Navigating the transition of IAS 1

To

IFRS 18

Presentation and Disclosure in Financial Statements

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1.0 Summary of Changes & New Requirements

- **Impact of the introduction of IFRS 18:**

  IFRS 18 replaces IAS 1 Presentation of Financial Statements

- **IFRS 18 introduces new requirements:**

  (a) present specified categories and defined subtotals in the statement of profit or loss

  (b) provide disclosures on management-defined performance measures (MPMs) in the notes to the financial statements

  (c) improve aggregation and disaggregation

- **Other Standards changes:**

  (a) To reflect the extended content of IAS 8, the IASB is changing the title of the standard to 'Basis of Preparation of Financial Statements' once IFRS 18 is effective.

  (b) Some of the requirements in IAS 1 are moved to IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors

  (C) The IASB also makes minor amendments to IAS 7 Statement of Cash Flows, IAS 33 Earnings per Share and IAS 34 Interim Financial reporting

- **Effective date and Application:**

  (a) An entity is required to apply IFRS 18 for annual reporting periods beginning on or after 1 January 2027 with earlier application permitted.

  (b) IFRS 18 requires retrospective application with specific transition provisions.

2.0 Background of the Publication of IFRS 18

In 2016

The IASB initiated its primary financial statements project in response to investors' concerns about the comparability and transparency of entities' performance reporting.

In 17th December 2019 to September 2020

The IASB published **ED/2019/7** General Presentation and Disclosures. After the comment period expired, the IASB redeliberated the proposals considering the comments received.

In 9th April 2024

The proposals have now been finalized in IFRS 18, with some modifications and published.

3.0 Objective of this standard

Better information for better decisions:

- Increasing comparability
- Increase transparency
- Increase usefulness of information

4.0 Three New requirements of IFRS 18

S.L.	New Requirements
1.	New required subtotals in statement of profit or loss, including operating profit
2.	Disclosures about management- defined performance measures (MPM)
3.	Enhanced guidance on grouping of information (Aggregation and Disaggregation)

5.0 New required subtotals in statement of profit or loss, including operating profit

5.1. IFRS 18 requires an entity to classify income and expenses included in profit or loss into the following categories:

Categories	Definition
Operating	Income and expenses that are not classified in other categories
Investing	The investing category comprises income and expenses from: • investments in associates, joint ventures and unconsolidated subsidiaries • cash and cash equivalents • other assets that generate a return individually and largely independently of the entity's other resources. For Example, • the share of profit of associates and joint ventures accounted for using the equity method • interest revenue from debt investments • dividends from equity investments • rental income and fair value gains or losses from investment properties.
Financing	• Income and expenses from liabilities from transactions that involve only the range of finance. for example, transaction costs

	• Interest expenses and effects of changes in interest rates from other liabilities
Income Tax	Income tax expenses arising from the application of IAS 12
Discontinued Operations	Income and expense from discontinued operations arising from the application of IFRS 5

5.2. Two new required subtotals to enable analysis:

- Operating Profit
- Profit before financing and income taxes

5.3. Illustrative statement of profit or loss

Statement of Financial Performance for 20X1–20X2 in Accordance with IAS 1

Year (amounts)	**20X2**	**20X1**
Revenue from the sale of goods	XXX	XXX
Cost of goods sold	XXX	XXX
Gross profit	**XXX**	**XXX**
Other income	XXX	XXX
Selling expenses	XXX	XXX
General and administrative expenses	XXX	XXX
Other expenses	XXX	XXX
Finance costs	XXX	XXX
Profit before tax	**XXX**	**XXX**
Income tax expense	XXX	XXX
Profit for the year from continuing operations	**XXX**	**XXX**
Loss for the year from continuing operations	XXX	XXX
Profit for the year	**XXX**	**XXX**

