



IFRS Accounting Standards In Practice

IFRS 18 *Presentation and Disclosure in
Financial Statements*

2025/2026

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1. Introduction

1.1. Overview of changes introduced by IFRS 18

IFRS 18 *Presentation and Disclosures in Financial Statements* was issued by the International Accounting Standards Board (IASB) in April 2024. IFRS 18 supersedes IAS 1 *Presentation of Financial Statements* and has resulted in numerous consequential amendments to IFRS® Accounting Standards including IAS 8 *Basis of Preparation of Financial Statements* (renamed from *Accounting Policies, Changes in Accounting Estimates and Errors*).

IFRS 18 introduces significant changes to numerous requirements, primarily how an entity:

- ▶ Presents its statement of profit or loss, including the classification of income and expenses and new mandatory subtotals;
- ▶ Aggregates and disaggregates information presented and disclosed in financial statements; and
- ▶ Discloses information about management-defined performance measures.

All of BDO's IFRS Accounting Standards In Practice publications may be accessed on BDO's [IFRS and Corporate Reporting microsite](#).

IFRS 18 is mandatorily effective for annual reporting periods beginning on or after 1 January 2027 (i.e. 31 December 2027 annual financial statements for entities with calendar year-ends), with early application permitted, subject to any relevant jurisdictional endorsement or early adoption restrictions.

The issuance of IFRS 9 *Financial Instruments*, IFRS 15 *Revenue from Contracts with Customers*, IFRS 16 *Leases*, and IFRS 17 *Insurance Contracts* fundamentally changed the measurement requirements of IFRS Accounting Standards for many transactions entities commonly enter into, and IFRS 18 is expected to have a similarly significant effect on how entities present their financial statements.

While IFRS 18 does not change any of the recognition and measurement requirements in IFRS Accounting Standards, the effect of the new standard should not be underestimated by entities. The IASB has given preparers approximately 3 years to prepare for the adoption of the standard, which is a similar implementation timeframe similar to that given for the implementation of IFRS 9, 15 and 16.

Before exploring the requirements of IFRS 18, it is useful to understand the history that led to the development and issuance of IFRS 18.

1.2. Background on Primary Financial Statements Project

IFRS 18 was developed as part of the primary financial statements project. This project was undertaken by the IASB because the board received feedback from stakeholders that IFRS Accounting Standards did not have detailed requirements on:

- ▶ classification of income and expenses in the statement of profit or loss;
- ▶ presentation of subtotals above 'profit or loss' (e.g. operating profit) in the statement of profit or loss; or
- ▶ aggregation and disaggregation of information presented in the primary financial statements or disclosed in the notes.

This lack of detailed requirements led to diversity in practice, such as many entities presenting an 'operating profit' subtotal, with entities defining this subtotal differently. This lack of consistency made comparison of entities' financial performance difficult.

From 2015 to 2019, the IASB undertook research activities to determine how they may improve IFRS Accounting Standards to address the above noted concerns. The IASB decided to introduce a basis for classifying items of income and expense in the statement of profit or loss into categories, which would result in mandatory subtotals in the statement of profit or loss and increased comparability between entities.

The IASB also decided to require entities to disclose information about management-defined performance measures,

which are subtotals of income and expenses that an entity uses in public communication that communicate management's view of an aspect of financial performance (e.g. 'adjusted profit'). IFRS 18 contains certain exclusions for specified subtotals, which do not trigger disclosures.

After performing research, the IASB issued an exposure draft *General Presentation and Disclosures* in December 2019.

The IASB deliberated on feedback received in response to the exposure draft and issued IFRS 18 in April 2024.

1.3. What's new in this version

This version of the publication has been updated with BDO's latest views and interpretations of IFRS 18. It includes a new section on management-defined performance measures (see section [6](#)) and provides further insights and illustrative examples.

Although various amendments were made throughout the publication, the following are the most significant new sections added or enhanced in this version of the publication:

Topic	Applicable section
Elaboration of the income taxes category	3.5
Clarification of the interaction between IFRS 5 <i>Non-current Assets Held for Sale and Discontinued Operations</i> and IFRS 18	3.6
Unit of account for assessing whether an entity invests in assets as a main business activity	3.7
Classification considerations per type of asset when an entity invests in assets as main business activity	3.8.1
Unit of account for classifying income and expenses from cash and cash equivalents	3.9.1
Foreign exchange losses relating to liabilities that arise from for transactions other than those that involve only the raising of finance	3.9.3
Updated guidance on common items of income and expense	3.9.5
Additional examples relating to the application of the aggregation and disaggregation criteria	4.3
Additional examples relating to the analysis of the most useful structured summary of operating expenses as well as the presentation and disclosure of it	4.4
Management-defined performance measures	6
Considerations for the successful implementation of IFRS 18	7.5



2. Overview

For a brief summary of IFRS 18 (and all IFRS Accounting Standards), refer to BDO's [IFRS Accounting Standards At a Glance publication](#).

For an introduction to the requirements of IFRS 18 via interactive online courses, refer to BDO's [IFRS Accounting Standards Training](#).

2.1. Key changes introduced by IFRS 18

Note that this section is not an exhaustive summary of all the effects of IFRS 18 and consequential amendments.

The most significant effects of IFRS 18 (and consequential amendments to IFRS Accounting Standards other than IFRS 18) relate to the following topics:

Key changes	Summary
Classification of income and expenses in the statement of profit or loss	All income and expenses are classified into one of five categories: ▶ The investing category ▶ The financing category ▶ The operating category ▶ The income taxes category ▶ The discontinued operations category Income and expenses are generally classified based on the characteristic of the income or expense (i.e. the type of asset or liability to which the income or expense relates); however, certain exceptions exist for entities with specified main business activities, resulting in certain income and expenses being classified in the operating category that would otherwise be classified in the investing and/or financing categories. See section 3 of this publication.
Principles of aggregation and disaggregation	A new set of principles has been introduced for how assets, liabilities, equity, reserves, income, expenses and cash flows are aggregated and disaggregated. Applying these requirements results in aggregation and disaggregation of items being presented in the primary financial statements and disclosed in the notes. See section 4 of this publication.
Totals and subtotals presented in the statement of profit or loss	Once an entity has classified individual items of income and expense into the appropriate categories and it has aggregated those items into appropriate levels of aggregation for presentation in the statement of profit or loss, mandatory and additional subtotals are presented as a result of the previous steps. For example, all entities are required to present 'operating profit' in the statement of profit or loss, which is the total of all income and expenses classified in the operating category. See section 5 of this publication.
Disclosure of management-defined performance measures	IFRS 18 requires entities to disclose information about management-defined performance measures (MPMs), which are a subtotal of income and expense 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 IFRS 18.118, or specifically required to be presented or disclosed by IFRS Accounting Standards. A common example of an MPM could be an 'adjusted profit' measure, which excludes share-based payments expenses and impairment of goodwill. See section 6 of this publication.

Key changes	Summary
Consequential amendments to IAS 7 <i>Statement of Cash Flows</i>	For entities that use the indirect method to prepare their statement of cash flows, the starting point will be typically operating profit or loss. Prior to the adoption of IFRS 18, the starting point in the statement of cash flows was profit or loss. IFRS 18 also eliminates the classification options for interest and dividend cash flows, which will increase consistency. Refer to BDO's IFRS Accounting Standards in Practice publication: IAS 7 Statement of Cash Flows. An edition to be published in 2026 will include a section on the consequential amendments to IAS 7, which were published as a result of IFRS 18.
Other changes	Statement of financial position ▶ IFRS 18 requires goodwill to be presented as a separate line item in the statement of financial position, separate from other intangible assets. IAS 1 did not require this disaggregation (IAS 1.54(c)). IAS 33 <i>Earnings per Share</i> ▶ Prior to the effective date of IFRS 18, IAS 33 permitted entities to disclose additional earnings per share amounts using a reported component of the statement of comprehensive income as the numerator. ▶ IFRS 18 amends IAS 33 and permits additional earnings per share amounts only when the numerator is: • A total or subtotal specified by IFRS 18 in IFRS 18.69, 86 or 118; or • A management-defined performance measure. ▶ Additional disclosure requirements in IAS 33 when an entity presents additional amounts per share other than basic and diluted earnings per share (e.g. adjusted operating profit per share). Disclosure requirements are more significant if the disclosed additional per share amount uses a management-defined performance measure as the numerator in the calculation.

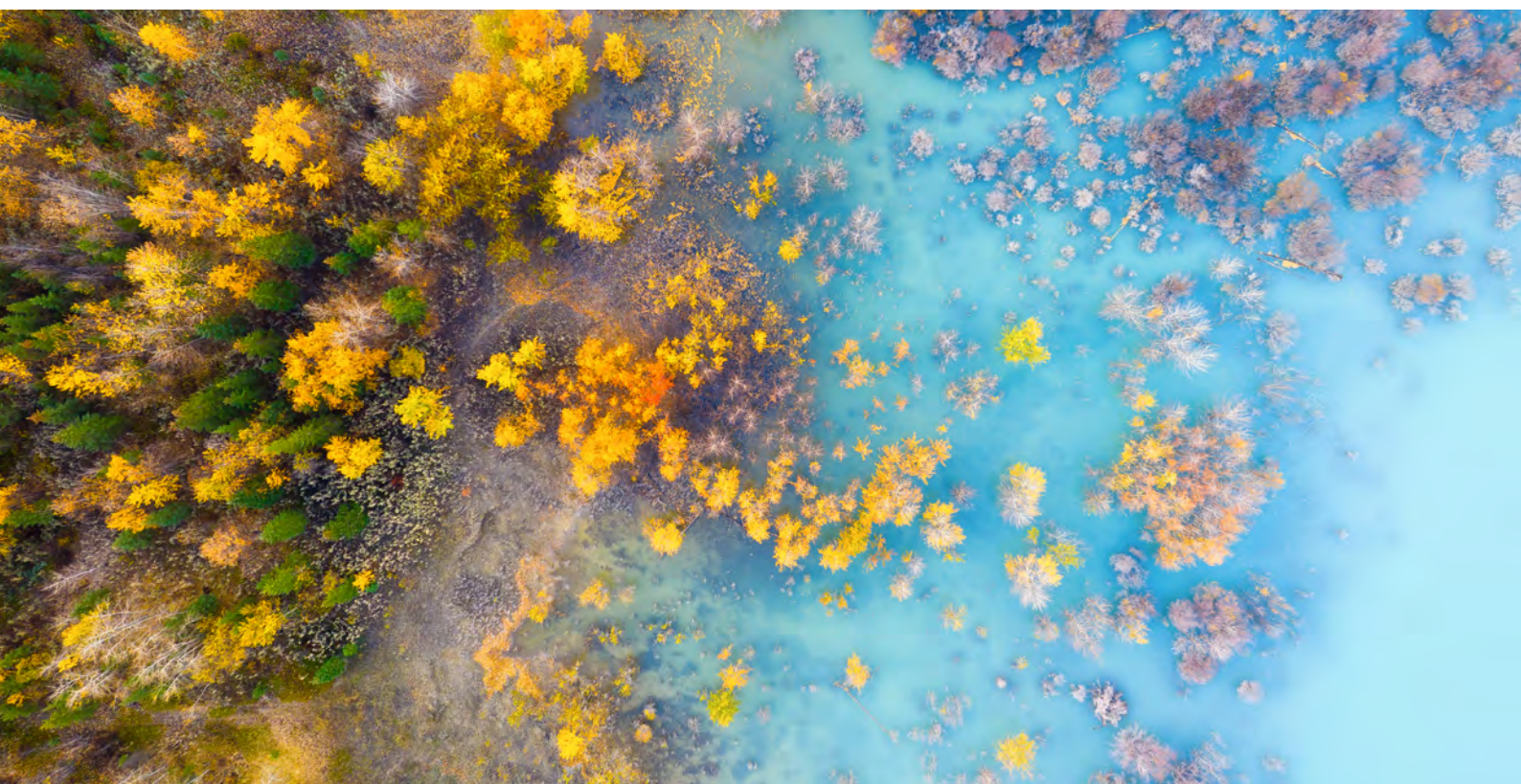
2.2. Topics substantially unchanged from IAS 1

Many requirements in IAS 1 were brought forward into IFRS 18 (or other IFRS Accounting Standards) substantially unchanged. A significant number of requirements from IAS 1 have been relocated to IAS 8 *Basis of Preparation of Financial Statements* (renamed from *Accounting Policies, Changes in Accounting Estimates and Errors*).

Certain other requirements were relocated from IAS 1 to other IFRS Accounting Standards, such as IFRS 7 *Financial Instruments: Disclosures*.

Topic	Summary
Most requirements applicable to the preparation of primary financial statements other than the statement of profit or loss	IFRS 18 does not significantly affect how the other primary financial statements (e.g. statement of financial position, statement of cash flows, statement of changes in equity, etc.) are prepared other than the introduction of new aggregation and disaggregation requirements (see section 4), with some exceptions, such as those noted above applicable to: ▶ The statement of financial position (separate presentation of goodwill); and ▶ The statement of cash flows (operating profit or loss being the starting point for the indirect method and the reduction of classification options for interest and dividend cash flows). See section 2.1 for additional considerations relating to the statement of cash flows.
Fair presentation and compliance with IFRS Accounting Standards	Relocated to IAS 8 substantially unchanged.
Going concern	Relocated to IAS 8 substantially unchanged.
Offsetting	Substantially unchanged from IAS 1.
Frequency of reporting	Substantially unchanged from IAS 1.

Topic	Summary
Comparative information	Substantially unchanged from IAS 1.
Consistency of presentation	Substantially unchanged from IAS 1.
Current/non-current classification of assets and liabilities	Substantially unchanged from IAS 1, including amendments made to IAS 1 affecting the classification of loans as current vs. non-current, which became effective for annual reporting periods beginning on or after 1 January 2024. See BDO's IFRS Accounting Standards In Practice Publication: IAS 1 Classification of Loans as Current or Non-Current .
Structure of notes	Substantially unchanged from IAS 1.
Disclosure of accounting policy information	Relocated to IAS 8 substantially unchanged.
Disclosures about judgements and sources of significant estimation uncertainty	Relocated to IAS 8 substantially unchanged.
Capital disclosures	Substantially unchanged from IAS 1.
Disclosures about puttable financial instruments classified as equity	Relocated to IFRS 7 substantially unchanged.
Miscellaneous other disclosures (declared dividends, cumulative preference dividends not recognised, domicile and legal form, description of the nature of the entity's operations, etc.)	Substantially unchanged from IAS 1.



3. Classification of Income and expenses

3.1. General considerations

3.1.1. Classification of income and expenses - general requirements

IFRS 18 requires entities to classify all items of income and expense recognised in profit or loss into one of five categories (IFRS 18.47):

- ▶ The investing category (section [3.2](#))
- ▶ The financing category (section [3.3](#))
- ▶ The operating category (section [3.4](#))
- ▶ The income taxes category (section [3.5](#))
- ▶ The discontinued operations category (section [3.6](#))

The structure of the statement of profit or loss is then based upon how items of income and expense are classified. For example, for an entity without specified main business activities where certain exceptions to the classification requirements apply (see section [3.8](#)), a typical statement of profit or loss may be as follows (this example includes certain subtotals which are not mandatory, but are commonly used by entities, such as gross profit - see section [5](#)):

Line item		Classification
Revenue	XXX	Operating category
Cost of sales	XXX	
Gross profit	XXX	
Other operating income	XXX	
Selling expenses	XXX	
Research and development	XXX	
General and administrative	XXX	
Operating profit	XXX	Mandatory specified subtotal
Fair value gains on investments in equity instruments	XXX	Investing category
Profit before financing and income taxes	XXX	Mandatory specified subtotal
Interest expense on borrowings and lease liabilities	XXX	Financing category
Profit before income taxes	XXX	Additional subtotal
Income tax expense	XXX	Income taxes category
Profit from continuing operations	XXX	Additional subtotal
Loss from discontinued operations	XXX	Discontinued operations category
Profit	XXX	Mandatory total



BDO comment – labelling of categories

IFRS 18 does not require an entity to label items of income and expense based on the five categories in IFRS 18. For example, in the illustration above, the fair value gains on investments in equity instruments are classified in the investing category, however, the term 'investing category' does not appear in the statement of profit or loss. The classification of items of income and expense into the five categories noted above is used to produce the mandatory specified subtotals in IFRS 18 as these subtotals are based on how income and expenses are classified. See section [5.1](#).

For example:

- ▶ 'Operating profit or loss' is required to be presented by IFRS 18.69(a), and it is defined as comprising all income and expenses classified in the operating category (IFRS 18.70).
- ▶ 'Profit or loss before financing and income taxes' is required to be presented by IFRS 18.69(b), and is defined as the total of (1) operating profit or loss (defined above) and (2) all income and expenses classified in the investing category (IFRS 18.71). Therefore, that subtotal comprises all income and expenses included in the operating and investing categories.

For more information on mandatory and additional subtotals, refer to section [5](#).



BDO comment – category names and inconsistency with the statement of cash flows

The operating, financing and investing categories are similarly titled to operating, financing and investing activities in IAS 7, however, the IASB did not aim to achieve alignment between how income and expenses are classified in the statement of profit or loss and how the associated cash flows are classified in the statement of cash flows. During the development of IFRS 18, some stakeholders suggested that the IASB avoid this matter by using different titles in IFRS 18 (e.g. 'non-operating' rather than the investing category), however, the IASB decided to use the category labels as proposed in the exposure draft (IFRS 18.BC87).

For example, an entity that operates a factory may sell items of property, plant and equipment, with the cash flows arising from the sale being classified as an investing activity in IAS 7 because the cash flows relate to 'the acquisition and disposal of long-term assets and other investments not included in cash equivalents' (IAS 7.6). However, the associated income or expense (the gain or loss on disposal of the item of property, plant and equipment) would typically be classified in the operating category in the statement of profit or loss because it would not meet the criteria to be classified in the investing category (IFRS 18.B48(a)) – see section [3.2](#).

The aggregation and disaggregation requirements (i.e. how items of income and expense are presented within the statement of profit or loss) are addressed in section [4](#). The requirements for presenting mandatory and additional subtotals are addressed in sections [5.1](#) and [5.2](#).

For entities that do not have specified main business activities, items of income and expenses are generally classified into these five categories according to the characteristics of the items of income and expense and the assets and liabilities associated with them. For example, fair value gains and losses on financial assets (e.g. equity instruments) measured at fair value through profit or loss are classified in the investing category because of the nature of the asset; the financial asset generates a return individually and largely independently of the entity's other resources (IFRS 18.B46(a) and 53(c)).



BDO comment – operating category as the 'residual'

It is important to emphasise that the operating category is a 'residual category', meaning that items of income and expense are always classified into the operating category unless they meet criteria to be classified into another category (IFRS 18.52). Therefore, it is necessary for entities to determine whether each item of income and expense may be (or is required to be) classified into one of the other four categories.

Because the operating category is the default or residual category for all items of income and expense, this publication first explains the classification requirements applicable to the other two primary categories: investing (section [3.2](#)) and financing (section [3.3](#)).

3.1.2. Classification of income and expenses – entities with specified main business activities

IFRS 18 contains exceptions to the general classification requirements for entities that have **specified main business activities** (IFRS 18.49). That is to say, for certain entities, the primary activities that are undertaken to run its business will affect how items of income and expense are classified. For entities with specified main business activities, certain items of income and expense that would otherwise be classified in the investing and/or financing categories are classified in the operating category. For example, if an entity has a main business activity of investing in financial assets (i.e. particular types of assets - IFRS 18.49(a)), then the fair value gains and losses on financial assets (e.g. debt or equity instruments) measured at fair value through profit or loss are classified in the operating category.

The specified main business activities requirements of IFRS 18 may be depicted graphically as follows, with certain income and expenses being classified out of the investing and financing categories into the operating category:

Line item		Classification
Revenue	XXX	Operating category
Cost of sales	XXX	
Gross profit	XXX	
Other operating income	XXX	
Selling expenses	XXX	
Research and development	XXX	
General and administrative	XXX	
Operating profit	XXX	Mandatory specified subtotal
Fair value gains on investments in equity instruments	XXX	Investing category
Profit before financing and income taxes	XXX	Mandatory specified subtotal ¹
Interest expense on borrowings and lease liabilities	XXX	Financing category
Profit before income taxes	XXX	Additional subtotal
Income tax expense	XXX	Income taxes category
Profit from continuing operations	XXX	Additional subtotal
Loss from discontinued operations	XXX	Discontinued operations category
Profit	XXX	Mandatory total

For entities with specified main business activities, certain income and expenses classified in the investing and financing categories may be classified in the operating category if criteria are met.

Structure of Section 3

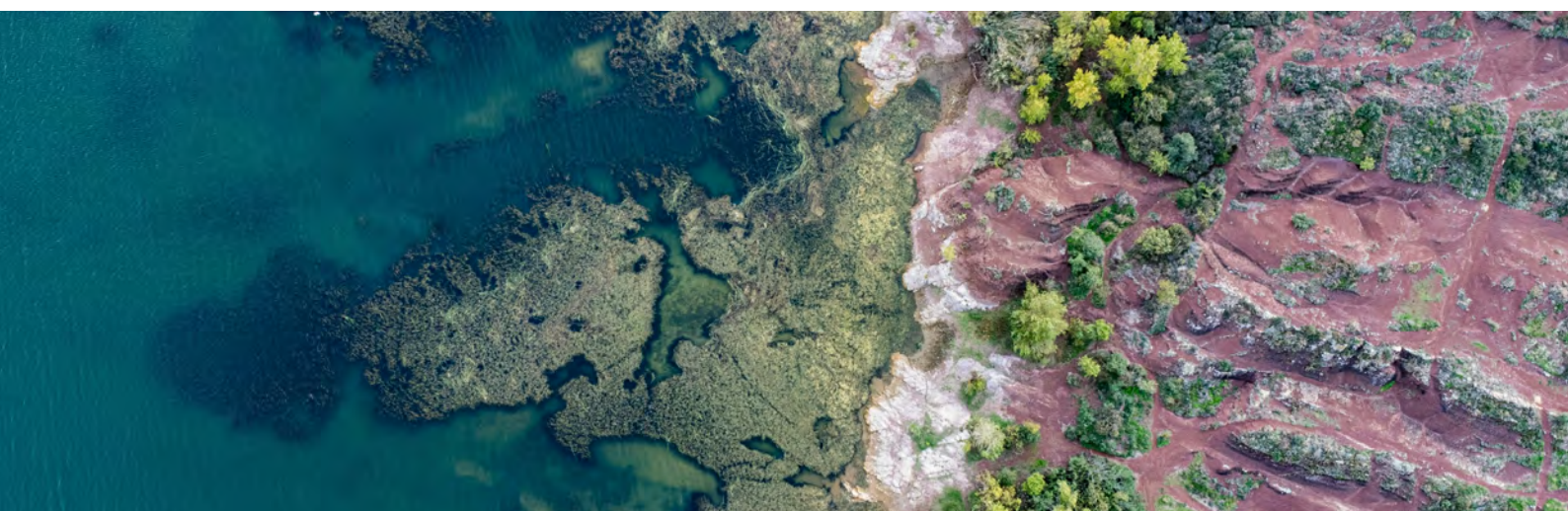
The following sections address how:

- ▶ Items of income and expense are classified into the five categories generally (sections 3.2 through 3.6);
- ▶ An entity assesses whether it has specified main business activities (section 3.7);
- ▶ If an entity does have specified main business activities, it applies additional requirements in classifying income and expenses (section 3.8); and
- ▶ An entity classifies specific items of income and expense where special requirements apply (section 3.9).

¹ There are also special considerations for certain items of income and expense, such as income and expenses related to cash and cash equivalents, hybrid contracts containing a host that is a liability, foreign exchange differences, etc. These special considerations are discussed in section 3.9 and 5.1.

IFRS 18 contains various classification requirements. In many cases, these requirements are illustrated in this publication using practice aids, such as flowcharts. The following practice aids can be found in this publication:

Practice aid	Includes or excludes specified main business activities	Applicable section
Criteria to classify income and expenses in the investing category for entities without specified main business activities	Excludes	3.2.3
Classification of gains and losses on the derecognition of an asset or liability (or group of assets and liabilities), the remeasurement of an asset (or disposal group) as held for sale, or a change in use	Excludes	3.2.11
Criteria to classify income and expenses in the financing category for entities without specified main business activities	Excludes	3.3.5
Classification requirements applicable to assets (and related income and expenses)	Includes	3.8.1
Classification requirements of specified income and expenses related to 'other' assets	Includes	3.8.1.3
Classification requirements applicable to liabilities (and related income and expenses)	Includes	3.8.2
Classification requirements for income and expenses relating to cash and cash equivalents	Includes	3.9.1
Classification requirements for income and expenses relating to derivatives and designated hedging instruments	Includes	3.9.2
Classification requirements for income and expenses relating to hybrid contracts containing a host liability where the embedded derivative is separated	Excludes	3.9.4.1
Classification requirements for income and expenses relating to hybrid contracts containing a host liability where the embedded derivative is not separated	Excludes	3.9.4.2



3.2. Investing category

This section discusses the requirements applicable to entities that do not invest in assets as a main business activity. See section [3.8.1](#) for guidance that applies to entities with such specified main business activities.

3.2.1. General classification requirements – specified assets

Except when an entity has specified main business activities, an entity classifies in the investing category specified income and expenses from (IFRS 18.53) certain assets (i.e. specified assets):

- (a) Investments in associates, joint ventures and unconsolidated subsidiaries;
- (b) Cash and cash equivalents; and
- (c) Other assets if they generate a return individually and largely independently of the entity's other resources.

'Specified income and expenses' restricts the types of income and expenses that are classified in the investing category. Said another way, not all income and expenses that relate to the assets listed in IFRS 18.53 may be classified in the investing category.

Guidance on each of these three classes of assets is provided below.

3.2.2. Specified income and expenses classified in the investing category

IFRS 18.53 requires that only specified income and expenses to be classified in the investing category if they arise from the three categories of assets noted above. These specified expenses are:

Income and expenses (IFRS 18.54)	Common examples (IFRS 18.54 and B47)
(a) The income generated by the assets	▶ Interest ▶ Dividends ▶ Rental income
(b) The income and expenses that arise from the initial and subsequent measurement of the assets, including on derecognition of the assets	▶ Depreciation ▶ Impairment losses and reversal of impairment losses ▶ Fair value gains and losses
(c) The incremental expenses directly attributable to the acquisition and disposal of the assets	▶ Transaction costs on financial assets classified as fair value through profit or loss ▶ Costs to sell assets, such as broker commissions on financial instruments

IFRS 18.53, which lists three classes of assets and IFRS 18.54, which specifies types of income and expenses, must be applied together. Only income and expenses that are listed in 18.54 and that arise from the classes of assets listed in IFRS 18.53 may be classified in the investing category.



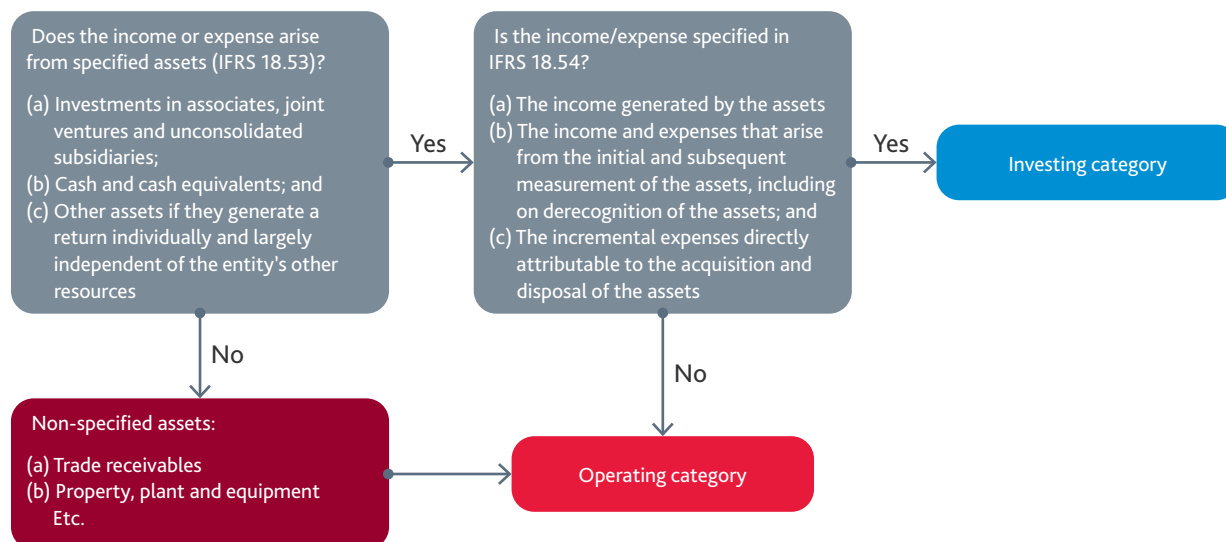
BDO comment – incremental expenses (IFRS 18.54(c))

IFRS 18.54(c) includes only 'incremental' expenses directly attributable to the acquisition and disposal of assets, therefore, not all directly attributable costs will meet the criteria to be classified in the investing category.

The IASB considered, but rejected alternative approaches, such as classifying all directly attributable expenses in the investing category, as this approach was seen as too complex and costly for an entity to apply. Such an approach could require, for example, an allocation of employee benefits if some employees engage in managing both an entity's investments and other activities (IFRS 18.BC109).

3.2.3. Practice aid – criteria to classify income and expenses in the investing category for entities without specified main business activities

This practice aid summarises the requirements to determine whether income or expenses are classified in the investing category, assuming that an entity does not have a main business activity of investing in such assets. As discussed in section 3.8.1, the requirements for classifying income and expense are significantly more complex for entities that have a specified main business activity of investing in assets.



Example 3.2-1 – classification of depreciation in the investing category

IFRS 18.B47 notes that depreciation is an example of 'income and expenses that arise from the initial and subsequent measurement of the assets', however, this does not mean that depreciation in general will be classified in the investing category.

For entities without specified main business activities, only depreciation relating to assets that meet the criterion in IFRS 18.53(c) may be classified in the investing category.

Fact pattern

Entity A owns an item of property, plant and equipment that it uses to manufacture widgets. Entity A also owns a building that it rents out to tenants to earn rental income. Entity A accounts for the building as investment property in the scope of IAS 40 *Investment Property*, and uses the cost model. Entity A does not have specified main business activities.

Analysis

Depreciation on the property, plant and equipment must be classified in the operating category because the depreciation does not arise from (IFRS 18.53):

- (a) Investments in associates, joint ventures and unconsolidated subsidiaries;
- (b) Cash and cash equivalents; and
- (c) Other assets if they generate a return individually and largely independently of the entity's other resources.

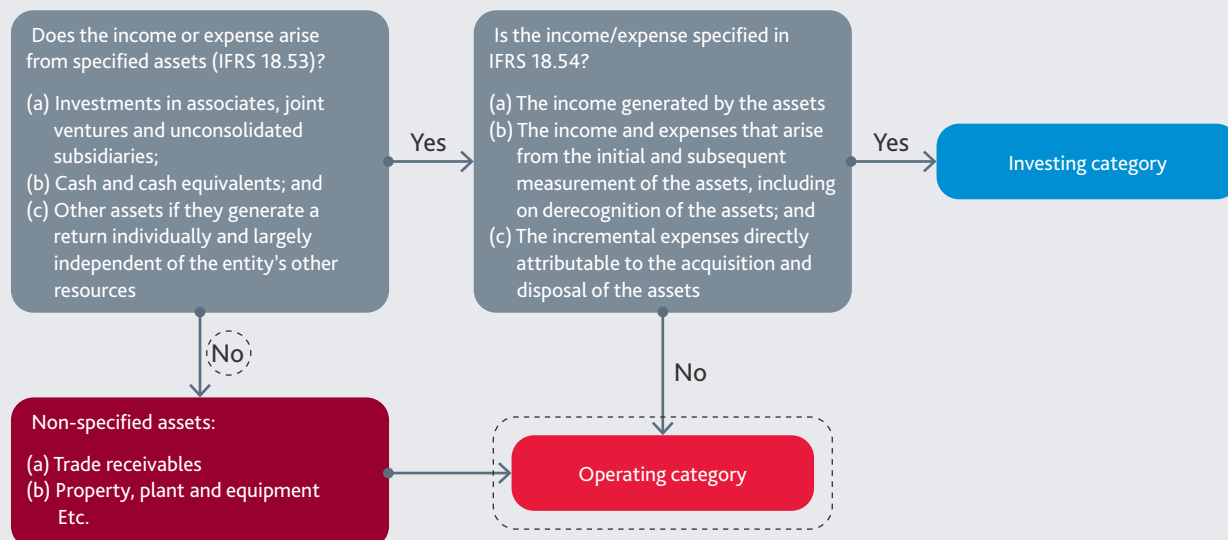
IFRS 18.B48 and B49 also emphasises that income and expenses from assets that an entity uses in combination to produce or supply goods or services do not generate a return individually and largely independently of the entity's other resources, and are therefore classified in the operating category. For example, income and expenses relating to assets that arise from the production or supply of goods and services, such as trade receivables.

Depreciation on the investment property is classified in the investing category because it is 'income and expenses

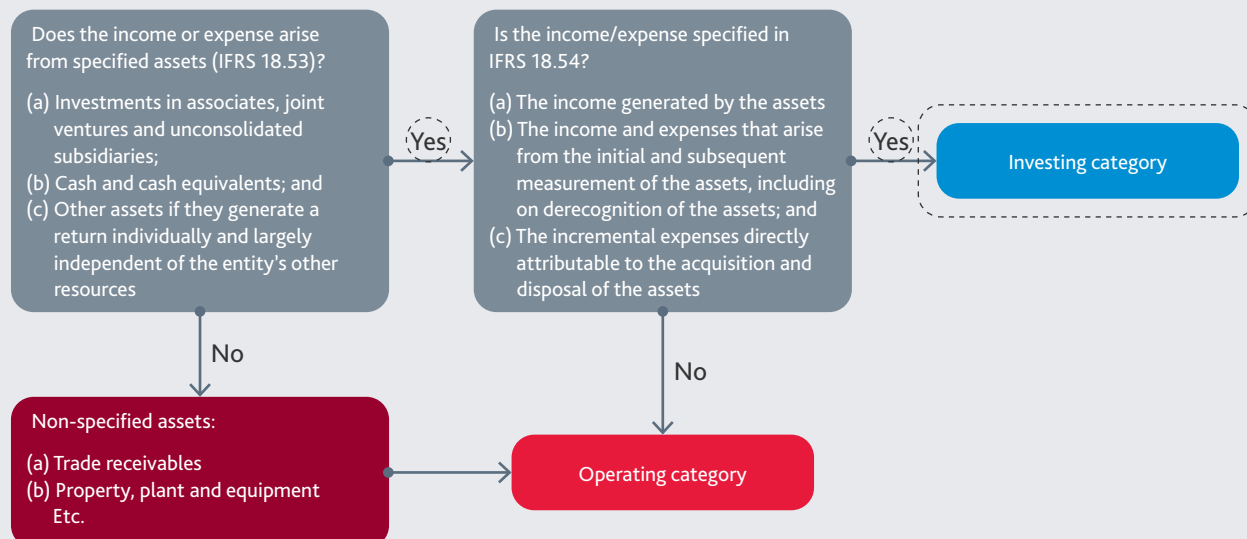
that arise from the initial and subsequent measurement of the asset' (IFRS 18.54) and the investment property is an asset that generates a return individually and largely independently of the entity's other resources (IFRS 18.53(c)). The associated lease income would also be classified in the investing category because that lease income is 'income generated by the asset'.

The above analysis may be demonstrated by applying the classification practice aid as follows:

Property, plant and equipment depreciation



Investment property depreciation





Example 3.2-2 – non-specified expenses related to specified assets

There may be instances where certain income and expenses relate to assets specified in IFRS 18.53, but because the income and/or expenses are not specified in IFRS 18.54, they must be classified in the operating category. This may produce a 'mismatch' between income and expenses related to a single asset.

For example, assume the same fact pattern as [example 3.2.1.](#), *with additional case facts.*

Fact pattern

Entity A owns an item of property, plant and equipment that it uses to manufacture widgets. Entity A also owns a building that it rents out to tenants to earn rental income. Entity A accounts for the building as investment property in the scope of IAS 40 *Investment Property*, and uses the cost model. Entity A does not have specified main business activities.

Entity A incurs cleaning and maintenance fees on the investment property.

Analysis

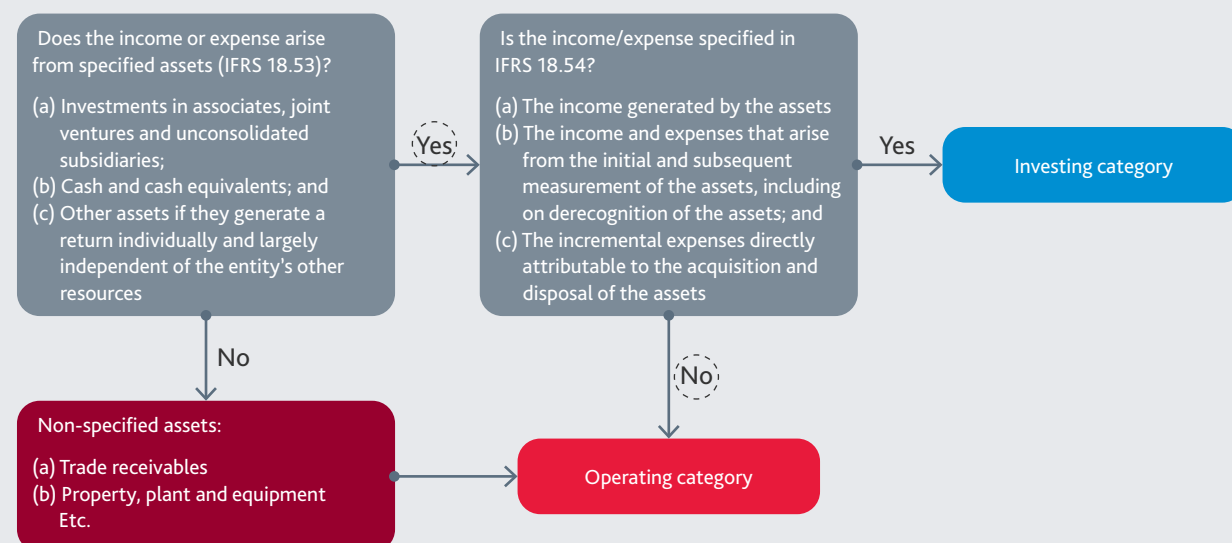
The rental income on the investment property is classified in the investing category for the reasons noted in Example 3.2-1. However, the cleaning and maintenance fees must be classified in the operating category, despite the fact that they are related to the investment property and are necessary in order to generate rental income. That is because they are not specified income and expenses in IFRS 18.54.

The cleaning and maintenance fees are not:

- (a) The income generated by the assets;
- (b) The income and expenses that arise from the initial and subsequent measurement of the assets, including on derecognition of the assets; or
- (c) The incremental expenses directly attributable to the acquisition and disposal of the assets.

As the cleaning and maintenance fees do not meet the criteria in IFRS 18.53-54, they must be classified in the operating category.

The above analysis may be demonstrated by applying the classification practice aid as follows:



3.2.4. Investments in associates, joint ventures and unconsolidated subsidiaries

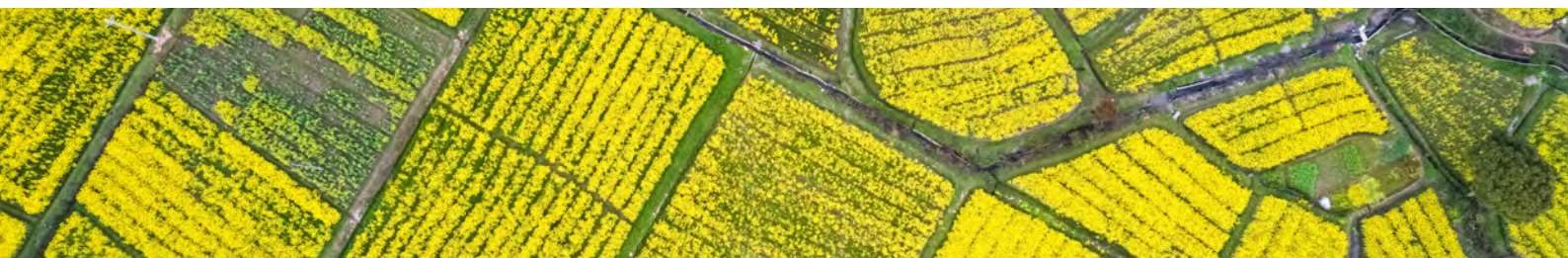
The classification of income and expenses related to investments in associates, joint ventures, and unconsolidated subsidiaries depends on the main business activities of the investor entity, the method of accounting, and whether the entity is preparing separate or consolidated financial statements.

Associates and joint ventures are generally accounted for using the equity method in accordance with IAS 28 *Investments in Associates and Joint Ventures*. If the equity method is applied to such investments, then the investor's share of profit or loss recognised in accordance with IAS 28 will always be classified in the investing category, regardless of whether the entity has specified main business activities (IFRS 18.55(a), IFRS 18.BC131-BC132). The IASB decided to require the classification of income and expenses related to equity accounted investments in the investing category to eliminate different methods of presentation in practice and to provide users of the financial statements with a consistent starting point for their analyses of equity accounted investments (IFRS 18.BC111).

However, there may be cases in which an entity accounts for investments in associates, joint ventures and unconsolidated subsidiaries using a basis of measurement other than the equity method. For example, an investment entity accounts for such investments at fair value through profit or loss (see IFRS 10 *Consolidated Financial Statements*).

These bases (other than the equity method) under which an investor accounts for its associates, joint ventures and unconsolidated subsidiaries are not relevant unless the entity has a main business activity of investing in such assets. If the entity does not have such a main business activity, the resulting income and expense from such investments will always be classified in the investing category (unless classified in the discontinued operations category, see section 3.6).

See section 3.8.1 for considerations for entities with specified main business activities. In certain cases, such entities may classify income and expenses related to investments in associates, joint ventures and unconsolidated subsidiaries not accounted for using the equity method in the operating category.



3.2.5. Cash and cash equivalents

Income and expense related to cash and cash equivalents (e.g. interest income) will always be classified in the investing category unless an entity has specified main business activities (IFRS 18.56).

The classification of cash and cash equivalents for entities that invest in financial assets or provide financing to customers as a main business activity is complex. Refer to section 3.9.1 for further information on these requirements and a flowchart that may be used in classifying income and expenses related to cash and cash equivalents for entities with specified main business activities.

3.2.6. Other assets that generate a return individually and largely independently of the entity's other resources

The third category of assets where specified income and expenses are classified in the investing category, is assets that generate a return individually and largely independently of the entity's other resources (IFRS 18.53(c)). This is the broadest of the three types of specified assets listed in IFRS 18.53 and could comprise a range of asset classes including (IFRS 18.B46):

- ▶ Debt or equity investments; and
- ▶ Investment properties, and receivables for rent generated by those properties.

It should be noted that the 'return' generated may be positive or negative; a negative return being generated does not preclude an asset from generating an individual and largely independent return (IFRS 18.B45).

Income and expenses that arise from such assets typically include (IFRS 18.B47):

- (a) Interest;
- (b) Dividends;
- (c) Rental income;
- (d) Depreciation;
- (e) Impairment losses and reversals of impairment losses;
- (f) Fair value gains and losses; and
- (g) Income and expenses from the derecognition of the asset, or its classification and remeasurement as held for sale.

3.2.7. Assets that do not generate a return individually and largely independently of the entity's other resources

IFRS 18.B48 notes that assets an entity uses in combination to produce or supply goods or services do not generate a return individually and largely independently of the entity's other resources. Such assets typically include:

- (a) Property, plant and equipment;
- (b) Assets that arise from the production or supply of goods and services for which the income and expenses are classified in the operating category (for example, receivables for such goods and services); and
- (c) If the entity provides financing to customers as a main business activity, any loans to a customer.



BDO comment – interaction between IFRS 18.B48 and classification of assets

How an asset is classified in the statement of financial position will affect how an entity assesses whether that asset generates a return individually and largely independently of the entity's other resources. For example, depending on how an entity intends to use a building, it may be classified as:

- ▶ Inventory: if the entity regularly sells buildings to customers (e.g. a homebuilder);
- ▶ Property, plant and equipment: if the entity uses the building in its operations (e.g. head office or a distribution centre); or
- ▶ Investment property: if the entity holds the building for rental income or for capital appreciation or both (e.g. commercial real estate).

Inventory and property, plant and equipment will typically not generate a return individually and largely independently of the entity's other resources because the production and sale of those assets require the entity to combine a variety of different resources in order to earn a return.

Investment property generates a return individually and largely independently of the entity's other resources because rental income and capital appreciation are earned independently of the entity's business activities. Therefore, income and expenses specified in IFRS 18.54 are classified in the investing category unless an entity invests in investment property as a main business activity (see section [3.8.1](#)).



Example 3.2-3 – classification of income and expenses relating to loans receivable

Assessing income and expenses related to assets that generate a return individually and largely independently of the entity's other resources will depend on the characteristics of the asset and the entity's operations.

Fact pattern

Entity H is a manufacturer and produces widgets. Entity H has loaned CU500 to a related party (Entity I) to provide that entity with financing. Entity H does not regularly make loans and issuing loans is not one of its main business activities. Entity H has recorded interest income on the loan.

Entity J is a financial institution and issues loans to borrowers as its main business activity. Entity J has loaned CU700 to a borrower to construct a new facility. Entity J has recorded interest income on the loan.

Assessment

Entities H and J both have to assess whether the loans receivable generates a return individually and largely

independently of the entity's other resources. This is necessary because the entities have to determine how to classify the interest income in the statement of profit or loss.

Entity H determines that the loan receivable does generate a return individually and largely independently of the entity's other resources because the loan receivable is a debt instrument as noted in IFRS 18.B46. The interest income earned on the loan is income generated by the asset (IFRS 18.54(a)), therefore, Entity H classifies the interest income on the loan receivable in the investing category because Entity H's main business activities do not include issuing loans.

Entity J determines that the loan receivable does not generate a return individually and largely independently of the entity's other resources because Entity J provides financing to customers as a main business activity (IFRS 18.B48(c)). As Entity J invests in loans as a main business activity, income and expenses related to those assets are classified in the operating category.

This example demonstrates that two entities that own identical underlying assets may classify income and expenses relating to that asset differently depending on whether they invest in those assets as a main business activity.

See section [3.8.1](#) for further explanations of investing in assets as a main business activity.

3.2.8. Derecognition of an asset or liability and remeasurement of an asset held for sale

IFRS 18.B60 requires that an entity classify income and expenses on the derecognition of an asset, or its classification as held for sale (e.g. a write-down required by IFRS 5 *Non-Current Assets Held for Sale and Discontinued operations*) and any subsequent measurement while held for sale, in the same category as it classified the income and expenses from the asset immediately before its derecognition.

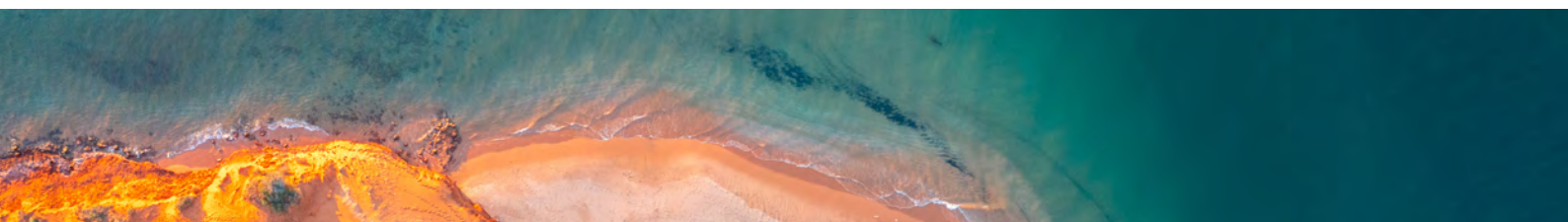
IFRS 18.B47(g) requires that income and expenses from the derecognition of a specified asset, or its classification and remeasurement as held for sale be classified in the investing category.

