7 would specify the classification of interest and dividend cash flows.

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?

Partially agree.

Agree with the proposed classification of interest and dividend cash flows but disagree with the indirect method of reporting cash flows from operating activities.



What IAS 7 calls the “indirect method” of reporting cash flows from operating activities is not a method of reporting cash flows at all. The reporting user does not see any cash flows here. All that is written in paragraphs 18 – 20 of IAS 7 is nothing more than a mandate for reporting preparers to deceive reporting users. These paragraphs allow companies to present what is not cash flows under the guise of cash flows. The proposed amendments extend this mandate to deceive reporting users for years to come.

If the IASB is determined to continue to cave in under the lobby of influential preparers who do not want to show the operating cash flows in their financial statements, then it should at least call a spade a spade. In this case, the Board should explicitly state in the standard that an entity may not present data on cash flows from operating activities in the statement of cash flows. As for the adjustments of operating profit or loss set out in paragraph 20 of IAS 7 (taking into account the amendments proposed in the ED), they could be positioned in the financial reporting as a fragment reconciliation of profits and losses with changes in assets and liabilities, but they certainly should not be disguised as cash flows. If the reporting user is deprived of useful information, then at least he will know about it.

Meanwhile, today there are no clear excuses for such a relaxation of requirements for financial reporting. At least the BC does not provide any justification for this. Data on all types of cash flows is very important for reporting users, maybe even more important than data on income and expenses. Some companies have difficulty collecting data on direct cash flows because they still use for accounting the medieval flat double-entry technic, which does not allow them to organize cash flow accounts in the way as income and expense accounts are organized. However, the deficiency of the lame accounting technic cannot serve as an excuse for depriving the reporting user of useful information.

The reporting user should get comprehensive data on direct cash flows. Moreover, any entity can provide such data in a non-burdensome way and show them in relation to profits and losses. As noted in the comments to question 1 the Conceptual Framework for Financial Reporting defines cash flows as indicators of entity's financial performance, along with profits and losses. This means that both types of data must be presented in the financial reporting together in such a way that the reconciliation between them is visible.

The adjustments of operating profit or loss set out in paragraph 20 of IAS 7 are an example of a fragment of such reconciliation. This fragment makes little sense and is of little use to the reporting user because it is just a fragment. It is futile to reconcile SOME cash flows and SOME changes in equity with SOME changes in assets and SOME changes in liabilities. For a complete reconciliation, you need to take ALL changes in money and ALL changes in equity with ALL changes in assets and ALL changes in liabilities. As noted repeatedly above in the comments to previous questions, this reconciliation is the best way to present the entity's financial performance in its financial reporting. This way is as simple as possible for the reporting preparer, since all data derives from the classical balance equality. At the same time, this method is maximally informative for the reporting user, since it allows him to see a complete picture of the entity's financial performance in all its aspects of operating, investing and financing activities.

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 amount of information in financial reporting today is so large that only a tiny percentage of it is actually used by users to make economic decisions. This percentage could be significantly higher if IFRS were focused on electronic information visualization tools. But the requirements of IFRS do not just ignore these tools, but actually block any opportunity to use them.

The ED regarding the requirements for data presentation forms looks as if it was prepared not in 2020, but in 1990. Financial reporting is a heavy paper folio with numbered pages of statements and notes, where the most advanced data visualization tool is a table with lines and columns, and the most advanced navigation tool is a column with numbers of notes. This is the image that the ED is really focused on. Anyone who thinks this image is exaggerated can look at the Illustrative Examples.