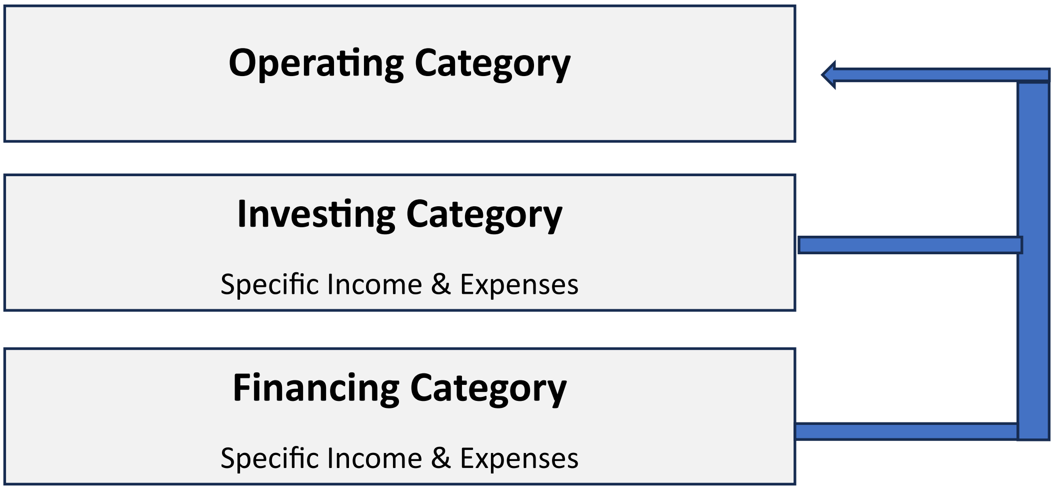
Transformed Statement of Financial Performance for 20X1–20X2 in Accordance with IFRS 18

Year (amounts)	20X2	20X1	Categories*
Revenue from the sale of goods	XXX	XXX	Operating
Cost of goods sold	XXX	XXX	
Gross profit	**XXX**	**XXX**	
Other operating income	XXX	XXX	
Selling expenses	XXX	XXX	
General and administrative expenses	XXX	XXX	
Research and development expenses	XXX	XXX	
Godwill impairment loss	XXX	XXX	
Other operating expenses	XXX	XXX	
Operating profit	**XXX**	**XXX**	
Share of profit and gains on disposal of associates and joint ventures	XXX	XXX	Investing
Profit before financing and income taxes	**XXX**	**XXX**	
Interest expenses on borrowings and lease liabilities	XXX	XXX	Financing
Interest expenses on pension liabilities and provisions	XXX	XXX	
Profit before income taxes	**XXX**	**XXX**	
Income tax expense	XXX	XXX	Income taxes
Profit for the year from continuing operations	**XXX**	**XXX**	
Loss for the year from continuing operations	XXX	XXX	Discontinued operations
Profit for the year	**XXX**	**XXX**	

**The 'Categories' column is presented to illustrate the structure of the statement of profit or loss. Category labels are not required to be presented in the statement of profit or loss*

5.4. Requirements for entities with specified main business activities

- For some companies, Financing and investing activities are their main activities
- These companies include income and expenses in their operating profit that for other companies would be included in the investing or financing categories.



Banks

The operating category for a bank would generally include income and expenses from, for example:

- the **net interest result**—including interest revenue and interest expenses; and
- the **fee and commission result**—including fee and commission revenue and fee and commission expenses.

The operating category would include some income and expenses that would otherwise be classified in the financing category. In most cases, banks would not present the 'profit before financing and income taxes' subtotal.

Insurers

The operating category for an insurer would generally include income and expenses that would otherwise be classified in the investing or financing categories, for example:

- the **insurance service result**—including insurance revenue and insurance service expenses; and
- the **net financial result**—including investment income and insurance finance income and expenses.

5.5. Classification of specific income and expenses

- **Foreign exchange differences**:
  Foreign exchange differences are classified in the same category as the income and expenses from the items that gave rise to those differences.
  For example, foreign exchange differences on a foreign-currency denominated receivable for a sale of goods are classified in the operating category (the same category as the sale of goods). However, an entity is permitted to classify foreign exchange differences in the operating category if classifying them in the same category as the income and expenses from the items that gave rise to them would involve undue cost or effort
- **Fair value gains and losses on derivatives:**
  The classification of fair value gains and losses on derivatives depends on whether the derivatives are used to manage exposure to identified risks and whether they are designated as hedging instruments
- **Income and expenses from hybrid contracts:**
  The classification of income and expenses from hybrid contracts comprising host liabilities and embedded derivatives depends on whether the embedded derivative is separated from the host liability and the nature of the hybrid contract.

6.0 Disclosures about management- defined performance measures (MPM) in a Single Note

6.1. Objectives

Management performance measures are useful because they provide insight into how management views an entity's financial performance.