This principle essentially 'backwards traces' the income and expenses arising from derecognition or classification as held for sale to the classification of income and expenses associated with that asset.

For example (IFRS 18.B60):

Gains and losses arising from the:	Classification (assuming no specified main business activities)
Disposal of property, plant and equipment	Operating category
Disposal of investment property	Investing category
Remeasurement of an associate previously accounted for using the equity method on the step acquisition of a subsidiary	Investing category

This same principle applies to the remeasurement of an asset when it is classified as held for sale in accordance with IFRS 5. IFRS 5.15 requires that an entity measure a non-current asset (or disposal group) classified as held for sale at the lower of its carrying amount and fair value less costs to sell. This may result in gains or losses being recognised throughout the period when an asset (or disposal group) is classified as held for sale.



These gains and losses are classified in a similar manner to the table above. For example:

Gains and losses arising from the remeasurement of an asset classified as held for sale (IFRS 5.15)	Classification (assuming no specified main business activities)
Property, plant and equipment; intangible assets	Operating category
Investment property	Investing category

Gains and losses arising from the measurement and remeasurement of an asset in accordance with IFRS 5 are not necessarily classified in the discontinued operations category, despite the fact that they arise from the application of the requirements of IFRS 5, however, this conclusion may differ for groups of assets where the criteria to present the gain or loss as a discontinued operation are met – see the following section on groups of assets. Only income and expenses from discontinued operations in accordance with IFRS 5 are classified in the discontinued operation (see section [3.6](#)).

Similar requirements exist for the derecognition of liabilities. See section [3.3](#).

These requirements apply to individual assets; however, a simplified classification approach exists for groups of assets and liabilities.

3.2.9. Derecognition of groups of assets and liabilities and remeasurement of an asset held for sale

An entity may dispose of groups of assets and liabilities in a single transaction, such as the sale of a group of related assets, or the sale of a subsidiary that holds assets and liabilities.

In certain cases, such a disposal may be classified as a discontinued operation in accordance with IFRS 5, and therefore, the resulting income and expenses (including a gain or loss on disposal) would be classified in the discontinued operations category (see section [3.6](#)).

However, an entity may dispose of a group of assets and liabilities that do not meet the criteria to be presented as a discontinued operation in accordance with IFRS 5, and therefore, income and expenses shall not be classified in the discontinued operations category. This raises the question of how an entity classifies the gains and losses arising from such a sale. For example, whether an entity is required to disaggregate the total gain or loss and allocate it to the various assets and liabilities, classifying a portion of the total gain or loss in the operating category (e.g. the portion related to property, plant and equipment) and another portion in the investing category (e.g. the portion related to investment property).

IFRS 18.B63 simplifies this matter by requiring that such a gain or loss always be classified in the operating category unless **all the assets** in the group (other than income tax assets) generated income and expenses that the entity classified in the investing category immediately before the transaction or other event.

This is a simplification of the overall principles in IFRS 18, however, the IASB decided that requiring an entity to allocate the gain or loss on derecognition of a group of assets (or a group of assets and liabilities) to the categories related to those assets (or assets and liabilities) could result in arbitrary allocations and be costly for preparers to apply (IFRS 18.BC204).

3.2.10. Change in use of an asset

A change in use of an asset may change the assessment of whether the asset is an asset specified in IFRS 18.53, and therefore, that specified income and expenses shall be classified in the investing category. For example, an entity may use an item of property, plant and equipment as its head office, but then change the use of the asset by moving to another facility and renting out the previous head office as an investment property. The asset would not have met the criteria in IFRS 18.53 (i.e. it is not a specified asset) prior to the change in use, but it would upon reclassification as an investment property because the building would then generate a return individually and largely independently of the entity's other resources (IFRS 18.53(c)).

Income and expenses up until the point of reclassification of the asset would be presented in accordance with the requirements of IFRS 18 as applied to that asset, with only income and expense from the date of reclassification being treated differently. For example, income and expenses related to the property plant and equipment would be classified in the operating category until the date of reclassification to investment property (e.g. depreciation on the building until the date of reclassification).

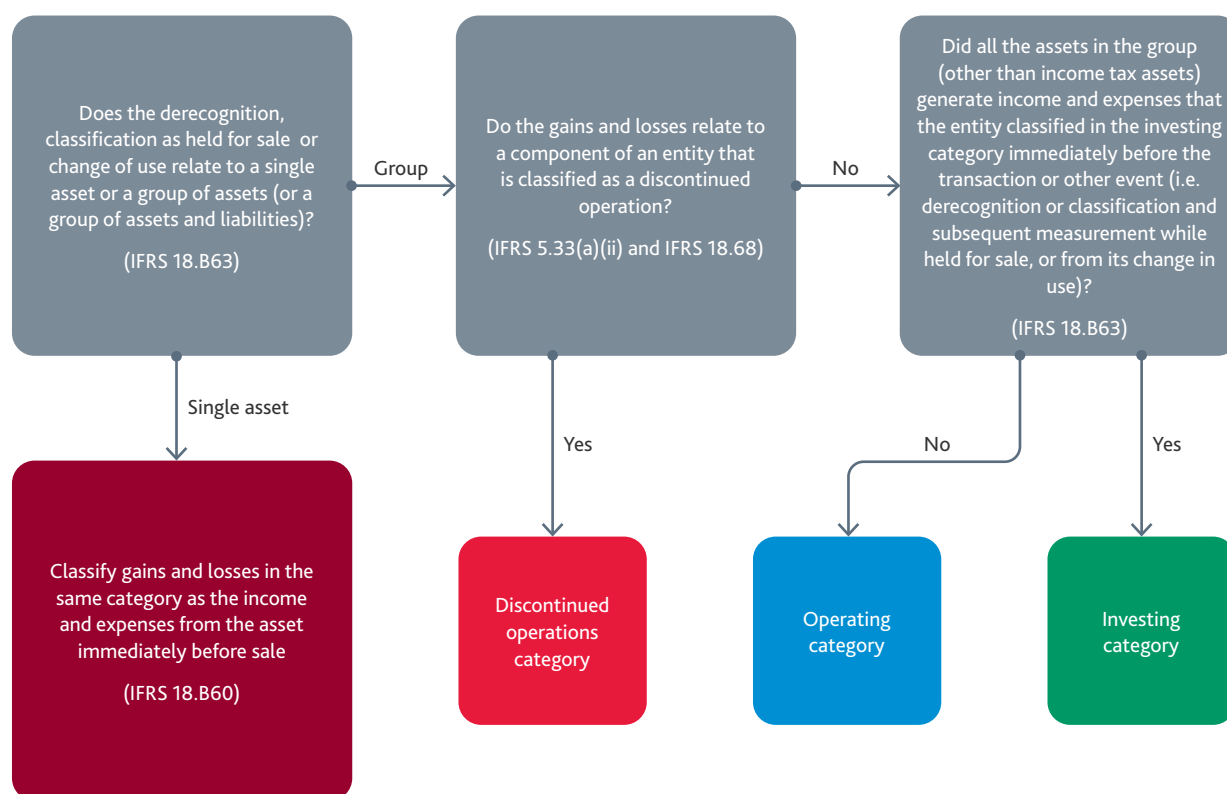
Only from that date of reclassification onwards would the income and expenses be classified in the investing category (assuming the entity does not invest in such assets as a main business activity).

IFRS 18.B62 requires an entity to classify the income and expenses from the transaction or other event that results in the reclassification in the category in which it classified income and expenses from the asset immediately before the transaction or event. For example, the transfer of an item of property, plant and equipment from the scope of IAS 16 *Property, plant and equipment* to IAS 40 may result in amounts being recognised in profit or loss (IAS 40.62(a) and 62(b)(i)). These amounts must be classified in the operating category because that is the category in which the entity classified income and expenses from the building immediately before the reclassification to investment property.

If a change in use applies to a group of assets as a result of a transaction or other event, then the requirements of IFRS 18.B63 discussed in the previous section apply. IFRS 18.B63 requires that such income or expenses always be classified in the operating category unless all the assets in the group (other than income tax assets) generated income and expenses that the entity classified in the investing category immediately before the transaction or other event.

3.2.11. Practice aid – classification of gains and losses on the derecognition of an asset or liability (or group of assets and liabilities), the remeasurement of an asset (or disposal group) as held for sale, or a change in use

This practice aid summarises which guidance an entity should apply in classifying income and expenses from the derecognition and/or remeasurement of assets (or groups of assets) while classified as held for sale or from a change in use.



3.2.12. Presentation of income and expenses classified in the investing category

IFRS 18 does not require a subtotal to be presented for all items classified in the investing category (e.g. 'investing profit or loss'). IFRS 18 requires 'profit or loss before financing and income taxes' to be presented (IFRS 18.69(b)), therefore, this subtotal will comprise the sum of income and expenses classified in the operating and investing categories. This relationship is depicted below:

Line item		Classification	Explanation
Revenue	XXX	Operating category	
Cost of sales	XXX		
Gross profit	XXX		
Other operating income	XXX		
Selling expenses	XXX		
Research and development	XXX		
General and administrative	XXX		
Operating profit	XXX	Mandatory specified subtotal	Sum of the operating category
Fair value gains on investments in equity instruments	XXX	Investing category	
Profit before financing and income taxes	XXX	Mandatory specified subtotal ¹	Sum of the operating and investing categories
Interest expense on borrowings and lease liabilities	XXX	Financing category	
Profit before income taxes	XXX	Additional subtotal	
Income tax expense	XXX	Income taxes category	
Profit from continuing operations	XXX	Additional subtotal	
Loss from discontinued operations	XXX	Discontinued operations category	
Profit	XXX	Mandatory total	Sum of all categories

See section 5 for further information on subtotals and totals presented in the statement of profit or loss.



¹ Profit before financing and income taxes is a mandatory subtotal for most entities, though an exception exists for entities that provide financing to customers as a main business activity and make a particular accounting policy choice – see section 5.1 'profit or loss before financing and income taxes – entities that provide financing to customers as a main business activity'.

3.3. Financing category

The classification requirements for the financing category focus on liabilities, whereas the investing category focuses on assets.

Classification of income and expenses in the financing category affects the determination of the mandatory subtotal 'profit or loss before financing and income taxes' (see section [5.1](#)). The financing category (and the related mandatory subtotal) is required by IFRS 18 because in the view of the IASB, many users of financial statements seek to analyse an entity's performance independently of how the entity is financed (IFRS 18.BC148). By isolating income and expenses related to financing in a separate category, and presenting a subtotal before those items, the operations of entities may be compared independently of how they are financed (e.g. debt vs. equity, the cost of debt financing, etc.).

3.3.1. General classification requirements

This section discusses the requirements applicable to entities that do not provide financing to customers as a main business activity. See section [3.8.2](#) for guidance that applies to entities with such specified main business activities (e.g. providing financing to customers as a main business activity).

To classify income and expenses arising from liabilities, an entity is required to distinguish liabilities between (IFRS 18.59):

- (a) liabilities that arise from transactions that involve only the raising of finance; and
- (b) liabilities other than those described in (a) — that is, liabilities that arise from transactions that do not involve only the raising of finance.

Separate requirements apply to income and expenses that relate to these two different types of liabilities.

3.3.2. Liabilities that arise from transactions that involve only the raising of finance

Liabilities that arise from transactions that involve only the raising of finance are where an entity (IFRS 18.B50):

- (a) receives finance in the form of cash, or an extinguishment of a financial liability, or receipt of the entity's own equity instruments; and
- (b) at a later date, will return in exchange cash or its own equity instruments.

For such liabilities, IFRS 18.60 requires entities to classify in the financing category the amounts included in the statement of profit or loss for:

- (a) income and expenses that arise from the initial and subsequent measurement of the liabilities, including on derecognition of the liabilities; and
- (b) the incremental expenses directly attributable to the issue and extinguishment of the liabilities — for example, transaction costs.

Certain exceptions to the income and expenses listed in IFRS 18.60 exist, such as income and expenses related to hybrid contracts that contain a host that is a liability and gains and losses on derivatives and designated hedging instructions – see 'exceptions to classification principles' below as well as sections [3.9.2](#), [3.9.3](#) and [3.9.4](#).



Examples of such liabilities include, along with associated specified income and expenses in IFRS 18.60:

Liabilities that arise from transactions that involve only the raising of finance (IFRS 18.B51)	Specified income and expenses classified in the financing category (IFRS 18.B52)
A debt instrument that will be settled in cash, such as debentures, loans, notes, bonds and mortgages—an entity receives cash and will return cash in exchange	▶ Interest expenses (for example, on debt instrument issued); ▶ Fair value gains and losses (for example, on a liability designated at fair value through profit or loss); ▶ Dividends on shares issued classified as liabilities; and ▶ Income and expenses from the modification and/or derecognition of the liability¹.
A liability under a supplier finance arrangement when the payable for goods or services is derecognised—an entity is discharged of the financial liability for the goods or services and will return cash in exchange;	
A bond that will be settled through delivery of an entity's shares—an entity receives cash and will return its own equity instruments in exchange;	
An obligation for an entity to purchase its own equity instruments—an entity receives its own equity instruments and will return cash in exchange.	

As IFRS 18 requires only a binary assessment – whether a liability arises from a transaction that involves only the raising of finance or not, examples of liabilities that do not meet this criterion are included in the following section.

3.3.3. *Liabilities that arise from transactions that do not involve only the raising of finance*

For liabilities that arise from transactions that do not involve only the raising of finance, the income and expenses that are to be classified in the financing category are more limited than 'pure financing' transactions.

For liabilities that arise from transactions that do not involve only the raising of finance (for example, the items listed below), an entity classifies in the financing category (IFRS 18.61):

- interest income and expenses, but only if the entity identifies such income and expenses for the purpose of applying other requirements in IFRS Accounting Standards; and
- income and expenses arising from changes in interest rates, but only if the entity identifies such income and expenses for the purpose of applying other requirements in IFRS Accounting Standards.

Any other income and expenses not included in IFRS 18.61 must be classified in the operating category. As mentioned above see 'exceptions to the classification principles' below as well as sections 3.9.2, 3.9.3 and 3.9.4 for special requirements applicable to gains and losses on derivatives, foreign exchange differences and hybrid contracts. Therefore, the practical distinction between liabilities that arise from transactions that do and do not involve only the raising of finance is that for the latter, a more restrictive number of income and expenses will be classified in the financing category.



¹ If as part of a supplier finance arrangement an entity derecognises a payable to a supplier and recognises a liability under that arrangement, then any income and expenses arising from that derecognition are classified in the operating category (IFRS 18.B61(b)).

The table below illustrates types of liabilities that arise from transactions that do not involve only the raising of finance, the rationale for why they are not considered 'pure financing' liabilities (IFRS 18.B53) and examples of income and expenses that will be classified in the financing category, assuming that the entity does not have specified main business activities (IFRS 18.61):

Liabilities that arise from transactions that do not involve only the raising of finance (IFRS 18.B53)	Rationale for classification (i.e. why the liability does not arise from transactions that involve only the raising of finance) (IFRS 18.B53)	Examples of income and expenses that will be classified in the financing category (IFRS 18.B54)
Payables for goods or services that will be settled in cash (IFRS 9)	The entity receives goods or services, not finance in the form specified by IFRS 18.B50(a).	Interest expenses on payables arising from the purchase of goods or services, applying IFRS 9.
Contract liabilities (IFRS 15)	The entity receives cash, but will settle the liability by delivering goods or services rather than cash or its own equity instruments as required by IFRS 18.B50(b).	Interest expenses on a contract liability with a significant financing component as specified by IFRS 15.
Lease liabilities (IFRS 16)	The entity receives a right-of-use asset, not finance in the form specified by IFRS 18.B50(a).	Interest expenses on a lease liability, applying IFRS 16.
Defined benefit pension liabilities (IAS 19 <i>Employee benefits</i>)	The entity receives employee services, not finance in the form specified by IFRS 18.B50(a).	Net interest expense (income) on a net defined benefit liability (asset), applying IAS 19.
Decommissioning or asset restoration provisions (IAS 37 <i>Provisions, Contingent Liabilities and Contingent Assets</i>)	The entity receives an asset (the increase in the carrying amount of assets), not finance in the form specified by IFRS 18.B50(a).	The increase in the discounted amount of a provision arising from the passage of time and the effect of any change in the discount rate on provisions, applying IAS 37.
A litigation provision (IAS 37)	The entity does not receive finance in the form specified by IFRS 18.B50(a).	



BDO comment – interaction between IFRS 18 financing category requirements and IAS 23 *Borrowing Costs*

IFRS 18's requirements applicable to interest income and expenses indirectly interact with the requirements of IAS 23, which requires entities to capitalise borrowing costs into the carrying amount of assets if certain criteria are met. If inventories or items of property, plant and equipment take a substantial period of time to get ready for their intended use or sale (i.e. they are 'qualifying assets' in IAS 23), then borrowing costs must be capitalised. For example, the long-term construction of a building may commonly include borrowing costs being capitalised into the carrying amount of the building as it is constructed.

Borrowing costs capitalised as a component of the carrying amount of a qualifying asset may result from liabilities that do and do not arise from transactions that involve only the raising of finance. That is because IAS 23 defines borrowing costs to include components from both categories (e.g. interest expense calculated using the effective interest rate method as described in IFRS 9, which would be applicable to financial liabilities such as bank loans, as well as interest in respect of lease liabilities recognised in accordance with IFRS 16).

Once borrowing costs are capitalised in the carrying amount of a qualifying asset, the classification requirements of IFRS 18 applicable to interest income and expenses no longer apply. That is because they are no longer interest income and expenses recognised in profit or loss, they are 're-characterised' based on the nature of the asset.

For example, Entity H constructs a building which it intends to occupy as its head office, therefore, the building is in the scope of IAS 16. Over the period of construction, Entity H recognised borrowing costs as part of the carrying amount of the building as required by IAS 23. Once construction is complete, the carrying amount comprises the following amounts:

Components of carrying amount	Amount
Materials and labour	CU10,000
Capitalised borrowing costs relating to bank loan – specific borrowings (IAS 23.12)	CU800
Capitalised borrowing costs relating to lease liabilities – general borrowings (IAS 23.14)	CU400
Total	CU11,200

As Entity H depreciates the building over its useful life, Entity H does not apply the requirements in IFRS 18.59-61 to classify the component of the depreciation expense that relates to capitalised borrowing costs (CU800 + CU400 = CU1,200) in the financing category. The entire amount of depreciation expense is reflected in the operating category (IFRS 18.B49(c)) because once those amounts are capitalised into the borrowing cost of an asset, the eventual recognition of those amounts in profit or loss are no longer characterised as being interest income and expense recognised in profit or loss; they are depreciation of an item of property, plant and equipment.

Therefore, Entity H would reflect a portion of interest income and expenses in profit or loss (those expenses not capitalised in accordance with IAS 23), with those expenses being subject to the classification requirements of IFRS 18 applicable to the financing category. The portion of interest income and expenses capitalised in accordance with IAS 23 would be subject to the classification requirements applicable to the income or expense recognised when the qualifying asset is eventually recognised in profit or loss (e.g. via depreciation, impairment, etc.).



BDO comment – income and expenses relating to liabilities that arise from transactions that do not involve only the raising of finance that will not be classified in the financing category (examples where IFRS 18.61 criteria are not met)

IFRS 18.B53 is only a list of examples, and does not consider every liability that may be recognised as a result of applying IFRS Accounting Standards. Income and expenses relating to liabilities that arise from transactions that do not involve only the raising of finance must be analysed to determine if they meet the criteria in IFRS 18.61 to be classified in the financing category.

Following are several examples of liabilities that arise from transactions that do not involve only the raising of finance and related income and expenses that do not meet the criteria in IFRS 18.61 to be classified in the financing category. The following examples are non-exhaustive.

Cash-settled share-based payment liabilities (IFRS 2 Share-based payment)

An entity may recognise a liability for a cash-settled share-based payment transaction that it incurs to receive a service (e.g. cleaning services). The services received would be classified in the operating category, however, the cash-settled share-based payment liability must be remeasured at each reporting period to fair value with changes in fair value recognised in profit or loss (IFRS 2.30). The movement in fair value from one period to the next would consider two elements:

1. The passage of time (i.e. the unwinding of the discount recognised); and
2. Any changes in estimate relating to the liability (e.g. an increase in the estimated liability due to changes in the share price of the entity).

For liabilities that arise from transactions that do not involve only the raising of finance, IFRS 18.61 permits only two types of income and expenses to be classified in the financing category (**emphasis added**):

- (a) interest income and expenses, **but only if the entity identifies such income and expenses** for the purpose of applying other requirements in IFRS Accounting Standards; and
- (b) income and expenses arising from changes in interest rates, **but only if the entity identifies such income and expenses** for the purpose of applying other requirements in IFRS Accounting Standards.

IFRS 2.30 requires the cash-settled share-based payment liability to be remeasured from one period to the next, however, IFRS 2 does not require the entity to identify interest income and expenses in performing this remeasurement. Said another way, IFRS 2 requires fair value measurement for such liabilities at each reporting date, with the total movement in that liability being recognised in profit or loss, with no disaggregation between the unwinding of the discount and other changes in fair value.

Therefore, in our view, the remeasurement of a cash-settled share-based payment liability must be classified in the operating category.

Modification gains and losses on contract liabilities (IFRS 15)

IFRS 15.21(b) requires an entity to account for a contract modification as if it were a part of the existing contract if the remaining goods or services are not distinct and, therefore, form part of a single performance obligation that is partially satisfied at the date of the contract modification. The effect that the modification has on the transaction price and the entity's measure of progress towards complete satisfaction of the performance obligation is recognised as an adjustment to revenue.

The effect recognised in profit or loss must be classified in the operating category because such a gain or loss is not interest income and expenses (IFRS 18.61(a)) or income and expenses arising from changes in interest rates (IFRS 18.61(b)). Additionally, because IFRS 15.21(b) requires the effect to be reflected as an adjustment to revenue, the effect must be reflected in the operating category because revenue is also classified in the operating category (IFRS 18.B49(a)).

Modification gains and losses on lease liabilities (IFRS 16)

IFRS 16.46 requires a lessee to account for a lease modification that is not accounted for as a separate lease by decreasing the carrying amount of the right-of-use asset, with an amount recognised in profit or loss relating to the partial or full termination of the lease (see section 5.7 of [IFRS Accounting Standards In Practice IFRS 16 Leases for a worked example](#)).

This gain or loss recognised in profit or loss must be classified in the operating category because such a gain or loss is not interest income and expenses (IFRS 18.61(a)) or income and expenses arising from changes in interest rates (IFRS 18.61(b)).

Change in estimate relating to a legal provision (IAS 37)

IAS 37.45-47 requires that a provision reflect the time value of money when the effect is material (i.e. provisions must be discounted). IAS 37.59 requires that a provision be reviewed at the end of each reporting period and adjusted to reflect the current best estimate. Therefore, from one reporting period to the next, the change in the carrying amount of a provision that is discounted will reflect:

- ▶ The unwinding of the discount due to the passage of time; and
- ▶ Any updates to the current best estimate.

While IAS 37 does not specify the presentation of these two items in the statement of profit or loss (IAS 37.60 refers to the unwinding of the discount as a borrowing cost), and diversity in practice exists, these two items will generally be reflected in different categories in the statement of profit or loss.

IFRS 18.B54(e) specifies that the increase in the discounted amount of a provision arising from the passage of time and the effect of any change in the discount rate is an example of interest income and expenses that meet the criteria in IFRS 18.61 to be classified in the financing category.

The income or expense relating to unwinding of discount (or change in discount rate) is classified in the financing category because the legal provision is a liability that arise from transactions that do not involve only the raising of finance and it is interest income and expenses (IFRS 18.61(a)).

The income or expense relating to the change in the best estimate of settlement is classified in the operating category because the legal provision is a liability that arise from transactions that do not involve only the raising of finance and it is not interest income and expenses (IFRS 18.61(a)) or income and expenses arising from changes in interest rates (IFRS 18.61(b)).

Therefore, updating the measurement of a liability may result in an entity needing to 'split' the total effect recorded in profit or loss between more than one category.



Example 3.3-1 – changes in provisions due to the unwinding of discount and adjustments of the best estimate of settlement

Fact pattern

Entity H is currently involved in an ongoing legal dispute. Due to limited court availability, the litigation is expected to take four years to be resolved.

Entity H does not anticipate a favourable outcome and, as a result, recognised a provision at the beginning of Year 1 in accordance with the requirements of IAS 37. Entity H's estimate of the legal settlement and the discount rate are as follows over time:

	Estimate of legal settlement (CU)	Discount rate
Beginning of Year 1	300,000	5%
End of Year 1	300,000	5%
End of Year 2	400,000	5%
End of Year 3	400,000	6%

Analysis

A legal provision is a liability that arises from a transaction that does not involve only the raising of finance. Interest income and expenses (IFRS 18.61(a)) or income and expenses arising from changes in interest rates (IFRS 18.61(b)) relating to such liabilities are classified in the financing category. Other income and expenses related to such liabilities are classified in the operating category. IFRS 18.B54(e) specifies that the increase in the discounted amount of a provision arising from the passage of time and the effect of any change in the discount rate is an example of interest income and expenses that meet the criteria in IFRS 18.61 to be classified in the financing category.

The following journals indicate the statement of profit or loss category to illustrate the effect that IFRS 18 has on the presentation of the expenses related to the provision. This example does not address how Entity H may present the expenses in the statement of profit or loss, only the required classification.

Beginning of Year 1

Statement of profit or loss category:

DR Legal provision expense CU246,811¹ Operating category

CR Legal provision CU246,811

CU246,811 is classified in the operating category because it is not interest income and expenses or income and expenses arising from changes in interest rates.

1: Present value (PV) of the future value of CU300,000 payable in 4 years discounted at 5%.

End of Year 1

Statement of profit or loss category:

DR Interest expense CU12,341² Financing category

CR Legal provision CU12,341

CU12,341 is classified in the financing category because it represents interest expense from unwinding of the discount.

At the end of Year 1 the provision has a carrying amount of CU259,152 (CU246,811 + CU12,341).

2: $\text{CU}246,811 * 5\%$ or

((PV of the future value of CU300,000 payable in 3 years discounted at 5%) - (PV of the future value of CU300,000 payable in 4 years discounted at 5%))

End of Year 2

Statement of profit or loss category:

DR Interest expense	CU12,958 ³	Financing category
DR Legal provision expense	CU90,703 ⁴	Operating category
CR Legal provision	CU103,661 ⁵	

CU12,958 is classified in the financing category because it is interest expense.

CU90,703 is classified in the operating category since it relates to the change in estimate of the legal settlement from CU 300,000 to CU 400,000. It is not interest income and expenses or income and expenses arising from changes in interest rates.

At the end of Year 2 the provision has a carrying amount of CU362,813 (CU259,152 + CU103,661).

3: $\text{CU}259,152 * 5\%$ or ((PV of the future value of CU300,000 payable in 2 years discounted at 5%) - (PV of the future value of CU300,00 payable in 3 years discounted at 5%))

4: (PV of the future value of CU400,000 payable in 2 years discounted at 5%) - (PV of the future value of CU300,000 payable in years 2 discounted at 5%)

5: $\text{CU}90,703 + \text{CU}12,958$ (remainder) or ((PV of the future value of CU400,000 payable in 2 years discounted at 5%) - (PV of the future value of CU300,000 payable in 3 years discounted at 5%))

End of Year 3:

Statement of profit or loss category:

DR Interest expense	CU14,547 ⁶	Financing category
CR Legal provision	CU14,547	

CU14,547 is classified in the financing category because it comprises both the unwinding of the discount and the effect of the change in the discount rate.

At the end of Year 3 the provision has a carrying amount of CU377,360 (CU362,813 + CU14,547).

6: (PV of the future value of CU400,000 payable in 1 year discounted at 6%) - (PV of the future value of CU400,000 payable in 2 years discounted at 5%).



Example 3.3-2 – Classification of income and expenses relating to a lease modification that decreases the scope of the lease

This example has been extracted from BDO's IFRS Accounting Standards in Practice IFRS 16 Leases. This example has been included to illustrate how income or expenses that arise from a lease modification are categorised in the statement of profit or loss.

Fact pattern

Entity B has a 10-year lease on 5,000 square metres of office space with annual payments of CU50,000 payable at the end of each year. The rate used to discount the payments due is Entity B's incremental borrowing rate of 6% as the rate implicit in the lease is not readily determinable. At the beginning of year six, Entity B and the lessor agree to reduce the lease to 2,500 square metres and reduce the remaining payments to CU30,000 a year. At the beginning of year six, Entity B's incremental borrowing rate is 5%.

IFRS 16 requirements

When a lease modification relates to a decrease of scope, the accounting modification is accounted for in two steps (IFRS 16.46):

1. Decreasing the right-of-use asset and lease liability by their relative amounts compared to the original lease recognising the difference in profit or loss; and
2. Remeasuring the lease liability using a revised discount rate with the off-set to the right-of-use asset.

Assessment

The modification is a decrease in scope from the original contract so the lease liability and right-of-use asset must be remeasured.

The lease liability immediately prior to the modification is CU210,618 and the right-of-use asset is CU184,002.

The scope of the decrease in the right-of-use asset is 50%, as the leased space has decreased from 5,000 square metres to 2,500.

Present value of years 6 – 10 (5 years), CU30,000 a year, 5% discount = 129,884

Entry required to adjust the carrying balances to reduce scope (step 1):

DR Lease liability	105,309	(210,618 original * 50%)
CR Right-of-use asset	92,001	(184,002 original * 50%)
CR Gain	13,308	(remainder)

Entry required to adjust lease liability to the required revised balance of CU 129,884 (step 2):

DR Right-of-use asset	24,575	(corresponds to liability adjustment)
CR Lease liability	24,575	(CU210,618 - CU105,309 + CU 24,575 = CU129,884)

IFRS 18 classification in the statement of profit or loss

A lease liability is a liability that arises from transactions that do not involve only the raising of finance (IFRS 18.B53(c)). Interest income and expenses (IFRS 18.61(a)) or income and expenses arising from changes in interest rates (IFRS 18.61(b)) relating to these liabilities are classified in the financing category. Other income and expenses are classified in the operating category.

IFRS 16 requires an entity to first decrease the right-of-use asset and lease liability based on the decrease in scope, resulting in a gain of CU13,308. This gain is classified in the operating category because the gain is the result of the partial derecognition of the lease liability and the right-of-use asset due to a decrease in scope. It is not interest income and expenses or income and expenses arising from changes in interest rates.

Although the lease liability is remeasured due to a change in the incremental borrowing rate (interest rate); the adjustment does not result in the recognition of income or expense. The amount by which the lease liability is remeasured (CU24,575) is offset against the right-of-use asset and is not recognised in profit or loss.

3.3.4. Income and expenses recognised on the derecognition of liabilities

The general classification requirements of IFRS 18 apply in classifying income and expenses recognised on the derecognition of a liability (IFRS 18.B61). Said another way, an entity must identify whether a derecognised liability arises from transactions that involve only the raising of finance, or not. The income and expenses recognised on derecognition will be classified accordingly.

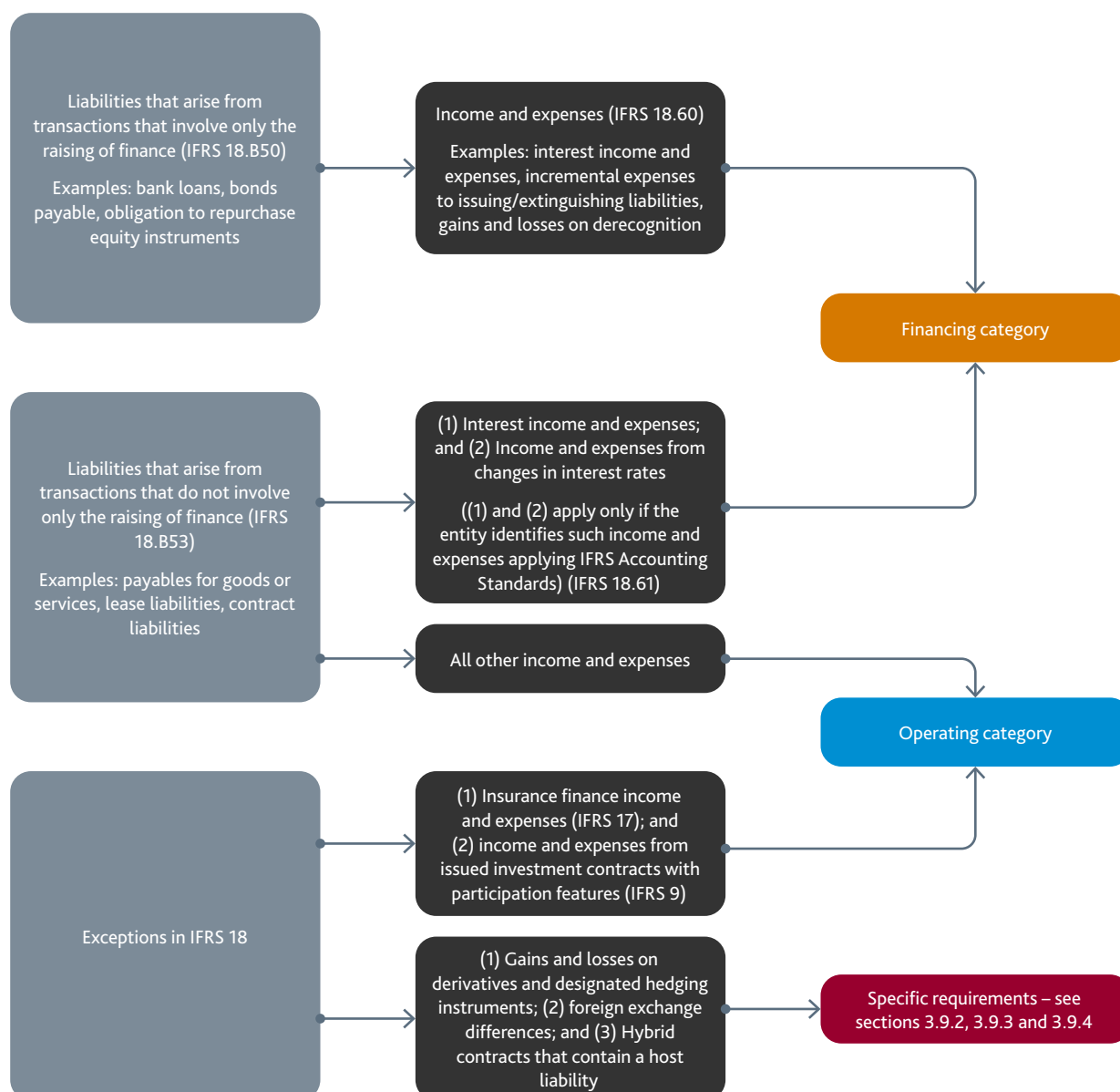
For example, assuming an entity does not provide financing to customers as a main business activity (IFRS 18.B61):

Income or expense recognised on derecognition of liability	Classification
A gain or loss is recognised on the early settlement of a bank loan	Financing category - the bank loan arises from a transaction that involves only the raising of finance (IFRS 18.60) and the gain or loss on derecognition arises from the derecognition of the liability (IFRS 18.60(a)).
A gain or loss is recognised when a payable to a supplier is derecognised as a result of a supplier financing arrangement with the recognition of a new liability	Operating category – the payable arises from a transaction that does not involve only the raising of finance (IFRS 18.61) and the gain or loss is not an item specified in IFRS 18.61(a)-(b), therefore, it must be classified in the operating category.



3.3.5. Practice aid – criteria to classify income and expenses in the financing category for entities without specified main business activities

This practice aid summarises the requirements to determine whether income or expenses are classified in the financing category, assuming that an entity does not have a main business activity of providing financing to customers. As discussed in section 3.8.2, the requirements for classifying income and expenses for entities with specified main business activities are significantly more complex in such cases.



3.3.6. Exceptions to classification principles

The classification principles applicable to liabilities are set out above, however, there are a number of exceptions:

Exception	Reference
Gains and losses on derivatives and designated hedging instruments	Section 3.9.2.
Foreign exchange differences	Section 3.9.3.
Hybrid contracts that contain a host that is a liability	Section 3.9.4.
Income and expenses from issued investment contracts with participation features recognised applying IFRS 9	See below.
Insurance finance income and expenses included in the statement of profit or loss applying IFRS 17	See below and section 8.5 for further information on the presentation requirements of IFRS 18 applicable to entities that issue insurance contracts in the scope of IFRS 17.

An entity always includes the following items in the operating category (IFRS 18.64):

- ▶ Income and expenses from issued investment contracts with participation features recognised applying IFRS 9; and
- ▶ Insurance finance income and expenses included in the statement of profit or loss applying IFRS 17.



BDO comment – insurance finance income and expenses

The requirement to classify insurance finance income and expense in the operating category applies even if an entity is not an 'insurance company' in the traditional sense. For example, a corporate entity may issue contracts that are permitted or required to be classified as insurance contracts in the scope of IFRS 17. Even if the issuance of such contracts is incidental to the entity's operations and the entity is not an 'insurance company' (i.e. it is not considered as such by law and regulation), IFRS 18.64 still requires the insurance finance income and expense to be classified in the operating category (IFRS 18.BC196-BC197) along with other income and expenses relating to the contracts (e.g. insurance revenue, insurance service result, etc.).

3.3.7. Presentation of income and expenses classified in the financing category

Prior to IFRS 18, IAS 1.82(b) required entities to present 'finance costs' as a separate line item in the statement of profit or loss. Finance costs were not defined in IAS 1, and entities applied a variety of accounting policies to determine which expenses were included in that line item. These may have included interest income and expenses, foreign exchange gains and losses, fair value gains and losses on derivatives used to manage risks associated with financing such as interest rate swaps, etc.

IFRS 18 did not bring this requirement forward from IAS 1, therefore, IFRS 18 contains no explicit requirement to present a single line item for finance costs. IFRS 18 also has no explicit requirement to present a subtotal for all items classified in the financing category (see section [5](#) for further information on subtotals).

Instead, entities are required to:

1. Classify income and expenses in the appropriate categories, which may result in certain expenses being classified in the financing category (e.g. interest expense on bank loans if the entity does not provide financing to customers as a main business activity);
2. Apply the aggregation and disaggregation requirements to determine appropriate groupings of items (see section [4](#)); and
3. Consider whether disaggregation of the line items presented in the statement of profit or loss is necessary in the notes (see section [4](#)).

The application of these requirements may change how an entity presents income and expenses related to financing compared to practice under IAS 1.

3.4. Operating category

The operating category is the residual category in IFRS 18, meaning that unless income and expenses are classified in another category, they must be classified in the operating category. Applying the requirements of IFRS 18 should result in an entity classifying in the operating category income and expenses from its main business activities (IFRS 18.B42), except for any such income and expenses from investments accounted for using the equity method, which are always classified in the investing category (see section 3.2).

For entities with specified main business activities (see section 3.8), the general requirements applicable to classifying income and expenses in the investing and financing categories are modified. That is because if an entity, for example, invests in assets as a main business activity (e.g. investing in real estate such as investment property), then specified income and expenses are presented in operating rather than investing (e.g. the fair value gains or losses on investment property when the fair value model is applied) to better reflect the entity's main business activities.

As the operating category is defined as a residual (i.e. it must be used when other categories do not apply), IFRS 18 does not contain specific criteria that must be met in order for income and expenses to be classified in the operating category. The following table is a non-exhaustive summary of income and expenses that are generally expected to be classified in the operating category, assuming that an entity does not have specified main business activities (see section 3.8):

Income and expenses	Examples of income and expenses classified in the operating category (assuming an entity does not have specified main business activities)
Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48) See section 3.2.	▶ Revenue from the sale of goods and services, including: ▶ Revenue from contracts with customers (IFRS 15) ▶ Insurance revenue (IFRS 17) ▶ Depreciation, impairment and gains and losses on disposal of property, plant and equipment ▶ Expenses arising from inventories (e.g. expenses when inventories are derecognised such as 'cost of sales' and similar items, net realisable value write-downs) ▶ Expenses related to trade receivables and contract assets (e.g. expected credit losses applying IFRS 9)
Income and expenses related to liabilities that arise from transactions that do not involve only the raising of finance and that are not (IFRS 18.61): Interest income and expenses; or Income and expenses arising from changes in interest rates. See section 3.3.	▶ Expenses related to the consumption of goods and services for which a liability is recognised (e.g. many executory contracts such as the acquisition of cleaning services, catering, repairs and maintenance not recognised as an asset, etc.) ▶ Remeasurement of cash-settled share-based payment liabilities (IFRS 2) ▶ Contract modifications gains and losses (IFRS 15) ▶ Modification gains and losses on lease liabilities (IFRS 16) ▶ Changes in the best estimate required to settle a provision (IAS 37)
Other items required to be classified in the operating category	▶ Income and expenses from issued investment contracts with participation features recognised applying IFRS 9 (see section 3.3) ▶ Insurance finance income and expenses included in the statement of profit or loss applying IFRS 17 (see section 3.3) ▶ Income and expenses related to business combinations, such as bargain purchase gains, income and expenses relating to the remeasurement of contingent consideration (IFRS 18.B49(f), BC144) (see section 3.9.5)

Income and expenses in the operating category include all income and expenses that are not included in other categories. Income and expenses cannot be excluded from the operating category on account of the income and expenses being volatile, unusual or non-recurring (IFRS 18.B42).



Example 3.4-1 – classification of 'extraordinary items'

IAS 1.87 specifically forbade entities from presenting line items labelled as 'extraordinary items' in the statement of profit or loss. IFRS 18 does not contain any explicit requirements concerning extraordinary items, however, entities would apply the general requirements of IFRS 18 applicable to classify income and expenses that an entity may consider 'extraordinary'.

Fact pattern

Entity G has significant manufacturing facilities that are destroyed by a tornado, resulting in material property, plant and equipment and inventories being derecognised as a result of their destruction.

Analysis

Entity G applies IFRS 18 to determine how to classify these expenses relating to the derecognition of property, plant and equipment and inventories. These assets do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48), and therefore, income and expenses relating to their derecognition are classified in the operating category (IFRS 18.B60).

See section 4 for further information on how an entity aggregates and disaggregates information in the profit or loss, which may affect how Entity G presents and discloses the expenses relating to the tornado.

See example 4.4-5 relating to the presentation of non-recurring items by function.

3.5. Income taxes category

Income and expenses are classified in the income taxes category if they are (IFRS 18.67):

1. Within the scope of IAS 12 *Income Taxes*; or
2. Foreign exchange differences related to income and expenses within the scope of IAS 12 (see section 3.9.3 for further information on the classification of foreign exchange differences).

To determine which income and expenses should be classified in the income taxes category, it is important to determine if the income taxes are recognised in profit or loss and if they are within the scope of IAS 12. Only income taxes within the scope of IAS 12 that are recognised in profit or loss are classified in the income taxes category.

The requirement of IFRS 18.67 to classify income taxes in the scope of IAS 12 in the income taxes category applies to the statement of profit or loss, however, not all income taxes within the scope of IAS 12 are recognised in profit or loss. Depending on where the related item is recognised, income taxes may also be recognised in other comprehensive income or directly in equity (IAS 12.61A).

For example, the movement in deferred tax relating to a revaluation surplus (if there are no previous revaluation losses) of a building classified as property, plant or equipment is recognised in other comprehensive income. The tax effect of the revaluation surplus is then also recognised in other comprehensive income. Furthermore, if applicable in a jurisdiction, tax arising from an adjustment to the opening balance of retained earnings due to a correction of a prior period error or due to a change in accounting policy (that is applied retrospectively) will be recognised directly in equity (IAS 12.62(a) and 12.62A(a)). These income taxes will therefore not be recognised in profit or loss and not be included in the income taxes category.



BDO comment – the scope of IAS 12 *Income Taxes*

IAS 12 scope

In many cases, identifying income and expenses within the scope of IAS 12 to be classified in the income taxes category will be straightforward. However, not all taxes are necessarily in the scope of IAS 12 creating uncertainty of how these taxes should be accounted for and subsequently classified and presented in the statement of profit or loss.

IAS 12 applies to all domestic and foreign income taxes which are based on taxable profits including taxes, such as withholding taxes, which are payable by a subsidiary, associate or joint arrangement on distributions to the reporting entity (IAS 12.2). IAS 12 does not address the accounting treatment of government grants and investment credits although it addresses the accounting for temporary differences arising from these grants or investment tax credits (IAS 12.4).

Furthermore, IAS 12 also applies to income taxes resulting from tax law that has been enacted or substantively enacted to implement the Pillar Two model rules issued by the Organisation for Economic Co-operation and Development (OECD), including those laws related to qualified domestic minimum top-up taxes described in these rules (IAS 12.4). Refer to [IFR Bulletin: 2023/04 - IASB issues Amendments to IAS 12 - International Tax Reform - Pillar Two Model Rules](#) for more information.

Taxes that might not be within the scope of IAS 12

The IFRS Interpretations Committee (the Committee) published an agenda decision in March 2006 – *Scope (IAS 12)*¹, which noted that IAS 12 applies to income taxes, which are defined as taxes that are based on taxable profit. That implies that (i) not all taxes are within the scope of IAS 12 but (ii) because taxable profit is not the same as accounting profit, taxes do not need to be based on a figure that is exactly accounting profit to be within the scope. The latter point is also implied by the requirement in IAS 12 to disclose an explanation of the relationship between tax expense and accounting profit. The Committee further noted that the term ‘taxable profit’ implies a notion of a net rather than gross amount.

Since not all taxes are based on taxable profits (net amount), not all taxes might fall within the scope of IAS 12. Examples of these taxes could include tonnage taxes (taxes based on tonnage transported, tonnage capacity or a notional profit based on the tonnage capacity) and production-based royalty payments. Refer to the agenda decisions of the Committee published in May 2009 – *Classification of tonnage taxes* and July 2012 – *Presentation of payments on non-income taxes*.

Judgement is required to determine if other taxes would fall within the scope of IAS 12, IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*, IAS 20 *Accounting for Government Grants and Disclosure of Government Assistance* or other IFRS Accounting Standards. To determine the correct accounting treatment, an entity should consider both statutory and economic factors.

Other examples of taxes that might not fall within the scope of IAS 12 include:

- ▶ taxes based on the taxable profits, but are subject to a minimum tax floor payable; and
- ▶ taxes measured at the higher of taxable profits or another base such as net assets.

Interest and penalties related to income taxes

The IFRS Interpretations Committee (the Committee) published an agenda decision in September 2017 – *Interest and penalties related to income taxes*. The Committee observed that entities do not have an accounting policy choice between applying IAS 12 and applying IAS 37 to interest and penalties. Instead, if an entity considers a particular amount payable or receivable for interest and penalties to be an income tax, then the entity applies IAS 12 to that amount. If an entity does not apply IAS 12 to a particular amount payable or receivable for interest and penalties, it applies IAS 37 to that amount.

Applying the March 2006 and September 2017 agenda decisions means that an entity needs to determine whether interest and penalties related to income taxes are within the scope of IAS 12. IFRS Accounting Standards are not clear about how this assessment should be performed, however, the basis under which interest and penalties are calculated (i.e. are they based on taxable profit, such as a percentage of taxable profit) may assist entities in making this determination.