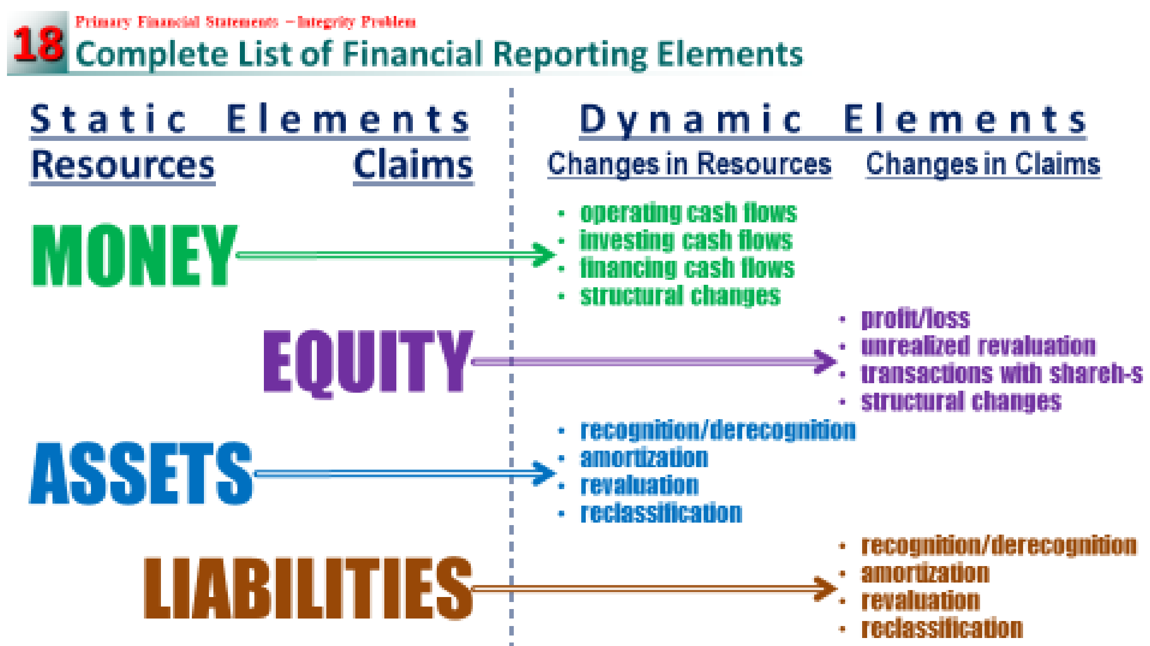
The main effect of Covid-19 that we are facing now and will face more and more in the long term is remote relationships, remote communications, remote information circulation. Everything is digitalizing. The Covid is not the root cause of why humanity refuses paper media and converts information into electronic form. The Covid is just an accelerator of this process.

Financial reporting does contain useful information, but due to their binding to paper formats, this information is extremely inconvenient to use on the verge of being impossible to use. If financial reporting does not say goodbye to its paper image in the coming years, investors will simply stop using it for making economic decisions, preferring other more convenient sources of information adapted to the digital age.

The ED cannot be released as a standard in the proposed version. If this happens, the binding of financial statements to paper format will be preserved for years to come. Then the dream of developing a single set of high-quality, understandable, enforceable and globally accepted accounting standards will be buried.

The standard should be conceptually revised in terms of requirements for data presentation forms. The standard should focus on electronic forms of data visualization and navigation. Every time the author of a standard thinks about some provision, he should forget about the paper format, about PDF and imagine instead a computer screen where hyperlinks work, windows open one in another, lines and sublines unfold, etc., etc. He should imagine not a set of stiff bureaucratic statements but an integral information system where the user can compose and structure information at his own discretion, where the user does not look at a rigid image imprinted in granite by an accountant, but displays the image on the screen in the form that is convenient for him.

At the 18th meeting of the Emerging Economies Group in December 2019 in Xiamen, a presentation was made, which, among other things, outlined the scheme of relationships between the elements of financial statements, on the basis of which it is possible to build a single electronic financial reporting without dividing it into separate statements and notes. The IASB has a video recording of this presentation. Here is one of the slides from it:



If the Board cannot quickly review the entire standard, it should, at least as a matter of urgency, replace paragraph 2 of the standard with the following text: "An entity shall apply this Standard in presenting and disclosing information in financial statements prepared as a hard copy or as an electronic hard copy equivalent". An entity is not required to apply this Standard to financial reporting in electronic form when it uses visualization and navigation tools that allow reporting users to compose and structure reporting information at their own discretion". This amendment to IAS 1 will benefit more than all the ED amendments together.

In recent years, the Board seems to be mired in narrow local issues. It has lost the ability "to see the forest behind the trees". Covid-19, which forced everyone to master remote communications, is not just a signal to change the agenda. This is the last call for the IASB to change the agenda.

We would be pleased to answer any questions and discuss any aspects of these comments.

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