Financial statement Preparer

- Can share their story in the financial statement and provide their view of the performance of the statement.

User of Financial statement

- Getting Clear the picture what management think about its performance.

6.2. Definition

MPMs are subtotals of income and expenses that meet all of the following criteria:

- are used in public communications outside financial statements, such as management commentary, press releases and investor presentations (NB: oral communications, written transcripts of oral communications or social media posts do not represent public communications for the purpose of identifying MPMs)
- are used to communicate to investors management's view of an aspect of the financial performance of the entity as a whole—it is presumed that a subtotal of income and expenses that an entity uses in public communications outside its financial statements communicates management's view of an aspect of the financial performance of the entity as a whole, unless the entity rebuts the presumption
- are not listed in IFRS 18 or specifically required by IFRS Accounting Standards that are

a. gross profit or loss (revenue minus cost of sales) and similar subtotals (see paragraph B123);
b. operating profit or loss before depreciation, amortization and impairments within the scope of IAS 36;
c. operating profit or loss and income and expenses from all investments accounted for using the equity method;
d. for an entity that applies paragraph 73, a subtotal comprising operating profit or loss and all income and expenses classified in the investing category;
e. profit or loss before income taxes; and
f. profit or loss from continuing operations.

6.3. Scope of MPM

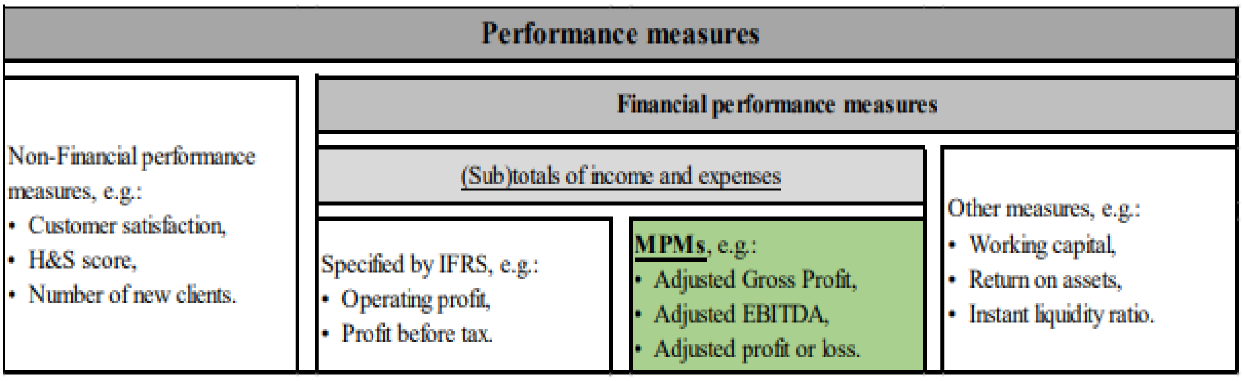


Figure 1. Scope of Management Performance Measures
Source: (IFRS Accounting, 2023, July)

6.4. Disclosure requirements for MPM's

Disclosure requiremenets for MPMs		
Reconciliation	➡	Reconciliation between MPM and the most directly comparable subtotal or total specified by IFRS Accounting Standards, including the income tax effect and effect on non-controlling interests
Why an MPM communicates management's view	➡	Includes an explanation of how the MPM is calculated and how the measure provides useful information about the entity's performance. Explanation should refer to individual reconciling items where necessary
Not necessarily comparable with other entities	➡	A statement that MPM provides management's view of an aspect of the entity's financial performance and is not necessarily comparable with measures provided by other entities
Changes in calculation	➡	Explanation of and reasons for any changes in how the entity calculates its MPMs or which MPMs it provides

6.5. Reconciliation between MPM and the Most Directly Comparable Subtotal Specified by IFRS

In the example, the adjusted operating profit in MPM disclosed in the financial report is a management view of operating profit, excluding incidental restructuring in country X. Through subtraction of restructuring costs and revenue adjustments, it is reconciled to the most direct subtotal, which in this case is operating profit. The two right columns affect income tax and non-controlling interests (later referred to as NCIs), as the entity is also obligated to include these effects for each reconciliation. The new standard does not include a graphical sample of the reconciliation. During the discussion at the IASB meeting in July

2023, there seemed to be an agreement that the standard would not require one specific methodology with regards to reconciliations but might propose examples to ease the process for entities having trouble accommodating the differences between MPM and the most directly comparable subtotal specified by IFRS. One of the points was of the new methodology was to show the MPM first (at the top), which then gets reconciled to a subtotal.