¹ As at the date of publishing, the IFRS Interpretations Committee is considering [amending this and another IFRS Interpretations Committee agenda decision](#) as a consequence of IFRS 18 being issued. The IFRS Interpretations Committee also published a [tentative agenda decision](#) in November 2025 titled *Presentation of Taxes or Other Charges that are Not Income Taxes within the Scope of IAS 12*.



BDO comment – interaction between IFRS 18 income tax category requirements and IAS 12 *Income Taxes*

As explained above, income taxes within the scope of IAS 12 (recognised in profit or loss) and related foreign exchange differences will be classified in the income taxes category in the statement of profit or loss.

If it has been determined that taxes are within the scope of IAS 12, the related income and expenses should be classified in the income taxes category. However, if the taxes are excluded from the scope of IAS 12, the related income and expenses should be assessed to determine if they should be classified in the investing, financing or discontinued operations category. If not, such taxes should be classified in the operating category since this category is a residual category.

In most cases, income and expenses related to taxes that are not within the scope of IAS 12 will be classified in the operating category because they generally would:

- ▶ not relate to assets that generate a return individually and largely independently of the entity's other resources (see sections [3.2.6](#) and [3.2.7](#));
- ▶ not relate to liabilities that arise from transactions that involve only the raising of finance (see section [3.3.2](#)); and
- ▶ not relate to interest income and expenses (or due to a change in interest rate) resulting from liabilities that arise from transactions that do not involve only the raising of finance (see section [3.3.3](#)).

Write-down and any recovery of deferred tax assets

In our view, the income taxes category also includes the write-down and any recovery of deferred tax assets recognised in profit or loss applying the recoverability requirements of IAS 12. This will also include the effect of uncertain tax treatments reflected in profit or loss within the scope of IFRIC 23 *Uncertainty over Income Tax Treatments*, because IFRIC 23 interprets how to measure items in the scope of IAS 12.

Interest and penalties related to taxes

An entity needs to determine whether interest and penalties related to income taxes are within the scope of IAS 12 or another IFRS Accounting Standard. Interest and penalties determined to be in the scope of IAS 12 should be classified in the income taxes category.

Interest and penalties related to taxes determined to be excluded from the scope of IAS 12 should first be assessed if they should be classified in the investing, financing or discontinued operations categories. If not, they should be classified within the operating category since this category is a residual category.



Example 3.5-1 – current tax payable and receivable

Entity A, a logistics entity, pays tonnage taxes based on the tonnage of cargo transported during the year. Since the tax is not based on taxable income, Entity A assessed that the tonnage taxes are not included within the scope of IAS 12.

Current tax payable

Assume that Entity A has an outstanding current tonnage tax payable at year-end that bears interest. The tax authorities also charged a penalty for the late payment. How should the interest expense and penalty be classified in the statement of profit or loss?

Since Entity A has assessed that the tonnage taxes do not fall within the scope of IAS 12, the related income and expenses cannot be classified in the income taxes category in the statement of profit or loss.

In our view, the requirements of IFRS 18.61 (income and expenses that relate to liabilities that arise from transactions that do not involve only the raising of finance) should be applied to classify income and expenses related to current tax payables that do not fall within the scope of IAS 12. IFRS 18.61 requires that interest income and expenses (identified by the entity in applying IFRS Accounting Standards) and income and expenses arising from changes in interest rates should be classified in the financing category. Other income or expenses relating to

these liabilities are classified in the operating category.

The interest expense should therefore be classified in the financing category and the penalty in the operating category.

Current tax receivable

Assume that Entity A has an outstanding current tonnage tax receivable at year-end that bears interest. How should the interest income be classified in the statement of profit or loss?

Since Entity A has assessed that the tonnage taxes do not fall within the scope of IAS 12, the related income and expenses cannot be classified in the income taxes category in the statement of profit or loss.

In our view, an entity should apply judgement and consider facts and circumstances to determine the most appropriate classification. For example, if an entity prepays the tax to earn interest on the balance, it might assess that the interest earned should be classified in the investing category since it generates a return individually and largely independently of the entity's other resources.

Conversely, if an entity prepays the tax to avoid penalties, it might determine that the tax balance results from the activities of the entity as a whole and should therefore be classified in the operating category.

3.6. Discontinued operations category

Income and expenses are classified in the discontinued operations category if they are income and expenses from discontinued operations as required by IFRS 5 (IFRS 18.68).



BDO comment – interaction between IFRS 5 and IFRS 18

This publication does not summarise all of the requirements of IFRS 5, however, the interaction between IFRS 5 and IFRS 18 requires an explanation of the fundamental requirements of IFRS 5.

IFRS 5 addresses two main topics:

- ▶ non-current assets or disposal groups (which may include both assets and liabilities) held for sale or distribution; and
- ▶ discontinued operations

Non-current assets or disposal groups held for sale or distribution

IFRS 5 defines a 'disposal group' as 'a group of assets to be disposed of, by sale or otherwise, together as a group in a single transaction, and liabilities directly associated with those assets that will be transferred in the transaction.' A non-current asset held for sale or distribution is similar to a disposal group, it however relates to a single non-current asset (such a building) and not a group of assets and liabilities.

Non-current assets or disposal groups are classified as held for sale or distribution when the sale or distribution is expected within one year from classification date (certain exceptions may apply per IFRS 5.B1). This would result in these assets and liabilities being classified as current assets and liabilities (and presented separately from other assets and liabilities as required by IFRS 5.38). IFRS 5.6-12A therefore sets out criteria that must be met for assets and liabilities to be classified as held for sale or distribution to prevent entities from reclassifying these assets and liabilities simply because of management's intention to sell or because they reached their final twelve months of expected use by the entity (IFRS 5.BC10).

Discontinued operations

A discontinued operation is defined in IFRS 5 as:

A component of an entity that either has been disposed of or is classified as held for sale and:
(a) represents a separate major line of business or geographical area of operations;

(b) is part of a single co-ordinated plan to dispose of a separate major line of business or geographical area of operations; or

(c) is a subsidiary acquired exclusively with a view to resale.

A 'component of an entity' is defined as 'operations and cash flows that can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the entity.'

A minor separate line of business or a geographical area of operation disposed of (that forms part of a single co-ordinated plan to dispose of) may be an operation that is discontinued but is not material enough to be disclosed as a discontinued operation in the statement of profit or loss.

Difference and interaction between a non-current asset or disposal group held for sale and a discontinued operation can generally be summarised as follows:



It is highly unlikely that the definition of a discontinued operation would be met by a single non-current asset held for sale (e.g. an item of property, plant and equipment classified as held for sale).

Conversely, a disposal group may be classified as a discontinued operation if it meets the definition of a discontinued operation when it represents a separate major, not minor, line of business or geographical area of operations.

Furthermore, not all discontinued operations would be a disposal group either since discontinued operations include components of an entity already sold and disposal groups relate to components of an entity in the process of being sold.

Classification of related income and expenses

The following table summarises the classification of income and expenses related to non-current assets and disposal groups held for sale or distribution as well as discontinued operations.

Item	Classification in the statement of profit or loss
Non-current asset held for sale or distribution	Operating or investing category
Disposal group held for sale or distribution that is not a discontinued operation	Operating or investing category
Discontinued operations	Discontinued operations category

See sections [3.2.8](#) and [3.2.9](#) for further explanation about the classification of income and expenses related to non-current assets and disposal groups held for sale or distribution.

Once an operation meets the definition of a discontinued operation, related income and expenses must be presented in the discontinued operations category (IFRS 18.68). Furthermore, to enhance comparability between different periods of an entity, the comparative periods presented in the financial statements must be restated to separately present the financial performance and position of the discontinued operations from that of the continuing operations (IFRS 5.34).

For a summary of the classification criteria related to these assets and liabilities, see section [3.2.11](#). Practice aid – *classification of gains and losses on the derecognition of an asset or liability (or group of assets and liabilities), the remeasurement of an asset (or disposal group) as held for sale, or a change in use.*

IFRS 5.33(a) requires the following total to be presented as a single line item in the statement of profit or loss:

- (i) the post-tax profit or loss of discontinued operations; and
- (ii) the post-tax gain or loss recognised on the measurement to fair value less costs to sell or on the disposal of the assets or disposal group(s) constituting the discontinued operation.

This single line item specified by IFRS 5.33(a) must be classified in the discontinued operations category in accordance with IFRS 18.68.

BDO comment – income and expense that will not be included in the 'single line item' – IFRS 5.33(a)

As explained above, income and expenses relating to a non-current asset held for sale or distribution or a disposal group held for sale or distribution that does not meet the definition of a discontinued operation will not be classified in the discontinued operations category.

For example, an entity may plan to dispose of an item of property, plant and equipment, such as a distribution centre, and classify it as an asset held for sale. IFRS 5.15 requires that asset to be measured at the lower of its cost and fair value less costs to sell. However, an impairment loss recognised as a result of applying IFRS 5.20 in this fact pattern would not be presented as a discontinued operation and would be excluded from the single line item to be reported in accordance with IFRS 5.33(a)(ii). That is because IFRS 5.33(a)(ii) includes only the post-tax gain or loss recognised relating to discontinued operations, meaning the definition of a discontinued operation must be met.

Similarly, the disposal of a single item of property, plant and equipment (such as a distribution centre in this example) will most likely never meet the definition of a discontinued operation, therefore, the write-downs recognised in accordance with IFRS 5.15 are not included in the single line item required by IFRS 5.33(a)(ii), and are not classified in the discontinued operations category. Instead, the entity applies the requirements applicable to the remeasurement of an asset (or disposal group) that is not a discontinued operation. See sections [3.2.8](#), [3.2.9](#) and [3.2.11](#).



3.7. Entities with specified main business activities – an entity's assessment of specified main business activities

3.7.1. Purpose of specified main business activities requirements

The general classification requirements of IFRS 18 (as explained in sections [3.2](#) - [3.6](#)) apply when an entity does not have specified main business activities, which are instances when the reporting entity:

- ▶ Invests in assets that generate a return individually and largely independently of the entity's other resources as a main business activity (IFRS 18.55-58); and/or
- ▶ Provides financing to customers as a main business activity (IFRS 18.65-66).

If an entity has one or more of these activities as a main business activity, then special considerations apply, which will result in certain income and expenses being classified in the operating category rather than the investing and financing categories. In some cases, entities may also have accounting policy choices relating to the classification of certain income and expenses (see sections [3.9.1](#) and [3.9.2](#)).

The IASB decided to require certain income and expenses to be classified in the operating category rather than the investing and/or financing categories for entities with specified main business activities because otherwise, operating profit would not include all of the income and expenses related to an entity's main business activities (IFRS 18.BC89(a)). Additionally, classifying certain income and expenses in the investing and financing categories would prevent certain entities from presenting key measures of operating performance in the operating category (IFRS 18.BC90).

For example, without the specified main business activities requirements, an entity that sells goods and services but also provides financing to customers as a main business activity (e.g. an entity that sells farm equipment and financing for each item of equipment sold) would not be permitted to present interest income and expenses in the operating category. If the entity provides financing to customers as a main business activity, the entity may use 'net financial margin' as a key measure of profits it generates from providing financing to customers. If the entity were unable to present finance income and expenses in the operating category, this would mean that the operating category would not include all of the entity's main business activities.

3.7.2. Level of assessment

An entity assesses whether it has specified main business activities at the reporting entity level (IFRS 18.B37, BC98). Therefore, a reporting entity that consists of its parent and consolidated subsidiaries performs this assessment at the group level. See section [3.7.7](#) 'considerations applicable to groups' below for further specific considerations for groups.

If an entity prepares separate financial statements, then the reporting entity would be the legal entity only, as any subsidiaries would not be consolidated. For an entity preparing separate financial statements, it would assess whether it invests in assets as a main business activity using groups of assets that are consistent with the categories used to determine their measurement basis applying IAS 27.10 (IFRS 18.B38). See section [3.7.5](#) for further considerations relating to whether an entity invests in unconsolidated subsidiaries as a main business activity.

When assessing if an entity invests in assets as a main business activity, this assessment is performed by assessing an individual asset or group of assets with shared characteristics. When making this assessment for financial assets, an entity is required to use groups of financial assets that are consistent with the classes of financial assets identified applying IFRS 7.6 (IFRS 18.B40).



BDO comment – grouping of financial assets for assessment of whether an entity invests in assets as a main business activity

IFRS 7.6 requires an entity to prepare disclosures by class of financial instrument, with an entity grouping financial instruments into classes that are appropriate to the nature of the information disclosed and that take into account the characteristics of those financial instruments.

Therefore, an entity may, for example, group financial assets into classes such as equity instruments vs. debt instruments. When assessing if it invests in such assets as a main business activity, it is possible for an entity to reach different conclusions for these classes of assets. For example, the entity may conclude that it invests in debt instruments as a main business activity, but not equity instruments.

An entity may also conclude that it invests in certain portfolios or subsets of financial assets as a main business activity, but not other financial assets, even if the nature of those assets are similar. This may occur in a reporting entity with diverse operations – for example, financial operations (e.g. banking) as well as non-financial (e.g. manufacturing) where the entity concludes that it invests in the financial assets managed as part of its banking operations as a main business activity, but not the other financial assets held by the manufacturing part of its operations. Refer to example 3.7-1 below for an example of an entity that invests in certain financial assets as a main business activity, but not others.



Example 3.7-1 unit of account for assessing whether an entity invests in assets as a main business activity

Entity Z operates two distinct main business activities; banking and manufacturing activities.

The banking operation holds significant financial assets such as bonds and publicly traded shares, as it is fundamental to the banking operation's business model to earn investment income. The manufacturing operation also holds some financial assets to earn additional investment income on excess cash, however, these investments are not key to the manufacturing operation's business model.

All of the financial assets held by Entity Z (both the banking and manufacturing operations) generate returns individually and largely independently of the entity's other resources, therefore, Entity Z is required by IFRS 18.58 to assess whether the entity invests in such assets as a main business activity. If it is determined that Entity Z does, then the income and expenses relating to those assets (e.g. fair value gains or losses, interest income, etc.) will be classified in the operating category rather than the investing category.

This raises the question of whether it is possible for Entity Z to conclude that it:

- ▶ Invests in the financial assets held by its banking operations as a main business activity; and
- ▶ Does not invest in the financial assets held by the manufacturing operations as a main business activity.

In our view, it is possible for an entity to conclude that it invests in certain assets as a main business activity, while concluding differently for other assets, even if the nature of those assets is similar. Although IFRS 18.B40 requires an entity to use groups of financial assets that are consistent with the classes of financial assets identified applying IFRS 7.6, IFRS 18.58 and IFRS 18.BC145 require (emphasis added) 'income and expenses related to assets invested it as main business activity' to be classified in the operating category. In our view, it is appropriate to consider this assessment at the level of the asset, meaning that a single reporting entity does not necessarily have to conclude that it does/does not invest in certain assets as a main business activity for the entire reporting entity.

Therefore, assuming sufficient evidence exists to support the assertions, Entity Z may conclude that it invests in the financial assets held by the banking operation as a main business activity but not the financial assets held by the manufacturing operation.

However, entities must carefully consider how assets are managed by divisions, subsidiaries, etc. within a single reporting entity, or else this view could otherwise result in income and expenses being classified in the operating or investing category arbitrarily. For example, if in the example above, the banking operation transferred financial assets to the manufacturing operation, it would be arbitrary to classify those transferred assets in the investing category only because they have been notionally transferred within a single, consolidated reporting structure. Entities should carefully consider how assets, particularly those that are interchangeable such as financial assets, are managed within a corporate reporting structure, such as whether portfolios of assets are managed distinctly from other portfolios.

In our view, it is not determinative whether operations are structured through individual subsidiaries, however, this may provide evidence of distinct business activities. However, see example 3.7-2, as it may be possible for consolidation adjustments to be necessary to adjust the assessment of specified main business activities within a group.

This view however only applies to 'other assets' included in the scope of IFRS 18.53(c) (e.g. most financial assets, investment property, etc.). IFRS 18 prescribes stricter requirements for income and expenses related to investments in associates, joint ventures and unconsolidated subsidiaries (IFRS 18.53(a)) and cash and cash equivalents (IFRS 18.53(b)). See sections 3.8.1.4 *Other assets* and 3.9.1 *BDO Comment - entities that invest in financial assets as a main business activity but also have other main business activities*.

3.7.3. Multiple main business activities

An entity may have more than one main business activity (IFRS 18.B30), and it is possible to have more than one specified main business activity. An entity also assesses whether it has specified main business activities independently for the two types of specified main business activities:

- ▶ Invests in assets that generate a return individually and largely independently of the entity's other resources as a main business activity (IFRS 18.55-58); and/or
- ▶ Provides financing to customers as a main business activity (IFRS 18.65-66).

For example, an entity may conclude that it:

1. Invests in assets as a main business activity (e.g. real estate), but it does not provide financing to customers as a main business activity;
2. Does not invest in assets as a main business activity, but it provides financing to customers as a main business activity (e.g. selling goods with associated financing); or
3. Invests in assets as a main business activity (e.g. financial assets) and also provides financing to customers as a main business activity (e.g. loans provided to borrowers by a bank).

An entity may also conclude that it invests in multiple types of assets as a main business activity. For example, an entity may conclude that it invests in both real estate and financial assets as a main business activity, which would result in many items of income and expense being classified in the operating category (e.g. fair value gains and losses on investment property, fair value gains and losses on financial assets, etc.).

Finally, an entity may conclude that certain aspects of its operations invest in assets as a main business activity, but not other aspects, even if the underlying assets are similar – see Example [3.7-1](#) above.

3.7.4. Evidence to be considered when making assessment

The assessment of whether an entity has specified main business activities is a matter of fact and not an assertion or an accounting policy choice (IFRS 18.B33, BC96). It is not optional for an entity to assess whether it has specified main business activities, and if it does, it is required to apply the requirements for entities with specified main business activities. Assessing whether an entity has specified main business activities will require judgement.

IFRS 18 notes two sources of evidence that an entity may use in assessing whether an entity has specified main business activities. These two sources could indicate that certain business activities (relating to investing in assets and/or providing financing to customers) are important indicators of operating performance (and is therefore a specified main business activity). These two sources are:

- ▶ Use of particular subtotals (IFRS 18.B34); and
- ▶ Segment information (IFRS 18.B36).

Use of subtotals as an indicator of operating performance, including indicators used outside of financial statements:

- ▶ If an entity uses a particular type of subtotal as an important indicator of operating performance, then investing in assets or providing financing to customers is likely to be a specified main business activity (IFRS 18.B34).
- ▶ These subtotals would be similar to gross profit (see section [5.2](#)), which includes income and expenses that would be classified in the investing or financing categories if the entity did not have specified main business activities.
- ▶ Evidence that subtotals similar to gross profit are important indicators of operating performance includes using subtotals to (IFRS 18.B35):
 - (a) Explain operating performance externally; or
 - (b) Assess or monitor operating performance internally.





BDO comment – use of subtotals as an indicator of operating performance

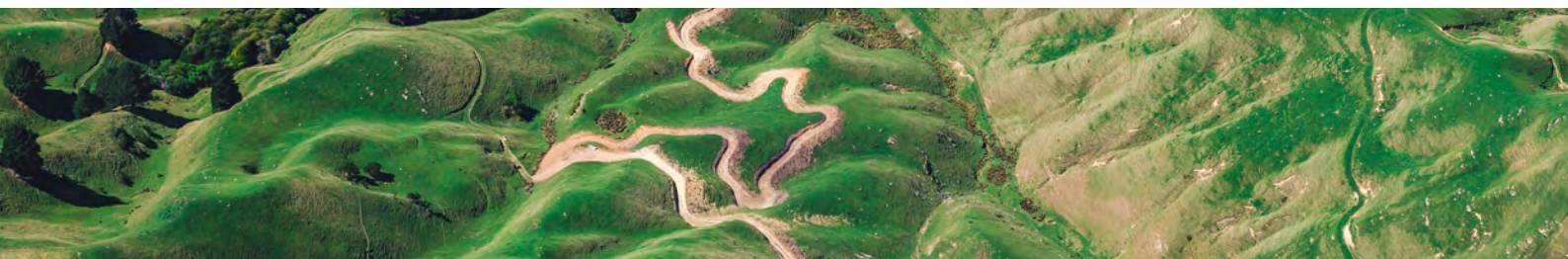
IFRS 18.B34-B35 does not include examples of subtotals which if used as an important indicator of operating performance may indicate that an entity invests in assets or provides financing to customers as a main business activity.

However, subtotals similar to gross profit are common in certain industries. For example, banking and lending institutions commonly use a subtotal of interest income less interest expense, which may be labelled as 'net financial margin' or 'net interest income'. Use of a subtotal in external and/or internal communications may indicate that an entity provides financing to customers as a main business activity.

IFRS 18.B34 refers to IFRS 18.B123 when it refers to subtotals similar to gross profit which if used, may indicate that an entity invests in assets or provides financing to customers as a main business activity. For example, IFRS 18.B123(a) notes 'net interest income' as a subtotal similar to gross profit or loss. An entity using net interest income to communicate information about financial performance may provide evidence that the entity has specified main business activities (e.g. providing financing to customers).

IFRS 8 Operating Segments (IFRS 18.B36):

- ▶ Information about segments may provide evidence that investing in assets or providing finance to customers is a main business activity if an entity applies IFRS 8, however, IFRS 8 is only mandatory for certain entities (IFRS 8.2), therefore, segment information may not provide evidence of main business activities for all entities that apply IFRS Accounting Standards..
- ▶ An entity's operating segments and reportable segments may provide evidence of whether the entity has specified main business activities. This assessment may vary depending on whether the operating segment is reportable or not (IFRS 18.B36):
 - (a) Reportable segment: if a reportable segment comprises a single business activity, this indicates that the performance of the reportable segment is an important indicator of the entity's operating performance and that the business activity of the reportable segment is a main business activity of the entity.
 - (b) Operating segment: if an operating segment comprises a single business activity, this indicates that the business activity might be a main business activity of the entity if the performance of the operating segment is an important indicator of the entity's operating performance.



BDO comment – reportable segments and operating segments

Reportable segments

If a reportable segment comprises a single business activity, then it is logical that that single business activity is an important indicator of the entity's performance. That is because a reportable segment is an operating segment that is identified according to the requirements of IFRS 8. Identification as a reportable segment in accordance with IFRS 8 means that the operating segment is (1) a component of an entity whose operating results are regularly reviewed by the entity's chief operating decision maker (IFRS 8.5(b)); and/or (2) meets quantitative thresholds in IFRS 8.13.

IFRS 18.B36(a) states that if a reportable segment comprises a single business activity, this indicates that the performance of the reportable segment is an important indicator of the entity's operating performance. Therefore, in many cases, such entities will be considered to have main business activities of that reportable segment, however, not all reportable segments comprise a single business activity, therefore, care must be taken in applying

IFRS 18.B36(a).

Operating segments

IFRS 18.B36(b) is less definitive for operating segments that are not reportable segments, that is, components of an entity that meet the definition of an operating segment but are not deemed to be reportable applying the requirements of IFRS 8. If a non-reportable segment comprises a single business activity, it is still possible that that operating segment's performance is an important indicator of the entity's performance, and therefore, the business activity of that segment may be a main business activity of the entity overall, but IFRS 18.B36(b) does not deem this to be the case as it does for reportable segments.

The assessment of a non-reportable operating segment's main business activities may therefore be part of the evidence an entity uses to assess whether the entity has specified main business activities, but it is not definitive.

3.7.5. Investing in associates, joint ventures and unconsolidated subsidiaries

It is not necessary for an entity to assess whether it invests in associates, joint ventures and unconsolidated subsidiaries as a main business activity if the entity accounts for such investments using the equity method. That is because if the equity method is applied to such investments, then income and expenses relating to such investments will always be classified in the investing category, regardless of whether an entity has specified main business activities (IFRS 18.B38; see section 3.2).

If an entity does not apply the equity method to such investments, then it must assess whether it invests in associates, joint ventures and unconsolidated subsidiaries as a main business activity. For example, an investment entity as defined in IFRS 10 may invest in associates and joint ventures together with subsidiaries as a main business activity, or a venture capital organisation may also invest in associates and joint ventures as a main business activity and not apply the equity method if certain accounting policies are elected (IAS 28.18).

In making an assessment of whether it invests in assets as a main business activity, an entity performs this assessment by individual asset or using groups of assets with shared characteristics (IFRS 18.B38). Therefore, it is possible for an entity to conclude that it invests in certain associates, joint ventures and unconsolidated subsidiaries as a main business activity, but not others.

3.7.6. Examples of entities with specified main business activities

Examples of entities that might invest in assets as a main business activity include (IFRS 18.B31):

- (a) investment entities as defined by IFRS 10;
- (b) investment property companies; and
- (c) insurers.

Examples of entities that might provide financing to customers as a main business activity include (IFRS 18.B32):

- (a) banks and other lending institutions;
- (b) entities that provide financing to customers to enable those customers to buy the entity's products; and
- (c) lessors that provide financing to customers in finance leases.



BDO comment – examples of entities with specified main business activities

The examples given in IFRS 18.B31 and B32 are non-exhaustive, and there may be many other types of entities with specified main business activities.

An example of an entity that provides financing to customers to enable those customers to buy the entity's products would include entities that provide significant financing terms for the sale of goods. For example, a company that sells heavy machinery may lease equipment to customers under a finance lease (IFRS 18.B32(c)) or legally transfer title to the equipment with a corresponding loan agreement to pay the selling entity over time through instalments of principal and interest.

3.7.7. Considerations applicable to groups

As noted above, the assessment of whether an entity has specified main business activities is made at the reporting entity level, being the entity and its subsidiaries as one unit of account. This assessment may differ, for example, at the consolidated level of the parent entity compared to a subsidiary, or intermediate parent entities' individual financial statements.

This may result in significant consolidation adjustments when a subsidiary is consolidated and its parent's assessment of whether it has specified main business activities differs from its own assessment. This may occur due to materiality. For example, a subsidiary may clearly invest in assets as a main business activity at the level of its own financial statements, but when this assessment is made at the consolidated level of its parent, taken together with other subsidiaries, the operations of that subsidiary may not be significant, resulting in a different assessment.



Example 3.7-2 – consolidation adjustments required for subsidiary upon consolidation

Fact pattern

Entity J is a holding company with no substantive operations. Entity J has three subsidiaries:

1. Entity K: a manufacturer of automotive parts
2. Entity L: a private lender providing loans to customers
3. Entity M: a real estate company that invests in commercial real estate for rental income and capital growth and measures the investment properties at fair value

Entity J prepares consolidated financial statements, and Entities K, L and M all prepare their own individual financial statements as well.

Entities K, L and M make the following assessments of whether they have specified main business activities in their individual financial statements:

Entity	Specified main business activities?
Entity K	No
Entity L	Yes; providing financing to customers and investing in assets (loans receivable from customers)
Entity M	Yes; investing in assets (real estate, being investment property measured at fair value – IAS 40)

At the consolidated level, Entity J assesses that it has no specified main business activities. That is because the operations of Entity K are significantly larger than Entities L and M. Entities L and M are not reportable segments in accordance with IFRS 8 and at the level of Entity J, subtotals similar to gross profit are not used as an important indicator of operating performance.

Assessment

Entities L and M are required to apply the requirements applicable to entities with specified main business activities in their individual financial statements. For example:

- ▶ Entity L: interest income and expenses are classified in the operating category rather than the investing and financing categories (IFRS 18.65(a)(i), 58).
- ▶ Entity M: rental income and fair value gains and losses on investment property are classified in the operating category rather than the investing category (IFRS 18.58).

In Entity J's consolidated financial statements, the requirements applicable to entities with specified main business activities do not apply, therefore, when consolidating Entities L and M, Entity J makes the following consolidation adjustments:

- ▶ Entity L: reclassifies interest income and expenses from the operating category to the investing and financing categories.
- ▶ Entity M: reclassifies rental income and fair value gains and losses on investment property from the operating category to the investing category.

This example is straightforward, however, for entities with complex structures and many subsidiaries, making

appropriate consolidation adjustments for assessments of specified main business activities may be complex and require consolidation procedures to be adjusted (e.g. adjustments to consolidation software to allow for income and expenses to be classified into different categories at different levels of consolidation).

It is also possible that depending on the precise facts and circumstances, sub-components of a reporting entity (e.g. individual subsidiaries, divisions, etc.) may conclude that certain subsidiaries or divisions invest in assets as a main business activity, while others do not – see Example 3.7-1. Example 3.7-2 is an illustration of consolidation adjustments that may be necessary; IFRS 18 does not necessarily require the assessment of whether an entity invests in assets as a main business activity to be consistent for the entire reporting entity (see example 3.7-1), however, in many cases this may be the conclusion reached by entities.

3.7.8. Change in assessment

An entity's assessment of whether it has specified main business activities is not a 'one time' assessment, because it is possible for an entity's assessment to change as its operations change over time.

IFRS 18 requires any change in an entity's assessment of whether it has specified main business activities to be reflected prospectively (IFRS 18.B41), therefore, comparatives are not restated.

IFRS 18.51(c)(i) requires an entity to disclose the fact the outcome of the assessment has changed and the date of the change.

IFRS 18.51(c)(ii) requires an entity to disclose the amount and classification of items of income and expense before and after the change in the assessment.



Example 3.7-3 – change in assessment of specified main business activities

Fact pattern

As at 31 December 20x4, Entity Y concludes that it does not invest in real estate assets (e.g. investment properties measured at fair value) as a main business activity. Therefore, it presents rental income of CU100 and fair value gains on investment property of CU240 in the investing category for the year-ended 31 December 20x4.

As at 1 January 20x5, Entity Y concludes that its main business activities have changed and it does invest in real estate assets as a main business activity. Therefore, it presents rental income of CU110 and fair value gains on investment property of CU225 in the operating category for the year-ended 31 December 20x5.

Assessment

In preparing its 31 December 20x5 financial statements, Entity Y applies IFRS 18.B41 and reflects its change in its assessment of whether it invests in assets as a main business activity prospectively (i.e. the 31 December 20x4 comparative period is not restated).

Entity Y provides disclosures required by IFRS 18.51(c)(i), being the fact of the change of the assessment and the date of the change (1 January 20x5). Entity Y also meets the disclosure requirement of IFRS 18.51(c)(ii) by disclosing the amount and classification of the items reclassified as a result of the change of the assessment:

Item of income/expense	31 December 20x5 classification	31 December 20x4 classification
Rental income	CU110 operating category	CU100 investing category
Fair value gains on investment property	CU225 operating category	CU240 investing category

3.7.9. Disclosures related to an entity's assessment of specified main business activities

IFRS 18.51 requires the following disclosures:

- (a) If an entity invests in assets as a main business activity, it shall disclose that fact.
- (b) If an entity provides financing to customers as a main business activity, it shall disclose that fact.
- (c) Those disclosures required when an entity changes its assessment of whether it has specified main business activities (see section 3.7.8 'change in assessment' above).

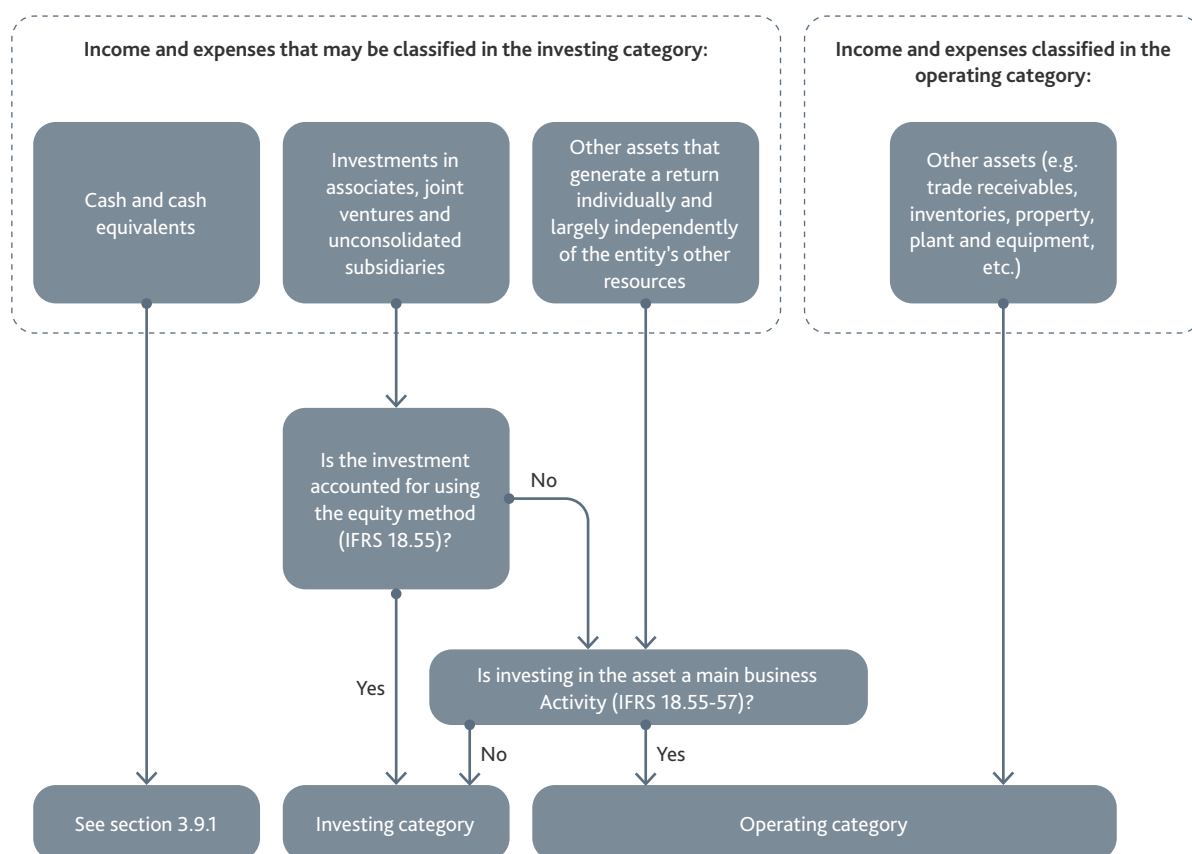
If any entity does not have any specified main business activities and no change in that assessment in the current period, none of the disclosures in IFRS 18.51 will be relevant.

3.8. Additional requirements for entities with specified main business activities

Sections 3.8.1 and 3.8.2 explain how the classification requirements of IFRS 18 differ for entities with specified main business activities. If an entity does not have any specified main business activities, these sections are not relevant, and an entity would apply the general classification requirements (see sections 3.1 - 3.6).

3.8.1. Investing in assets as a main business activity

If an entity invests in assets as a main business activity, the general classification requirements of IFRS 18 are modified. The classification requirements applicable to assets (and related income and expenses) are summarised as follows:



The following sections explain how the classification requirements of IFRS 18 apply to entities that invest in assets as a main business activity, by each of the four classes of assets in the above flowchart.

3.8.1.1. Cash and cash equivalents

See section [3.9.1](#) for the requirements applicable to classifying income and expenses relating to cash and cash equivalents.

In summary, if an entity invests in financial assets as a main business activity (and therefore classifies incomes and expenses from financial assets in the operating category), then it is also required to classify income and expenses from cash and cash equivalents in the operating category as well (IFRS 18.56(a)).

If the entity provides financing to customers as a main business activity (see section [3.8.2](#)), then the classification requirements are more complex.

3.8.1.2. Investments in associates, joint ventures and unconsolidated subsidiaries

As noted in sections [3.2](#) and [3.8](#), it is not necessary for an entity to assess whether it invests in associates, joint ventures and unconsolidated subsidiaries as a main business activity if the entity accounts for such investments using the equity method. That is because if the equity method is applied to such investments, then income and expenses relating to such investments will always be classified in the investing category, regardless of whether an entity has specified main business activities (IFRS 18.B38; see section [3.2](#)).

However, if the equity method is not applied to such investments, then an entity must assess if it invests in those assets as a main business activity (see section [3.2.4](#)). If the entity determines that it does have a main business activity of investing in those assets, then it classifies income and expenses relating to those assets in the operating category.

For example, an investment entity as defined in IFRS 10 may invest in associates and joint ventures together with subsidiaries as a main business activity and would therefore measure those investments at fair value through profit or loss. An investment entity would classify those fair value gains and losses in the operating category.

3.8.1.3. Other assets

IFRS 18 has stricter requirements for the classification of income and expenses arising from cash and cash equivalents and investments in associates, joint ventures and unconsolidated subsidiaries than for other assets (e.g. most financial assets, investment properties, etc.).

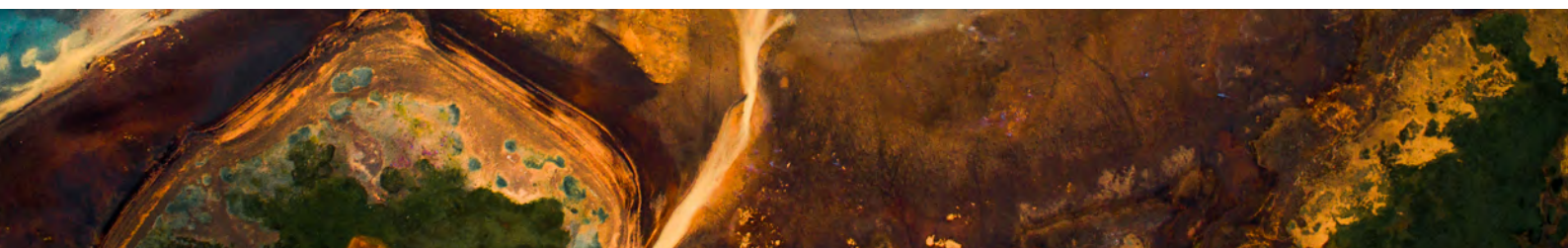
IFRS 18 does not consider the reason that a specific asset is held when it holds:

- ▶ cash and cash equivalents if an entity invests in financial assets as a main business activity, all income and expenses related to cash and cash equivalents are classified within the operating category (see section [3.9.1](#), *BDO Comment - entities that invest in financial assets as a main business activity but also have other main business activities*); and
- ▶ joint ventures and associates accounted for using the equity method, regardless of the main business activity, all specified income and expenses related to such investments are classified in the investing category (see section [3.2.4](#)).

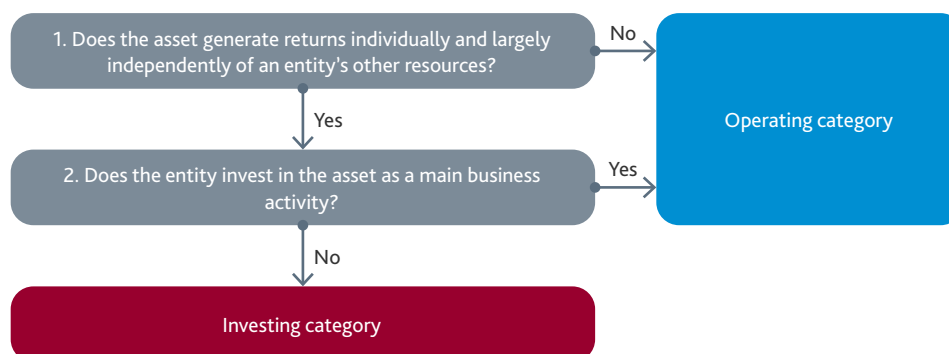
These restrictions were included in IFRS 18 to provide more useful information to the users of the financial statements (IFRS 18.BC111 and BC136).

However, for other assets, an entity considers the reason why an individual asset is held. Income and expenses related to assets that do not generate a return individually and largely independently of the entity's other resources will always be included in the operating category.

To classify income and expenses related to other assets, an entity should, in our view, assess if the asset generates returns individually and largely independent of an entity's other resources (IFRS 18.53(c)) and if not, whether the entity invests in that asset as a main business activity (IFRS 18.49 and B34).



The classification requirements of specified income and expenses related to 'other' assets are illustrated as follow:



3.8.1.4. Other assets that generate a return individually and largely independently of the entity's other resources

If an entity invests in assets as a main business activity, it classifies income and expenses relating to those assets in the operating category rather than the investing category (IFRS 18.58).

These types of assets typically include (IFRS 18.B46):

- ▶ Debt or equity investments; and
- ▶ Investment properties, and receivables for rent generated by those properties.

As noted in section 3.2, these income and expenses are:

Income and expenses (IFRS 18.54)	Common examples (IFRS 18.54 and B47)
(a) The income generated by the assets	▶ Interest ▶ Dividends ▶ Rental income
(b) The income and expenses that arise from the initial and subsequent measurement of the assets, including on derecognition of the assets	▶ Depreciation ▶ Impairment losses and reversal of impairment losses ▶ Fair value gains and losses
(c) The incremental expenses directly attributable to the acquisition and disposal of the assets	▶ Transaction costs on financial assets classified as fair value through profit or loss ▶ Costs to sell assets, such as broker commissions on financial instruments





BDO comment – multiple classes of assets

As noted in Example [3.7-1](#), an entity may invest in one or more classes of assets as a main business activity but not others. Said another way, an entity may only classify in the operating category income and expenses specified in IFRS 18.54 for assets that it invests in as a main business activity.

For example, an entity may invest in real estate as a main business activity but not financial assets. Therefore, it would classify income and expenses relating to its real estate assets (e.g. rental income, fair value gains and losses on investment property) in the operating category, but not income and expenses relating to its financial assets.

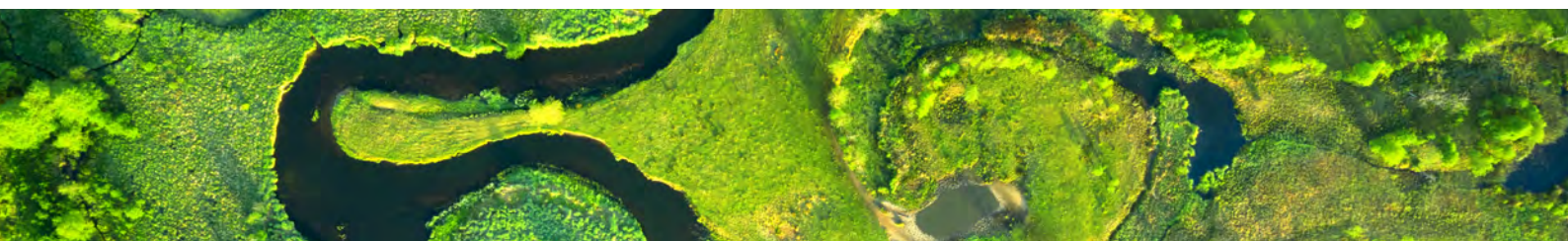
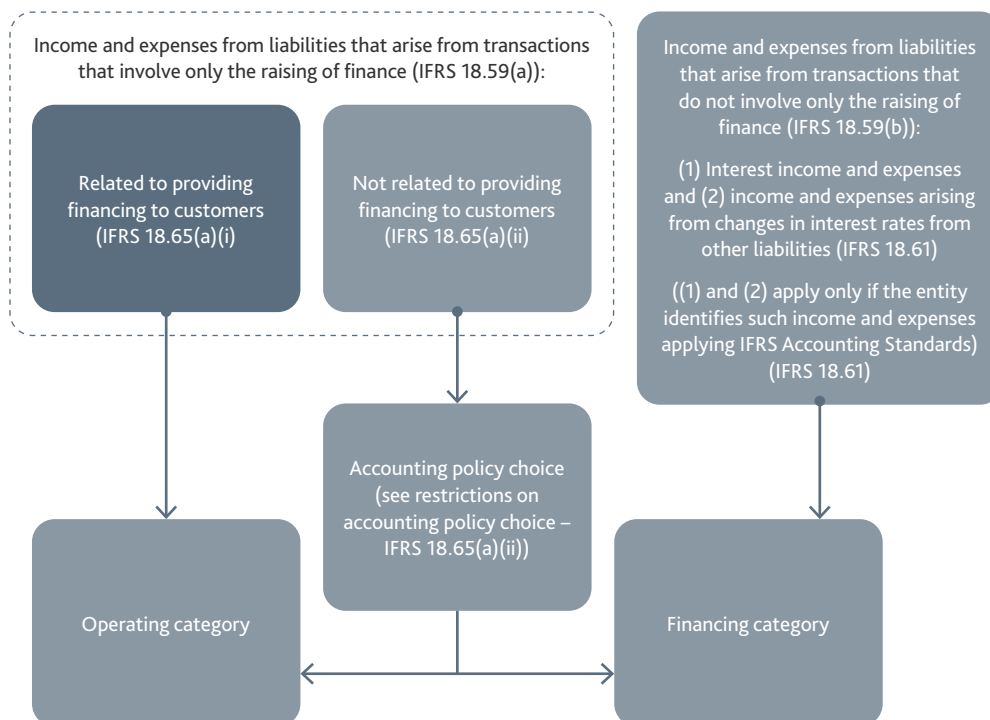
'Investing in assets' as a main business activity is not a binary classification for all asset classes, it is an assessment made for individual classes (or subclasses, see example 3.7-1) of assets, with the conclusion affecting the classification requirements applicable to classes of assets separately.

3.8.1.5. Other assets that do not generate a return individually and largely independently of the entity's other resources

For assets that do not generate a return individually and largely independently of the entity's other resources, associated income and expenses are classified in the operating category. See sections [3.2](#) and [3.8.1.3](#).

3.8.2. Providing financing to customers as a main business activity

If an entity provides financing to customers as a main business activity, the general classification requirements of IFRS 18 are modified. The classification requirements applicable to liabilities (and related income and expenses) are summarised as follows:



3.8.2.1. Liabilities that arise from transactions that involve only the raising of finance

For entities that provide financing to customers as a main business activity, liabilities that arise from transactions that involve only the raising of finance must be further sub-categorised into liabilities that (IFRS 18.65(a)):

- (i) Relate to providing financing to customers; and
- (ii) Do not relate to providing financing to customers.

For 'pure financing' liabilities that relate to providing financing to customers, associated income and expenses are always classified in the operating category.



BDO comment – classification of income and expenses from 'pure financing' liabilities that relate to providing financing to customers

If an entity provides financing to customers as a main business activity, then income and expenses related to liabilities that arise from transactions that involve only the raising of finance are classified in the operating category.

For example, banks and other lending institutions commonly receive loans from investors or other lenders and then lend those funds to the bank's customers with the goal of earning a margin on the interest rate differential between the loan payable and the loans receivable. If a lending institution borrows money in order to loan the proceeds to its customers, then that borrowing would be 'related to providing financing to customers'. Therefore, the income and expenses noted in IFRS 18.60 would be classified in the operating category in accordance with IFRS 18.65(a)(i):

- (a) income and expenses that arise from the initial and subsequent measurement of the liabilities, including on derecognition of the liabilities; and
- (b) the incremental expenses directly attributable to the issue and extinguishment of the liabilities—for example, transaction costs.

Determining whether liabilities are related to providing financing to customers may be challenging to determine in practice.

For 'pure financing' liabilities that do not relate to providing financing to customers, an accounting policy choice exists to classify the related income and expenses specified in IFRS 18.60 in either the operating category or the financing category (IFRS 18.65(a)(ii)). However, there are two restrictions on this accounting policy choice:

- ▶ if an entity cannot distinguish between the liabilities that relate to providing financing to customers and those that do not, an entity is required to classify income and expenses from all such liabilities in the operating category (IFRS 18.66).
- ▶ Consistency with IFRS 18.56(b)(ii): the accounting policy choice must be consistent with the accounting policy selected for the classification of income and expenses related to cash and cash equivalents for entities that provide financing to customers as a main business activity, do not invest in financial assets as a main business activity and where the income and expenses from cash and cash equivalents do not relate to providing financing to customers (IFRS 18.56(b)(ii)). See [3.9.1](#) for further information on classifying income related to cash and cash equivalents.



BDO comment – accounting policy choice in IFRS 18.56(b)(ii) and effect on the classification of income and expenses arising from certain derivatives (IFRS 18.B59)

The accounting policy selected above applies to the classification of all income and expenses relating to 'pure financing' liabilities that do not relate to providing financing to customers as well as gains and losses on certain derivative financial instruments (see section [3.9.2](#)) if:

- (1) a derivative is used for purposes other than managing identified risks;
- (2) the derivative is related to a transaction that involves only the raising of finance;
- (3) the entity provides financing to customers as a main business activity; and
- (4) the derivative does not relate to providing financing to customers.

The accounting policy selected above for 'pure financing' liabilities that do not relate to providing financing to customers affects the classification of gains and losses on certain derivatives because IFRS 18.B73(a) and B59

requires consistency in how income and expenses from derivatives are classified if those derivatives have the four characteristics noted in the preceding paragraph. Therefore, if an entity elected to present income and expenses from all 'pure financing' liabilities in the operating category, the entity would also present income and expenses from derivatives that have the four characteristics noted above in the operating category as well.

See section [3.9.2](#) for discussion of this accounting policy choice as it relates to gains and losses on certain derivative financial instruments.



Example 3.8.2-1 – consistency of accounting policy choice for the classification of income and expenses related to (1) 'pure financing' liabilities that do not relate to providing financing to customers; and (2) cash and cash equivalents

Applying the requirement of IFRS 18.56(b)(ii) to ensure a consistent accounting policy choice may be challenging to understand, therefore, this worked example demonstrates the requirements.

Fact pattern

Entity G provides financing to customers as a main business activity, as it sells farm equipment and provides extended financing terms to customers. Entity G holds cash and cash equivalents and earns interest income on those assets; however, Entity G does not invest in financial assets as a main business activity and the income and expenses arising from cash and cash equivalents does not relate to providing financing to customers.

To finance its operations, Entity G has several bank loans. Some of the bank loans are specific to providing financing to customers, and others are not. Entity G is able to distinguish between the liabilities that relate to providing financing to customers and those that do not. In accordance with IFRS 18.65(a)(i), Entity G classifies income and expenses on the bank loans that are specific to providing financing to customers in the operating category.

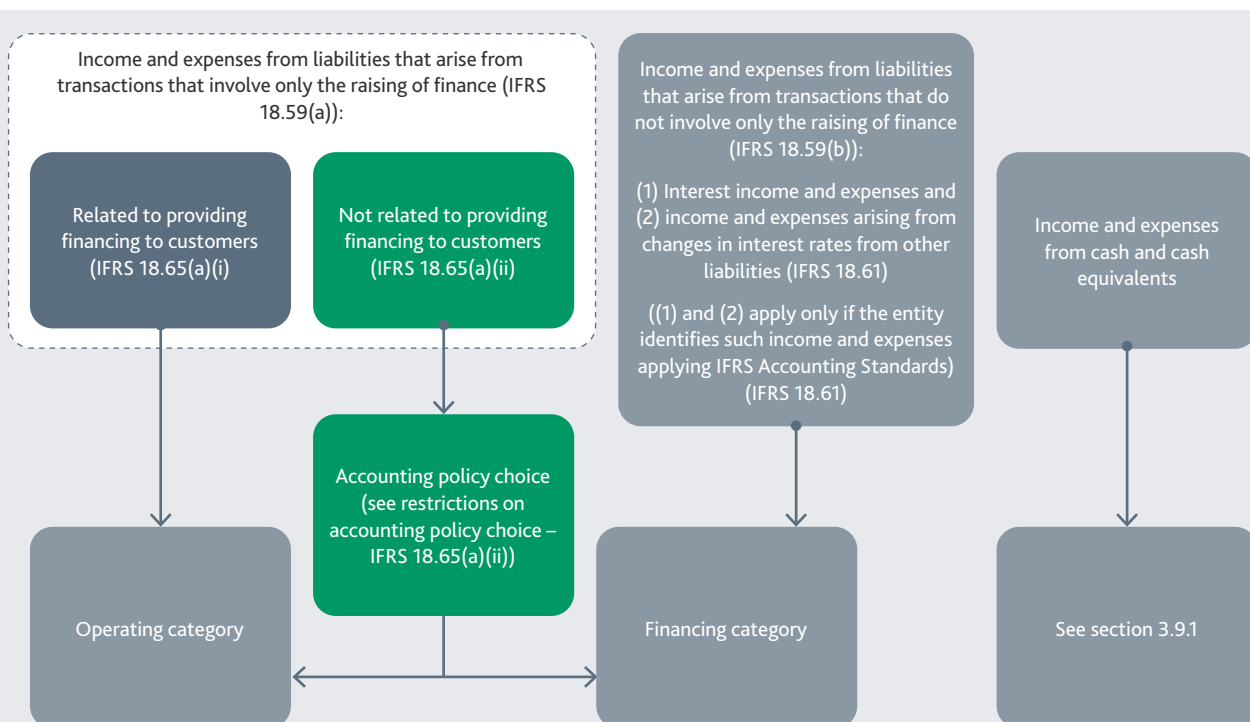
Entity G is assessing how it may classify income and expenses relating to its bank loans that are not specifically related to providing financing to customers.

Assessment

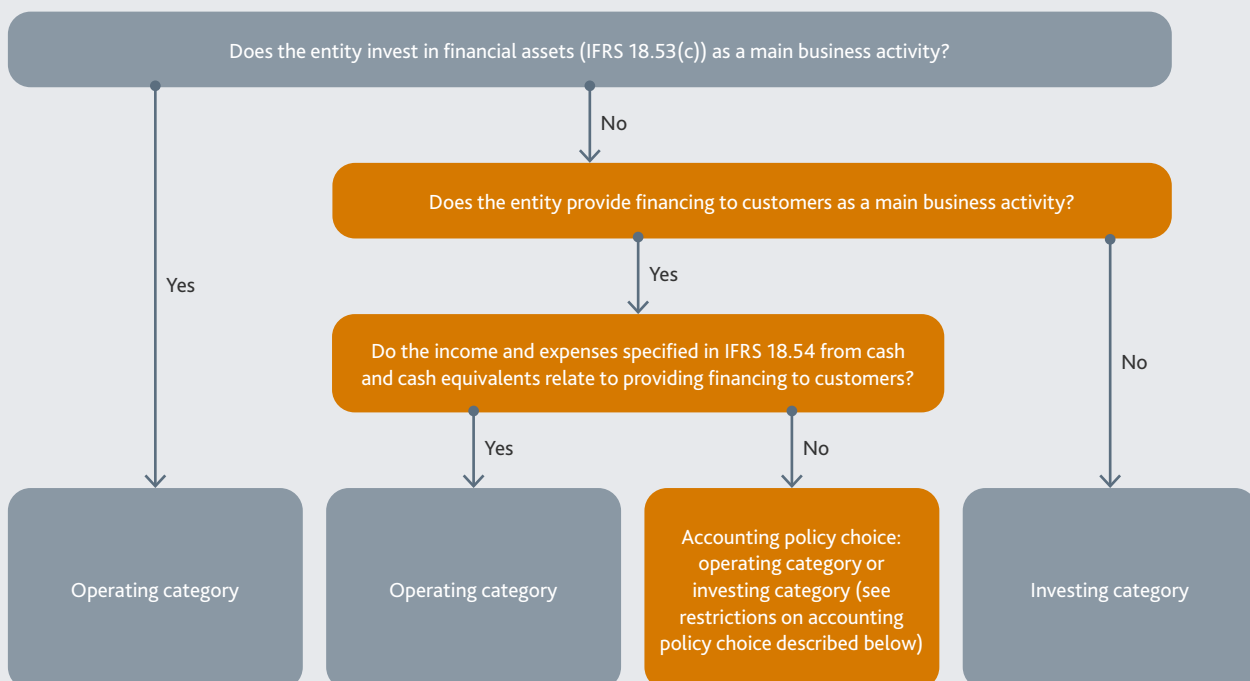
For the bank loans that are not specifically related to providing financing to customers, Entity G has an accounting policy choice to make concerning how related income and expenses are classified. Entity G is able to distinguish between the liabilities that relate to providing financing to customers and those that do not (IFRS 18.66), therefore, it may select either the operating category or financing category.

Entity G's application of the classification flowchart for income and expenses for entities that provide financing to customers as a main business activity is as follows, with the 'non-customer specific' bank loans in green:





At the same time, Entity G must also select an accounting policy relating to how it classifies income and expenses arising from cash and cash equivalents. Entity G's application of the classification flowchart for income and expenses from cash and cash equivalents (see section [3.9.1](#)) is as follows, with Entity G's assessment in orange:



Because of its particular facts and circumstances, Entity G now has a choice of classifying income and expenses relating to:

- ▶ 'Pure financing' liabilities not related to providing financing to customers in the operating or financing category; and
- ▶ Cash and cash equivalents in the operating or investing category.

In accordance with IFRS 18.56(b)(ii), this accounting policy choice must be consistent, meaning, if Entity G classifies income and expenses relating to the 'pure financing' liabilities not related to providing financing to customers in the operating category, it must make the same accounting policy choice for income and expenses relating to cash and cash equivalents.

If Entity G selected the financing category for 'pure financing' liabilities not related to providing financing to customers in the financing category (i.e. not the operating category), Entity G must classify income and expenses relating to cash and cash equivalents in the investing category.

Accounting policy choice for entities with more than one main business activities

Entities may have different specified main business activities within a group structure. For example, Entity G in this example may have another operation within its reporting structure that does not provide financing to customers as a main business activity – e.g. a retailer operation. This raises the question of whether Entity G can select different accounting policies as described above for different operations. For example, classify the income and expenses from cash and cash equivalents from the farm equipment operations in the operating category, but the similar income and expenses for the retailer operation in the investing category.

In our view, Entity G must apply a single accounting policy choice (as required by IFRS 10.B87), and cannot select one classification for the farm equipment operation and another for the retailer operation. This means that if, for example, Entity G decided to classify all of the income and expenses from 'non-customer specific' bank loans in the operating category, and consequently also classified income and expenses from cash and cash equivalents in the operating category, then this accounting policy choice applies to the entire reporting entity. Therefore, any income and expenses from cash and cash equivalents held by the retailer operation would also be classified in the operating category.

This differs from the fact that an entity may determine that it invests in assets as a main business activity differently in a single reporting entity (see Example 3.7-1). This is because accounting policy choices must be applied consistently for the reporting entity as a whole. Additionally, the requirement in IFRS 18.56(b)(ii) refers to 'the income and expenses from cash and cash equivalents that do not relate to providing financing to customers', which in our view, refers to all of those cash and cash equivalents held by the entity.

3.8.2.2. Liabilities that arise from transactions that do not involve only the raising of finance ('other liabilities')

For other liabilities, income and expenses are classified into the operating and financing categories based on the general requirements of IFRS 18 (see section 3.3). No exceptions exist for entities that provide financing to customers as a main business activity.

Therefore, for example, an entity that provides financing to customers as a main business activity would classify interest expense relating to lease liabilities in the financing category. See section 3.3 for other examples of the classification of income and expenses relating to 'other liabilities'.

3.8.2.3. Cash and cash equivalents

See section 3.9.1 for the requirements applicable to classifying income and expenses relating to cash and cash equivalents.

In summary, if an entity provides financing to customers as a main business activity but does not invest in financial assets as a main business activity, the entity may have an accounting policy choice to make concerning the classification of income and expenses relating to cash and cash equivalents subject to the restriction mentioned in section 3.9.1.

3.9. Considerations for specific items of income and expense

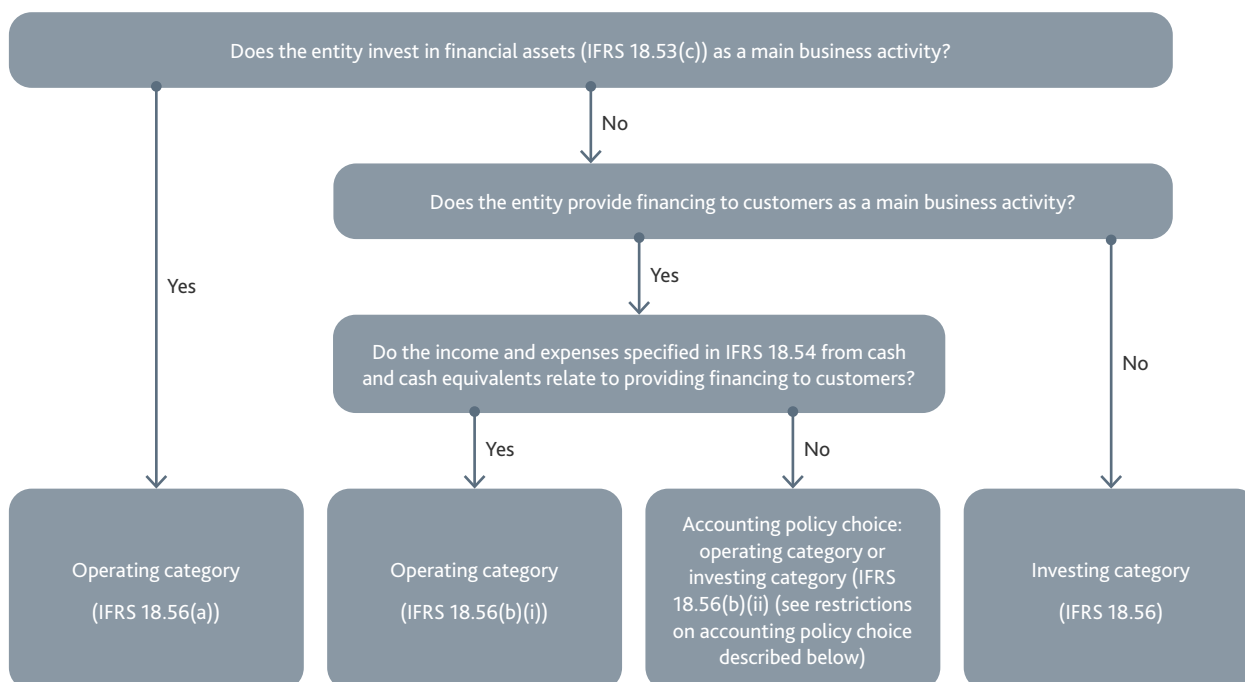
This section addresses specific requirements for classification income and expense related to the following assets where the general requirements discussed in section 3.1-3.8 do not apply:

- ▶ Cash and cash-equivalent (see section 3.9.1)
- ▶ Derivatives (see section 3.9.2)
- ▶ Foreign exchange differences (see section 3.9.3)
- ▶ Hybrid contracts (see section 3.9.4)

Section [3.9.5](#) addresses the classification requirements of IFRS 18 applicable to specific income and expenses where no specific rules apply, but the application of IFRS 18's requirements are illustrated.

3.9.1. Cash and cash equivalents

The classification requirements for income and expenses relating to cash and cash equivalents (e.g. interest income) are summarised as follows:



In summary:

- ▶ An entity that invests in financial assets as a main business activity will always classify income and expenses related to cash and cash equivalents in the operating category (IFRS 18.56(a)). This conclusion remains unchanged even if an entity invests in financial assets as a main business activity and it provides financing to customers as a main business activity (i.e. it has more than a single specified main business activity).
- ▶ If an entity does not invest in financial assets as a main business activity and does not provide financing to customers as a main business activity, income and expenses related to cash and cash equivalents will always be classified in the investing category (IFRS 18.56).
- ▶ Where an entity does not invest in financial assets as a main business activity, but does provide financing to customers as a main business activity, it must determine if the income and expenses related to cash and cash equivalents relate to providing financing to customers (IFRS 18.56(b)):
 - If they do, income and expenses are classified in the operating category (IFRS 18.56(b)(i)).
 - If they do not, an accounting policy choice exists to classify income and expenses either in the operating or the investing category, subject to two restrictions (see below) (IFRS 18.56(b)(ii)).

The accounting policy choice noted above is subject to two restrictions:

1. It must be consistent with the accounting policy choice selected for 'pure financing' liabilities that do not relate to providing financing to customers, which is discussed in section [3.8.2](#), see [Example 3.8.2-1](#).
2. If an entity cannot distinguish between cash and cash equivalents that relate to providing finance to customers and those that do not, an entity is required to classify income and expenses from all cash and cash equivalents in the operating category (IFRS 18.57).



BDO comment – entities that invest in financial assets as a main business activity but also have other main business activities

As discussed in Example 3.7-1, entities may invest in financial assets as a main business activity (e.g. banking operations) but also have other main business activities (e.g. retail operations). This raises the question of whether such an entity must classify all of the income and expenses from its cash and cash equivalents in the operating category in accordance with IFRS 18.56(a), or whether the income and expenses from cash and cash equivalents held in operations that do not invest in financial assets as a main business activity may be classified in the investing category.

In our view, 'splitting' the classification of income and expenses relating to cash and cash equivalents is not in accordance with the requirements of IFRS 18. If an entity invests in financial assets as a main business activity, IFRS 18.56(a) requires that all income and expenses from cash and cash equivalents should be classified in the operating category. IFRS 18.BC136 explains that entities that invest in financial assets as a main business activity holds large amounts of cash and cash equivalents for operating purposes and continuously rebalances their investment portfolios. The IASB determined that, for these entities, all income and expenses related to cash and cash equivalents are to be classified in the operating category.

Additionally, in our view, the precise wording of IFRS 18.56 indicates that the classification of income and expenses relating to cash and cash equivalents in the operating category applies to all such income and expenses as long as an entity invests in financial assets as a main business activity.



BDO comment – unit of account for accounting policy choice – income and expenses from cash and cash equivalents when an entity provides financing to customers as a main business activity (IFRS 18.56(b)(ii))

The accounting policy choice in IFRS 18.56(b)(ii) described above is only relevant if any entity (1) does not invest in financial assets as a main business activity; and (2) provides financing to customers as a main business activity. This raises the question of whether it is possible for an entity to hold cash and cash equivalents for more than one business activity – essentially, must the entity apply the accounting policy choice in IFRS 18.56(b)(ii) for the entire reporting entity, or may it be applied to a lower unit of account?

For example, assume that an entity has two separate bank accounts for two separate main business activities:

- ▶ Farm equipment sales: the entity provides financing to customers as a main business activity, but does not invest in financial assets as a main business activity, meaning the accounting policy choice in IFRS 18.56(b)(ii) is relevant (for income and expenses specified in IFRS 18.54 from cash and cash equivalents that do not relate to providing financing to customers); and
- ▶ Retail operations: the entity operates retail locations, selling fertilizer and other farm supplies.

Both main business activities operate independently from each other.

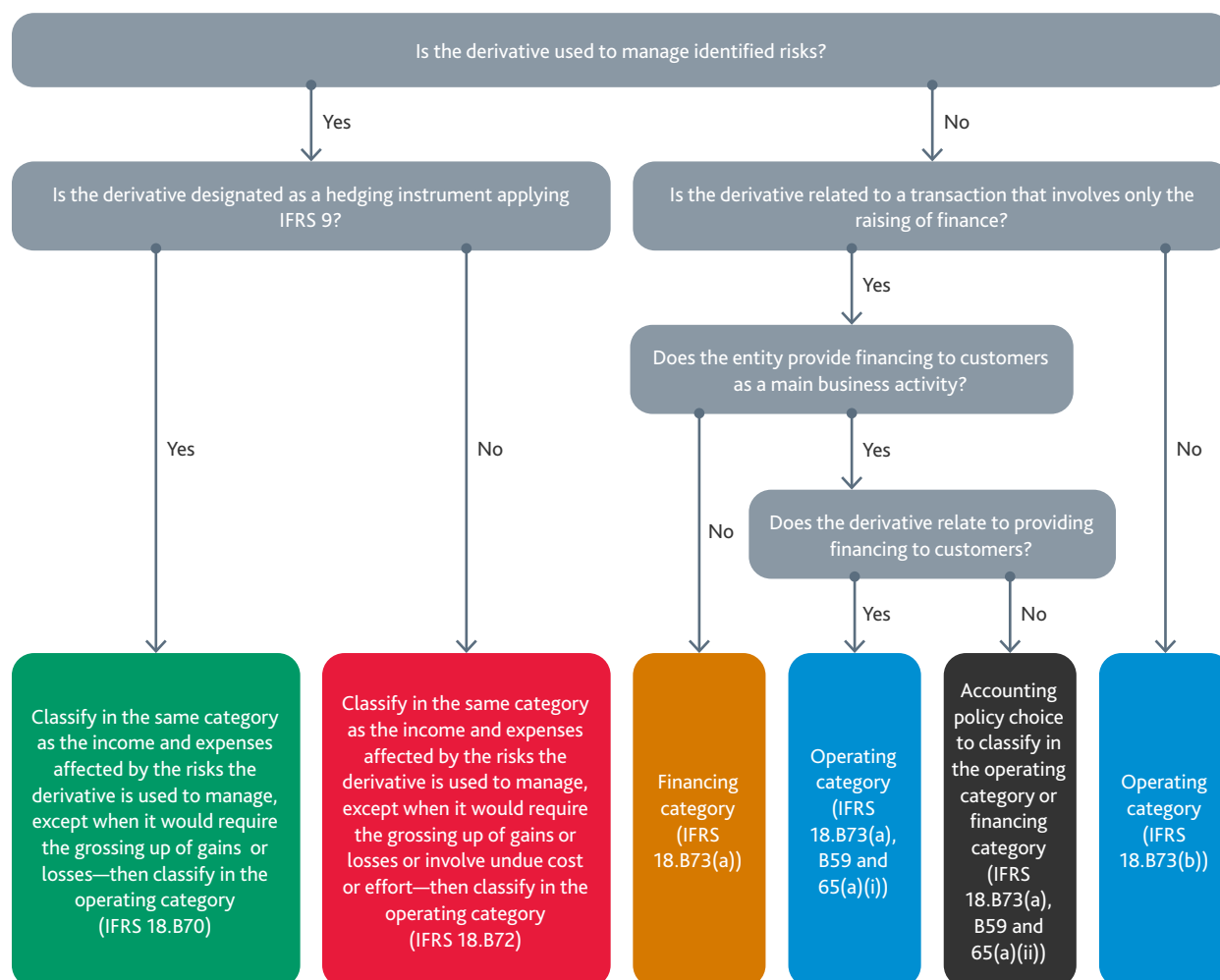
The question is: can the entity elect to apply the accounting policy choice in IFRS 18.56(b)(ii) for its farm equipment sales business in one way, and use a different classification for income and expenses from cash and cash equivalents for its retail operations? For example, can the farm equipment sales business elect to present the income and expenses from cash and cash equivalents in the operating category as per IFRS 18.56(b)(ii), with the retail operation classifying the income and expenses from its cash and cash equivalents in the investing category (IFRS 18.53(b))?

In our view, this is not in accordance with the requirements of IFRS 18. Accounting policy choices must be uniform for an entity as a whole (unless otherwise specified in an IFRS Accounting Standard). IFRS 18.56(b)(ii) applies to the income and expenses from cash and cash equivalents that do not relate to providing financing to customers for the entire reporting entity – the farm equipment sales and the retail operations, therefore, a single accounting policy choice is to be applied for all such income and expenses. Consequently, the entity must classify all income and expenses from cash and cash equivalents in the operating or investing category as per IFRS 18.56(b)(ii).

3.9.2. Gains and losses on derivatives and designated hedging instruments

The classification requirements for income and expenses relating to derivatives and designated hedging instruments are summarised as follows:

Gains and losses on derivatives and designated hedging instruments (IFRS 18.B70-B76)



The flowchart is explained in the following sub-sections.

3.9.2.1. Derivatives used to manage identified risks

Derivative contracts may be used to manage identified risks, such as:

Derivative financial instrument	Identified risk that may be managed
Interest rate swap that swaps fixed interest payments for variable or vice versa	Interest rate risk
Foreign currency forward contract to buy or sell foreign currency at a future date at a fixed exchange rate	Foreign currency risk
Option contract to sell an equity instrument at a pre-determined price in the future	Other price risk

Derivatives may be designated as hedging instruments in a qualifying hedge accounting relationship in IFRS 9, or they may not. Regardless of whether hedge accounting is applied, gains and losses included in the statement of profit or loss

are generally classified in the same category as the income and expenses affected by the risks the financial instrument is used to manage (IFRS 18.B70). The ineffective portion of a gain or loss is also reflected in the same category as the effective portion (IFRS 18.B71).

Gains and losses are not classified in the same category as the income and expenses affected by the risks when hedge accounting is not applied and (i) doing so would require the grossing up of gains or losses; or (ii) doing so would involve undue cost or effort. If either (i) or (ii) apply, then all gains and losses are instead classified in the operating category (IFRS 18.B72).

The undesignated component of a designated hedging instrument has its gains and losses recorded in the same category as the gains and losses on the designated component (IFRS 18.B71).

For example, if an interest rate swap is used to manage interest rate risk on a bank loan that arises from transactions that involve only the raising of finance, the gains and losses recognised in profit or loss relating to that swap are classified in the financing category to 'match' where income and expenses related to the bank loan are classified in accordance with IFRS 18.60. This 'matching' occurs regardless of whether the entity applies hedge accounting, as long as the derivative is used to manage identified risks (IFRS 18.B70, B72). Any ineffective portion would also be classified in the financing category (IFRS 18.B71).

3.9.2.2. 'Grossing up' of gains and losses on derivatives used to manage identified risks

The 'matching' of the gains and losses on derivatives recognised in profit or loss with the classification of the income and expenses affected by the financial instrument used to manage that risk is required unless in order to achieve this effect, the entity would be required to 'gross up' gains and losses. If this is the case, all such gains and losses on the derivative are classified in the operating category (IFRS 18.B70).

Grossing up of gains and losses might arise from situations in which (IFRS 18.B74):

- ▶ An entity uses such financial instruments to manage the risks of a group of items with offsetting risk positions (see IFRS 9.6.6.1 for the criteria for a group of items to be an eligible hedged item); and
- ▶ The risks managed affect line items in more than one category of the statement of profit or loss.

For example, an entity may use a derivative to manage both the net currency risk on revenue (classified in the operating category) and interest expense (classified in the financing category). In such cases, presenting gain or loss on the derivative in each category would result in grossing up gains and losses, as an entity would present a larger gain or loss in each category than the gain or loss that occurred on the derivative (IFRS 18.B75).

3.9.2.3. Derivatives used for purposes other than managing identified risks

Entities may hold derivatives that are not used to manage identified risks. For example, an entity may:

- ▶ Issue share purchase warrants on their own equity instruments which fail the 'fixed for fixed' test in IAS 32, and are therefore measured at fair value through profit or loss.
- ▶ Hold and/or issue derivatives as part of trading activities with an aim of earning profit rather than managing specific risk exposures. This may be common for banks and financial institutions.

If derivatives are used for purposes other than managing identified risks and they are not related to a transaction that involves only the raising of finance, gains and losses must be classified in the operating category (IFRS 18.B73(b)).

If derivatives are used for purposes other than managing identified risks and they are related to a transaction that involves only the raising of finance, two further assessments are necessary:

- ▶ If the entity does not provide financing to customers as a main business activity, then gains and losses are classified in the financing category (IFRS 18.B73(a)), which for example, results in those gains and losses 'matching' the interest income and expenses arising from the liabilities related to transactions that involve only the raising of finance (IFRS 18.60).
- ▶ If the entity does provide financing to customers as a main business activity:
 - If the derivative does relate to providing finance to customers, gains and losses are classified in the operating category (IFRS 18.B73(a)).
 - If the derivative does not relate to providing finance to customers, the entity has an accounting policy choice of classifying gains and losses in the operating or financing category (IFRS 18.65(a)(ii)).



BDO comment – accounting policy choice in IFRS 18.65(a)(ii) available to entities that provide financing to customers as a main business activity

As noted above, if (1) a derivative is used for purposes other than managing identified risks; (2) the derivative is related to a transaction that involves only the raising of finance; (3) the entity provides financing to customers as a main business activity; and (4) the derivative does not relate to providing financing to customers; then an entity has an accounting policy choice to classify gains and losses in the operating or financing category (IFRS 18.65(a)(ii)).

This accounting policy choice is the same as the one discussed in section [3.8.2](#), where for 'pure financing liabilities', an entity that provides financing to customers as a main business activity may classify income and expenses on liabilities that do not relate to providing financing to customers in either the operating or financing category.

As this is the same accounting policy choice, an entity must be consistent. Therefore, two different classes of income and expenses must be classified consistently for entities that provide financing to customers as a main business activity:

- ▶ Gains and losses on derivatives where the accounting policy election described above is available; and
- ▶ Other income and expenses (e.g. interest expense) on 'pure financing liabilities' that do not relate to providing financing to customers.

All income and expenses for the two classes of transactions must be classified consistently: all such expenses in the operating category or the financing category.

Additionally, as this is a single accounting policy choice, this choice is subject to the restrictions noted in section 3.8.2 concerning consistency in the policy selected for the classification of cash and cash equivalents (see sections [3.8.2](#) and [3.9.1](#)).



3.9.3 Foreign exchange differences

Foreign exchange differences are included in profit or loss when a monetary item is denominated in a currency other than the entity's functional currency. For example, if an entity has the Euro as its functional currency but holds trade receivables denominated in US dollars, foreign exchange gains and losses will be recognised in profit or loss in accordance with IAS 21.

Foreign exchange differences included in profit or loss applying IAS 21 are classified in the same category as the income and expenses from the items that give rise to the foreign exchange differences, unless doing so would involve undue cost or effort (IFRS 18.B65).

For example, an entity classifies foreign exchange differences as follows (IFRS 18.B66):

Source of foreign exchange difference	Explanation
A trade receivable denominated in a foreign currency	Operating category, as trade receivables are assets that do not generate a return individually and largely independently of the entity's other resources, meaning associated income and expenses are classified in the operating category.
Liabilities that arise from transactions that involve only the raising of finance such as a loan payable (the entity does not provide financing as a main business activity)	Financing category, as that matches the income and expenses arising from the debt (e.g. interest expense).

Judgement is required to determine the amount of foreign exchange differences that should be classified in different categories.

3.9.3.1. Income and expenses classified in more than one category

While IFRS 18.B65 requires that foreign exchange differences be classified in the same category as the related income and expenses, this guidance is challenging to apply to income and expenses related to liabilities that arise from transactions that do not involve only the raising of finance, as income and expenses from such transactions may be included in both the operating and investing categories. For example, a lease liability will result in some income and expenses being classified in the financing category (e.g. finance expense) and other income and expenses in the operating category (e.g. gains or losses on the modification of the lease liability which result in a decrease in scope). Consequently, IFRS 18.B67 was introduced to clarify the classification of these foreign exchange differences, given that the related item (e.g. certain liabilities) may have income and expenses classified in both the operating and financing categories.

For example, an entity may enter into a service agreement (e.g. consulting services) denominated in a foreign currency with a supplier to pay the supplier on deferred terms (e.g. the first 6 months of services paid over 18 months). This transaction would give rise to two elements:

1. The service expenses, which would generally be classified in the operating category as service is provided over the 6-month period; and
2. The finance expense due to the deferred credit terms, which would be classified in the financing category because the resulting liability does not arise from transactions that involve only the raising of finance and the finance expense arising from the deferred payment terms are interest expense identified by applying IFRS Accounting Standards (IFRS 18.61).

This transaction would also give rise to foreign exchange differences in the scope of IAS 21 because it is denominated in a foreign currency. Therefore, foreign exchange differences would arise because of the difference between when the financial liability is recognised at the date services are provided and when the financial liability is settled.

IFRS 18.B67 requires an entity to exercise judgement to determine how to classify these foreign exchange differences (i.e. in the operating category or the financing category). The classification of foreign exchange differences described in this paragraph is not an accounting policy choice, but the result of the application of judgement. After that judgement is applied, all foreign exchange differences relating to that liability (and similar liabilities) must be classified in that single category.



BDO comment – considerations when making the judgement in IFRS 18.B67

IFRS 18.B67 states that an entity should exercise judgement to determine whether foreign exchange differences related to transactions not solely involving the raising of finance should be classified within the operating or financing category. However, the standard does not provide additional guidance on the factors that entities should consider when making this judgement.

In our view, an entity should consider all relevant facts and circumstances when assessing the most appropriate classification of foreign exchange differences. Factors to consider might include but are not limited to:

Factor	Comment
Main driver of expense	It might be more appropriate to classify foreign exchange differences in the same category as the main driver of the expense relating to the liability – that is, where the majority of income and expenses relating to the liability are classified. For example, in most cases, the finance expense is the most significant expense related to lease liabilities, therefore it might be more appropriate to classify the related foreign exchange difference in the same category as the finance expense - the financing category. In contrast, defined benefit obligations may have a more significant amount of the related income and expenses classified in the operating category (current service expense) rather than the finance expense on the obligation. Therefore, it might be more appropriate to classify the related foreign exchange difference in the same category as the current service expense - the operating category.
Duration of liability	The longer the duration of the liability, the greater the financing component is, indicating that it might be more appropriate to classify the related foreign exchange differences in the financing category. For example, if a lease is for a period of 15 years, it may indicate that the decision to lease the asset was a financing decision, meaning the associated foreign exchange differences should be classified in the financing category.

3.9.3.2. Undue cost or effort

If applying these requirements would involve undue cost or effort, an entity is required to classify the affected foreign exchange differences entirely in the operating category (IFRS 18.B68). This assessment of 'undue cost or effort' is not made for the reporting entity as a whole (i.e. all foreign exchange differences), but for each item that gives rise to foreign exchange differences.



BDO comment – effect on systems and process

Many entities' systems will not be designed to capture the information required by IFRS 18 for the classification of foreign exchange differences. Entities may have captured foreign exchange differences in a single line item in the statement of profit or loss previously, while some entities may have recorded exchange differences relating to financing (e.g. bank loans) as part of 'finance costs'.

The work effort involved to apply these new requirements will differ from entity to entity. 'Undue cost or effort' is generally considered to be a high threshold, meaning that an entity is not permitted to simply classify all foreign exchange differences in the operating category by virtue of there being costs associated with modifying their systems and processes to comply with the requirements of IFRS 18.

See section [7.5.2](#) for further systems and process related considerations regarding IFRS 18

3.9.3.3. Hyperinflationary entities – the net monetary position

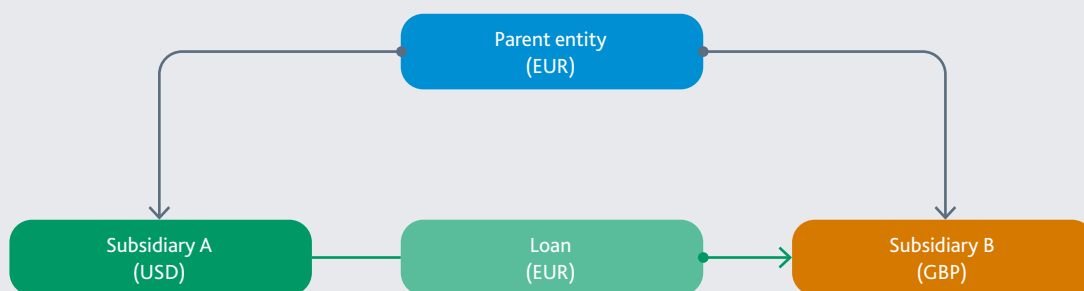
Entities that apply IAS 29 *Financial Reporting in Hyperinflationary Economies* may present the gain or loss on the net monetary position with other income and expense items associated with the net monetary position (e.g. interest income and expenses and foreign exchange differences). If an entity does not present the gain or loss on the net monetary position in this manner, it must be classified in the operating category (IFRS 18.B69).

3.9.3.4. Foreign exchange differences relating to intercompany loan arrangements

Foreign exchange differences that arise from intercompany balances between a parent company and its subsidiaries, as well as among fellow subsidiaries, present a classification issue. This is because, while intercompany balances and transactions are eliminated in the consolidated financial statements, the eliminated loans result in foreign exchange differences that are not eliminated in the consolidated financial statements. This is because the monetary item represents a commitment to convert one currency into another and exposes the reporting entity to a gain or loss through currency fluctuations (IAS 21.45).



Example 3.9.3-1 – classification of foreign exchange differences on intercompany loans



Subsidiary A and Subsidiary B forms part of the same group. Subsidiary A's functional currency is USD and Subsidiary B's is GBP. The parent entity's functional currency is Euro.

Subsidiary A issued a loan to Subsidiary B. The loan is denominated in Euro and is repayable in monthly instalments over 24 months (including interest).

Classification of income and expenses in the separate financial statements

Subsidiary A classifies the income and expenses (including the related foreign exchange differences) related to the loan in the investing category. Subsidiary B classifies the income and expenses (including the related foreign exchange differences) related to the loan in the financing category.

Classification of foreign exchange differences in the consolidated financial statements

When the parent entity consolidates Subsidiaries A and B, it eliminates both the loan receivable and loan payable as well as the intercompany interest income and expense between Subsidiary A and Subsidiary B. However, the foreign exchange differences recognised in profit or loss by the subsidiaries are not eliminated.

This raises the question in which category these foreign exchange differences should be classified.

This issue was raised to the IFRS Interpretations Committee at its September 2025 meeting. As at the date of publishing, the IFRS Interpretations Committee had yet to publish a final agenda decision, however, in their tentative agenda decision, two views arose:

- ▶ The foreign exchange differences should be classified in the operating category as the default category in accordance with IFRS 18.52; and
- ▶ The foreign exchange differences should be classified in the same category in which the income and expenses from the intragroup loan would have been classified before their elimination on consolidation, or, if doing so would involve undue cost or effort, in the operating category.

All members of the Committee agreed on the first view. The Committee was however split on the second view and therefore the Committee did not conclude on the matter in their tentative agenda decision.

Please refer to the related [IFRS Foundation work plan page](#) for up to date information on this issue.

3.9.4 Hybrid contracts containing a host that is a liability

Hybrid contracts containing a host that is a liability may include, for example:

- ▶ Convertible notes with conversion options that are not closely related to the host contract;
- ▶ Lease liabilities with embedded derivatives not closely related to the host contract; and
- ▶ Insurance contract liabilities with embedded derivatives not closely related to the host contract.

The embedded derivatives may either be separated or if certain criteria are met, an entity may elect to measure the entire hybrid instrument at fair value through profit or loss (IFRS 9.4.3.5). Hybrid contracts may also not have the embedded derivative accounted for separately from the host contract if the embedded derivative is considered closely related to the host contract.

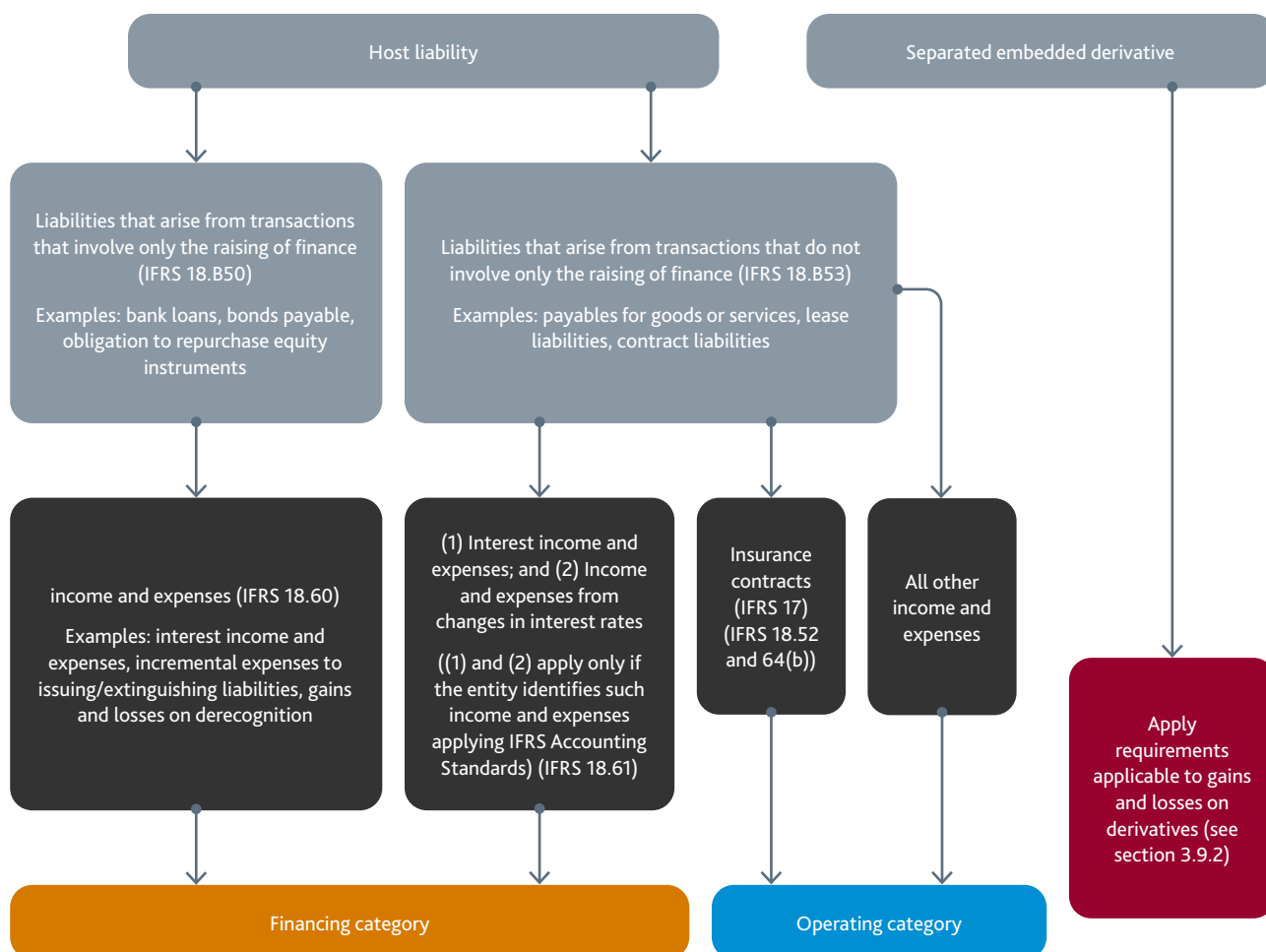
IFRS 18.B56-B57 set out detailed classification requirements applicable to income and expenses related to hybrid contracts containing a host liability, with the primary distinction being whether the embedded derivative is separated from the host liability or not.



3.9.4.1. Hybrid contracts containing a host liability – embedded derivative is separated from the host liability (IFRS 18.B56(a))

The classification requirements for income and expenses relating to hybrid contracts containing a host liability where the embedded derivative is separated are summarised as follows (assuming that the entity does not provide financing to customers as a main business activity):

Income and expenses from hybrid contracts with host liabilities – embedded derivative is separated from the host liability (entities that do not provide financing to customers as a main business activity)



In summary, income and expenses relating to the hybrid instrument are classified separately for the host liability and the separated embedded derivative(s):

- ▶ The general requirements of IFRS 18 apply in classifying income and expenses relating to host liabilities. This flowchart summarises the same requirements as described in section 3.3, meaning that they assume that an entity does not provide financing to customers as a main business activity. If an entity does provide financing as a main business activity, it must apply the requirements described in section 3.8.2 to the host liability.
- ▶ The requirements applicable to derivatives apply to the embedded derivative that is separated from the host liability (see section 3.9.2).

These requirements are consistent with the fact that when an embedded derivative is separated from the host contract, the two components (the host liability and the embedded derivative) are accounted for separately from one another. Therefore, the classification requirements of IFRS 18 apply to those two components separately.



Example 3.9.4-1 – classification of income and expenses arising from a convertible note – embedded derivative is separated from the host liability

Fact pattern

Entity M issues a convertible note where the principal of the loan may be converted into Entity M's equity instruments at the option of the holder at any time. The conversion option does not meet the 'fixed for fixed' criterion because the currency of the note differs from the functional currency of Entity M, meaning that the amount of 'cash' that would be settled upon conversion is not fixed in the functional currency of Entity M. Entity M does not elect to use the fair value option in IFRS 9.4.3.5.

Entity M does not provide financing to customers as a main business activity.

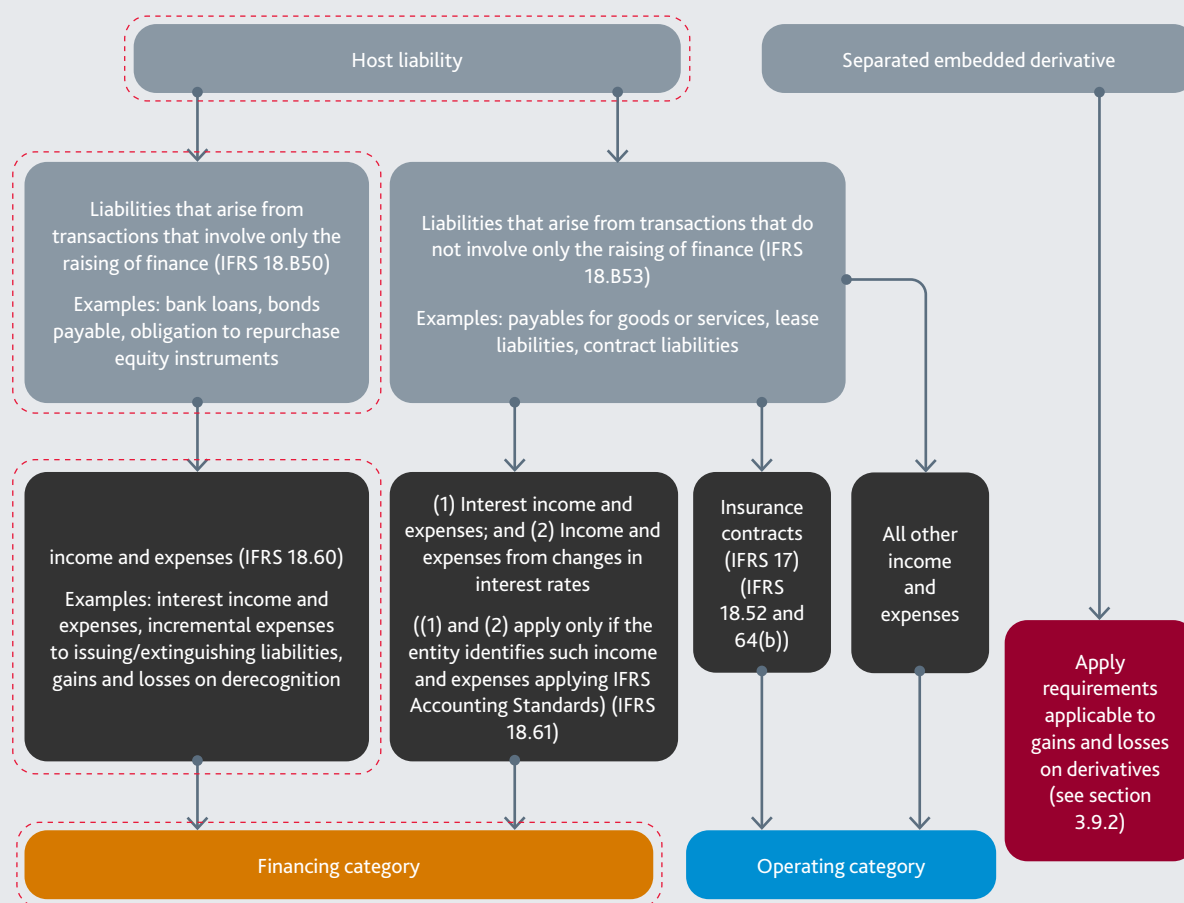
Entity M separates the embedded derivative from the host contract at initial recognition, as it does not elect to use the fair value option. The host liability is measured at amortised cost and the embedded derivative is measured at fair value through profit or loss.