Adjusted operating profit (MPM)	60,000	Tax effect	NCI
- Restructuring in Country X (incl. In employee benefits)	-5,000	1,000	-800
- Revenue adjustment (incl. in revenue)	-6,000	1,200	-
Operating Profit (IFRS-specified)	**49,000**		

Figure 4. Reconciliation of the MPM
Source: Own elaboration based on FASB IASB Joint Educational Meeting (2022, September)

7.0 Hypothetical Case study of MPM

The case is based on ABC Company, whose data were drawn from accounting books for two consecutive years, from 2022 to 2023. The company has decided to implement IFRS 18. The Company tax rate is 27.5%. The statement of Profit and loss is given below:

Statement of Financial Performance for 2023 in Accordance with IFRS 18

Year (amounts)	2023	2022
Revenue from the sale of goods	22,132,991.00	16,381,185.00
Cost of goods sold	(15,447,701.00)	(11,298,542.00)
Gross profit	**6,685,290.00**	**5,082,644.00**
Other income	265,245.00	102,756.00
Selling expenses	(1,701,360.00)	(1,192,527.00)
General and administrative expenses	(2,554,044.00)	(2,208,843.00)
Other operating expenses	(444,009.00)	(401,108.00)
Operating profit	**2,251,122.00**	**1,382,922.00**
Investment income	145,000.00	99,000.00
Investment costs	(9,000.00)	(6,000.00)
Profit before financing and income tax	**2,387,122.00**	**1,475,922.00**
Finance income	-	-
Finance costs	(8,058.00)	(2,882.00)
Profit before tax	**2,379,064.00**	**1,473,041.00**
Income tax expense	128,469.00	154,669.00
Profit for the year from continuing operations	**2,250,595.00**	**1,318,372.00**
Loss for the year from continuing operations	-	-
Profit for the year	**2,250,595.00**	**1,318,372.00**

Since IFRS 18 proposes an introduction of management performance measures. The company is decided to disclose one measures that meet MPM definition and scope that is adjusted Earnings Before Interests Taxes Depreciation and Amortization (EBITDA). The company will reconcile the MPM to the most directly comparable subtotal or total specified within IFRS, including the effect of tax and non-controlling interests. In this case, the study of non-controlling interests is disregarded, as the company under investigation does not invest in shares of any other company and is 100% owned by its parent company.

For reconciliation purposes, the company decided to adjust the subtotals by following incomes/ expenses:

- Incidental incomes
- Incidental Expense
- Incidental cost reduction
- Internal group costs
- Depreciation and amortization cost
- Interest received from Occasional loans
- Exchange rates gain/loss from interest on occasional loan

Internal group costs are 352,095 and 320,195 for 2022 and 2023 respectively

List of Incidental Income and Expenses in ABC Company for 2022–2023

Adjustable income & Expenses	**2023**	**2022**
Incidental incomes	Settlement with a customer over a dispute is 46,518	Insurance compensation for a car broken in an accident is 22,741
Incidental expenses	Tax non-compliance fine is 14,743	Costs of repair of car broken in an accident is 5,210

Question: Now prepare a single note for Financial Statement Disclosure to comply IFRS 18.

Solutions:

IFRS 18 requires companies to disclose information about MPMs, which will increase transparency and investors' understanding of how the measures compare with the measures defined by IFRS Accounting Standards. Investors use MPMs to get insight into how management views the company's financial performance, how the company is managed and how its financial performance is developing.

The IFRS 18 has defined, A management-defined performance measure is a subtotal of income and expenses that

a) an entity uses in public communications outside financial statements;
b) an entity uses to communicate to users of financial statements management's view of an aspect of the financial performance of the entity as a whole; and
c) is not listed in paragraph 118, or specifically required to be presented or disclosed by IFRS Accounting Standards.

In order to comply IFRS 18, Management has selected one measure, that is Adjusted EBITDA, to disclose which is met the scope of MPM and reconcile the MPM to the most directly comparable subtotal or total specified within IFRS, including the effect of tax. The company is 100% owned parent company so there is no impact of non-controlling interest.