During the reporting period where the convertible note remains outstanding, the host liability and the embedded derivative give rise to the following income and expenses:

Component	Income and expenses
Host liability	Interest expense accounted for applying the effective interest method (IFRS 9)
Embedded derivative (conversion option)	Fair value gains and losses (IFRS 9)

Assessment – host liability

Entity M classifies the interest expense relating to the host liability as follows (the relevant assessment is circled in red dotted lines using the classification flowchart from earlier in this section):



Explanation:

- ▶ The host liability is a liability that arises from a transaction that involves only the raising of finance because Entity M receives finance in the form of cash and will return cash or its own equity instruments in exchange at a later date (IFRS 18.B50).
- ▶ Income and expenses that arise from the initial and subsequent measurement of that liability are therefore classified in the financing category (IFRS 18.60).

Assessment – embedded derivative

Entity M classifies the fair value gains and losses relating to the embedded derivative conversion option as follows (the relevant assessment is circled in red dotted lines using the classification flowchart from section 3.9.2, which addresses the classification of gains and losses on derivatives):

Gains and losses on derivatives and designated hedging instruments (IFRS 18.B70-B76)



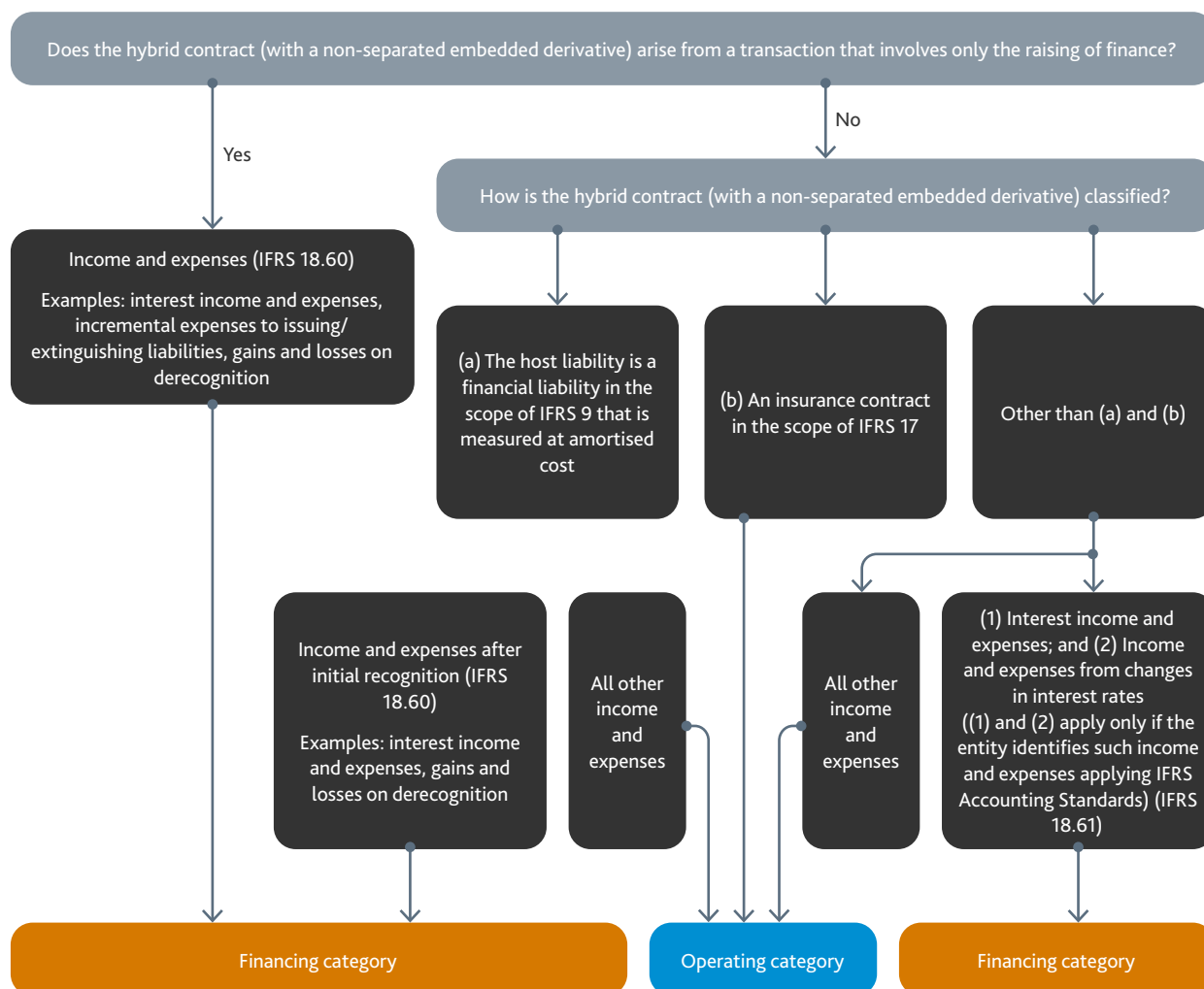
Explanation:

- ▶ The embedded derivative conversion option is not used to manage identified risks (e.g. foreign currency or interest rate risk).
- ▶ The derivative relates to a transaction that involves only the raising of finance, as the derivative is embedded in a host liability that is considered to be a liability that arises from transactions that involve only the raising of finance. See the section immediately above which explains this classification of the host liability.
- ▶ Entity M does not provide financing to customers as a main business activity.
- ▶ Therefore, the fair value gains and losses on the derivative are classified in the financing category.

3.9.4.2. Hybrid contracts containing a host liability – embedded derivative is not separated from the host liability (IFRS 18.B56(b)-(c))

The classification requirements for income and expenses relating to hybrid contracts containing a host liability where the embedded derivative is not separated are summarised as follows (assuming that the entity does not provide financing to customers as a main business activity):

Income and expenses from hybrid contracts with host liabilities – embedded derivative is not separated from the host liability (entities that do not provide financing to customers as a main business activity)



In summary, income and expenses relating to the hybrid instrument with a non-separated embedded derivative are classified as follows:

- ▶ If the hybrid contract arises from a transaction that involves only the raising of finance, all income and expenses noted in IFRS 18.60 are classified in the financing category, consistent with other 'pure financing' liabilities (IFRS 18.B56(b)).
- ▶ If the hybrid contract arises from a transaction that does not involve only the raising of finance, the classification depends on the nature of the hybrid contract/the host liability (IFRS 18.B56(c)):
 - If the host liability is a financial liability within the scope of IFRS 9 that is measured at amortised cost, then income and expenses specified in IFRS 18.60 arising after initial recognition are classified in the financing category (IFRS 18.B56(c)(i)). All other income and expenses are classified in the operating category.
 - If the hybrid contract is an insurance contract in the scope of IFRS 17, income and expenses are classified in the operating category (IFRS 18.B56(c)(ii)).
 - In all other cases, an entity applies the requirements applicable to liabilities that arise from transactions that do not involve only the raising of finance (IFRS 18.B56(c)(iii)). However, if a hybrid contract falls within the scope of IFRS 18.B56(c)(iii) and is accounted for at fair value through profit or loss using the fair value option (IFRS 9.4.3.5), no income and expenses will be classified in the financing category because that contract will not give rise to (1) interest income and expenses; or (2) income and expenses from changes in interest rates (IFRS 18.61). See Example 3.9.4-4.

The above flowchart assumes that an entity does not provide financing to customers as a main business activity. If an entity does provide financing to customers as a main business activity, then conclusions will differ. For example, for an entity that provides financing to customers as a main business activity, income and expenses relating to a hybrid contract (with a non-separated embedded derivative) arising from a transaction that involves only the raising of finance will be classified in the operating category rather than the financing category (IFRS 18.65(a)(i)).



BDO comment – reasons why an embedded derivative may not be accounted for separately from the host contract

Note that these requirements apply to hybrid contracts where the embedded derivative is not separated from the host contract regardless of the reason for the embedded derivative not being separated (IFRS 18.B57). This may be the case because of:

- ▶ IFRS 9.4.3.3: an embedded derivative may be identified in a host contract, but it is not separated and accounted for as a derivative if it is considered 'closely related' to the host contract (see criteria in IFRS 9.4.3.3).
- ▶ IFRS 9.4.3.5: an entity is permitted to designate the entire hybrid contract as at fair value through profit or loss (meaning the embedded derivative is not accounted for separately) if criteria in IFRS 9.4.3.5 are met.

If the criteria in IFRS 9.4.3.3 are met, an embedded derivative is not accounted for separately from the host contract, however, the contract is still technically a 'hybrid contract', meaning the special considerations in IFRS 18 still apply. See Example [3.9.4-3](#) for an illustration of the non-separated embedded derivatives hybrid contract flowchart being used to analyse how income and expenses are classified arising from a contract where the embedded derivative is not separated because it is considered closely related to the host contract.



Example 3.9.4-2 – classification of income and expenses arising from a convertible note – embedded derivative is not separated from the host liability because the fair value option is elected (IFRS 9.4.3.5)

Fact pattern

Entity N issues a convertible note where the principal of the loan may be converted into Entity N's equity instruments at the option of the holder at any time. The conversion option does not meet the 'fixed for fixed' criterion because the currency of the note differs from the functional currency of Entity N meaning that the amount of 'cash' that would be settled upon conversion is not fixed in the functional currency of Entity N. Entity N elects to use the fair value option in IFRS 9.4.3.5, meaning the entire hybrid instrument is measured at fair value through profit or loss.

Entity N does not provide financing to customers as a main business activity.

During the reporting period where the convertible note remains outstanding, the hybrid contract gives rise to the following income and expenses:

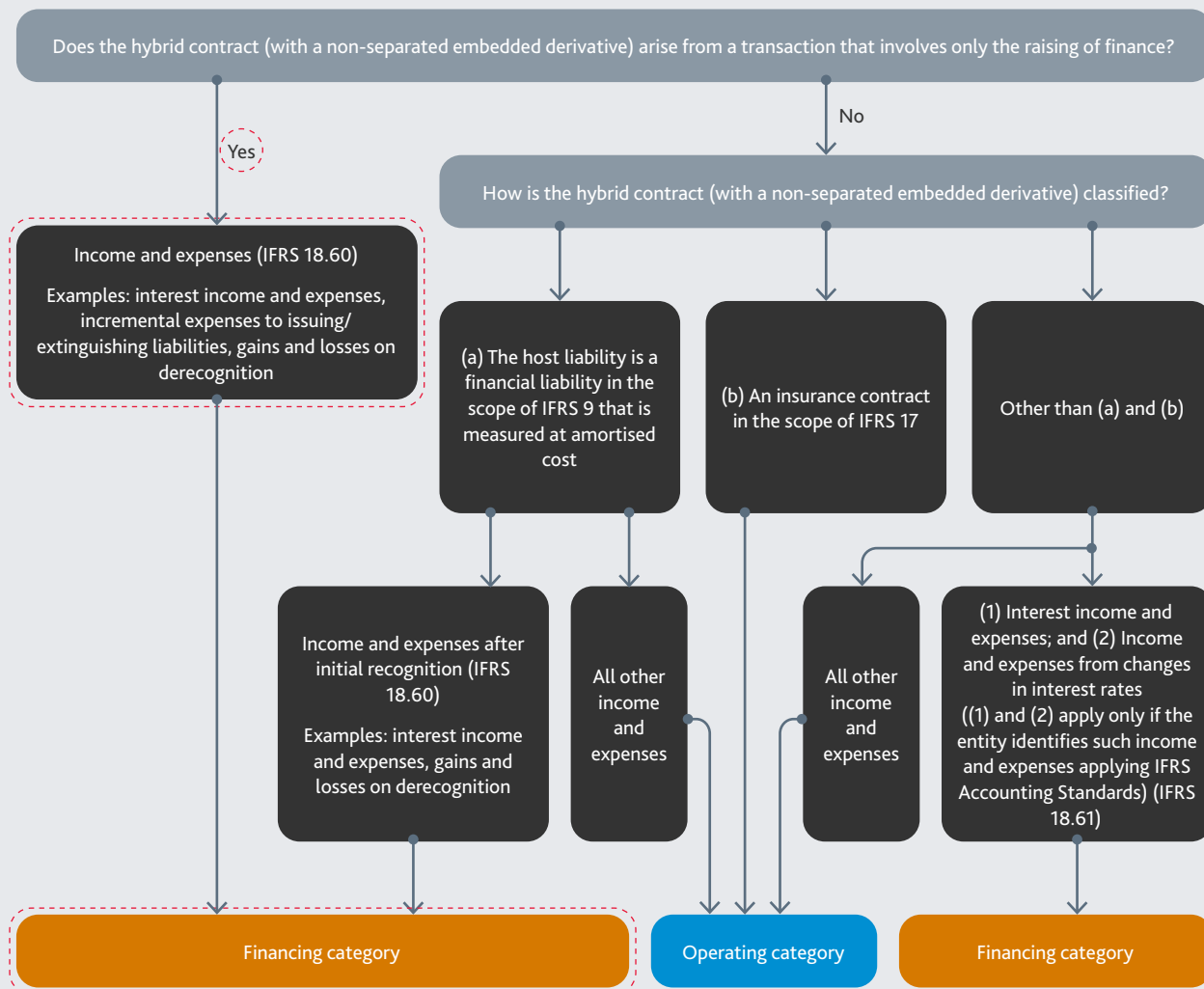
Component	Income and expenses
Hybrid contract	Fair value gains and losses (IFRS 9)

While the convertible note may result in coupon interest payments to note holders, interest expense is not recognised on the hybrid contract because it is not measured at amortised cost. For a financial liability measured at fair value through profit or loss, the entire movement in the carrying amount from one reporting period to the next is reflected as fair value gains and losses (except for changes in credit risk relating to that liability, which are reflected in other comprehensive income – see IFRS 9.5.7.7).

Assessment – hybrid contract

Entity N classifies the fair value gains and losses related to the hybrid contract as follows (the relevant assessment is circled in red dotted lines using the classification flowchart from earlier in this section):

Income and expenses from hybrid contracts with host liabilities – embedded derivative is not separated from the host liability (entities that do not provide financing to customers as a main business activity)



Explanation:

- ▶ The fair value gains and losses on the hybrid contract being remeasured to fair value at each reporting period are classified in the finance category because the hybrid contract arises from a transaction that involves only the raising of finance. That is because Entity N receives finance in the form of cash and will return cash in exchange at a later date (IFRS 18.B50).
- ▶ Note that the amount of the change in fair value of the hybrid contract that is attributable to changes in the credit risk of the liability will be presented in other comprehensive income (IFRS 9.5.7.7). Amounts presented in other comprehensive income are not subject to the classification requirements of IFRS 18 other than the requirement to distinguish amounts that will and will not be reclassified to profit or loss when specific conditions are met (IFRS 18.88).



Example 3.9.4-3 – classification of income and expenses arising from a hybrid contract in the scope of IFRS 18.B56(c)(iii) - embedded derivative is not separated from the host liability because it is considered closely related to the host contract (IFRS 9.4.3.3)

Fact pattern

Entity O enters into a lease contract as a lessee for a period of 5 years where the underlying asset is a shop in a shopping mall. Lease payments are CU100 per month, however, Entity O must also pay 5% of its monthly turnover as a variable lease payment.

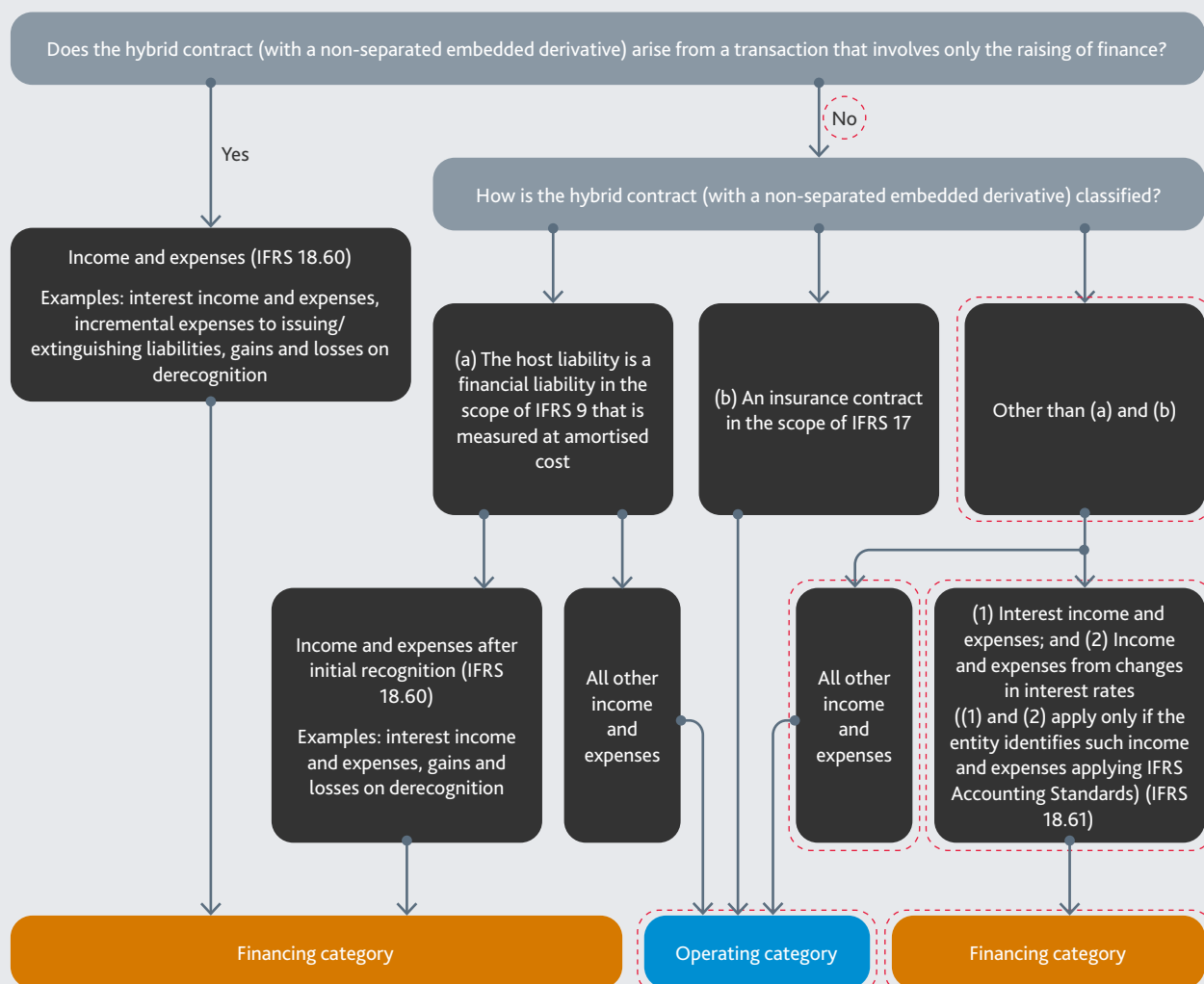
The turnover-based lease payment term is identified as an embedded derivative in the host contract; however, it is not accounted for separately because it is considered closely related to the host contract. That is because IFRS 9.B4.3.8(f) specifies that variable lease payments related to sales are closely related to the host contract.

During the reporting period where the lease remains outstanding, the hybrid contract gives rise to the following income and expenses:

Component	Income and expenses
Turnover-based lease payments	Variable lease payments recognised in profit or loss as the underlying sales occur (IFRS 16.38(b))
Recognised lease liability (fixed lease payments)	Interest expense on the lease liability recognised (IFRS 16.36)

Assessment

Income and expenses from hybrid contracts with host liabilities – embedded derivative is not separated from the host liability (entities that do not provide financing to customers as a main business activity)



Explanation:

- ▶ The hybrid contract (the lease) does not arise from a transaction that involves only the raising of finance. That is because Entity O receives a right-of-use asset, not finance in the form specified by IFRS 18.B50(a).
- ▶ The hybrid contract is not (a) a financial liability in the scope of IFRS 9 that is measured at amortised cost; or (b) an insurance contract in the scope of IFRS 17, therefore, the 'other' requirements apply.
- ▶ The interest expense recognised on the lease liability is classified in the financing category because it is an interest expense that is identified for the purpose of applying IFRS 16 (IFRS 18.61(a)).

- The variable lease payments recognised in profit or loss are classified in the operating category because they are not (1) interest income and expenses; or (2) income and expenses from changes in interest rates.



Example 3.9.4-4 – classification of income and expenses arising from a hybrid contract (host contract is executory) in the scope of IFRS 18.B56(c)(iii) - embedded derivative is not separated from the host liability because the fair value option is elected (IFRS 9.4.3.5)

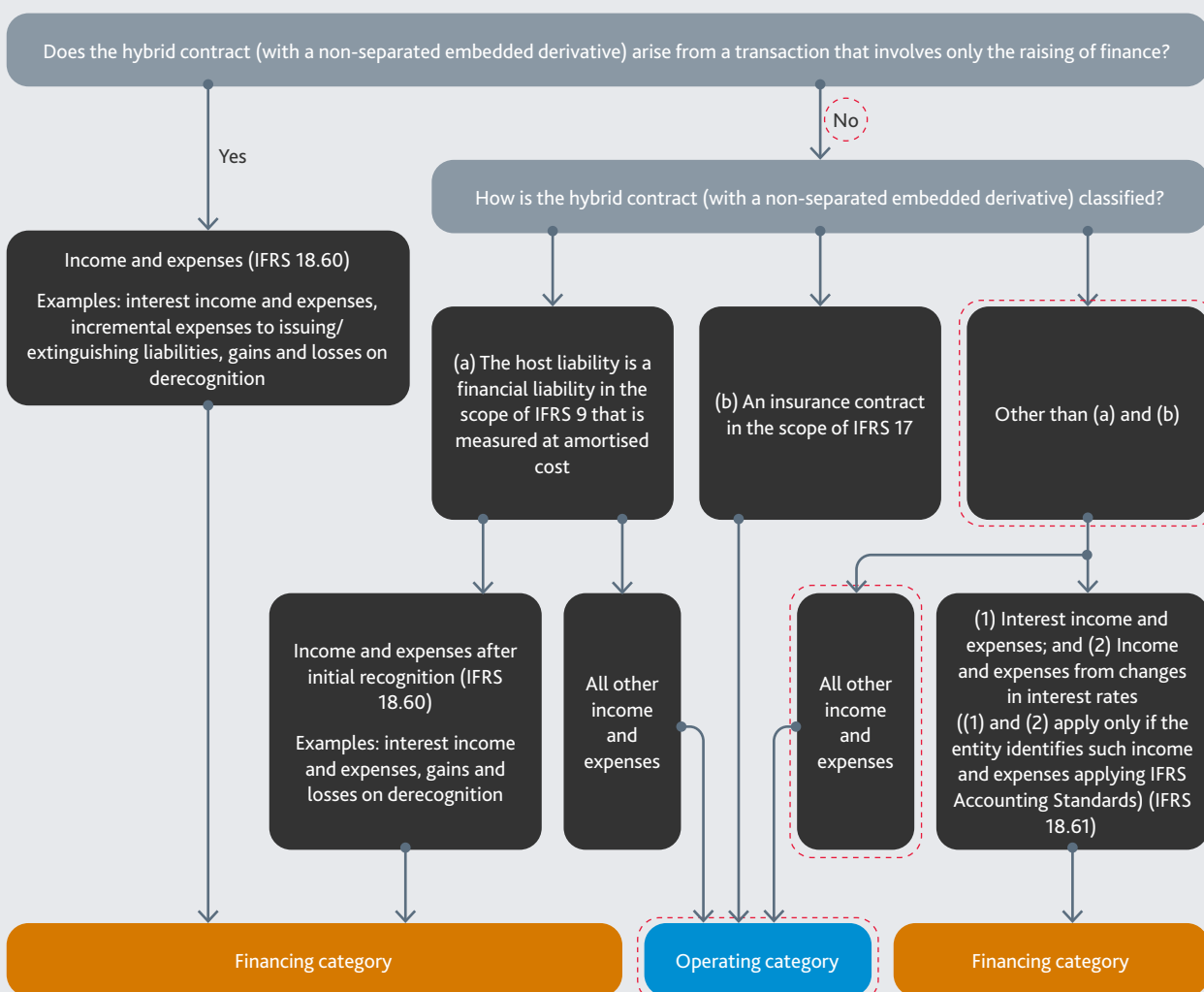
Fact pattern

Entity P enters into a contract to purchase a commodity (e.g. oil). The purchase contract contains embedded derivatives and Entity P elects to measure the entire purchase contract at fair value through profit or loss in accordance with IFRS 9.4.3.5.

During the reporting period where the purchase contract remains outstanding, the hybrid contract gives rise to the following income and expenses:

Component	Income and expenses
Hybrid contract	Fair value gains and losses (IFRS 9)

Assessment



Explanation:

- ▶ The hybrid contract (the purchase contract) does not arise from a transaction that involves only the raising of finance. That is because Entity P is receiving a commodity, not finance in the form specified by IFRS 18.B50(a).
- ▶ The hybrid contract is not (a) a financial liability in the scope of IFRS 9 that is measured at amortised cost; or (b) an insurance contract in the scope of IFRS 17, therefore, the 'other' requirements apply.
- ▶ The fair value gains recognised in profit or loss are classified in the operating category because they are not (1) interest income and expenses; or (2) income and expenses from changes in interest rates.

3.9.5. Guidance on common items of income and expense

The following section provides practical guidance on the classification of common items of income and expense applying the requirements of IFRS 18. Where the classification of the items may differ depending on whether an entity has specified main business activities, that consideration has been noted. Where the classification of that item is addressed in another section of this publication, the reference to that section is provided. The order of items is presented based on the sequencing of the related IFRS Accounting Standard.

This section sets out how items of income and expenses will generally be classified applying the requirements of IFRS 18 discussed in the preceding sections, however, this section should be taken as broad guidance only. The classification of particular income and expenses will depend on facts and circumstances.

Item of income or expense	Classification	Explanation
Inventories expensed, including write-downs to net realisable value and reversals of write-downs (IAS 2)	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See sections 3.2 and 3.4 .
Income taxes expenses, both current and deferred (IAS 12)	Income taxes	Income and expenses within the scope of IAS 12 are classified in the income taxes category. See section 3.5 .
Depreciation of property, plant and equipment (IAS 16)	Generally operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). Property, plant and equipment typically does not generate a return individually and largely independently of the entity's other resources, however, this may not always be the case. See section 3.4 .
Gains and losses from the sale of property, plant and equipment (IAS 16)	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See section 3.4 .
Finance expense on employee benefit liabilities (IAS 19)	Financing	Liability arises from transactions that do not involve only the raising of finance (IFRS 18.59(b)) and are interest income and expenses identified for purposes of applying IFRS Accounting Standards (IFRS 18.61(a)). See section 3.3 .
Current service cost on post-employment benefits (IAS 19)	Operating	Liability arises from transactions that do not involve only the raising of finance (IFRS 18.59(b)) but current service cost is not (a) interest income and expenses identified for purposes of applying IFRS Accounting Standards; or (b) income and expenses arising from changes in interest rates. See section 3.3 .

Item of income or expense	Classification	Explanation
Government grants recognised in income (IAS 20)	Depends on facts and circumstances and accounting policy choices	Income related to government grants may be: (a) Recognised in profit or loss (e.g. a wage subsidy), which would result in the effect of the grant being recognised in the operating category because it does not relate to specified assets or liabilities that arise from transactions that involve only the raising of financing. (b) Recognised as a reduction of the cost of an associated asset (e.g. property, plant and equipment), which would result in the effect of the grant being recognised in the same category as the associated depreciation (e.g. operating for property, plant and equipment). (c) Recognised as deferred income and amortised into income on a systematic basis, which would result in the effect of the grant being recognised in the operating category as such a deferral would be a liability that arises from transactions that do not involve only the raising of finance (IFRS 18.59(b)) and the amortisation of income is not (a) interest income and expense or (b) income and expenses arising from changes in interest rates. The classification of other government grants (e.g. those relates to debt or investment properties) will depend on facts and circumstances
Foreign exchange differences (IAS 21)	Depends on classification of related income and expenses	See section 3.9.3 .
Income and expenses related to associates and joint ventures (IAS 28, IFRS 10) – equity method is applied	Investing	If the associate or joint venture is accounted for using the equity method, income and expenses will always be classified in the investing category. See section 3.8.1 .
Income and expenses related to associates and joint ventures (IAS 28, IFRS 10) – equity method is not applied	Operating or investing	If the equity method is not applied, the classification will depend on whether the entity invests in associates and joint ventures as a main business activity. See section 3.8.1 .
Gain or loss on net monetary position (IAS 29)	Depends on approach adopted	Entities that apply IAS 29 may present the gain or loss on the net monetary position with other income and expense items associated with the net monetary position (e.g. interest income and expenses and foreign exchange differences). If an entity does not present the gain or loss on the net monetary position in this manner, it must be classified in the operating category (IFRS 18.B69).
Impairment of assets and reversals of impairment where applicable (IAS 36)	Generally operating	Most impairment losses will be recognised in the operating category as the impairment will relate to assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). For example, property, plant and equipment, intangible assets, goodwill, etc.

Item of income or expense	Classification	Explanation
		In some cases, impairments recognised in accordance with IAS 36 may relate to assets that generate a return individually and largely independently of the entity's other resources (IFRS 18.53(c)) and are within the scope of IAS 36. For example, an investment property measured at cost that is impaired in accordance with IAS 36 would have the resulting impairment classified in the investing category (IFRS 18.B47(e)). If the entity invests in such assets as a main business activity, then the impairment would also be classified in the operating category (IFRS 18.58).
Provisions recognised as an expense (e.g. lawsuits, restructuring provisions) (IAS 37)	Operating	Liability arises from transactions that do not involve only the raising of finance (IFRS 18.59(b)) but such an expense is not (a) interest income and expenses identified for purposes of applying IFRS Accounting Standards; or (b) income and expenses arising from changes in interest rates. See section 3.3 .
Finance expense on provision liabilities (IAS 37)	Financing	Liability arises from transactions that do not involve only the raising of finance (IFRS 18.59(b)) and are interest income and expenses identified for purposes of applying IFRS Accounting Standards (IFRS 18.61(a)). Increases in the discounted amount of a provision due to the passage of time and effects of changes in discount rate, are classified in the financing category (IFRS 18. B54). See section 3.3.
Amortisation of intangible assets (IAS 38)	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See section 3.4. If an entity accounts for intangible assets using the revaluation model (e.g. certain intangibles with an active market, including some cryptocurrencies), fair value gains and losses are recognised in other comprehensive income rather than profit or loss, therefore, these classification requirements do not apply.
Depreciation of investment property accounted for using the cost model (IAS 40)	Operating or investing	Generally classified as investing, as these are assets that generate a return individually and largely independently of the entity's other resources (IFRS 18.53(c)) and income and expenses that arise from the subsequent measurement of that asset (IFRS 18.54(b)). If the entity invests in such assets as a main business activity, then depreciation would be classified in the operating category (IFRS 18.58).
Fair value gains and losses on investment property accounted for using the fair value model (IAS 40)	Operating or investing	Generally classified as investing, as these are assets that generate a return individually and largely independently of the entity's other resources (IFRS 18.53(c)) and income and expenses that arise from the subsequent measurement of that asset (IFRS 18.54(b)). If the entity invests in such assets as a main business activity, then fair value gains and losses would be classified in the operating category (IFRS 18.58).

Item of income or expense	Classification	Explanation
Depreciation of right-of-use assets classified as investment property accounted for using the cost model (IFRS 16 and IAS 40)	Operating or investing	Generally classified as investing, as these are assets that generate a return individually and largely independently of the entity's other resources (IFRS 18.53(c)) and income and expenses that arise from the subsequent measurement of that asset (IFRS 18.54(b)). If the entity invests in such assets as a main business activity, then depreciation would be classified in the operating category (IFRS 18.58).
Fair value gains and losses on biological assets and agricultural produce at the point of harvest (IAS 41)	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See section 3.4 .
Share-based payments related to employee compensation (IFRS 2)	Operating	Classified in the operating category because the expense does not meet the criteria to be classified in any of the other four categories.
Share-based payments related to other services obtained (IFRS 2)	Operating	Expense is not an income tax or related to a discontinued operation. Expense is not classified in the investing category because it does not relate to investments in associates, joint ventures and unconsolidated subsidiaries, cash equivalents or other assets that generate a return individually and largely independently of the entity's other resources (IFRS 18.53). If the transaction is an equity-settled share-based payment, the expense is not classified in the financing category because it does not relate to a recognised liability (IFRS 18.59). If the expense is a cash-settled share-based payment transaction, it may arise from a recognised liability, however, that liability would not arise from transactions that involve only the raising of financing (IFRS 18.59(b)). The expense recognised on such a liability would not be interest income and expenses or income and expenses arising from changes in interest rates (IFRS 18.61), therefore, it must be classified in the operating category.
Bargain purchase gain (IFRS 3)	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). IFRS 18.B49(f) requires income and expenses arising from business combinations to be classified in the operating category.
Transaction costs incurred relating to a business combination (IFRS 3)	Operating	
Gain or loss on contingent consideration recognised as a result of a business combination (IFRS 3)	Operating	
Remeasurement of associate or joint venture accounted for using the equity method upon step acquisition of a subsidiary (IFRS 3)	Investing	IFRS 18.B60(c) specifies that the remeasurement of an investment in an associate previously accounted for using the equity method on the step acquisition of a subsidiary is classified in the investing category. See section 3.2 .

Item of income or expense	Classification	Explanation
Remeasurement of associate or joint venture <u>not</u> accounted for using the equity method upon step acquisition of a subsidiary (IFRS 3)	Operating or investing	If the acquirer does not account for the associate or joint venture using the equity method, the classification will depend on whether the entity invests in associates and joint ventures as a main business activity. See section 3.8.1 .
Results of discontinued operations (IFRS 5)	Discontinued operations	Income and expenses presented as a single line item in accordance with IFRS 5.33(a) are classified in the discontinued operations category. See section 3.6 .
Income and expenses related to cash and cash equivalents	Operating or investing	For entities without specified main business activities, income and expenses will be classified in the investing category. See section 3.9.1 .
Income and expenses on hybrid contracts containing a financial liability	Operating or financing	See section 3.9.4 .
Interest income on financial assets measured at amortised cost or fair value through other comprehensive income (IFRS 9)	Operating or investing	Classification will depend on whether the entity invests in financial assets as a main business activity. See section 3.2 and 3.8.1 .
Interest expense on financial liabilities measured at amortised cost (IFRS 9)	Operating or financing	Classification will depend on the assessment of multiple factors, including whether: (a) The liability arises from transactions that involve only the raising of finance; (b) The entity provides financing to customers as a main business activity; (c) The financial liability relates to providing financing to customers; and (d) If (a)-(c) are all 'yes', certain accounting policy choices made by the entity. See sections 3.3 and 3.8.2 for an explanation of classification of income and expenses arising from liabilities.
Gains and losses on investments in debt and equity instruments measured at fair value through profit or loss (IFRS 9)	Operating or investing	Classification will depend on whether the entity invests in financial assets as a main business activity. See sections 3.2 and 3.8.1 .
Gains and losses on derivatives measured at fair value through profit or loss (IFRS 9)	Depends on facts and circumstances	See section 3.9.2 .
Gains and losses on the derecognition of financial assets (IFRS 9)	Operating or investing	Classification will depend on whether the entity invests in financial assets as a main business activity. See section 3.2 and 3.8.1 .

Item of income or expense	Classification	Explanation
Gains and losses on the derecognition of financial liabilities (IFRS 9)	Operating or financing	Classification will depend on the assessment of multiple factors, including whether: (e) The liability arises from transactions that involve only the raising of finance; (f) The entity provides financing to customers as a main business activity; (g) The financial liability relates to providing financing to customers; and (h) If (a)-(c) are all 'yes', certain accounting policy choices made by the entity. See sections 3.3 and 3.8.2 for explanation of classification of income and expenses arising from liabilities.
Modification gains and losses on financial assets (IFRS 9)	Operating or investing	Classification will depend on whether the entity invests in financial assets as a main business activity. See section 3.2 and 3.8.1.
Modification gains and losses on financial liabilities (IFRS 9)	Operating or financing	Classification will depend on the assessment of multiple factors, including whether: (a) The liability arises from transactions that involve only the raising of finance; (b) The entity provides financing to customers as a main business activity; (c) The financial liability relates to providing financing to customers; and (d) If (a)-(c) are all 'yes', certain accounting policy choices made by the entity. See section 3.3 and 3.8.2 for explanation of classification of income and expenses arising from liabilities.
Expected credit losses on trade receivables (IFRS 9)	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See section 3.4.
Expected credit losses on lease receivables relating to investment property	Operating or investing	Assets that generate a return individually and largely independently of the entity's other resources, including rent receivables generated by investment properties (IFRS 18.53(c) and IFRS 18.B64) and income and expenses that arise from the subsequent measurement of that asset (IFRS 18.54(b)), therefore, classified in the investing category for entities without specified main business activities. If the entity invests in such assets as a main business activity, then expected credit losses would be classified in the operating category (IFRS 18.58).
Expected credit losses on related party loans receivable (IFRS 9)	Operating or investing	Assets that generate a return individually and largely independently of the entity's other resources (IFRS 18.53(c)) and income and expenses that arise from the subsequent measurement of that asset (IFRS 18.54(b)), therefore, classified in the investing category for entities without specified main business activities. If the entity invests in such assets as a main business activity, then expected credit losses would be classified in the operating category (IFRS 18.58).

Item of income or expense	Classification	Explanation
Fair value gains and losses on unconsolidated subsidiaries and investments in associates and joint ventures for investment entities (IFRS 10)	Operating	Investment entities would be expected to invest in such assets as main business activities, meaning that all income and expenses are recognised in the operating category (IFRS 18.58). See section 3.2.4 .
Revenue from contracts with customers (IFRS 15)	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See section 3.4 .
Finance income on contract assets (IFRS 15)	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See section 3.4 .
Finance expense on contract liabilities (IFRS 15)	Financing	Liability arises from transactions that do not involve only the raising of finance (IFRS 18.59(b)) and are interest income and expenses identified for purposes of applying IFRS Accounting Standards (IFRS 18.61(a)). See section 3.3 .
Modification gains or losses on contracts (IFRS 15)	Operating	See section 3.3 .
Depreciation of right-of-use assets not classified as investment property (IFRS 16)	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See section 3.4 .
Finance expense on lease liabilities (IFRS 16)	Financing	Liability arises from transactions that do not involve only the raising of finance (IFRS 18.59(b)) and are interest income and expenses identified for purposes of applying IFRS Accounting Standards (IFRS 18.61(a)). See section 3.3 .
Variable lease payments not included in the measurement of the lease liability recognised in profit or loss (e.g. rent based on a percentage of sales) (IFRS 16)	Operating	See Example 3.9.4-3 .
Short-term or low-value lease payments recognised in profit or loss	Operating	No lease liability is recognised, therefore, expense cannot be related to a liability, which is necessary for financing classification. The lease expense is therefore classified in the operating category since it is the default category. See section 3.4 .
Lease modification gains or losses recognised in profit or loss (IFRS 16)	Operating	See section 3.3 .
Operating lease income related to assets other than investment property (e.g. property, plant and equipment subject to an operating lease – from the perspective of the lessor) (IFRS 16)	Generally operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). Property, plant and equipment typically does not generate a return individually and largely independently of the entity's other resources, however, this may not always be the case. See section 3.4 .

Item of income or expense	Classification	Explanation
Selling profit or loss on finance leases (i.e. the difference between the initial carrying amount of the net investment in the lease and the carrying amount of the asset derecognised) (IFRS 16)	Operating or investing	Finance leases result in the derecognition of the asset subject to the lease (e.g. an item of property, plant and equipment). IFRS 18.B60 requires any income and expenses on the derecognition of an asset to be classified in the same category as the income and expenses from the asset immediately before its derecognition. In many cases, this will result in operating classification of the selling profit or loss on the finance lease because the asset subject to the finance lease will have been considered an asset that an entity uses in combination to produce or supply goods or services that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). For example, property, plant and equipment. The selling profit could be classified in the investing category if the asset being derecognised in the finance lease was considered an asset that generated a return individually and largely independently of the entity's other resources, and therefore, the income and expenses related to it were classified in the investing category prior to derecognition (IFRS 18.B47). For example, an investment property that is derecognised when it is leased under a finance lease. If an entity invests in such assets (e.g. investment property) as a main business activity, then the selling profit would be classified in the operating category (IFRS 18.55(b), IFRS 18.58).
Finance income on finance leases (IFRS 16)	Operating or investing	Finance income on the net investment in the lease is classified in the investing category unless the entity invests in such assets as a main business activity. That is because the net investment in the lease is an asset that generates a return individually and largely independently of the entity's other resources (IFRS 18.53(c)), and the finance income is income generated by that asset (IFRS 18.54(a)). If the entity invests in net investments in leases as a main business activity (e.g. the entity is a leasing company), then the finance income would be classified in the operating category (IFRS 18.55(b), IFRS 18.58).
Income and expense arising from insurance contracts (e.g. insurance revenue, insurance service expenses, insurance finance income, etc.) (IFRS 17)	Operating	See sections 3.3 and 8.1.5 .

3.10. Interim financial reports prepared in accordance with IAS 34

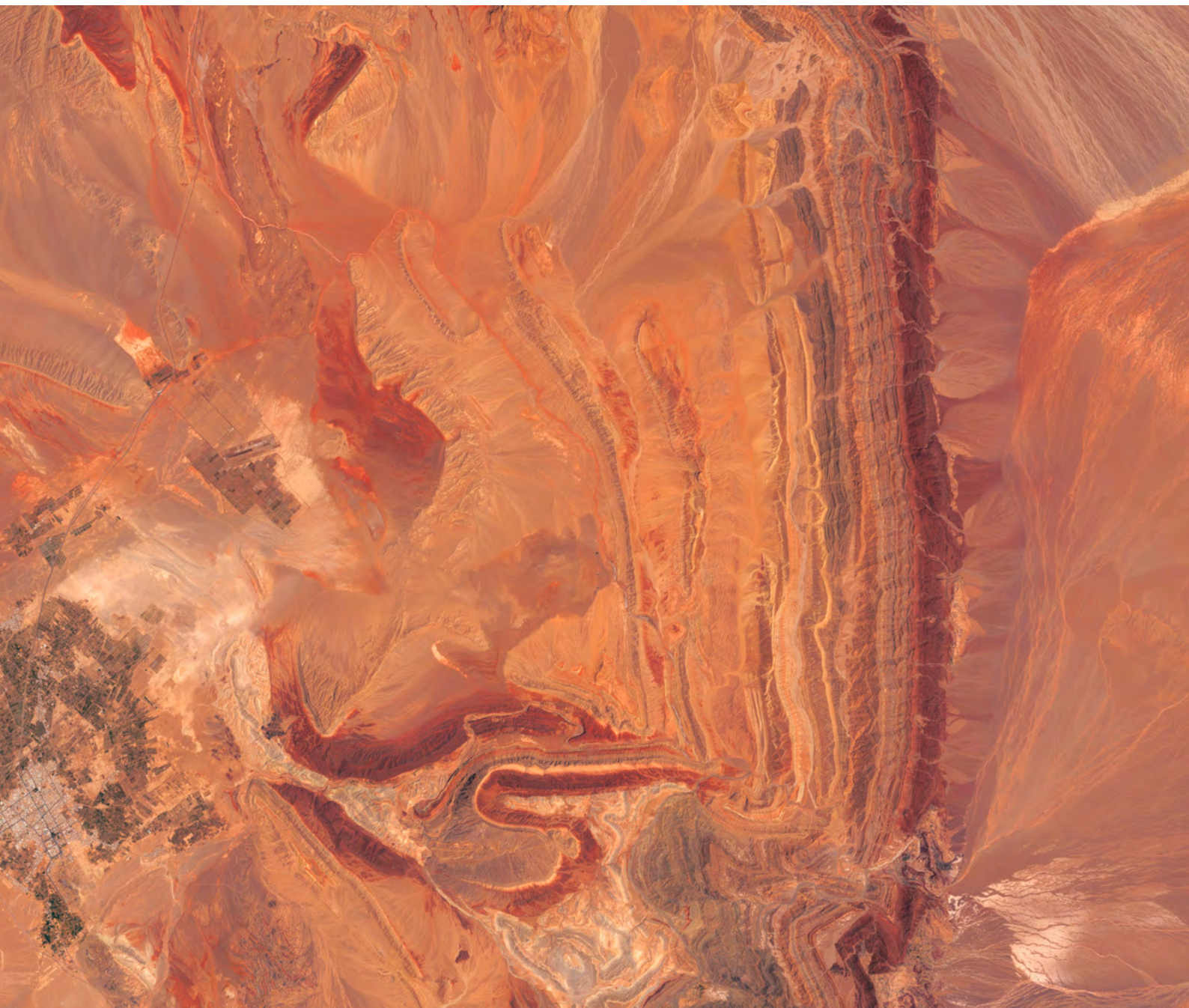
If an entity applies IAS 34 *Interim Financial Reporting*, IFRS 18 will affect those reports, regardless of whether they are a complete set of financial statements or a set of condensed interim financial statements.

If an entity prepares a complete set of financial statements as part of its interim financial report, all of the requirements of IFRS 18 discussed in this publication apply.

If an entity prepares condensed interim financial statements (the more common approach), then IFRS 18 will also affect how an entity prepares those condensed interim financial statements. Once an entity has transitioned to IFRS 18 (i.e. past the year of transition where special requirements apply – see section 7.4), an entity will use headings and subtotals that were included in the most recent annual financial statements (IAS 34.10). For example, the manner in which an entity classifies its income and expenses and presents mandatory subtotals (e.g. operating profit) and additional subtotals should be consistent from the most recently published annual financial statements and condensed interim financial statements.

IFRS 18's requirements for aggregation and disaggregation also apply to interim financial statements (IAS 34.10).

Management-defined performance measures are addressed in section 6. It should be emphasised that IAS 34.16A(m) will require entities to provide disclosures about these measures in interim financial reports as required by IFRS 18.121-125.



4. Principles of aggregation and disaggregation

IFRS 18 sets out new principles for aggregating and disaggregating of information. These principles are applicable to not only items of income and expense, but assets, liabilities, cash flows, equity and reserves also (IFRS 18.41). For example, how similar assets are aggregated for presentation purposes in the statement of financial position, and whether an entity presents its operating expenses by function, nature or a mixed presentation model.

Similar items are aggregated for practical reasons, and also to meet the objective of IFRS 18.16, which is for the primary financial statements to provide a 'structured summary' of a reporting entity's assets, liabilities, equity, income, expenses and cash flows. For purposes of presentation, an 'item' comprises an individual item (e.g. a single asset) or any aggregation or disaggregation of such items (IFRS 18.41).

The following sections discuss the requirements of IFRS 18 applicable to where information is presented or disclosed (i.e. the primary financial statements or the notes) and how information is aggregated and disaggregated. Materiality (whether information is presented or disclosed) remains an overriding factor, which is considered in applying the requirements of IAS 8.



BDO comment – aggregation in IAS 1 vs. IFRS 18

IFRS 18 has more specific requirements applicable to the roles of the primary financial statements and notes, how an entity aggregates and disaggregates information more generally and the use of labelling. The extent to which entities must change their existing presentation in IAS 1 (other than the requirements applicable to classification of items of income and expenses and specified subtotals), will depend on an entity's precise facts and circumstances.

The adoption of IFRS 18 may result in entities revisiting decisions made about presentation and disclosure that had been made previously, which are not necessarily incompatible with the requirements of IFRS 18, but by changing presentation and disclosure practices, may improve the usefulness of information provided.

4.1. The roles of the primary financial statements and notes

IFRS 18.16 defines the roles of the primary financial statements and IFRS 18.17 defines the role of the notes to the financial statements:

Primary financial statements (e.g. statements of financial position, profit or loss, cash flows, etc.) – IFRS 18.16	Notes to the financial statements – IFRS 18.17
To provide structured summaries of a reporting entity's recognised assets, liabilities, equity, income, expenses and cash flows, that are useful to users of financial statements for: (a) obtaining an understandable overview of the entity's recognised assets, liabilities, equity, income, expenses and cash flows; (b) making comparisons between entities, and between reporting periods for the same entity; and (c) identifying items or areas about which users of financial statements may wish to seek additional information in the notes.	To provide material information necessary: (a) to enable users of financial statements to understand the line items presented in the primary financial statements; and (b) to supplement the primary financial statements with additional information to achieve the objective of financial statements.

IAS 1 did not define the roles of these two components of financial statements.

These roles have been defined in order to assist entities in determining whether to include information in the primary financial statements or in the notes (IFRS 18.18). Based on the defined roles, information presented in the primary

financial statements (i.e. a structured summary) is more aggregated than information provided in the notes, which typically disaggregates information provided in the primary financial statements (IFRS 18.18(a)). For example, a single line item may be presented in the statement of financial position for 'financial assets measured at fair value through profit or loss', with that amount disaggregated in a corresponding note into different classes of financial assets.

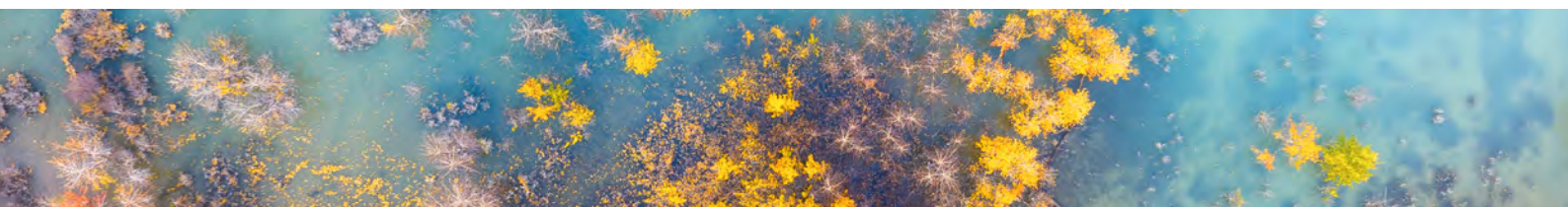
In some cases, a specific IFRS Accounting Standard may specify disaggregation requirements for notes to financial statements (e.g. a disaggregation of items of property, plant and equipment by asset class in IAS 16), however, those presentation and disclosure requirements remain subject to materiality (IFRS 18.19). Entities are also required to consider whether to provide additional disclosures when compliance with specific requirements in IFRS Accounting Standards is insufficient to enable users of financial statements to understand the effect of transactions and other events and conditions on the entity's financial position and performance (IFRS 18.20).

4.2. Principles of aggregation and disaggregation

In determining how to aggregate and disaggregate information presented in the primary financial statements and disclosed in the notes to the financial statements, IFRS 18.41 requires an entity to:

Requirement	Example
(a) classify and aggregate assets, liabilities, equity, income, expenses or cash flows into items based on shared characteristics;	Presentation of financial assets in the statement of financial position by classification in IFRS 9 (e.g. amortised cost, fair value through profit or loss, fair value through OCI).
(b) disaggregate items based on characteristics that are not shared in the primary financial statements and in the notes;	If an entity presents expenses by nature, disaggregating operating expenses by the nature of those expenses (e.g. presenting wages and benefits separately from depreciation).
(c) aggregate or disaggregate items to present line items in the primary financial statements that fulfil the role of the primary financial statements in providing useful structured summaries;	Applying the aggregation and disaggregation principles in (a) and (b) in order to provide a useful structured summary of information in the primary financial statements.
(d) aggregate or disaggregate items to disclose information in the notes that fulfils the role of the notes in providing material information; and	For assets that are aggregated in the statement of financial position (e.g. financial assets), disclosing a disaggregation by asset class in the notes to the financial statements, considering the requirements of IFRS 18 and IFRS 7.
(e) ensure that aggregation and disaggregation in the financial statements do not obscure material information.	Considering materiality in assessing whether to aggregate otherwise similar items, such as an individually material expected credit loss recorded on a single financial asset vs. expected credit losses recorded on a portfolio of smaller financial assets.

In order to meet the requirements of IFRS 18.41, an entity must always disaggregate items whenever the resulting information is material (IFRS 18.42), however, this disaggregation need not always be in the primary financial statements. as Disaggregated information may be provided in the notes to the financial statements, however, this is not a 'free choice' by an entity. Entities must consider the roles of the financial statements in determining where to provide information about the material item.



Examples of income, expenses, assets, liabilities and items of equity that have sufficiently dissimilar characteristics to warrant separate presentation in the primary statements or disclosure in the notes:

Assets and liabilities - statement of financial position (IFRS 18.B111)	Income and expenses – statement of profit or loss (IFRS 18.B79)
▶ Property, plant and equipment disaggregated into classes (IAS 16); ▶ Receivables disaggregated into amounts receivable from trade customers, related parties, prepayments and other amounts; ▶ Inventories disaggregated, applying IAS 2, into items such as merchandise, production supplies, materials, work in progress and finished goods; ▶ Trade payables disaggregated, applying IAS 7, to provide separately the amounts of those payable that are part of supplier finance arrangements; ▶ Provisions disaggregated according to their nature, such as, provisions for employee benefits, decommissioning liabilities, or other items; and ▶ Equity capital and reserves disaggregated into various classes, such as paid-in capital, share premium and reserves.	▶ Write-downs of inventories and reversals ▶ Impairment losses and reversals for property, plant and equipment ▶ Income and expenses from restructuring of an entity's activities and reversals ▶ Income and expenses from: • Disposals of property, plant and equipment; • Disposals of investments (e.g. equity accounted for associates); • Litigation settlements; • Reversals of provisions; and • Non-recurring income and expenses.

4.2.1. Line items required by IFRS Accounting Standards

Certain IFRS Accounting Standards may require specific line items to be presented in primary financial statements (e.g. IFRS 18.75(b)(i) – interest revenue calculated using the effective interest method), however, this separate presentation is not required if doing so is not necessary for the statement to provide a useful structured summary (IFRS 18.23). For example, a corporate entity with immaterial amounts of interest revenue calculated using the effective interest rate method may conclude that presenting that line item separately in the statement of profit or loss is not necessary.

4.2.2. Additional line items

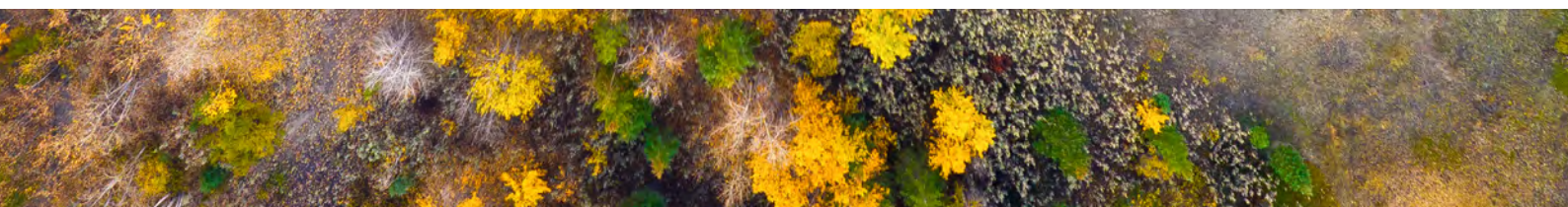
An entity is required to present additional line items (and subtotals – see section 5.2) if such presentation is necessary for a primary financial statement to provide a useful structured summary (IFRS 18.24). However, any additional line items (and subtotals) must (IFRS 18.24):

- comprise amounts recognised and measured in accordance with IFRS Accounting Standards;
- be compatible with the statement structure required by IFRS 18 (e.g. all categorisation requirements and mandatory subtotals);
- be consistent from period to period; and
- be displayed no more prominently than the totals and subtotals required by IFRS Accounting Standards.

4.2.3. Characteristics to use in assessing the need to aggregate and disaggregate information

Whether an entity is determining how to aggregate or disaggregate information in the statement of profit or loss to provide a useful structured summary of the entity's income and expenses or how to aggregate and disaggregate information more generally (e.g. line items and note disclosure), an entity is required to use judgement (IFRS 18.B78).

This judgement is based on an assessment of whether the items have characteristics that are shared (similar characteristics) or characteristics that are not shared (dissimilar characteristics). Such characteristics for items presented in the primary financial statements or disclosed in the notes include:



Characteristics (IFRS 18.B78 and 18.B110)	Applicable statement	Example of items with dissimilar characteristics
Nature	Statement of profit or loss	Salaries and wages vs. depreciation of property, plant and equipment.
	Statement of financial position	Property, plant and equipment vs. investment property. Example IV-2 relating to IFRS 18 of the IASB's illustrative examples: <i>Disclosures about Uncertainties in the Financial Statements</i> explains that property, plant and equipment with high carbon emissions could have sufficient dissimilar characteristics than those with low carbon emissions to allow disaggregation in the notes. Refer to BDO's publication IFRB 2025/10 IASB publishes illustrative examples: Disclosures about Uncertainties in the Financial Statements .
Function (role) within the entity's business activities	Statement of profit or loss	Operating expenses classified into selling, finance, and research and development .
	Statement of financial position	Disclosure of assets and liabilities per reportable segment (IFRS 8.21(b)).
Persistence (including the frequency of the item of income or expense or whether it is recurring or non-recurring)	Statement of profit or loss	Impairment of property, plant and equipment arising from poor sales vs. impairment of property, plant and equipment due to change in regulation requiring change of use of the asset.
Measurement basis	Statement of profit or loss	Fair value adjustments vs. interest recognised applying the effective interest rate.
	Statement of financial position	Financial assets at fair value through profit or loss vs. amortised cost.
Measurement uncertainty or outcome uncertainty (or other risks associated with an item)	Statement of profit or loss	Fair value adjustments through profit or loss (steady-state companies vs. start-ups).
	Statement of financial position	Equity instruments at fair value through profit or loss of steady-state companies vs. start-ups).
Size	Statement of profit or loss	Salaries and wages, which are quantitatively material vs. advertising expenses, which are not quantitatively material.
	Statement of financial position	Inventory, which is quantitatively material vs. trade receivables, which are not quantitatively material.
Geographic location or regulatory environment	Statement of profit or loss	Revenue in jurisdictions where the majority of income is earned vs. emerging/growing jurisdictions where an entity has recently expanded.

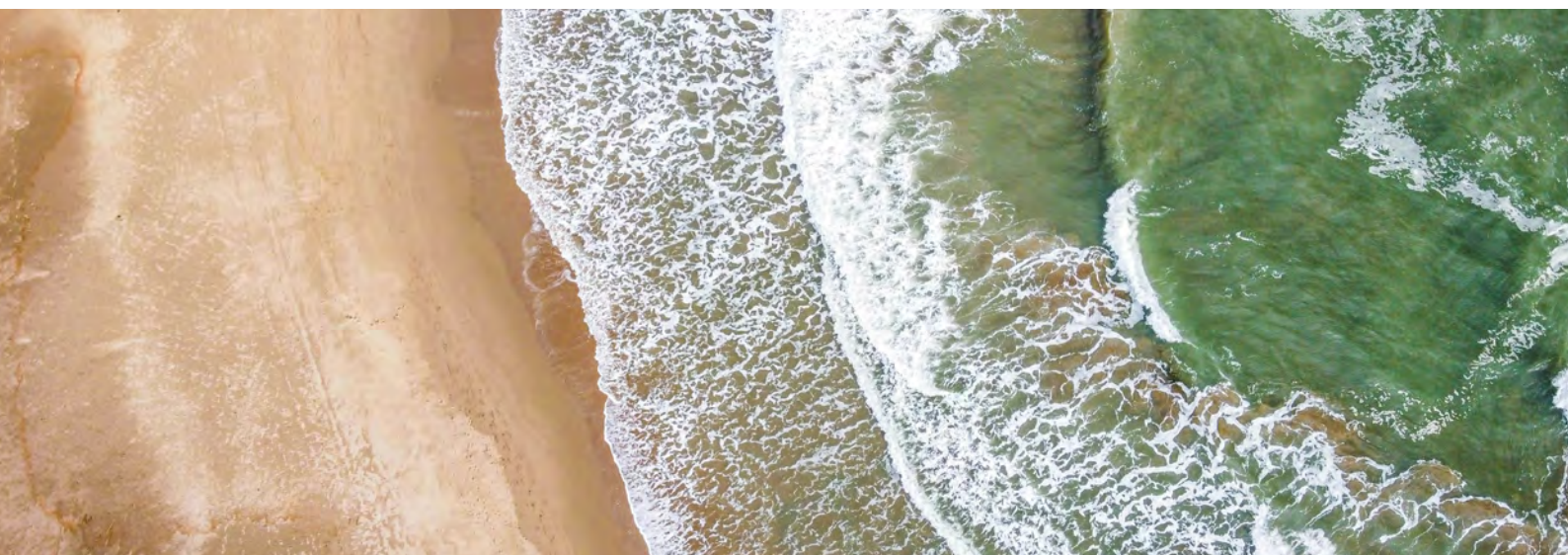
	Statement of financial position	Regulatory assets vs. office equipment.
Tax effects	Statement of profit or loss	If different tax rates apply to items of income or expense.
	Statement of financial position	Assets and liabilities arising from income taxes within the scope of IAS 12 and those arising from other taxes outside the scope of IAS 12 (see section 3.5).
Whether the income or expense arise on initial recognition of a transaction or event from a subsequent change in estimate relating to a transaction or event	Statement of profit or loss	'Day 1' gains on financial assets recognised in accordance with IFRS 9 vs. the release of deferred gains to profit or loss over time (IFRS 9.B5.1.2A).
Duration and timing of recovery or settlement (including current or non-current classification)	Statement of financial position	Property, plant and equipment vs. Office building classified as held for sale.
Liquidity	Statement of financial position	Investments in listed shares traded in an active market vs. investments in shares in a private company that are rarely traded.
Restrictions on the use of an asset or on the transferability of a liability	Statement of financial position	Deposits held for customers vs. current account.

4.2.4. Application of requirements to the statement of profit or loss

After applying the requirements to classify items of income and expense into the five categories (see section 3), an entity must determine how to present those items in the statement of profit or loss, and provide corresponding disclosures in the notes. This publication focuses on the aggregation and disaggregation requirements of IFRS 18 that are applicable to the statement of profit or loss. Therefore, the remaining topics in section 4 are written in the context of the statement of profit or loss.

4.3. Line items in statement of profit or loss

IFRS 18.75-76 requires certain line items to be presented in the statement of profit or loss (subject to materiality). The following table summarises these requirements, comparing them to the requirements of IAS 1:



Line items required to be presented in the statement of profit or loss (IFRS 18.75-76)	Required by IAS 1?
Revenue, presenting separately: ▶ Interest revenue calculated using the effective interest method (IFRS 9); and ▶ Insurance revenue (IFRS 17)	▶ Yes
Operating expenses, presenting separate line items as required by IFRS 18.78 and 82(a) – see section 4.4	Yes, however, IAS 1 did not require this analysis of operating expenses to be provided in the statement of profit or loss; disclosure could be provided in the notes. IFRS 18 requires this analysis to be in the statement of profit or loss – see section 4.4
Share of profit or loss of associates and joint ventures accounted for using the equity method (IAS 27, 28)	▶ Yes
Income tax expense or income (IAS 12)	▶ Yes
A single amount for the total of discontinued operations (IFRS 5)	▶ Yes
IFRS 9 amounts: ▶ Interest revenue calculated using the effective interest method ▶ Impairment losses (including reversals of impairment losses or impairment gains); ▶ Gains and losses arising from the derecognition of financial assets measured at amortised cost; ▶ Reclassification gains and losses; and ▶ Recycling of gains and losses from OCI to profit or loss.	▶ Yes ▶ Yes ▶ Yes ▶ Yes ▶ Yes
IFRS 17 amounts: ▶ Insurance revenue; ▶ Insurance service expenses; ▶ Income or expenses from reinsurance contracts held; ▶ Insurance finance income or expenses; and ▶ Finance income or expenses from reinsurance contracts held.	▶ Yes ▶ Yes ▶ Yes ▶ Yes ▶ Yes
An allocation of profit or loss for the reporting period attributable to: ▶ Non-controlling interests; and ▶ Owners of the parents.	▶ Yes ▶ Yes



BDO comment – line items required by IAS 1 but not required by IFRS 18

IAS 1.82(b) requires 'finance costs' to be presented as a single line item. This requirement was not brought forward into IFRS 18, unlike the majority of the other line item disclosure requirements in IAS 1 (IFRS 18.BC242).

This is a consequence of the fact that IFRS 18 has a financing category for income and expenses (see section [3.3](#)). An entity applies the requirements of IFRS 18 in determining how to aggregate and disaggregate information in the financing category into line items and whether disaggregation is required in the notes.

For example, an entity may determine that interest expenses on bank loans and lease liabilities classified in the financing category should be aggregated into a single 'interest expense' line item in the statement of profit or loss, with corresponding disclosure in the notes to disaggregate that line item, if the resulting information from disaggregation is considered material.



BDO comment – Disaggregation of realised and unrealised gains and losses on financial instruments measured at fair value through profit or loss

Certain regulatory requirements require entities to differentiate between its realised and unrealised gains or losses related to financial instruments in the statement of profit or loss.

Question: would it be appropriate for an entity to disaggregate these realised and unrealised gains or losses on financial instruments measured at fair value through profit or loss in the statement of profit or loss?

In our view, it is not appropriate to present realised and unrealised gains or losses on financial instruments measured at fair value through profit or loss in the statement of profit or loss since doing so would result in line items being presented that do not comprise amounts recognised and measured in accordance with IFRS Accounting Standards, which is a requirement of IFRS 18.24(a). An entity might however disclose the recognised and unrecognised gains and losses within the notes together with the method it used to calculate these gains and losses.

The rational is as follows:

IFRS 18.41 requires that income or expenses should be disaggregated that:

- ▶ have dissimilar characteristics (IFRS 18.41(b));
- ▶ provide a useful structured summary (IFRS 18.41(d)); and
- ▶ do not result in obscured material information (IFRS 18.41(e)).

IFRS 18.24 requires that an entity shall present additional line items if such presentations provide a useful structured summary of the statement of profit or loss. Those line items shall:

- (a) be recognised and measured in accordance with IFRS Accounting Standards;
- (b) be compatible with structure of the statement of profit or loss;
- (c) be consistent from period to period;
- (d) be displayed no more prominently than the totals and subtotals required by IFRS Accounting Standards.

Although disaggregating the realised and unrealised gains or loss might be compatible with the structure of the statement of profit or loss, be consistently presented between periods and be displayed with no more prominence than other totals and subtotals, these amounts would not be recognised and measured in accordance with IFRS 9 Financial Instruments. The reason for this can be illustrated with the following example.

Assume that an entity holds financial assets. IFRS 9.5.2.1(c) requires that the financial assets (shares) be measured to fair value and that the fair value adjustments should be recognised in profit or loss (IFRS 9.5.7.1).

IFRS Accounting Standards do not define realised and unrealised gains. Although IFRS 13.93(f) mentions realised and unrealised gains, no further requirements for determining such gains and losses are provided.

For example, assume that Entity H purchased listed shares during 20x0 for CU100 and sold the shares during 20x3 for CU500. From 20x0 to 20x3, the fair value of the shares increased by CU100 per annum. Entity H sells the shares on 31 December 20x3 for CU500. In total, Entity H realised a gain of CU400 (CU500 selling price – CU100 original cost) on the shares, however, it recognised CU300 of that gain in the annual reporting periods from 20x0 to 20x2 as the shares are required to be remeasured at fair value at the end of each reporting period.

To present CU400 in the statement of profit or loss for the year ended 31 December 20x3, Entity H would have to present:

Realised gain	CU400	(CU500 selling price – CU100 original cost)
Unrealised loss	<u>(CU300)</u>	**remainder
Net gain	CU100	(CU500 selling price – CU400 20x2 carrying amount)

**The unrealised loss of CU300 represents the change in the unrealised gain or loss recognised cumulatively from 20x0 to 20x2. In our view, this method of presentation does not comply with the requirements of IFRS 18.24 because it is not accurate that Entity H incurred an unrealised loss of CU300 in the year ended 31 December 20x3, therefore, this amount would not comprise amounts recognised and measured in accordance with IFRS Accounting Standards (IFRS 18.24(a)).



BDO comment – Disaggregation of interest or dividend income from 'pure' fair value movements financial instruments measured at fair value through profit or loss

In contrast to the above BDO comment, in some cases it may be appropriate to disaggregate fair value movements for certain financial assets on a basis other than realised vs. unrealised gains and losses, depending on the precise facts and circumstances.

Assume that a financial entity such as a bank measures the following financial instruments at fair value through profit or loss:

- ▶ interest rate swap (IRS) receiving a floating interest rate and paying a fixed interest rate; and
- ▶ investments in listed shares that pay dividends annually.

The IRS is an economic hedge of interest rate risk, but is not designated in a qualifying hedge accounting relationship.

IFRS 9.5.2.1(c) requires that financial assets (shares) to be measured to fair value and that the fair value adjustments should be recognised in profit or loss (IFRS 9.5.7.1).

IFRS 7.21 requires that an entity must disclose material accounting policy information, including information about the measurement basis for financial instruments. IFRS 7.B5(e) explains that such disclosure could include how an entity determines the net gains or net losses on each category of financial instrument. The paragraph elaborates further that net gains or losses on items measured at fair value through profit or loss could include interest or dividend income. IFRS 7.B5(e) therefore contemplates the possibility to disaggregate interest or dividend income from fair value gains or losses as a matter of accounting policy.

This raises the question of whether it is permissible to disclose dividend income, interest income, or interest expense separately from the 'pure' fair value of the same financial instrument in the statement of profit or loss.

The interest rate swap and dividend income are considered separately below.

Interest rate swap

The fair value of an IRS is affected by the difference in present value of the fixed cash flows (paid in this example) and the variable cash flows (received in this example). Net interest receivable or payable also accrues with the passage of time prior to being settled.

The IRS is required to be measured at fair value (IFRS 9.5.2.1(c)) and cannot be disaggregated in the statement of financial position between the IRS and accrued interest payable or receivable because the IRS is a single financial instrument, and is therefore a single unit of account. The disaggregated line items would not meet the requirements of IFRS 18.24(a) because it would not consist of amounts recognised and measured in accordance with IFRS Accounting Standards.

IFRS 9.5.7.1 requires that fair value adjustments should be recognised in profit or loss. IFRS 9 does not specifically consider whether fair value adjustments may be disaggregated between different line items in the statement of profit or loss.

In our view, the interest income or expense may be disaggregated from the 'pure' fair value movements of a financial instrument measured at fair value through profit or loss.

Entities should however also consider the views of their local regulators, as specific jurisdictions may prohibit such presentation.

If the interest income is presented separately, it should be disclosed as part of the material accounting policy information (if material) per IFRS 7.B5(e). To avoid obscuring material information, this interest income or expenses should be described in such a manner (in the primary financial statements or notes) that users of the financial statements are able to understand to which instruments (or type of instruments) it relates.

However, if the interest income is presented separately, it should not be presented in the line item 'interest revenue calculated using the effective interest method' as required by IFRS 18.75(b)(i) since the interest income is

not calculated using the effective interest method. That is because only instruments classified at amortised cost and fair value through other comprehensive income (for debt instruments) have interest income calculated using the effective interest method.

Dividend income

The appropriateness of the disaggregation of dividend income and the 'pure' fair value adjustment depends on if the holder is before or after the 'ex-dividend date.' The 'ex-dividend date' refers to the specific date on which a share begins trading without the value of its next declared dividend. Said another way, if a dividend is declared and a share is purchased after the 'ex-dividend date', the holder will not be entitled to that declared dividend.

The measurement of the fair value of the shares after the 'ex-dividend date' will therefore exclude dividends. Conversely, the measurement of the fair value of the shares before the 'ex-dividend date' will include dividends declared since an investor will also pay to obtain the declared dividend.

In our view, it would not be appropriate to disaggregate dividend income and the fair value of adjustments of shares for shares purchased after the 'ex-dividend date' since the holder is not entitled to any dividends.

The dividend income may however be disaggregated from the 'pure' fair value movements of a financial instrument measured at fair value through profit or loss if obtained before the 'ex-dividend date.'

Entities should however also consider the views of their local regulators as specific jurisdictions may prohibit such presentation.

If the dividend income (related to dividends declared but not yet received) is presented separately from fair value adjustment, it should be disclosed as part of the material accounting policy information (if material) per IFRS 7.B5(e).

4.4. Analysis of the most useful structured summary of operating expenses – use of characteristics of nature and function

In the operating category, an entity shall classify and present expenses in line items in a way that provides the most useful structured summary of its expenses, using one or both of the following characteristics (IFRS 18.78):

- (a) The nature of expenses; or
- (b) The function of the expenses within the entity.

This analysis of operating expenses must be presented in the statement of profit or loss (IFRS 18.78), whereas IAS 1 permitted the analysis to be provided in the notes to the financial statements (IAS 1.99-100). Entities may still determine that the line items presented for operating expenses in the statement of profit or loss require additional disaggregation in the notes.

An explanation of nature vs function is provided below:

	Nature	Function	'Mixed' presentation
Description	Allocation of expenses based on the nature of the economic resources consumed to accomplish the entity's activities without reference to the activities in relation to which the economic resources were consumed (IFRS 18.80).	Allocation of expenses based on the activity to which the consumed resources relate (IFRS 18.81).	An entity may present an analysis of operating expenses where some expenses are classified by nature and others by function (IFRS 18.B81).
Example	Salaries and wages, depreciation, inventories expensed	Cost of goods sold, research and development, administrative expenses	See Example 4.4-2 below



BDO comment – 'mixed' basis of presentation - IAS 1 vs. IFRS 18

IAS 1 did not explicitly permit a mixed basis of presenting line items in the statement of profit or loss, however, many entities have applied this basis of presentation in the past, while providing disclosures required by IAS 1.104 – specific information about the nature of expenses for depreciation, amortisation and employee benefits. IFRS 18.83 expands this disclosure requirement – see section [4.4.3](#) below.

4.4.1. Factors considered in assessing which presentation to use

An entity does not have a free accounting policy choice in determining the presentation basis of operating expenses. IFRS 18.B80 requires an entity to consider:

Factor to be considered	Example
(a) What line items provide the most useful information about the main components or drivers of the entity's profitability;	Use of cost of sales by a retail entity, as it provides relevant information about whether the revenue generated from the sale of goods covers what, for retailers, are mainly direct costs, and by what margin.
(b) What line items most closely represent the way the business is managed and how management reports internally;	An entity with multiple major functions may classify expenses by those functions, whereas an entity with a single function (e.g. a lender) may classify expenses by nature.
(c) What standard industry practice entails; and	If certain industries have common practice in how operating expenses are classified, using the industry accepted approach may make comparison easier between entities.
(d) Whether the allocation of particular expenses to functions would be arbitrary to the extent that the line item presented would not provide a faithful representation of the function.	Allocating impairment of a large group of assets (e.g. property, plant and equipment, right-of-use assets, etc.) by function (e.g. research and development, administration, etc.) may be arbitrary as assets may be used in multiple functions.

4.4.2. Presentation of operating expenses by nature

If entities present operating expenses by nature, the amounts presented need not be the amounts recognised as an expense for the period (IFRS 18.B84). For example, a manufacturer may incur the following expenses during the year (amounts prior to a portion being recognised in the carrying amount of assets):

► Wages:	CU100
► Electricity:	CU80
► Depreciation:	CU45

A portion of these expenses will be included in the carrying amount of the entity's unsold finished goods inventories for the period. An entity could, for example, present in the statement of profit or loss as follows:

Revenue	CU300
Wages	(CU100)
Electricity	(CU80)
Depreciation	(CU45)
Change in carrying amount of inventories	CU25 - (IFRS 18.B84(a))
Operating profit	CU100

4.4.3. Presentation of operating expenses by function

Entities that present operating expenses by function are subject to certain additional requirements.

If an entity presents one or more line items comprising expenses classified by function in the operating category of the statement of profit or loss, it is required to (IFRS 18.82):

- (a) Present a separate line item for its cost of sales, if the entity classifies operating expenses in functions that include a cost of sales function. That line item shall include the total of inventory expense described in IAS 2.38.
- (b) Disclose a qualitative description of the nature of the expenses included in each function line item.

The requirements of IFRS 18.82 also apply to an entity that uses a mixed presentation, as such a presentation will include 'one or more line item comprising expenses classified by function'.

Entities are also required to present a single note for all line items comprising expenses classified by function, disclosing (IFRS 18.83):

- (a) The total for each of:
- Depreciation (IAS 16, IAS 40, IFRS 16)
 - Amortisation (IAS 38)
 - Employee benefits (IAS 19) and share-based payments relating to services received from employees (IFRS 2)
 - Impairment losses and reversals (IAS 36)
 - Write-downs and reversals (IAS 2)
- (b) For items (a)(i)-(v):
- The amount related to each line item in the operating category; and
 - A list of any line items outside the operating category that also include amounts related to the total.

This allocation disclosure required by IFRS 18.83 is intended to enhance the understandability of the composition of the line items.



Example 4.4-1 – disclosure of expenses by function

Fact pattern

Entity H classifies all of its operating expenses by function in the statement of profit or loss. Certain expenses specified by IFRS 18.83 are also presented in categories other than the operating category (e.g. depreciation of investment property measured at cost, which is presented in the investing category as Entity H does not have main business activities of investing in investment properties).

Entity H must comply with the disclosure requirements of IFRS 18.83.

Analysis

Entity H presents the following note to meet the requirements of IFRS 18.83:

Line items presented in the statement of profit or loss	Depreciation of property, plant and equipment and investment property	Employee benefits	Totals
Operating category:			
Cost of sales	70	90	160
Research and development	35	45	80
Administration	<u>25</u>	<u>65</u>	90
Totals*	130	200	
Investing category:			
Depreciation of investment property**	100	-	100

* IFRS 18.83 requires the totals for each of the items noted in IFRS 18.83(a)(i)-(v) classified in the operating category to be disclosed.

** Depreciation of investment property is not presented by function because it is classified in the investing category. Only expenses classified in the operating category may be presented by function.

4.4.4. Presentation of operating expenses - mixed presentation

In considering the factors in IFRS 18.B80, an entity may determine that a mixed presentation is most appropriate, where certain line items are presented by function (e.g. cost of sales) and others are presented by nature (e.g. expected credit losses on trade receivables, salaries and wages not included in cost of sales, etc.) (IFRS 18.B81).

If an entity uses a mixed presentation, with some line items being comprised of expenses classified by nature and other line items classified by function, each line item must be aggregated on the basis of only one of those characteristics (nature or function) (IFRS 18.79). For example, an entity may determine that it should present 'cost of sales' (a function basis of presentation) while all other expenses are presented on the basis of their nature.

A mixed presentation also requires appropriate labelling to be used or else line items may be misleading. For example, if an entity presents cost of sales, with all other expenses classified on the basis of nature, then certain expenses will be classified in the cost of sales category (e.g. some salaries and depreciation expenses, such as salaries and depreciation included in the cost of inventories expensed) with others presented outside of this line item (e.g. salaries of the finance department, depreciation of property, plant and equipment that is not allocated to cost of sales). Appropriate labelling must be used to ensure line items clearly identify the expenses included in each line item, such as (IFRS 18.B82):

- ▶ Cost of sales
- ▶ Salaries other than those included in cost of sales
- ▶ Depreciation other than those included in cost of sales



BDO comment – nature and function for income and expenses not classified in the operating category

The requirement to present operating expenses by nature, function or a mixed presentation applies only to items classified in the operating category, not the other four categories being: investing, financing, income taxes and discontinued operations.

Income and expenses classified into categories other than the operating category are presented by their nature.



Example 4.4-2 – operating expense presentation by nature vs. function vs. mixed

Fact pattern

Retail Entity D has applied the classification requirements of IFRS 18 and classified the following expenses into the operating category (all amounts in thousands of CU):

▶ Salaries and wages (IAS 19):	100
▶ Depreciation (IAS 16):	150
▶ Inventories expensed (IAS 2):	360
▶ Distribution expenses (shipping goods to customers):	40
▶ Share-based payments to employees (IFRS 2):	60
▶ Depreciation of right-of-use assets (IFRS 16):	85

Entity D also earned CU1,000 of revenue.

The following is a summary of the operating category in the statement of profit loss, under three mutually exclusive scenarios:

- ▶ Scenario A: all expenses are presented by nature
- ▶ Scenario B: all expenses are presented by function
- ▶ Scenario C: cost of sales is presented (function) with all other expenses presented by nature

As noted earlier in this section, Entity D does not have a free choice of which presentation method to use, however, these scenarios are included to demonstrate the effect of the different presentation methods, as well as

judgements made by Entity D in determining how much information to present in the statement of profit or loss and the corresponding notes.

Scenario A: all expenses are presented by nature

Note that Scenario A does not elect to use the option in IFRS 18.B84 to present operating expenses before the allocation of amounts to the carrying amount of assets (e.g. inventories). Therefore, inventories expensed represent the amount of inventories expensed in the period applying the requirements of IAS 2.

Line item	Amount (thousands of CU)
Revenue	1,000
Salaries and wages	(100)
Depreciation (Note X)	(235)
Inventories expensed*	(360)
Share-based payments to employees	(60)
Distribution expenses	(40)
Operating profit	205

Note X: depreciation consists of:

► Depreciation of property, plant and equipment:	150
► Depreciation of right-of-use assets:	85
► Total	235

*In this scenario, Entity D is presenting expenses by nature only, therefore, it is not required to disclose the portion of depreciation, salaries, etc. that are included in inventories expensed in the period, because those amounts were included in the carrying amount of inventories when they were derecognised. In other words, the disclosures requirement in IFRS 18.83 does not apply to Entity D in this scenario.

Scenario B: all expenses are presented by function

Line item	Amount (thousands of CU)
Revenue	1,000
Cost of goods sold*	(400)
Gross profit**	600
Research and development	(300)
Administration	(95)
Operating profit	205

*Cost of goods sold consists of inventoried expensed (360) plus 40 of distribution expenses.

**See section 5.2 for further information on the use of additional subtotals. Entities are not required to present the 'gross profit' subtotal; however, it may be common for many entities, especially those that present cost of goods sold.

In Scenario B, Entity D must comply with the disclosure requirements of IFRS 18.83, which results in a single note that provides disclosure of certain expenses by nature and their respective allocations to functional categories.

Scenario C: cost of sales is presented (function) with all other expenses presented by nature ('mixed' presentation)

Line item	Amount (thousands of CU)
Revenue	1,000
Cost of goods sold*	(400)
Gross profit	600
Salaries not included in cost of goods sold	(100)
Depreciation not included in cost of goods sold (Note X)	(235)
Share-based payments to employees	(60)
Operating profit	205

Note X: depreciation consists of:

► Depreciation of property, plant and equipment:	150
► Depreciation of right-of-use assets:	85
► Total	235

*Cost of goods sold is calculated in the same manner as Scenario B.

In Scenario C, Entity D must comply with the disclosure requirements of IFRS 18.83, which results in a single note that provides certain expenses by nature and their respective allocations to functional categories.



BDO comment – presentation or disclosure of nature of amounts expensed or incurred

IFRS 18.B84 requires that (*emphasis added*):

An entity will either present expenses by nature, or applying paragraph 83, disclose some expenses by nature. The amounts presented or disclosed need not be the amounts recognised as an expense in the period. They could include amounts that have been recognised as part of the carrying amount of an asset.

Disclosure in the notes

IFRS 18.83(a) require that the 'total' for depreciation, amortisation, employee benefits (comprising share-based payments to employees as well as employee benefits in the scope of IAS 19 such as salaries, fringe benefits and post-employment benefits), impairment losses (and reversals) per IAS 36 and write-downs to net realisable value (and reversals) as per IAS 2 be disclosed for each line item comprising expenses classified by function in the operating category.

IFRS 18.B84 clarifies that the amounts ('total') disclosed are not required to be the amounts expensed in the statement of profit or loss during the period presented but can also include amounts capitalised to the carrying amount of assets. For example, an entity may incur CU100 of salary expenses in a reporting period, with some of those expenses recognised in profit or loss, and others recognised in the carrying amount of assets such as inventories, property, plant and equipment, etc.

Many entities maintain inventories at both the beginning and end of the financial year, meaning that an amount of salaries, depreciation, etc. incurred will be reflected in the carrying amount of inventories (assuming that salary expenses, depreciation, etc. form part of the cost of inventories).

To illustrate this issue, consider inventories produced by a manufacturing entity. Manufacturing costs related to inventories may not be recognised in profit or loss in the period they are incurred because some inventories will remain unsold at the end of the period. Additionally, entities' information systems may not be designed to differentiate certain expenses recognised in profit or loss (e.g. depreciation) between inventory produced in prior periods and inventory produced in the current period when presenting cost of sales. IFRS 18.B84 therefore provides an option to disclose the amount 'incurred' rather than expensed. Applying this method of disclosure, entities would disclose the amount of the specified expenses in IFRS 18.83(a) even if a portion of those expenses are recognised in the carrying amount of assets at the end of the period.

If an entity discloses the costs incurred rather than expensed, IFRS 18.B84(b) requires an entity to also provide a qualitative explanation of that fact and to identify the assets involved. See Example 4.4-3 below.

Presentation in the statement of profit or loss

Per IFRS 18.B84 an entity may also present the expenses incurred (and not expensed) by nature in the statement of profit or loss. If this is the case, IFRS 18.B84(a) requires that an entity should then present an additional line item for the change in the carrying amount of the affected assets.

For example:

Extract of the statement of profit or loss	Currency units
Revenue	X
Raw materials consumed	(X)
Employee benefits	(X)
Depreciation	(X)
Utilities	(X)
Change in inventory (finished goods and work in progress)	(X)
Operating profit	X

By presenting an additional line item for the change in the carrying amount of the affected asset, an entity adjusts the incurred costs to reflect the costs that have been expensed, similar to how the change in net working capital is presented in the statement of cash flows (presented using the indirect method) to adjust income and expenses in the statement of cash flows with the actual cash inflows and outflows.



Example 4.4-3 – Disclosure of the nature of amounts expensed or incurred (basic example)

A manufacturing entity manufactures and sells widgets. Assume that there are no opening inventory and no work-in-progress at period end. The entity presents 'cost of sales' as a functional line item in the statement of profit or loss, as well as 'administration'.

The following production-related information is available (the superscripted numbers below are used to explain how these amounts correspond to the presentation and disclosures that follow in the example):

	Total incurred	Capitalised into inventory expensed in the year – cost of sales line item	Capitalised into ending inventory balance	Recognised in profit or loss – administration line item
	CU	CU	CU	CU
Production costs				
Raw materials	20,000	18,000	2,000	-
Wages	40,000	31,000 ^{4&8}	5,000 ⁴	4,000 ⁶
Depreciation (right-of-use assets)	2,000	1,500 ^{5&9}	300 ⁵	200 ⁷
Depreciation (property, plant and equipment)	5,000	4,000 ^{5&9}	400 ⁵	600 ⁷
Water and electricity	500	400	50	50
Totals	67,500	54,900¹	7,750³	4,850²

The following was presented in the financial statements:

	20x2 CU
Statement of profit or loss	
Cost of sales	(54,900) ¹
Administration	(4,850) ²
Statement of financial position	
Inventory	7,750 ³

The following is required to be presented in the notes by IFRS 18.83(a) and (b):

Operating expenses by nature (IFRS 18.83(a), (b) and 18.B84)

	1. If costs incurred are disclosed	2. If expense is disclosed
	20x2 CU	20x2 CU
Cost of sales includes		
Employee benefits	36,000 ⁴	31,000 ⁸
Depreciation	6,200 ⁵	5,500 ⁹
Administration includes		
Employee benefits	4,000 ⁶	4,000 ⁶
Depreciation	800 ⁷	800 ⁷
Totals		
Employee benefits	40,000	35,000
Depreciation	7,000	6,300

4: CU31,000 + CU5,000

5: CU1,500 + CU300 + CU4,000 + CU400

6: CU4,000

7: CU200 + CU600

8: CU31,000

9: CU1,500 + CU4,000

The method selected by an entity will result in different figures being disclosed when operating expenses required to be disclosed by IFRS 18.83(a) include amounts recognised as part of the carrying amount of an asset, such as inventory. For example, the difference between the figures presented in the above table for methods #1 and #2 relating to employee benefits is CU5,000 (CU36,000 – CU31,000), which is the amount of wages recognised as part of the carrying amount of inventories.

Regardless of which method is chosen to disclose the nature of the expenses included in functional line items, IFRS 18.82(b) requires an entity to disclose a qualitative description of the nature of expenses included in each function line item. For example, this disclosure may be illustrated as follows:

'In addition to employee benefits and depreciation, the cost of sales line item also includes raw material expenses and variable production overheads such as utilities. The administration line item also includes employee benefits, depreciation and utilities not related to the production of inventories.'

If the costs incurred are disclosed, additional disclosures are required by IFRS 18.B84(b), for example:

'Not all amounts disclosed above related to cost of sales have been recognised in profit or loss. A portion of depreciation related to property, plant and equipment and right-of-use assets and employee benefits expense have been capitalised to the carrying amount of inventory, therefore, some of the amount disclosed above is recognised in the carrying amount of inventory at reporting date.'



Example 4.4-4 – presentation or disclosure of nature of amounts expensed or incurred (interaction with other notes)

When an entity presents the amounts incurred per the nature of functional line items disclosure, the interaction with other notes in the financial statements should be considered. Line items such as write-down to net realisable value should be consistent between the inventory note and the nature of function line items note.

Below is an extract of a manufacturing entity's statement of profit or loss. It carries out research and development activities as well. All research and development activities are, however, expensed during the year incurred (i.e. no expenses are reflected in the carrying amount of assets).

Statement of profit or loss

	CU
Revenue	1,000
Cost of sales	<u>(500)</u>
Gross profit	500
Research and development	(150)
Other operating expenses	<u>(100)</u>
Operating profit	250

The following information is disclosed in the notes:

Property, plant and equipment

	CU
Carrying amount 1 January 20x0	1,000
Movements during the year:	
Additions	80
Depreciation	<u>(120)</u>
Carrying amount 1 January 20x0	960

Defined benefit obligation

	CU	
Carrying amount 1 January 20x0	300	
Movements during the year:		
Current service costs	50	B
Interest expense	<u>5</u>	
Total amounts recognised in profit or loss	55	
Actuarial gain	(20)	
Total amounts recognised in other comprehensive income	<u>(20)</u>	
Carrying amount 31 December 20x0	335	

Employee benefits

	CU	
Short-term employee benefits	200	C
Post-employee benefits	50	B
Termination benefits ¹	30	
Share-based payments	<u>60</u>	D
Total employee benefits expense	340	

1: Termination benefits are included in the line item 'Other operating expenses' in the statement of profit or loss

IFRS 18.82(b) and 18.83 require additional information to be disclosed for line items comprising expenses classified by function (see section 4.4). Per IFRS 18.B84, the amounts presented or disclosed does not need to be the amount expensed in profit or loss but could include amounts that have been recognised as part of the carrying amount of an asset (see Example 4.4-3).

1. Disclosure of operating expenses by nature based on amounts incurred (including costs capitalised to assets)

If the entity decides to disclose the amounts recognised as part of the carrying amount of assets, the following must be disclosed:

Operating expenses by nature			Calculations ¹
	Cost of sales / capitalised to inventory	Research and development	Total
Depreciation of property, plant and equipment	100	20	120
Employee benefits	200	50	250
Share-based payments	40	20	60
	340	90	430

'In addition to depreciation, employee benefits and share-based payments, the cost of sales line item also includes raw material expenses and variable production overheads. Similarly, the research and development line item also includes other costs such as consumables and utilities.'

Not all amounts disclosed above related to cost of sales have been recognised in profit or loss. A portion of depreciation related to property, plant and equipment and right-of-use assets and employee benefits expense have been capitalised to the carrying amount of inventory, therefore, some of the amount disclosed above is recognised in the carrying amount of ending inventories.'

1. The 'Calculations' column does not form part of the disclosure. It is included in this example to illustrate how amounts disclosed in the 'Operating expenses by nature' note ties up to the other notes disclosed. As can be seen in this example, the different notes correlate since the amounts incurred during the year were disclosed.

2. Disclosure of operating expenses by nature based on amount recognised as an expense in profit or loss

If the entity decides to disclose the amounts recognised as part of the carrying amount of assets, the following must be disclosed (IFRS 18.83(a) and 18.B84(b)):

Operating expenses by nature			
	Cost of sales	Research and development	Total
Depreciation of property, plant and equipment	90	20	110
Employee benefits	190	50	240
Share-based payments	35	20	55
	315 ¹	90 ²	405 ³

'In addition to depreciation, employee benefits and share-based payments, the cost of sales line item also includes raw material expenses and variable production overheads. Similarly, the research and development line item also includes other costs such as consumables and utilities.'

1. In this case, cost of sales relates solely to amounts recognised in profit or loss for the current year. It therefore includes costs included in the opening balance of inventory sold during the year and excludes costs incurred during the year but capitalised to the closing inventory balance, as those items have not yet been sold.
2. Since no research and development costs were capitalised to intangible assets. The amounts incurred equate to the amounts expensed.
3. In this case, the total amounts disclosed in the 'Operating expenses by nature' note do no tie up to the other notes disclosed since the amounts disclosed as part of the 'Cost of sales' column relate solely to amounts recognised in profit or loss for the current year where the amount disclosed in the other notes relate to amounts incurred during the current year. The amounts disclosed relating to research and development however do not create a difference between 'Operating expenses by nature' note and the other notes since the research and development amounts incurred equate to the amounts expensed.



Example 4.4-5 – presentation of non-recurring items by function

Fact pattern

Entity A presents operating expenses by function in the statement of profit or loss. During the year, Entity A's warehouse was hit by a cyclone, damaging some inventory as well as the warehouse itself. This led to the recognition of both a write-down to the net realisable value relating to inventory and an impairment loss relating to the warehouse (property, plant and equipment). These losses are material.

Prior to the cyclone, Entity A used the following structure for its statement of profit or loss (extract provided):

Statement of profit or loss	CU
Revenue	XXX
Cost of sales	(XX)
Gross profit	XX
Other operating income	XX
Other operating expenses	XX
Operating profit	X

Inventory recognised as an expense is included in the 'cost of sales' line item and impairment losses are usually included in the 'other operating expenses' line item.

Presentation of loss due to cyclone damage

Entity A presents operating expenses by function based on the activity to which the consumption of resources relates. This raises the question whether it is appropriate to present the loss related to the cyclone damage as a separate line item?

To determine the most appropriate presentation of these losses, an entity should consider the general presentation requirements of IFRS 18, including:

- ▶ presenting information about its income and expenses in a structured summary within the statement of profit or loss to provide useful information (see section 4.1).
- ▶ aggregating or disaggregating line items to achieve a useful structured summary (see section 4.2).
- ▶ presenting or disclosing non-recurring income and expenses separately if they have sufficiently dissimilar characteristics (IFRS 18.B79 and IFRS 18.BC55); and
- ▶ if operating expenses are presented by function, ensuring that the allocation of expenses to functions is not arbitrary. If it would not provide a faithful representation of the functions, entities should present the expenses by nature instead (see section 4.4, IFRS 18.B80(d)).

IFRS 18.B17 explains that an entity shall aggregate items based on shared characteristics. Both the write-down to net realisable value and the impairment loss relate to the same cyclone damage and therefore have shared characteristics. The cyclone is not expected to recur in the future and is regarded as a 'non-recurring' expense.