List of Incidental Income and Expenses in ABC Company for 2022–2023, management seems these income and expenses are non-recurring.

Adjustable income & Expenses	**2023**	**2022**
Incidental incomes	Settlement with a customer over a dispute is 46,518	Insurance compensation for a car broken in an accident is 22,741
Incidental expenses	Tax non-compliance fine is 14,743	Costs of repair of car broken in an accident is 5,210

The reconciliation of adjusted EBITDA and EBIT with the subtotal presented in the statement of financial performance is presented in the following Table:

Reconciliation of Adjusted EBITDA and EBIT

	2023		2022	
	Amount	**Tax Effect**	**Amount**	**Tax Effect**
Adjusted EBITDA	**3,284,290**		**2,211,128**	
- depreciation and amortization	(576,849)	(158,633)	(432,542)	(118,949)
Adjusted EBIT	**2,707,441**		**1,778,586**	
- Internal group costs	(352,095)	(96,826)	(320,195)	(88,054)
- incidental incomes	46,518	12,792	22,741	6,254
- incidental expenses	(14,743)	(4,054)	(5,210)	(1,433)
Profit before financing and income tax	**2,387,122**		**1,475,922**	

For all two years, ABC Company used adjusted EBITDA and adjusted EBIT as their MPMs. Incidental transactions are excluded from financial profits before evaluating the company's performance. Further, internal group costs are subtracted from the financials to receive adjusted EBIT, which is further corrected by depreciation and amortization costs, which concludes with adjusted EBITDA. Both are presented on reports regarding company and total capital group performance, meeting the MPM definition. While EBIT and EBITDA are commonly presented measures by companies, the computation presented in the Table provides precious information to the users of financial statements, as they have direct and accessible data as to how EBIT and EBITDA presented in various companies' reports were calculated and what transactions were subtracted from the profits. That highly increases transparency.

Further that the Company does not change the calculation of an MPM, which ceases to use a previously disclosed MPM

8.0 Aggregation and disaggregation of information

IFRS 18 enhanced the requirements for labelling, aggregation and disaggregation with the following key changes:

- Items must be disaggregated if the resulting disaggregated information is material.
- Use the label "other" only if an entity is unable to find a more informative label and
- Entities that classify expenses by function will be required to disclose the amount included in each line item for depreciation, amortization, employee benefits, impairment losses and write down of inventories.

Presentation of operating expenses

IFRS 18 requires entities to classify and present operating expenses in a way that provides the most useful structured summary of its expenses using one or both of these the characteristics of:

- **the nature of the expense**
  for example,

Sales		**XXX**
Expenses:		
Purchases, delivery charges and other direct costs	XXX	
Changes in inventory	XXX	
Depreciation Expense	XXX	
Rent Expense	XXX	
Employee benefit expenses	XXX	
Utilities Expense	XXX	
Total Expenses		**XXX**
Operating profit		**XXX**

- **the function of the expenses within the entity**

  for example,

Year (amounts)	20X2	20X1
Revenue from the sale of goods	XXX	XXX
Cost of goods sold	XXX	XXX
Gross profit	**XXX**	**XXX**
Other operating income	XXX	XXX
Selling expenses	XXX	XXX
General and administrative expenses	XXX	XXX
Research and development expenses	XXX	XXX
Godwill impairment loss	XXX	XXX
Other operating expenses	XXX	XXX
Operating profit	**XXX**	**XXX**

In deciding how to present operating expenses, an entity is required to consider factors such as what line items provide the most useful information about the main components or drivers of the entity's profitability and industry practice.

An entity that presents one or more-line items for operating expenses classified by function is required to disclose amounts for specified expenses by nature in a single note to the financial statements.