In our view, material, non-recurring operating expenses may be presented separately and not within functional line items (unless another presentation is required by a regulator or enforcer within a specific jurisdiction - see below).

Presenting these losses separately on the face of the statement of profit or loss provides a useful structured summary that allows users of the financial statements to:

- ▶ identify items for which users may seek further information in the notes; and
- ▶ compare financial performance between periods, as this loss is a one-time occurrence and is not expected to recur, since it is not comparable with prior or future periods.

This separate presentation is illustrated below:

Statement of profit or loss	CU
Revenue	XXX
Cost of sales	(XXX)
Gross profit	XX
Loss due to cyclone damage*	(YZ)
Other operating income	XX
Other operating expenses	(XX)
Operating profit	X

* Inventory write-down and property, plant and equipment impairment

Narrative information about the cyclone damage and the disaggregation of the loss between the write-down to net realisable value and impairment losses will be further disclosed in the notes.

Views of reporting regulators or enforcers

According to IFRS 18.82, the cost of sales line item, which is a functional line item, is required to include the total inventory expense as per IAS 2.38. This consists of costs previously included in the measurement of inventory that has been sold, unallocated production overheads, and abnormal amounts of production costs of inventories.

Certain regulators or enforcers may believe that while separate presentation of non-recurring items is permitted or required by IFRS 18, it would not be appropriate to exclude costs that by function are part of cost of sales. The following presentation may therefore be appropriate, which includes the amount of inventory write-downs in the calculation of gross profit:

Statement of profit or loss	CU
Revenue	XXX
Cost of sales excluding write-off due to cyclone damage	(Y)
Inventory write-off due to cyclone damage	(XXX)
Gross profit	XX
Property, plant and equipment impaired due to cyclone damage	(Z)
Other operating income	XX
Other operating expenses	(XX)
Operating profit	X



Example 4.4-6 – presentation of foreign exchange differences by nature and function

An entity has both trade receivables and trade payables denominated in foreign currencies.

It presents the following line items in its statement of profit or loss:

	CU
Revenue	xxx
Cost of sales	(xxx)
Gross profit	xxx

IFRS 18.B65 requires that foreign exchange differences recognised in profit or loss be classified in the same category as the income and expenses relating to the items that give rise to the foreign exchange differences, unless doing so would involve undue cost or effort (see section [3.9.3](#)).

IFRS 18 does not set out specific requirements relating to the line item (or line items) the foreign exchange differences should be presented in.

This raises the question of whether it would be appropriate for entities to present foreign exchange differences in the same line item as the income or expense that they relate to (as either a line item by nature or a functional line item)? For example, the foreign exchange differences relating to trade receivables in the revenue line item in the statement of profit or loss.

Aggregation with the revenue line item

Would it be appropriate for an entity to present the foreign exchange differences related to trade receivables in the same line item as revenue?

In our view, foreign exchange differences should not be presented together with the related revenue.

IFRS 18.41(b) requires separate presentation of items that do not share the same characteristics. Additionally, IFRS 18.80 states that, when presenting operating expenses by nature, entities should disclose expenses based on the nature of the resources consumed, without reference to the specific activities for which those resources were used.

It is not appropriate to present foreign exchange differences together with the related revenue in the same line item, as this would combine items of different natures (contrary to IFRS 18.80) and fail to disaggregate items with dissimilar characteristics (per IFRS 18.41(b)).

Therefore, as an example, it would be inappropriate to present foreign exchange differences related to trade receivables in the revenue line item.

Aggregation with the cost of sales line item

Would it be appropriate for an entity to present the foreign exchange differences related to trade payables in the same line item as cost of sales?

Generally, in our view, it is more appropriate to present foreign exchange separately from cost of sales, although aggregated presentation might be appropriate when certain facts and circumstances apply.

Under IFRS 18.81, when presenting expenses by function, entities must allocate and aggregate operating expenses based on the activity to which the consumed resource relates. While IFRS 18.81(b) allows expenses relating to resources of several natures to be allocated to the same line item, foreign exchange differences generally do not relate to the cost of sales activity. Instead, they generally arise from the entity's short-term financing decisions. If accounts payable were settled immediately, no foreign exchange difference would occur.

4.4.5. Consistency of presentation, disclosure and classification

Entities are required to maintain a consistent method of presentation from one period to the next, as the method selected is an accounting policy. Any change in the basis of presentation (e.g. from operating expenses being presented entirely by nature to a mixed presentation basis) must (IFRS 18.30):

- (a) Arise from a significant change in the nature of the entity's operations or arise from a review of its financial statements, and it is concluded that another presentation would be more appropriate considering the criteria in IAS 8; or
- (b) Arise from a requirement in an IFRS Accounting Standard which requires a change in presentation.

Any change in presentation basis (e.g. a change in judgement concerning aggregation of income and expenses) is accounted for as a change in accounting policy, therefore, comparative information must be restated.

4.5. Labels and descriptions used

Entities are required to describe items presented in the primary financial statements (line items and subtotals) or items disclosed in the notes in a way that faithfully represents the characteristics of the item (IFRS 18.43). Labels will often apply to items that have been aggregated (e.g. a 'salaries and wages' line item will generally comprise thousands of individual transactions).

An entity is required to provide all descriptions and explanations necessary for a user of financial statements to understand the item. In some cases, this may be achieved simply (e.g. utility expenses), however, in other cases, more judgement may be required.

4.5.1. Use of 'other'

Entities may only present or disclose items as 'other' if another more informative label cannot be found (IFRS 18.B25).

For example, if many immaterial items are aggregated with the label 'other expenses' being used in the statement of profit or loss, an entity may find a more informative label by aggregating items that share similar characteristics and describing them in a way that faithfully represents the similar characteristics.

If an entity uses the 'other' label because a more informative label cannot be found, additional requirements apply (IFRS 18.B26):

- (a) For any aggregation using the 'other' label: the entity shall use a label that describes the aggregated item as precisely as possible (e.g. 'other operating expenses' or 'other finance expenses' rather than 'other expenses').
- (b) For an aggregation of immaterial items, the entity shall consider whether the aggregated amount is sufficiently large that users might reasonably question whether it includes items for which information could be material (i.e. material items being obscured by immaterial items). In such cases, the entity is required to disclose further information, for example:
 - i. An explanation that no items for which information would be material are included in the amount; or
 - ii. An explanation that the amount comprises several items for which information would not be material, with an indication of the nature and amount of the largest item.

These additional requirements around the use of the 'other' label have been introduced to address user concerns that overuse of the label has obscured useful information in financial statements.

4.5.2. Labelling of subtotals

Requirements applicable to the labelling of mandatory and additional subtotals presented in the statement of profit or loss are discussed in section [5](#).

5. Totals and subtotals presented in the statement of profit or loss

Once an entity has classified individual items of income and expense into the appropriate categories (section 3), and it has aggregated those items into appropriate levels of aggregation for presentation in the statement of profit or loss (section 4), mandatory and additional subtotals are presented as a result of the previous steps.

For example, for an entity without specified main business activities (see section 3.8), a typical statement of profit or loss may be as follows (a mixed presentation method for operating expenses has been used – see section 4.4):

Line item		Classification
Revenue	XXX	Operating category
Cost of sales	XXX	
Gross profit	XXX	
Other operating income	XXX	
Selling expenses	XXX	
Research and development	XXX	
General and administrative	XXX	
Operating profit	XXX	Mandatory specified subtotal
Fair value gains on investments in equity instruments	XXX	Investing category
Profit before financing and income taxes	XXX	Mandatory specified subtotal
Interest expense on borrowings and lease liabilities	XXX	Financing category
Profit before income taxes	XXX	Additional subtotal
Income tax expense	XXX	Income taxes category
Profit from continuing operations	XXX	Additional subtotal
Loss from discontinued operations	XXX	Discontinued operations category
Profit	XXX	Mandatory total

As noted in this example, certain line items are mandatory, and others are additional (i.e. those that are not mandatory but meet the criteria in IFRS 18 to be disclosed in addition to mandatory subtotals). Sections 5.1 and 5.2 discuss the requirements of IFRS 18 applicable to mandatory and additional subtotals in the statement of profit or loss.

5.1. Mandatory subtotals

Mandatory subtotals are based on how the entity has classified its income and expenses into the five categories. The categorisation of expenses into these categories (and the assessment of whether the entity has specified main business activities) is necessary as it affects how subtotals are calculated.

IFRS 18 only requires two mandatory subtotals be presented before profit or loss (IFRS 18.69):

Mandatory subtotal – introduced by IFRS 18	Explanation
Operating profit	The total of all income and expenses classified in the operating category.
Profit or loss before financing and income taxes*	The total of operating profit or loss and all income and expenses classified in the investing category.

*Certain entities are not permitted to present this subtotal; see section 5.1.3 below.

IFRS 18 also requires these totals and subtotals, consistent with the requirements of IAS 1:

Mandatory subtotal – consistent with IAS 1	Explanation
Profit or loss	The total of income less expenses included in the statement of profit or loss.
Total other comprehensive income	The total of amounts recorded in other comprehensive income.
Total comprehensive income	The total of profit or loss and other comprehensive income.

There is no requirement in IFRS 18 for an entity to present:

- ▶ Profit or loss before income taxes (all income and expenses other than those classified in the income taxes category, and the discontinued operations category if applicable); or
- ▶ Profit or loss from continuing operations (all income and expenses other than those classified in the discontinued operations category).

However, it is expected that many entities will consider these additional subtotals to be useful, and will therefore present them as additional subtotals (see section 5.2).

IFRS 18 also does not require any mandatory subtotal related to the investing category (e.g. total investing income).

5.1.1. Operating profit

As operating profit includes all income and expenses classified in the operating category, operating profit is a default or residual subtotal, meaning that it includes all income and expenses of the entity unless they are classified into another category.

5.1.2. Profit or loss before financing and income taxes

As profit or loss before financing and income taxes is defined as the total of operating profit or loss and all income and expenses classified in the investing category, this subtotal is essentially all income and expenses before income and expenses classified in the remaining three categories: (1) financing; (2) income taxes; and (3) discontinued operations.

The IASB decided to require this subtotal because many users of financial statements seek to analyse an entity's performance independently of how the entity is financed (IFRS 18.BC148). For example, an entity may earn significant operating profits, but due to significant borrowing costs, it may be unprofitable overall. Separating the cost of financing from the operating profits provides useful information to users, including the ability to compare the operations of two or more entities independent of the cost of financing those entities.

In certain cases, entities do not present the profit or loss before financing and income taxes subtotal; see 5.1.3 below.

5.1.3. Profit or loss before financing and income taxes – entities that provide financing to customers as a main business activity

As discussed in sections 3.8.2 and 3.9.2, for entities that provide financing to customers as a main business activity, entities have an accounting policy choice for how income and expenses related to liabilities that arise from transactions that involve only the raising of financing but are not related to providing financing to customers are presented. This choice also affects how gains and losses on certain derivatives and income and expenses relating to cash and cash equivalents are classified (see sections 3.9.2 and 3.9.1).

For entities that elect to classify such income and expenses in the operating category, IFRS 18.73 does not permit an entity to present the profit or loss before financing and income taxes subtotal. This is not an optional exemption – in such cases, IFRS 18.73 forbids the profit or loss before financing and income taxes subtotal from being presented.

However, in this case, entities shall determine whether to present an additional subtotal (see section [5.2](#) below) after operating profit and before the financing category. However, if an entity presents an additional subtotal in this manner (e.g. the total of operating profit or loss and all income and expenses classified in the investing category), the entity shall not label the subtotal in a way that implies the subtotal excludes financing amounts (e.g. profit before financing) (IFRS 18.74).

5.2. Additional subtotals

IFRS 18 requires entities to present additional line items (including subtotals) if such presentation is necessary for a primary financial statement to provide a useful structured summary. However, any additional line items (and subtotals) must (IFRS 18.24):

- (a) comprise amounts recognised and measured in accordance with IFRS Accounting Standards;
- (b) be compatible with the statement structure described in section [4.1](#);
- (c) be consistent from period to period; and
- (d) be displayed no more prominently than the totals and subtotals required by IFRS Accounting Standards.

IFRS 18.24 is not optional; it is a requirement for an entity to consider whether additional subtotals should be presented in order for the statement of profit or loss (and all primary financial statements) to provide a useful structured summary.

Additional subtotals may be presented 'within' other subtotals, including those required by IFRS 18. For example, operating profit or loss comprises the total of all income and expenses classified in the operating category, however, entities may also present subtotals such as 'gross profit', 'net interest income', or 'net interest margin', as long as those subtotals meet the requirements of IFRS 18.24. Such subtotals may be common in certain industries.

5.2.1. Additional subtotals and management-defined performance measures

Additional subtotals could also meet the definition of MPMs resulting in additional disclosure requirements (see sections [6.2](#) and [6.3](#)). However, certain subtotals of income and expenses that meet the definition an MPM (such as gross or operating profit) are not deemed to be an MPM per IFRS 18.118 (see section [6.2.2](#)). By excluding these subtotals from the definition of an MPM, entities are not required to provide any MPM-related disclosures for these subtotals.



6. Management-defined performance measures

6.1. Introduction

One of the key concepts introduced by IFRS 18 is management-defined performance measures (MPMs). IFRS 18 defines MPMs and includes specific disclosure requirements related to MPMs.

MPMs are subtotals of income and expenses that an entity uses in public communications outside financial statements to communicate management's view of an aspect of the financial performance of the entity as a whole. Subtotals of income and expenses specifically required to be presented or disclosed by IFRS Accounting Standards are not MPMs. IFRS 18.118 also lists certain subtotals of income and expenses which are deemed not to be MPMs (IFRS 18.117 and Appendix A).

Many entities may include non-GAAP or Alternative Performance Measures (APMs) in their narratives and other analyses such as management discussion and analysis. MPMs, as defined in IFRS 18, are a subset of APMs. Users of financial statements noted that information about MPMs is useful as it provides insight into how the business is managed, how management views the entity's financial performance, and the persistence of the entity's financial performance (IFRS 18.BC325). Agreeing that MPMs can provide useful information about an entity's financial performance, the IASB introduced disclosure requirements related to MPMs to improve transparency of these measures. The IASB observed that including such measures in the financial statements will make the measures subject to the same disclosure requirements, regardless of an entity's jurisdiction, and likely bring them within the scope of audit (IFRS 18.BC326).



BDO comment – MPM disclosures

Entities that have historically disclosed APMs and other non-GAAP measures may already be subject to disclosure requirements from regulators. For example, if an entity discloses 'adjusted profit', many securities regulators have historically imposed disclosure requirements about those APMs, such as reconciliations to GAAP amounts, explanations of the amounts, etc. See section [6.4.3](#) for further considerations relating to MPMs and the interaction with other regulatory requirements.

However, these types of disclosures have generally been contained outside of the financial statements, for example, in management discussion & analysis (MD&A), strategic reports, etc. IFRS 18 requires disclosures relating to MPMs to be included in the financial statements in a single note (IFRS 18.122). For entities subject to audit, this 'single MPM note' will also be audited, which may be a significant change in practice for many entities where information that is traditionally outside of the financial statements has historically not been subject to audit.

For each MPM, IFRS 18 requires an entity to disclose information including a description of the aspect of financial information communicated by the MPM, the method of calculation of the MPM and a reconciliation between the MPM and the most directly comparable subtotal specified by IFRS 18 or other IFRS Accounting Standards (IFRS 18.123).

Subsequent subsections provide detailed analysis of the requirements related to MPMs.

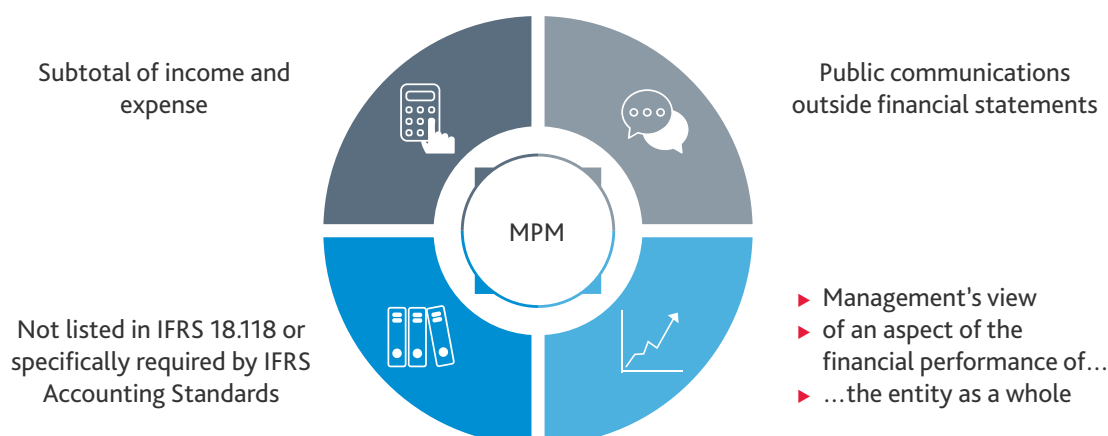
It should be noted that an entity might have no MPMs, one MPM or more than one MPM. For example, an entity that publicly communicates its financial performance to users of financial statements using only totals and subtotals required to be presented or disclosed by IFRS Accounting Standards does not have any MPMs within the disclosure requirements of IFRS 18 (IFRS 18.B113).

6.2 What are management-defined performance measures?

IFRS 18.117 defines a management-defined performance measure as 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

Four components of the definition of an MPM



The following subsections discuss the above noted four components of the definition of an MPM.

6.2.1 Subtotal of income and expenses

The definition of MPMs in IFRS 18 is limited only to subtotals of income and expenses. Other measures that are not subtotals of income and expenses, e.g. adjusted cash flow measures or debtor turnover ratio, are not MPMs within the scope of IFRS 18.

Some stakeholders suggested that the IASB include in the definition of MPMs measures other than subtotals of income and expenses (for example, subtotals of assets and liabilities, or measures of cash flow) to bring about transparency and discipline in communicating these other measures (IFRS 18.BC332). While acknowledging the observation, the IASB decided to restrict the definition of MPMs to subtotals of income and expenses, as widening the definition would involve substantial work that would go beyond the scope of the IASB's project focused on the reporting of financial performance in the statement of profit or loss and the related notes (IFRS 18.BC333).



BDO comment – Can an entity disclose measures other than those that meet the definition of MPMs in the financial statements?

IFRS 18.20 requires an entity to consider whether to provide additional disclosures when compliance with the specific requirements in IFRS Accounting Standards is insufficient to enable users of financial statements to understand the effect of transactions and other events and conditions on the entity's financial position and financial performance.

The IASB did not specifically prohibit the disclosure of measures that do not meet the definition of MPMs in the financial statements as such requirements might discourage best practice for voluntary disclosures that are useful to users of financial statements (IFRS 18.BC372).

Therefore, an entity is not prohibited from disclosing measures that do not meet the definition of MPMs in the financial statements as long as such disclosure is to enable users of financial statements to understand the effect of transactions and other events and conditions on the entity's financial position and financial performance. The entity may include information about these measures in the single note on MPM disclosures as required by IFRS 18.122 (see section 6.3.1). However, the information in the note is required to be labelled in a way that clearly distinguishes the information required to be disclosed as per the MPM disclosure requirements from the other information (IFRS 18.B132). The disclosures of such other measures must also comply with the requirements of IFRS 18 related to faithful representation of the characteristics of the items.

An entity would also need to carefully consider the view of jurisdictional regulators on the disclosures of measures that do not meet the definition of MPMs in the financial statements.

It is not required for a subtotal of income and expenses to be presented in the statement of profit or loss to meet the definition of an MPM. A subtotal that meets the definition of an MPM as per IFRS 18.117 is an MPM irrespective of whether it is presented in the statement of profit or loss (IFRS 18.B118).

The following are several examples of measures that are not MPMs as they are not subtotals of income and expenses:

Nature (IFRS 18.B116)	Example
Subtotals of only income or only expenses	▶ Adjusted revenue ▶ Employee benefit expenses, excluding share-based payment expenses
Assets, liabilities, equity or combinations of these elements	▶ Net working capital ▶ Net debt
Financial ratios (A numerator or denominator of a financial ratio may be an MPM. See section 6.2.1.1 below)	▶ Debtor turnover ratio ▶ Debt to equity ratio ▶ Loan to value (LTV) ratio ▶ Loan recovery rate
Measures of liquidity or cash flows	▶ Free cash flows
Non-financial performance measures	▶ Product recall rate ▶ Employee turnover rate ▶ Customer retention ratio

IFRS 18.118 lists certain subtotals of income and expenses that are specifically excluded from the definition of MPMs. See section [6.2.2](#) below for further details.

6.2.1.1. Subtotal is a numerator or denominator of a financial ratio

A financial ratio is not an MPM as it is not a subtotal of income and expenses. However, a subtotal that is the numerator or denominator in a financial ratio is an MPM if the subtotal would meet the definition of an MPM if it were not part of a ratio (IFRS 18.B117).

For example, an entity measures 'adjusted operating profit per share' as (adjusted operating profit / number of equity shares outstanding). Adjusted operating profit per share is not an MPM as it is not a subtotal of income and expenses. But 'adjusted operating profit', which is the numerator of the ratio, is a subtotal of income and expenses. Therefore, the disclosure requirements related to MPMs apply to adjusted operating profit.



BDO comment – Does the numerator or denominator in a financial ratio that is a subtotal of income and expenses meet the definition of an MPM if the numerator or denominator is not used in public communications outside financial statements by itself?

IFRS 18.B117 includes within the scope of MPM disclosures those numerators or denominators in a financial ratio that are subtotals of income and expenses and would meet the definition of an MPM if they were not part of a ratio.

One of the criteria in the definition of an MPM is that the entity uses the subtotal in public communications outside financial statements. Therefore, a question arises as to whether the subtotal that is a numerator or denominator in a financial ratio is required to be used in public communications outside financial statements by itself to meet the definition of MPM.

For instance, an entity uses adjusted operating profit per share in its public communications outside financial statements. Adjusted operating profit, which is the numerator in the ratio is a subtotal of income and expenses. However, the entity does not use adjusted operating profit by itself in public communications.

In our view, the numerator or denominator, in such cases, would be considered to meet the definition of MPM if it meets all the criteria in the definition of MPM, except the requirement related to use in public communications outside financial statements. In other words, the numerator or denominator should be a subtotal of income and expenses, which is used to communicate management's view of an aspect of financial performance of the entity as a whole and should not be listed in IFRS 18.118 or specifically required to be presented or disclosed

by IFRS Accounting Standards. It is not required that the numerator or denominator by itself be used in public communications outside financial statements. It is sufficient that the financial ratio in which the subtotal is used as a numerator or denominator is used in public communications outside financial statements.

It should be noted that the disclosure requirements related to MPMs apply to such numerator or denominator; and not to the financial ratio.

6.2.2 Not listed in IFRS 18.118 or specifically required by IFRS Accounting Standards

The IASB observed that some subtotals are not defined by IFRS Accounting Standards, but are commonly used in financial statements and are well understood by users of financial statements. Therefore, the IASB decided to exclude such subtotals from the scope of MPM disclosure requirements (IFRS 18.BC362).

These excluded subtotals are listed in IFRS 18.118 as below:

- (a) gross profit or loss (revenue minus cost of sales) and similar subtotals (see section 6.2.2.1 below);
- (b) operating profit or loss before depreciation, amortisation 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 provides financing to customers and applies the accounting policy choice of classifying in the operating category income and expenses from liabilities that do not relate to the provision of financing to customers as per IFRS 18.73 (see section 5.1.3 for the requirements of IFRS 18.73), 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.



BDO comment – Is EBITDA (earnings before interest, tax, depreciation and amortisation) an MPM?

The IASB considered whether to define EBITDA in IFRS 18, as many entities compute EBITDA in different ways, however, the IASB decided not to do so. The IASB observed that, although EBITDA is one of the most commonly used measures in communications to users of financial statements, it is not used by entities in some industries, such as banking and insurance (IFRS 18.BC363).

The IASB included the subtotal 'operating profit or loss before depreciation, amortisation and impairments within the scope of IAS 36' in the list of exclusions because, in the IASB's view, the measure is well defined (IFRS 18.BC364). The IASB decided not to describe this subtotal as 'EBITDA' because doing so would imply that operating profit or loss is the same as what users of financial statements understand 'earnings before interest and tax' to be, which might not be the case (IFRS 18.BC365).

In some cases, EBITDA may be an accurate description of operating profit or loss before depreciation, amortisation and impairments within the scope of IAS 36, for example if an entity has no income and expenses in the investing category such that all its earnings are included in operating profit. In such cases, an entity would not be prevented from labelling the subtotal operating profit before depreciation, amortisation and specified impairments within the scope of IAS 36 as 'EBITDA'. (IFRS 18.BC366).

Therefore, if an entity uses EBITDA as a performance measure in its public communications outside financial statements, there are two scenarios:

1. EBITDA, for the entity, is an accurate labelling of operating profit before depreciation, amortisation and specified impairments within the scope of IAS 36:
In this case, EBITDA would be exempted from the MPM disclosure requirements as operating profit before depreciation, amortisation and specified impairments within the scope of IAS 36 is excluded from the scope of MPM disclosures.
2. EBITDA, for the entity, is different from operating profit before depreciation, amortisation and specified impairments within the scope of IAS 36:
In this case, EBITDA would be considered an MPM as it is not one of the exclusions specified in IFRS 18.118 or a subtotal specifically required by IFRS Accounting Standards.



BDO comment – Can additional subtotals meet the definition of MPMs?

IFRS 18.24 requires an entity to present additional subtotals if such presentations are necessary for a primary financial statement to provide a useful structured summary.

IFRS 18.117(c) excludes from the definition of MPMs those subtotals that are specifically required to be presented or disclosed by IFRS Accounting Standards.

In our view, although IFRS 18.24 generally requires an entity to provide additional subtotals when necessary to provide a useful structured summary, these are not specifically required. Therefore, in our view, additional subtotals would meet the definition of an MPM, provided the other criteria of the definition are met.

6.2.2.1 Subtotals similar to gross profit

A subtotal is similar to gross profit when it depicts the difference between a type of revenue and directly related expenses incurred in generating that revenue. The following are some examples of subtotals similar to gross profit (IFRS 18.B123):

- a) net interest income
- b) net fee and commission income
- c) insurance service result
- d) net financial result (investment income minus insurance finance income and expenses)
- e) net rental income

Such subtotals are excluded from the definition of MPMs.

6.2.3 Public communications outside financial statements

To meet the definition of an MPM, a subtotal of income and expenses is required to be included in public communications outside financial statements.

IFRS 18 does not define public communications, but it provides a non-exhaustive list of which public communications would be considered to be included or excluded from this definition (IFRS 18.B119).

Modes of communication	
Included in public communications	Excluded from public communications
Management commentary	Oral communications
Press releases	Written transcripts of oral communications
Investor presentations	Social media posts

The IASB decided to provide exclusions for oral communication, written transcripts of oral communications and social media posts because the IASB expected these forms of communication to contain information about MPMs already included in other forms of communication. Another reason for these exclusions was to address stakeholder concerns that these forms of communication are the most challenging to monitor. (IFRS 18.BC336).





BDO comment – Are there any exemptions to private entities from providing MPM disclosures?

The IASB considered whether to provide specific requirements for private entities. However, the IASB concluded that the intention of the requirements to provide transparency and discipline over performance measures communicated to users outside financial statements applies regardless of whether the entity is private or public. (IFRS 18.BC342). Therefore, there is no exemption for private entities from providing disclosures related to MPMs.

However, many private entities do not make public communications outside financial statements. Therefore, many private entities will not make any public communications which trigger the MPM disclosure requirements. If a private entity uses subtotals of income and expenses in public communications outside financial statements that meet the definition of MPMs, the entity would be required to provide the applicable disclosures for those MPMs. Some jurisdictional regulators may require private entities to file narrative and other reports, which may be available to the general public. If a private entity uses MPMs in such filings, the entity would be required to provide the applicable disclosures for those MPMs in the financial statements. Refer to 'BDO comment - Measures made available to users through regulatory filings – Do they meet the definition of MPMs?' in section [6.2.4](#).

6.2.3.1 MPM to relate to the same reporting period as the financial statements

IFRS 18.B120 clarifies that MPMs relate to the same reporting period as the financial statements. It further states that specifically, a subtotal:

- relating to interim financial statements but not to the annual financial statements can only be an MPM in the interim financial statements; and
- relating to annual financial statements but not to interim financial statements can only be an MPM in the annual financial statements.

An entity is required to consider only public communications related to the reporting period to identify MPMs for the reporting period. However, at times, entities issue public communications after the date of issue of its financial statements. If an entity routinely issues such public communications, the entity is required to consider public communications related to the previous reporting period to identify MPMs for the current reporting period (IFRS 18.B121).

For example, Entity A routinely issues investor presentations a few days after the issue of its financial statements. When Entity A prepares its financial statements for the annual reporting period ended 31 December 20X2, Entity A is required to consider the investor presentations related to the annual reporting period ended 31 December 20X1 to identify MPMs to be disclosed for the annual reporting period ended 31 December 20X2.

Expected cessation of an MPM included in the previous reporting period

At times, a measure used in public communications related to the previous reporting period may not be expected to be included in the public communications to be issued relating to the current reporting period. If sufficient evidence exists to support this assertion, the entity is not required to identify such measure as MPMs for the current reporting period. However, disclosure requirements related to a change to or a cessation of an MPM apply (see section [6.3.6](#)) (IFRS 18.B122).

6.2.4 Management's view of an aspect of the financial performance of the entity as a whole

To meet the definition of an MPM, a subtotal of income and expenses must be used by the entity to communicate to users of financial statements management's view of an aspect of the financial performance of the entity as a whole (IFRS 18.117(b)).

Three elements of the criterion



6.2.4.1 Management's view

The IASB's intention behind developing the MPM disclosure requirements and the disclosure objective of these requirements is to provide information to users to understand management's view of the entity's financial performance (IFRS 18.BC325).

6.2.4.1.1 Presumption about communicating management's view

IFRS 18 contains a rebuttable presumption that a subtotal of income and expenses used in public communications outside financial statements communicates to users of financial statements management's view of an aspect of the financial performance of the entity as a whole (IFRS 18.119).

The IASB expects the presumption to provide rigour and discipline in the assessment of whether a measure communicates management's view by setting out a condition usually expected to be true. The IASB observed that it is reasonable to expect that the inclusion of a subtotal in public communications is for the purpose of communicating to users of financial statements management's view of an aspect of its financial performance. (IFRS 18.BC349).

Rebuttal of presumption

The presumption about communicating management's view is a rebuttable presumption. The IASB has noted that the presumption is not intended to result in disclosure of information about a large number of subtotals. The rebuttable presumption provides an objective process for an entity to determine which measures in its public communications to disclose in its financial statements to meet the objective of the disclosures for MPMs (IFRS 18.BC347).

IFRS 18 permits an entity to rebut the presumption about the MPM communicating management's view if it has reasonable and supportable information available that demonstrates that:

- the subtotal does not communicate to users of financial statements management's view of an aspect of the financial performance of the entity as a whole; and
- the entity has a reason for using the subtotal in its public communications other than communicating management's view of an aspect of the financial performance of the entity as a whole (IFRS 18.B124).

To rebut the presumption, an entity must meet both of the criteria above.

It should be noted that the requirements related to the rebuttal apply to a subtotal and not to individual items of income and expense that comprise the subtotal. Therefore, an entity is not permitted to rebut the presumption on the basis of information that demonstrates that an individual item (or items) of income or expense within the subtotal does not represent management's view.

IFRS 18 provides examples of reasonable and supportable information that might be considered to demonstrate the above criteria being met:

Criterion	Examples
(a) The subtotal does not communicate management's view of an aspect of the financial performance of the entity as a whole	▶ The entity communicates the subtotal without prominence (IFRS 18.B125(a)) (see further discussion below) ▶ Management does not use the subtotal internally to assess or monitor the entity's financial performance (IFRS 18.B125(b)) (see further discussion below).
(b) The entity has a reason for using the subtotal in its public communications other than communicating management's view of an aspect of the financial performance of the entity as a whole	▶ The subtotal is required in a public communication by law or regulation (IFRS 18.B129(a)) (see BDO comment below on measures made available to users through regulatory filings) ▶ The subtotal communicates performance related to financial statements prepared in accordance with an accounting framework other than IFRS Accounting Standards (IFRS 18.B129(b)) ▶ The subtotal is used in a public communication to satisfy a request from an external party (IFRS 18.B129(c)) ▶ The subtotal is used in a public communication for the purpose of communicating information other than financial performance (IFRS 18.B129(d)).

Subtotal communicated without prominence

IFRS 18 clarifies that the determination of whether a subtotal is communicated without prominence is a matter of judgement. It provides examples of factors that may be considered in exercising this judgement, as below (IFRS 18.B126):

Examples of factors	Demonstrates	
	Prominence	Lack of prominence
(a) The extent of references to the subtotal	Numerous references	Few references
(b) the content of commentary or analysis about or relying on the subtotal	▶ Use of the subtotal to support management analysis and to provide explanation of reasons for changes in the subtotal ▶ A comparison of the subtotal to competitors' subtotals or industry benchmarks	A description of the subtotal as information that does not communicate management's view and subtotal provided only in response to frequent requests from some users

Subtotal not used internally

At times, an entity might adjust the subtotal communicated in public communications for use internally by management. In such cases, the entity is required to use its judgement to assess whether the subtotal it uses internally is sufficiently similar to the subtotal used in its public communications. The more similar the subtotals are, the more likely it is that the subtotal used in the entity's public communications communicates to users of financial statements management's view of an aspect of the financial performance of the entity as a whole. (IFRS 18.B128). A subtotal used only internally by management does not meet the definition of an MPM as it is not used in public communications (IFRS 18.B127).

Change in an entity's use of a subtotal

In some situations, an entity might change its use of a subtotal to communicate to users of its financial statements management's view of an aspect of the financial performance of the entity as a whole, resulting in a subtotal becoming or ceasing to be an MPM. For example, Entity A began using a subtotal in its public communications in response to frequent requests from some users. At that time, the subtotal did not communicate management's view of an aspect of the entity's financial performance and the presumption about communicating management's view was rebutted. After a period of time, management started using the measure to internally assess and monitor the entity's financial performance. As a result, the measure met the definition of an MPM.



BDO comment – Measures made available to users through regulatory filings – Do they meet the definition of MPMs?

Jurisdictional regulators often require entities to file narrative and other reports, which may be available to the general public. Regulators may require entities to disclose certain measures in their regulatory filings which may be subtotals of income and expenses and which may not be specifically required by IFRS Accounting Standards. Two questions arise in respect of such filings:

1. Are such regulatory filings considered to be public communications?
2. Are the measures disclosed considered to communicate management's view of an aspect of the financial performance of the entity as a whole?

Public communications

IFRS 18 does not specify whether regulatory filings that are available to the general public are considered to be public communications or not. In our view, if a particular regulatory filing is available to users, without requiring an approval from the entity or the regulatory authority, such filings would be considered to be public communication. We also believe that such filings are public communications even if accessing them requires the user to register and/or pay a nominal fee to access the public communication, as some jurisdictions require a small fee to be paid to access this publicly available information.

Management's view

IFRS 18.B129 provides examples of reasonable and supportable information that demonstrates that an entity has a reason for using a subtotal in its public communications other than to communicate management's view. One of the examples is that the subtotal is required by law or regulation. However, the IASB also observed that a subtotal required for regulatory purposes might also be used to communicate management's view of an aspect of the entity's financial performance (IFRS 18.BC351).

Therefore, the mere fact that a regulatory authority requires disclosure of a particular subtotal is not a sufficient reason in isolation to rebut the presumption of communicating management's view. A subtotal required to be disclosed by a regulatory authority may also be used by management internally to assess the entity's financial performance. In such cases, the subtotal would meet the definition of an MPM, provided the other criteria are met.

If the subtotal is included in regulatory filings only because of regulatory requirements and the subtotal is not used by management internally to assess the entity's financial performance, the presumption of communicating management's view may be rebutted.

In some cases, the regulatory authority does not specifically require disclosure of a particular subtotal of income and expenses, but the entity includes a subtotal of income and expenses in its regulatory filings voluntarily. In such cases, the presumption about communicating management's view would apply, unless it is rebutted on some other ground.



BDO comment – If the presumption about communicating management's view is rebutted, is the fact of rebuttal required to be disclosed?

No.

In the IASB's view, the disclosure in the financial statements of measures that are not MPMs would not provide useful information. Therefore, the IASB decided not to require a disclosure of rebuttal of the presumption about communicating management's view (IFRS 18.BC355).

6.2.4.2 *An aspect of the financial performance*

IFRS 18 does not define 'an aspect of the financial performance'. At times, judgement may be needed to determine whether a measure communicates management's view of an aspect of the entity's financial performance. A measure need not relate to the overall financial performance of the entity, but may relate only to an element of the financial performance. However, the measure must relate to *an aspect of the financial performance of the entity as whole* (see section [6.2.4.3](#)).

The focus of MPM's is on communicating management's view of an aspect of the entity's performance and not management's performance. A subtotal used solely for the purpose of measuring management's performance, for example, a measure used internally to determine management remuneration, would not meet the definition of MPMs. However, in some cases, such a measure may be used internally to evaluate management performance and externally to communicate management's view of an aspect of the entity's performance. (IFRS 18.BC344). In such cases, it would meet the definition of MPMs, provided the other criteria are met.

6.2.4.3 *Entity as a whole*

The definition of an MPM requires the measure to communicate management's view of an aspect of the financial performance of the *entity as a whole*.

For example, XYZ Group uses a performance measure 'profit or loss before non-recurring expenses and non-recurring income' in its public communications. This measure is a subtotal of income and expenses and is not one of the subtotals listed in IFRS 18.118 which are excluded from the definition of MPMs. The measure would typically not be a subtotal similar to gross profit as it would typically consist of multiple expenses that are not directly related to generating the revenue included in profit. The measure communicates management's view of an aspect of the financial

performance of XYZ Group as a whole, since it excludes non-recurring income and expenses from profit or loss for the entire group. Such measure would meet the definition of an MPM, provided the other criteria are met.

In contrast, consider another scenario, where XYZ Group presents a measure 'profit or loss before non-recurring expenses' of Subsidiary S. This measure does not relate to an aspect of the financial performance of XYZ Group as a whole. Therefore, it would typically not be expected to meet the definition of an MPM, although this requires the exercising of judgement (see BDO comments below).



BDO comment – Can a subtotal of income and expenses related to reportable segments, disclosed in accordance with IFRS 8, meet the definition of an MPM?

If such subtotal does not provide information about an aspect of the financial performance of the *entity as a whole*, the subtotal would not meet the definition of an MPM (IFRS 18.B114).

Sometimes, a subtotal related to a reportable segment could provide information about an aspect of the financial performance of the entity as a whole. For example, a subtotal of income and expenses relating to a segment containing a single main business activity is presented in the statement of profit or loss. In such cases, the subtotal would meet the definition of an MPM, provided the other criteria of the definition are met (IFRS 18.B115).



BDO comment – Judgement required to determine whether the measure relates to entity as a whole

We expect that the determination of whether a measure provides information about an aspect of the financial performance of the *entity as a whole* would often involve application of judgement, as there is limited guidance in IFRS 18 on this determination.

6.2.4.4 Other considerations

6.2.4.4.1 Changes in the entity's use of an MPM, including addition or cessation of an MPM

An entity may change the method of calculation of an MPM, add a new MPM, cease the use of a previously disclosed MPM or change the method of determining the income tax effect of its reconciling items. In these cases, the entity is required to provide additional disclosures to explain the change and the reason for the change. The entity is also required to provide restated comparative information, unless impracticable to do so. (IFRS 18.124). See section [6.3.6](#) for details of disclosure requirements in case of changes to MPMs.



BDO comment – Is the identification and calculation of an MPM an accounting policy choice?

No (IFRS 18.124(c)).

The IASB acknowledged that many similarities exist between the definition of an 'accounting policy' and the determination of an MPM. However, unlike an accounting policy, an MPM is not determined in the context of preparing and presenting financial statements in accordance with IFRS Accounting Standards. It is defined to communicate an aspect of the entity's financial performance *outside* the financial statements (IFRS 18.BC368).

If identification and calculation of an MPM were treated as an accounting policy choice, the requirements of IAS 8 related to accounting policies (for example, selection and application of accounting policies, consistency of accounting policies, changes in accounting policies, etc.) would be applicable to MPMs also. However, as identification and calculation of MPMs is not an accounting policy choice, these requirements of IAS 8 do not apply to MPMs.

However, when there is a change in an MPM or an addition or cessation of an MPM, the entity is required to disclose restated comparative information, unless impracticable to do so (IFRS 18.124). The entity is required to apply the requirements in IAS 8.50-53 to assess whether restating the comparative information is impracticable.

6.2.4.4.2 Restrictions on the calculation of MPMs

The IASB decided against placing any specific restrictions on the calculation of subtotals of income and expenses that are MPMs (IFRS 18.BC357). However, MPMs are required to comply with the general requirements for information included in the financial statements, including the following:

- a) an MPM needs to faithfully represent the aspect of an entity's financial performance it purports to represent;
- b) the disclosures supporting an MPM need to meet the requirements on aggregation and disaggregation (e.g. when disclosing reconciling items); and
- c) an entity is required to provide comparative information for an MPM and related disclosures (IFRS 18.BC358).

The requirement for faithful representation

An entity is required to describe in a clear and understandable manner the aspect of performance the MPM communicates, including the meanings of terms it uses in its descriptions. The entity is then required to apply the terms and the descriptions to produce a faithful representation—complete, neutral and free from error (IFRS 18.BC359).



BDO comment – Is an MPM required to be calculated using accounting policies applied by the entity in its financial statements or accounting policies in compliance with IFRS Accounting Standards?

IFRS 18 does not specify which accounting policies an entity is required to apply when calculating MPMs.

However, IFRS 18.B134(b) provides additional disclosure requirements if the MPM is calculated by using accounting policies other than those used in the statement of financial performance or different from those required or permitted by IFRS Accounting Standards.

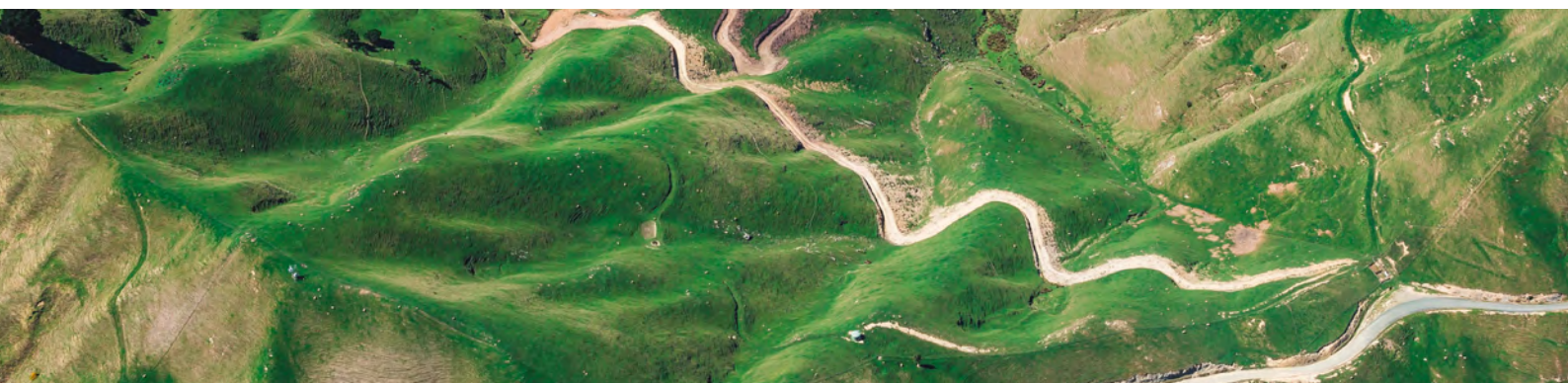
This indicates that an entity is not prohibited from using accounting policies different from the ones applied in its financial statements or required/ permitted by IFRS Accounting Standards.

Does this mean that management has absolute discretion in determining the method of calculation of an MPM?

No.

The MPM to be disclosed is required to comply with the general requirements for information included in the financial statements, including that it faithfully represents the aspect of an entity's financial performance it purports to represent (IFRS 18.BC357-361). However, an MPM is by definition always management-defined, therefore, 'faithful representation' is considered in the context of whether the MPM provides information about management's view.

Additionally, jurisdictional regulators often issue guidance on the nature of APMs or non-GAAP measures that may or may not be permitted to be used in public communications outside financial statements. For example, a regulator may specifically forbid entities from making public communications which make certain adjustments to subtotals presented in financial statements. Entities subject to the regulatory oversight of these authorities are required to comply with such guidance. The measures included in public communications in compliance with such guidance are required to be disclosed in the financial statements in accordance with IFRS 18, if the measures meet the definition of MPMs.





BDO comment – Is the definition of an MPM met if the measure adjusts profit or loss by including income and expenses not recognised in the financial statements rather than excluding income and expenses recognised in the financial statements?

Commonly encountered MPMs include subtotals that exclude certain expenses that are required to be included in profit or loss. For example, 'adjusted profit' which excludes certain expenses, such as 'non-recurring items', share-based payments, impairments, etc. The amounts excluded in such MPMs are typically the amounts recognised in the statement of profit or loss in accordance with IFRS Accounting Standards.

An entity may, at times, use a measure that adjusts profit or loss by including income and expenses not recognised in the financial statements rather than excluding income and expenses recognised in the financial statements. For example, Entity A determines the operating profit to be CU100 in accordance with IFRS Accounting Standards. It uses an 'adjusted operating profit' measure of CU125 in its public communication, which is arrived at by adding CU25 of revenue to operating profit that is not accounted for applying IFRS 15 (for example, recognising revenue based on when contracts are signed rather than when control of goods and services is transferred to customers). IFRS 18 does not provide any specific requirements on the determination of whether such measures would meet the definition of an MPM.

In IFRS 18.BC331, the IASB notes that *measures that adjust a total or subtotal specified in IFRS Accounting Standards, such as adjusted profit or loss, are management-defined performance measures*. It does not specify whether such an adjustment is required to be an inclusion or exclusion of amounts recognised in the financial statements from a total or subtotal calculated applying IFRS Accounting Standards.

In our view, in such cases, the determination of whether the measure meets the definition of an MPM requires judgement.

When a measure is calculated using an adjustment that is not hypothetical (for example, adjusted profit calculated by addition to revenue assuming revenue recognition over a period of time instead of at a point in time for the actual contracts with customers, thereby accelerating revenue recognition), we would typically expect the definition of an MPM to be met.

If the measure is calculated considering a hypothetical scenario (for example, the estimated revenue that the entity would have achieved had a flood not caused the shutdown of its factory), the determination of whether the definition of an MPM is met would require greater judgement. This needs to be analysed on a case-to-case basis considering the specific facts and circumstances.

In both the above situations, the measure to be disclosed must meet the requirement of 'faithful representation' of the aspect of financial performance it purports to represent (IFRS 18.BC358).

As discussed in the above BDO comment, wherever applicable, an entity would also be required to comply with the guidance issued by jurisdictional regulators when it proposes to include such measures in its public communications. In practice, many regulators may forbid such adjustments to be made in public communications, making this question irrelevant.