9.0 Changes in Other Standards

9.1. Amendments to IAS 7

The IASB amended IAS 7 to:

- require all entities to use the operating profit subtotal as the starting point for the indirect method of reporting cash flows from operating activities

Sample Cashflow starting point before IFRS 18 Application:

Indirect method

Cash flows from operating activities	$	$
Profit before tax		xxx
Adjustments for:		
Depreciation on non-current assets		xxx
Armotisation of intangible assets		xxx

Sample Cashflow starting point after IFRS 18 Application:

Indirect method	
Cashflow from operating activities	
Operating profit	XXX
Adjustments for:	

- remove the presentation alternatives for cash flows related to interest and dividends paid and received as follows:

– for entities with no specified main business activities:

» Interest and dividends received will always be classified as cash flows from investing activities

» Interest and dividends paid will always be classified as cash flows from financing activities

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Previous presentation:

Finance costs		xxx
Investment income		xxx
Operating profit before working capital changes		xxx
Working capital adjustments:		
Increase in inventory		xxx
Decrease in gross trade receivables		xxx
Increase in prepaid expenses		xxx
Increase in trade payables		xxx
Decrease in accrued expenses		xxx
Cash generated from operations		xxx
Finance cost paid	xxx	
Tax paid	xxx	xxx
Net cash inflow/ (outflow) from operating activities		xxx

Presentation after IFRS 18:

Cashflow from Investing activities	
Investment/Dividend income received	XXX
Interest income received	XXX
Cashflow from financing activities	
Dividend Paid	XXX
Interest expense paid	XXX

– for entities that invest in assets or provide financing to customers as a main business activity, the entity is required to:

» Determine how to classify dividends received, interest received and interest paid in the statement of cash flows by referring to how— applying IFRS 18— it classifies dividend income, interest income and interest expenses in the statement of profit or loss

» Classify the total of each of these cash flows in a single category in the statement of cash flows (that is, either as operating, investing or financing activities)

» Classify dividends paid as cash flows from financing activities

9.2. Amendments of IAS 8

Changes the title

Accounting Policies, Changes in Accounting Estimates and Errors → Basis of Preparation of Financial Statements

IAS 1 paragraphs have been moved to IAS 8

IAS 1

1. Fair Presentation and compliance with IFRSs
2. Going concern
3. Accrual Basis of Accounting

→

IFRS 18

Basis of preparation—general matters

- Fair Presentation and compliance with IFRS Accounting standard
- Going concern
- Accrual Basis of Accounting

9.3. Amendments of IAS 33

In addition to reporting basic and diluted earnings per share, companies were permitted under IAS 33 Earnings per Share to disclose earnings per share calculated based on any component of the statement of comprehensive income. The amendments to IAS 33 permit a company to disclose these additional earnings per share only if the numerator is either a total or subtotal identified in IFRS 18 or an MPM.

Accordingly, we think that the Board should require an entity to disclose the reconciliation between items excluded from the management performance measure and items excluded from adjusted EPS to clarify the relationship between the excluded items in the management performance measure and adjusted EPS as follows.

Category	Items excluded	Gross	Tax and NCI	Net
Items excluded from the management performance measure	Restructuring expenses	-300	30	-270
	Impairment of goodwill	-200	20	-180
	Impairment of plant	-400	40	-360
	subtotal	**-900**	**90**	**-810**
Items excluded from finance income/expenses	Early redemption of debt	-50	5	-45
	subtotal	**-50**	**5**	**-45**
Items excluded from the adjusted EPS		**-950**	**95**	**-855**

'Items excluded' from the management performance measure

'Items excluded' from adjusted EPS
(all adjustments, net of tax and NCI)

Requiring the presentation of adjusted EPS in the financial statements, when an entity presents adjusted EPS outside the financial statements

9.4. Amendments of IAS 34

IAS 34 Interim Financial Reporting was amended to require companies to disclose information about MPMs in interim financial statements. Some of the other changes (including those about subtotals) also apply to condensed financial statements in interim reports

10.0 Effective Date & Application

An entity is required to apply IFRS 18 for annual reporting periods beginning on or after 1 January 2027. Earlier application is permitted. If an entity applies IFRS 18 for an earlier period, it is required to disclose that fact in the notes.

An entity is required to apply IFRS 18 retrospectively applying IAS 8. However, an entity is not required to present the quantitative information specified in IAS 8:28(f) (i.e. the adjustment for each financial statement line item affected and the related effect on basic and diluted EPS, for each period presented).

Instead, in its annual financial statements, an entity is required to disclose, for the comparative period immediately preceding the period in which IFRS 18 is first applied, a reconciliation for each line item in the statement of profit or loss between:

- the restated amounts presented applying IFRS 18
- the amounts previously presented applying IAS 1.

THANK YOU

Disclaimer

This paper is prepared for only study matter. To complete this paper, we have collected data from different publications like IFRS Foundation, Deloitte and others.

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