6.3 Disclosures of MPMs

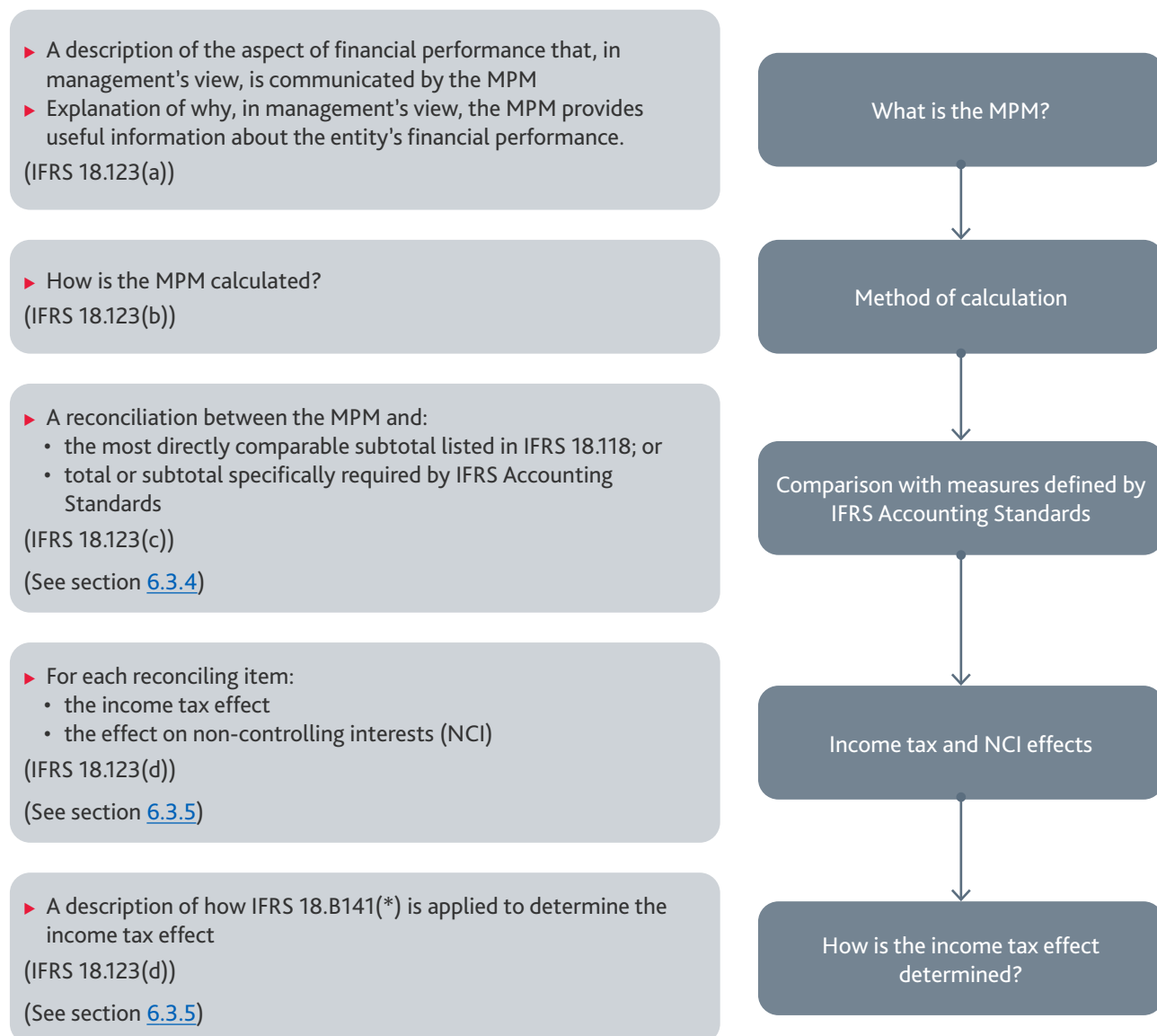
IFRS 18.121 identifies two disclosure objectives for MPM disclosures:

To provide information to help users of financial statements understand:

the aspect of financial performance that, in management's view, is communicated by an MPM

how the MPM compares with the measures defined by IFRS Accounting Standards

To meet the above disclosure objectives, IFRS 18 requires the disclosure of the following information for each MPM:



(*) IFRS 18.B141 permits an entity to determine the income tax effect using the statutory rate applicable to the transaction or based on a reasonable pro rata allocation of the current and deferred tax or by using another method that achieves a more appropriate allocation.

6.3.1 Single note disclosure

IFRS 18 requires the disclosure of information related to MPMs to be made in a single note (IFRS 18.122), i.e. an entity is not permitted to disclose the information to MPMs by cross-referencing other notes in the financial statements. The IASB's intention behind this requirement was to prevent fragmentation of information disclosed and to improve transparency (IFRS 18.BC370).

IFRS 18 does not prohibit an entity from disclosing other information in the note that includes the MPM disclosures. But, in this case, the entity is required to label the information in a way that clearly distinguishes the disclosures related to MPMs (IFRS 18.B132).

6.3.2 Management's statement on MPMs

The single note on MPM disclosures is required to include a statement that the MPMs:

- ▶ provide management's view of an aspect of the financial performance of the entity as a whole; and
- ▶ are not necessarily comparable with measures sharing similar labels or descriptions provided by other entities (IFRS 18.122).

6.3.3 Labelling of information

An entity is required to label and describe each MPM in a clear and understandable manner that does not mislead users of financial statements (IFRS 18.123).

To meet this requirement, the entity is required to disclose information that enables a user of financial statements to understand the items of income or expense included and excluded from the subtotal (IFRS 18.B134).

IFRS 18 specifically requires an entity to label and describe the measure in a way that faithfully represents its characteristics in accordance with the requirements of IFRS 18.43 (see section 4.5 for the requirements of IFRS 18.43) (IFRS 18.B134). To achieve this faithful representation, the entity is required to:

- label the measure in a way that represents the characteristics of the subtotal (for example, using the label 'operating profit before non-recurring expenses' only for a subtotal that excludes from operating profit all expenses identified by the entity as non-recurring); and
- explain the meaning of terms it uses in its descriptions that are necessary to understand the aspect of financial performance being communicated (for example, explaining how the entity defines 'non-recurring expenses') (IFRS 18.B135).

Differences in the method of calculation of MPMs from accounting policies applied in the financial statements – specific disclosures

If the method of calculating the MPM differs from the accounting policies applied in the statement of financial performance, IFRS 18.B134(b) requires the following specific disclosures:

Scenario	Disclosure requirement
Method of calculation of the MPM differs from the accounting policies applied for the items in the statement of financial performance, but the method of calculation is permitted by IFRS Accounting Standards	▶ The fact that the method of calculation of the MPM differs from the accounting policies applied in the statement of financial performance ▶ The calculation used for the MPM
Method of calculation of the MPM differs from accounting policies required or permitted by IFRS Accounting Standards	▶ The fact that the method of calculation is not permitted by IFRS Accounting Standards ▶ The calculation used for the MPM ▶ If necessary, an explanation of the meaning of the terms used, as discussed above (IFRS 18.B135)

6.3.4 Reconciliation

IFRS 18 requires an entity to reconcile each MPM to either of the following:

- ▶ the most directly comparable subtotal listed in IFRS 18.118 or
- ▶ total or subtotal specifically required to be presented or disclosed by IFRS Accounting Standards.

These subtotals are:

Subtotals listed in IFRS 18.118 (see section 6.2.2)	Totals or subtotals specifically required to be presented or disclosed by IFRS Accounting Standards (see section 5.1)
▶ Gross profit or loss (revenue minus cost of sales) and similar subtotals; ▶ Operating profit or loss before depreciation, amortisation and impairments within the scope of IAS 36; ▶ Operating profit or loss and income and expenses from all investments accounted for using the equity method; ▶ For an entity that applies paragraph 73, a subtotal comprising operating profit or loss and all income and expenses classified in the investing category; ▶ Profit or loss before income taxes; and ▶ Profit or loss from continuing operations.	▶ Operating profit or loss ▶ Profit or loss before financing and income taxes (not permitted for certain entities – see section 5.1.3) ▶ Profit or loss ▶ Total other comprehensive income ▶ Total comprehensive income

Note: A secondary reconciliation may be required (see section 6.3.4.1 below)

For each reconciling item, the entity is required to provide the following disclosures (IFRS 18.B137):

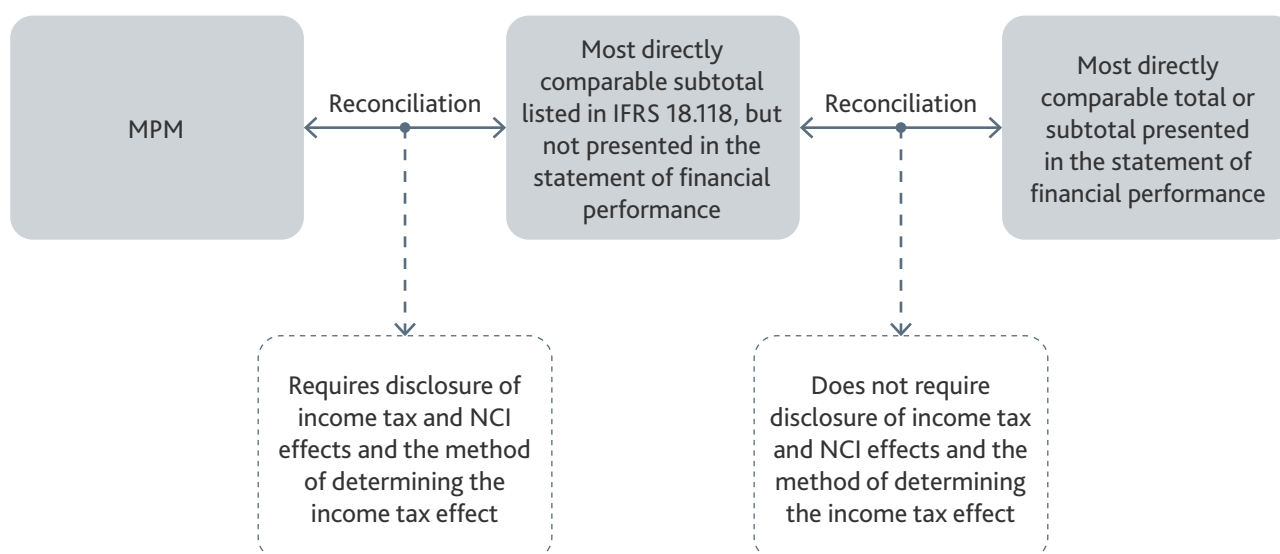
Disclosure requirement	Applicability of the disclosure requirement
a) The amount(s) related to each line item in the statement of financial performance.	Applicable for each reconciling item, irrespective of the number of reconciling items.
b) A description of how the item: ▶ is calculated ▶ contributes to the MPM providing useful information.	Applicable for each reconciling item, if there are more than one reconciling item, where each reconciling item is calculated using a different method or contributes to providing useful information in a different way. For example, an MPM may be calculated by excluding multiple items of expenses on account of the following two reasons: (i) They were identified as outside management's control (ii) They were identified as non-recurring. In such cases, the entity would be required to disclose which item contributed to which type of adjustment to explain how the MPM provides useful information. (IFRS 18.B138)

For disclosure (b) above, a single explanation might apply to more than one or all reconciling items collectively. For example, an entity might exclude several items of income or expense in calculating an MPM for being identified as non-recurring. In such a case, a single explanation that includes the entity's definition of 'non-recurring' that applies to all reconciling items might satisfy the requirement in (b) above (IFRS 18.B139).

6.3.4.1 Requirement of a secondary reconciliation

An entity is permitted to reconcile an MPM to the most directly comparable subtotal listed in IFRS 18.118, which may be a total or subtotal that is not presented in the statement(s) of financial performance. In such cases, the entity is further required to reconcile that total or subtotal to the most directly comparable total or subtotal presented in the statement(s) of financial performance. The entity is not required to disclose the information required by IFRS 18.123(d)-(e) (i.e. income tax effect, the effect on NCI and a description of the method of determining the income tax effect) for this secondary reconciliation (IFRS 18.B140).

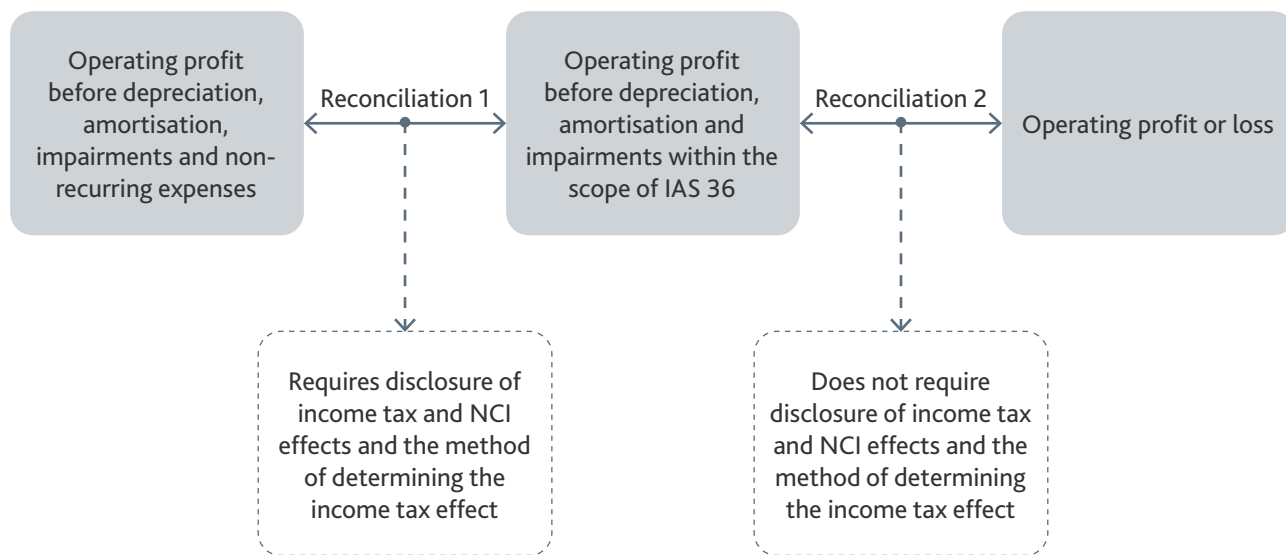
The following diagram depicts the two reconciliations required if an entity elects to reconcile an MPM to the most directly comparable subtotal listed in IFRS 18.118 but that is not presented in the statement of financial performance:



For example, Entity A uses an MPM 'operating profit before depreciation, amortisation, impairments and non-recurring expenses' in its public communications outside financial statements.

Entity A elects to reconcile the MPM to 'operating profit before depreciation, amortisation and impairments within the scope of IAS 36', which is a subtotal listed in IFRS 18.118. Entity A does not present 'operating profit before depreciation, amortisation and impairments within the scope of IAS 36' in its statement of financial performance. However, it is permitted to reconcile the MPM to this subtotal as this subtotal is listed in IFRS 18.118. For this reconciliation, Entity A is required to provide disclosure of the income tax effect, effect on NCI and the method of determining the income tax effect in accordance with IFRS 18.123(d)-(e).

Entity A is further required to reconcile 'operating profit before depreciation, amortisation and impairments within the scope of IAS 36' to 'operating profit or loss', which is the most directly comparable subtotal presented in the statement of financial performance. For this reconciliation, Entity A is not required to provide disclosure of the income tax effect, effect on NCI and the method of determining the income tax effect in accordance with IFRS 18.123(d)-(e).



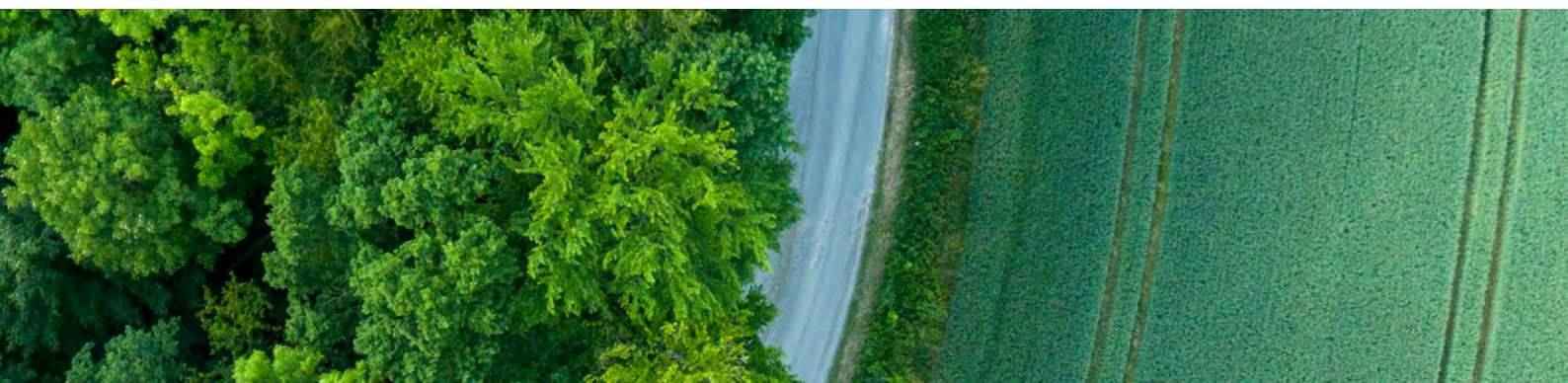
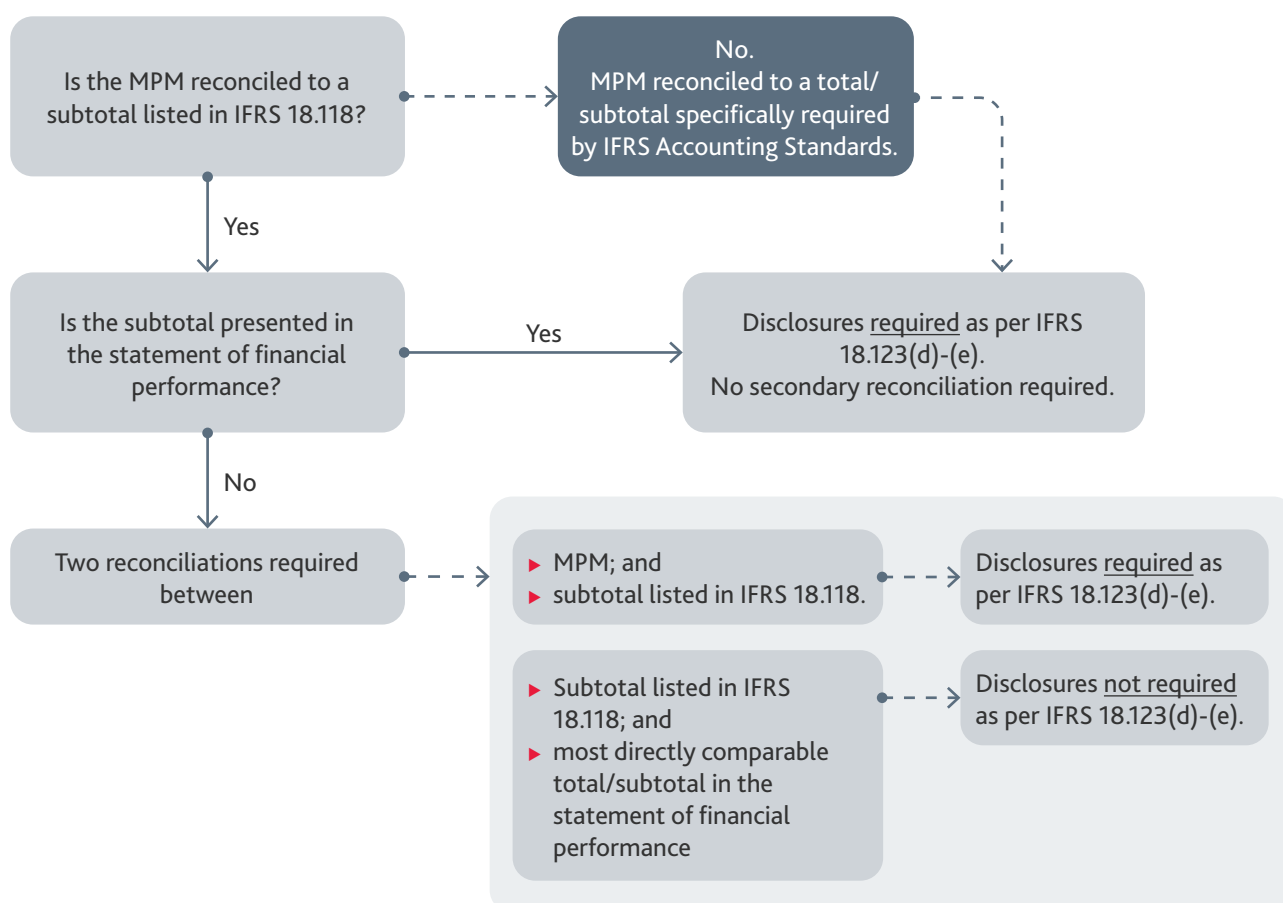
In contrast to the above example, consider another scenario where Entity A presents the subtotal 'Operating profit before depreciation, amortisation and impairments within the scope of IAS 36' in the statement of financial performance as an additional subtotal in accordance with IFRS 18.24.

Entity A uses the same MPM 'operating profit before depreciation, amortisation, impairments and non-recurring expenses' in its public communications outside financial statements.

Entity A reconciles the MPM to 'operating profit before depreciation, amortisation and impairments within the scope of IAS 36', which is a subtotal listed in IFRS 18.118. In this case, Entity A is not required to reconcile this subtotal to 'operating profit or loss' as it has already presented this subtotal 'operating profit before depreciation, amortisation and impairments within the scope of IAS 36' in the statement of financial performance.

Entity A will be required to provide the disclosure of income tax effect, effect on NCI and the method of determining the income tax effect in accordance with IFRS 18.123(d)-(e) (see section 6.3.5) for the reconciliation between the MPM and operating profit before depreciation, amortisation and impairments within the scope of IAS 36.

The following flowchart summarises these requirements:





BDO comment – Disclosure of the secondary reconciliation

In our view, the 'secondary' reconciliation between the IFRS 18.118 subtotal and the most directly comparable total/subtotal in the statement of financial performance may be disclosed as part of the MPM to IFRS 18.118 subtotal reconciliation, which will generally be presented in a tabular format. This may be achieved by adding additional columns or rows to the reconciliation. See Section 6.5 for an illustration of MPM disclosures, including the tabular reconciliation. Note that this example does not include an illustration of the secondary reconciliation noted above.



BDO comment – Does IFRS 18 specify a particular format for the reconciliation of MPM?

No.

The IASB considered whether to provide a specific format but decided against it because the most appropriate format for the reconciliation will depend on the specific MPM (IFRS 18.BC382).

The illustrative examples on IFRS 18 include an example of the note on MPMs, which includes an illustrative reconciliation.

6.3.5 Income tax effect and effect on non-controlling interests

IFRS 18.123(d) requires an entity to disclose the income tax effect and the effect on non-controlling interests (NCI) for each item disclosed in the reconciliation between an MPM and the most directly comparable subtotal listed in IFRS 18.118 or total or subtotal specifically required to be presented or disclosed by IFRS Accounting Standards.

The income tax effect and the effect on NCI are not permitted to be disclosed on a cumulative basis for all reconciling items together. The income tax effect and effect on NCI may be different for each reconciling item. For example, XYZ Group uses an MPM 'operating profit before impairments and restructuring expenses'. In XYZ Group's consolidated financial statements, it has recognised impairments and restructuring expenses in multiple group entities in various jurisdictions. The income tax rules applicable to these adjustments may vary by jurisdiction or by nature of the adjustment within the same jurisdiction. Similarly, the effect on NCI may be different for each group entity depending on the proportion of non-controlling interests in the entity. Therefore, the income tax effect and the effect on NCI are required to be disclosed separately for each reconciling item.

The IASB decided to require this disclosure to enable users of financial statements to calculate an adjusted earnings per share measure. The disclosure of income tax effect and effect on NCI for each reconciling item provides the users the information needed to calculate the adjusted earnings per share measure based on only the adjustments they want to consider in their analysis (IFRS 18.BC384-385).

IFRS 18.B141 permits an entity to use any of the following approaches to determine the income tax effect:

Simplified approach	Alternative approaches	
At the statutory tax rate(s) applicable to the transaction(s) in the tax jurisdiction(s) concerned	Based on a reasonable pro rata allocation of the current and deferred tax of the entity in the tax jurisdiction(s) concerned	By using another method that achieves a more appropriate allocation in the circumstances

An entity is also required to disclose how it applies the requirements of IFRS 18.B141 to determine the effect tax effect (IFRS 18.123(e)).

If an entity uses more than one method to calculate the income tax effects of reconciling items, the entity is required to disclose how it determined the tax effects for each reconciling item (IFRS 18.B142).

It should be noted that the income tax effect must be disclosed even if the MPM is a pre-tax subtotal as the intention behind the requirement is to provide the users the information about the tax effects of the adjustments made in the determination of the MPM.

6.3.6 Disclosure requirements in case of changes to MPMs

An entity may change the method of calculating an MPM, add a new MPM, cease using a previously disclosed MPM or change the approach used for determining the income tax effects of the reconciling items. In such cases, the entity is required to disclose the following:

- (a) an explanation that enables users to understand the change, addition or cessation and its effects;
- (b) the reasons for the change, addition or cessation; and
- (c) restated comparative information to reflect the change, addition or cessation unless it is impracticable to do so (IFRS 18.124).

If an entity does not disclose restated comparative information because it is impracticable to do so, the entity is required to disclose that fact (IFRS 18.125).

The selection of an MPM as well as the method of calculation of the MPM and the method of determining the income tax effect on the reconciling items are not accounting policy choices as defined in IAS 8. Therefore, the disclosure requirements of IAS 8 for changes in accounting policies do not apply in case of changes to or addition or cessation of an MPM.

However, in assessing whether restating the comparative information is impracticable, the entity is required to apply the requirements of IAS 8.50-53 related to impracticability in respect of retrospective application or retrospective restatement (IFRS 18.124).

6.4 Other considerations

6.4.1 Presentation of an MPM in the statement of financial performance

The IASB considered prohibiting an entity from presenting MPMs in the statement of financial performance. However, IFRS 18.24 requires an entity to present additional subtotals if such presentations are necessary to provide a useful structured summary (see section 5.2). Prohibiting an entity from presenting an MPM in the statement of financial performance could prevent the entity from complying with the requirements of IFRS 18.24. Therefore, the IASB decided against introducing such a prohibition (IFRS 18.BC374).

An entity presenting an MPM in the statement of financial performance would still be required:

- ▶ to comply with the requirements of IFRS 18.24 (see below) for subtotals presented in the statement of financial performance (IFRS 18.BC375); and
- ▶ to disclose all the information required for MPMs in a single note (IFRS 18.BC374).

IFRS 18.24 requires the additional subtotals to:

- a) comprise amounts recognised and measured in accordance with IFRS Accounting Standards;
- b) be compatible with the statement structure created by the requirements listed in IFRS 18.22;
- c) be consistent from period to period; and
- d) be displayed no more prominently than the totals and subtotals required by IFRS Accounting Standards.

See section 5.2



BDO comment – Presentation of MPMs in the statement of financial performance – jurisdictional requirements

It should be noted that although IFRS 18 does not prohibit an entity from presenting an MPM in the statement of financial performance, an entity needs to consider the views of the jurisdictional regulators in this respect. Certain jurisdictional regulators may prohibit such presentation and entities subject to their oversight would need to comply with their requirements.

Presentation/ disclosure of additional basic and diluted earnings per share with an MPM as the numerator

IAS 33.73B permits an entity to disclose additional basic and diluted earnings per share where the numerator is an MPM. However, such additional earnings per share is required to be disclosed in notes and is not permitted to be presented in the statement of financial performance (IAS 33.73B).

6.4.2 Practical considerations

Entities will need to develop systems and processes to identify measures used in public communications that meet the definition of MPMs. Entities would typically have systems in place to monitor their public communications to ensure compliance with regulatory requirements. Entities may need to modify these systems to identify MPMs.

In some cases, the disclosure requirements related to reconciliation of MPMs and income tax and NCI effects of the reconciling items may involve significant additional effort. Entities need to carefully consider these requirements before using measures that meet the definition of MPMs in their public communications.

6.4.3 Interaction with other regulatory requirements

In a number of jurisdictions, regulators have issued specific guidelines on disclosure of non-GAAP or Alternative Performance Measures (APMs).

The following are some examples of such guidelines issued by regulators:

Regulatory authority	Guidelines
The European Securities and Markets Authority (ESMA)	▶ Guidelines on Alternative Performance Measures ▶ Guidelines on Alternative Performance Measures (Questions and answers)
The International Organization of Securities Commissions (IOSCO)	▶ Statement on Non-GAAP Financial Measures
US Securities and Exchange Commission (US SEC)	▶ Final Rule: Conditions for Use of Non-GAAP Financial Measures ▶ Compliance and Disclosure Interpretations on Non-GAAP Financial Measures

The MPM disclosure requirements of IFRS 18 may be aligned with such jurisdictional regulatory requirements in many aspects such as describing the measure used in a clear and understandable manner, appropriate labelling, reconciliation of the measure to the most directly comparable total or subtotal presented in the financial statements etc. IFRS 18 requires MPM disclosures to be made in the financial statements, whereas the jurisdictional requirements typically require the disclosures to be made outside the financial statements.

The scope of jurisdictional requirements for APMs or non-GAAP measures may differ from that of IFRS 18. Often, the scope of jurisdictional requirements may be wider than IFRS 18, as they may include measures within their scope that are not subtotals of income and expenses. At times, jurisdictional requirements may place specific prohibitions on use on certain measures which may be subtotals of income and expenses.

These jurisdictional requirements will continue to apply even after IFRS 18 becomes effective and entities subject to them need to ensure compliance with them.

Regulators may be in the process of updating (or have already updated) these guidelines to take into account the practical effects of IFRS 18 and MPM disclosure requirements. For example, prior to the introduction of IFRS 18, a regulator may have issued disclosure requirements concerning 'non-GAAP' information presented outside of financial statements which defines any information presented within financial statements as being 'GAAP' and therefore not subject to the disclosure requirements of their rule. Upon IFRS 18 being issued, as MPMs are required to be presented in the financial statements, that rule issued by the regulator would deem MPMs to be 'GAAP' and therefore not within the scope of their disclosure requirements. In such instances, regulators have generally updated (or are planning to update) their rules to take into account the effects of IFRS 18 and the fact that what has traditionally been considered 'non-GAAP' information will now be presented in financial statements.

Entities also need to closely monitor any changes in the jurisdictional requirements for APMs or non-GAAP measures in light of MPM requirements of IFRS 18.

6.5 Illustration of MPM disclosures

The following illustration is adapted from the example included in Illustrative Examples (IE8) on IFRS 18. It should be noted that the illustration does not cover all the disclosure requirements related to MPMs as per IFRS 18.

ABC Group's management-defined performance measures

Labelling of the MPM (IFRS 18.B134, B135(a))	ABC Group uses the following management-defined performance measures (MPMs) in its public communications: ▶ Operating profit before non-recurring expenses and gains or losses on disposal of subsidiaries, associates and joint ventures (also referred to as 'adjusted operating profit' for brevity) ▶ Profit from continuing operations before non-recurring expenses and gains or losses on disposal of subsidiaries, associates and joint ventures (also referred to as 'adjusted profit from continuing operations' for brevity)
Management statement (IFRS 18.122)	These measures provide management's view of certain aspects of the financial performance of ABC Group as a whole. These measures are not specified by IFRS Accounting Standards and therefore might not be comparable to apparently similar measures used by other entities.
Management statement (IFRS 18.122)	To provide management's view of ABC Group's financial performance, the following two types of adjustments have been made to operating profit and profit from continuing operations:
A description of the aspect of financial performance communicated by the MPM and explanation of the reason (IFRS 18.123(a), B134, B135) A description of how the item contributes to the MPM providing useful information, separately for each type of adjustment (IFRS 18.B137(b), B138-B139)	1. Non-recurring expenses: Operating profit and profit from continuing operations have been adjusted for items of expenses that ABC Group does not expect to arise for several future annual reporting periods. ABC Group's management believes adjusting operating profit and profit from continuing operations for such items provides information that is helpful in understanding trends in ABC Group's underlying profitability. 2. Gains or losses on disposal of subsidiaries, associates and joint ventures: In accordance with its 5-year business plan, ABC group plans to dispose of subsidiaries, associates and joint ventures in certain jurisdictions (refer to Note X for further information). ABC Group's management believes adjusting operating profit and profit from continuing operations for gains and losses from these disposals provides information that is helpful in understanding the financial performance of ABC Group from regular operations. This adjustment is not considered 'non-recurring' as the disposals of these subsidiaries, associates and joint ventures will be completed over the next two years.
Adjustments in the calculation of the MPM (IFRS 18.123(b)) Disclosure of which item contributes to which type of adjustment (IFRS 18.B138)	The following items of income and expenses are included in the above adjustments for the current and comparative reporting period: 1. Non-recurring expenses: i) Impairment losses (or reversals thereof) of property, plant and equipment (including right-of-use assets) and intangible assets (for information related to impairments refer to Note X Property, plant and equipment, Note X Intangible assets and Note X Research and development expenses) ii) Non-recurring litigation expenses (for information related to litigation expenses refer to Note X Provisions and Note X General and administrative expenses)

iii) Losses of inventory due to natural calamity (for information related to losses of inventory refer to Note X Loss of inventory due to flood in Country C)

2. Gains or losses on disposal of subsidiaries, associates and joint ventures:

i) Gains or losses on disposal of associates and joint ventures (for information related to gains or losses on disposal of associates and joint ventures, refer to Note X Disposal of associates and joint ventures).

ABC Group assesses non-recurrence of litigation expenses on a case-by-case basis. ABC Group generally categorises litigation expenses arising from intellectual property disputes, regulatory violations and employee claims as 'non-recurring'. This classification is based on ABC Group's proactive approach of having in place measures designed to prevent such events from occurring.



Reconciliation (IFRS 18.123(c), B136-B140)

Reconciliation of the MPMs to the subtotals presented in the statement of financial performance:

MPM 20X2

(in CU'000)

		Adjusting items			
	IFRS	Impairment losses	Losses of inventory due to natural calamity	Gains on disposal of associates and joint ventures	MPM
Cost of Sales		-	1,000	-	
Research and development expenses		1,500	-	-	
Goodwill impairment loss		2,000	-	-	
Operating profit / Adjusted operating profit	60,000	3,500	1,000	-	64,500
Share of profit and gains on disposal of associates and joint ventures		-	-	(3,200)	
Income tax expense		-	(200)	480	
Profit from continuing operations / Adjusted profit from continuing operations	35,000	3,500	800	(2,720)	36,580
Profit attributable to non-controlling interests		175	56	-	

Income tax effect for each reconciling item (IFRS 18.123(d), B141)

Effect on NCI for each reconciling item (IFRS 18.123(d))

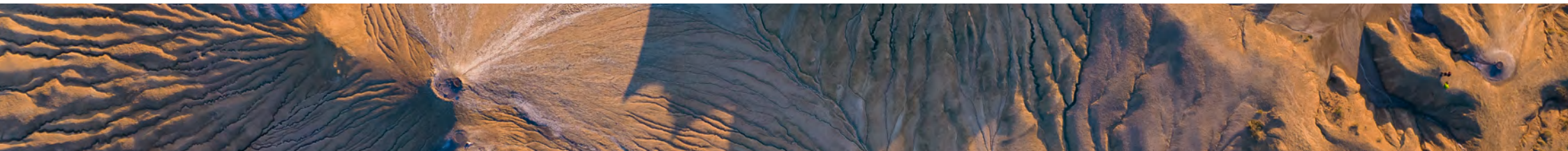
A description of the determination of the income tax effect (IFRS 18.123(e), B141)

Impairment losses	Impairment losses incurred in 20X2 did not yield any tax benefits because they were not eligible for tax deductions in Country A and Country B.
Losses of inventory due to natural calamity	The tax effect of these losses is calculated based on the statutory tax rate applicable in Country C at the end of 20X2, which was 20%.
Gains on disposal of associates and joint ventures	The tax effect of gains on disposal of associates and joint ventures is calculated based on the statutory tax rate applicable in Country D, at the end of 20X2, which was 15%.

MPM 20X1

(in CU'000)

		Adjusting items		
	IFRS	Non-recurring litigation expenses	Gains on disposal of associates and joint ventures	MPM
	General and administrative expenses	2,500	-	
	Operating profit / Adjusted operating profit	56,000	2,500	-
				58,500
	Share of profit and gains on disposal of associates and joint ventures	-	(2,500)	
Income tax effect for each reconciling item (IFRS 18.123(d), B141)	Income tax expense	(375)	500	
	Profit from continuing operations / Adjusted profit from continuing operations	31,000	2,125	(2,000)
				31,125
Effect on NCI for each reconciling item (IFRS 18.123(d))	Profit attributable to non-controlling interests	106	-	
A description of the determination of the income tax effect (IFRS 18.123(e), B141)	Non-recurring litigation expenses	The tax effect of these losses is calculated based on the statutory tax rate applicable in Country F at the end of 20X1, which was 15%.		
	Gains on disposal of associates and joint ventures	The tax effect of gains on disposal of associates and joint ventures is calculated based on the statutory tax rate applicable in Country G, at the end of 20X1, which was 20%.		



7. Effective date and transition requirements

7.1. Required transition approach

IFRS 18 is effective for annual reporting periods beginning on or after 1 January 2027 (IFRS 18.C1).

For example, entities with the following annual reporting period ends would be required to apply IFRS 18 in annual financial statements as follows:

Annual reporting period ending	IFRS 18 mandatorily effective for the first time in annual reporting period ending:
31 March	31 March 2028
30 June	30 June 2028
30 September	30 September 2028
31 December	31 December 2027

Earlier application is permitted, however, early application in many jurisdictions may be subject to endorsement of IFRS 18 (e.g. endorsement by the European Union for entities that comply with IFRS as endorsed by the European Union).

Specific requirements apply to interim financial reports – see section [7.4](#).

When an entity applies IFRS 18, it must do so retrospectively. Retrospective application means that an entity must restate all comparative periods presented to comply with the requirements of IFRS 18. Adopting IFRS 18 for the first time will primarily affect the statement of profit or loss, however, it is possible that the application of IFRS 18 may also affect other primary financial statements along with notes to the financial statements if, for example, entities change the level of aggregation in financial statements.

However, an entity is not required to present the quantitative information specified in IAS 8.28(f) (amount of the adjustment for each line item affected and if IAS 33 is applicable, the amount of the adjustment for basic and diluted earnings per share) (IFRS 18.C2). Instead, an entity applies the 'IFRS 18-specific' transition disclosures.



BDO comment – effect of retrospective application

The work effort involved in transitioning to IFRS 18 should not be underestimated simply because IFRS 18 does not modify the measurement requirements of IFRS Accounting Standards, unlike IFRS 9, 15, 16 or 17.

Depending on the level of complexity of an entity, the time and effort involved in transitioning to the requirements of IFRS 18 may vary significantly. For entities with complex operations, particularly large groups, systems and processes will need to be developed around the following areas (this list is not exhaustive):

- ▶ Classifying all items of income and expense into the five categories, including assessing the effect of the more complex areas of this process (e.g. assessing whether an entity has specified main business activities, specific requirements applicable to hybrid contracts, derivatives, etc.);
- ▶ Assessing the impact of the new requirements of IFRS 18 applicable to the presentation of foreign exchange differences (see section [3.9.3](#)), as systems may not capture foreign exchange by individual assets and liabilities;
- ▶ Determining the appropriate level of aggregation and disaggregation in the primary financial statements and the notes to the financial statements;
- ▶ Making accounting policy choices permitted by IFRS 18 where applicable;
- ▶ Assessing the effect of other requirements modified by IFRS 18 (e.g. management-defined performance measures, consequential amendments to earnings per share (IAS 33), the statement of cash flows (IAS 7)).

As IFRS 18 requires retrospective application, entities will need to ensure they have developed the appropriate processes to present their financial statements under the 'old requirements' (IAS 1), and then restate those amounts under the 'new requirements' (IFRS 18 and consequential amendments) for the period that will be

restated as comparatives when IFRS 18 is applied for the first time (e.g. the year-ended 31 December 2026 presented as comparatives in the 31 December 2027 financial statements).

7.2. Disclosures required upon transition

When IFRS 18 is applied for the first time, entities are required to disclose for the comparative period immediately preceding the period in which IFRS 18 is first applied (e.g. the 31 December 2026 comparative for 31 December 2027 financial statements), a reconciliation between (IFRS 18.C3):

- (a) The restated amounts presented applying IFRS 18; and
- (b) The amounts previously presented applying IAS 1.

For example, if an entity previously presented certain line items outside of how the entity defined 'operating profit' under IAS 1, but those amounts are required to be classified in the operating category in accordance with IFRS 18, the entity would need to reconcile the line items affected.

The reconciliation required by IFRS 18.C3 is permitted, but not required, to be provided for the current period or earlier comparative periods (IFRS 18.C6).

7.3. Change in election for associates and joint ventures (IAS 28)

IAS 28.18 permits an accounting policy choice to be made at the initial recognition of each associate or joint venture for certain entities. This accounting policy choice is available for venture capital organisations, mutual funds, unit trusts and similar entities including investment-linked insurance funds. The accounting policy choice permits an entity to elect to measure an investment in an associate or joint venture at fair value through profit or loss in accordance with IFRS 9 rather than to apply the equity method in accordance with IAS 28. This accounting policy choice is available for each associate or joint venture separately.

At the date of initial application of IFRS 18 (e.g. 1 January 2026, the first date of the comparative period for entities with calendar year-ends that provide only a single comparative period), an entity is permitted to change this previous election if the change is from the equity method to fair value through profit or loss in accordance with IFRS 9 (IFRS 18.C7). An entity is not permitted to change its election in the opposite manner (i.e. from fair value through profit or loss in accordance with IFRS 9 to the equity method). If an entity prepares separate financial statements, it must make a corresponding change (IAS 27.11) in those separate financial statements. This change in policy is reflected retrospectively applying IAS 8.



BDO comment – reason for 're-election' being available on transition to IFRS 18

The reason the IASB permitted an entity to change its accounting policy from equity method to fair value through profit or loss when that choice is normally only available on the initial recognition of the investment is because IFRS 18 may change how an entity presents income and expenses associated with equity method investments.

For example, if a venture capital organisation previously elected to use the equity method prior to IFRS 18 being adopted, without the ability to change this election on adoption of IFRS 18, the venture capital organisation would be required to present income and expense associated with the associate or joint venture in the investing category. That is because income and expenses associated with associates or joint ventures accounted for using the equity method are always classified in the investing category (IFRS 18.BC131-132). This may not produce useful information for users of financial statements for venture capital organisations (and similar entities) since investing in associates and joint ventures may be part of the entities' main business activities.

Allowing the entity to change this election and measure associates and joint ventures at fair value through profit or loss in accordance with IFRS 9 will change the classification of income and expenses from investing to operating if the entity invests in such assets as a main business activity (see section [3.8.1](#)).

7.4. Interim financial reports

The general effect of IFRS 18 on interim financial reports is discussed in section 3.10, however, specific requirements apply for condensed interim financial statements in the first year of applying IFRS 18 (e.g. quarters 1, 2 and 3 or half-year condensed interim financial statements in 2027 for entities with an annual period commencing on or after 1 January 2027).

These transition requirements are necessary because IAS 34.10 requires an entity to include 'each of the headings and subtotals that were included in its most recent annual financial statements'. This would imply that for an entity's quarter 1 condensed interim financial statements as at 31 March 2027, they should use headings and subtotals included in the entities 31 December 2026 annual financial statements, which would be prepared in accordance with IAS 1, not IFRS 18.

However, IFRS 18.C4 modifies this requirement for condensed interim financial statements in the first year of applying IFRS 18. IFRS 18.C4 requires entities to present in condensed interim financial statements each heading it expects to use in applying IFRS 18 and the subtotals required by IFRS 18, despite IAS 34.10's requirement. Effectively, IFRS 18.C4 'overrides' the requirement in IAS 34.10.

The 'default' requirement in IAS 34.10 to use the same heading and subtotals as the most recent annual financial statements does not apply again until an entity has issued its first annual financial statements prepared in accordance with IFRS 18.



Example 7.4-1 – condensed interim financial statements (IFRS 18.C4 and IAS 34.10)

Entity W has a calendar year-end and prepared its 31 December 2026 annual financial statements in accordance with the requirements of IAS 1 (i.e. it is not an early adopter of IFRS 18).

Entity W prepares condensed interim financial statements for the half-year ended 30 June each year.

In applying IAS 1, Entity W excluded from operating profit certain items of income and expenses that will be required to be classified in the operating category in accordance with IFRS 18 (the affected items of income and expense).

Entity W is considering on what basis it prepares its annual and condensed interim financial statements.

Analysis

	31 December 2026 annual financial statements	30 June 2027 condensed interim financial statements	31 December 2027 annual financial statements	30 June 2028 condensed interim financial statements
Analysis of affected items of income and expenses and applicable subtotals (e.g. operating profit)	Affected items of income and expense are excluded from operating profit as IFRS 18 is not yet applicable.	IFRS 18.C4 applies. Affected items of income and expense are presented using headings that Entity W expects to use in applying IFRS 18 in its 31 December 2027 financial statements and presents subtotals in accordance with IFRS 18. This would include presenting affected items of income and expense in the operating category.	Affected items of income and expense are presented in the operating category as required by IFRS 18.	IAS 34.10 applies. Entity W prepares its condensed interim financial statements using each of the headings and subtotals that were included in its most recent annual financial statements (31 December 2027).

7.4.1. Disclosures required upon transition – interim financial statements

For interim financial statements prepared in the first year of applying IFRS 18, as part of the disclosures required by IAS 34.16A(a) (information about accounting policies and changes therein), entities are required to disclose reconciliations for each line item presented in the statement of profit or loss for the comparative periods immediately preceding the current and cumulative current periods. The reconciliations are required between (IFRS 18.C5):

- (a) the restated amounts presented applying the accounting policies for the comparative period and the cumulative comparative period when the entity applies IFRS 18; and
- (b) the amounts previously presented applying the accounting policies for the comparative period and cumulative comparative period when the entity applied IAS 1.'

This reconciliation is permitted, but not required, to be provided for the current period or earlier comparative periods (IFRS 18.C6).



Example 7.1-2 – condensed interim financial statements and reconciliation disclosure required (IFRS 18.C5)

Entity Y has a calendar year-end and prepared its 31 December 2026 annual financial statements in accordance with the requirements of IAS 1 (i.e. it is not an early adopter of IFRS 18).

Entity Y prepares condensed interim financial statements for each quarter (Q1 – 31 March, Q2 – 30 June, Q3 – 30 September). In each condensed interim financial statement, the statement of profit or loss includes the current interim period and the cumulative interim period for the current financial year to date in accordance with IAS 34.20(b). For example, the Q3 30 September 2027 condensed interim financial statements include a statement of profit or loss for:

- ▶ The 3 months ended 30 September 2027 (the current interim period); and
- ▶ The 9 months ended 30 September 2027 (the cumulative interim period).

Comparative information for the immediately preceding financial year:

- ▶ The 3 months ended 30 September 2026 (the prior year comparative interim period); and
- ▶ The 9 months ended 30 September 2026 (the prior year cumulative interim period).

Therefore, Entity Y presents 4 statements of profit or loss in its 30 September 2027 condensed interim financial statements.

In applying IAS 1, Entity Y excluded from operating profit certain items of income and expenses that will be required to be classified in the operating category in accordance with IFRS 18 (the affected items of income and expense).

Entity Y is considering how it complies with the reconciliation disclosure required by IFRS 18.C5 in its 30 September 2027 condensed interim financial statements.

Analysis

To comply with IFRS 18.C5, Entity Y must reconcile both of its 3 months and 9 months ended statements of profit or loss related to the comparative period (30 September 2026). IFRS 18.C5 requires this reconciliation for 'each line item presented in the statement of profit or loss for the comparative periods immediately preceding the current and cumulative current periods'.

Therefore, Entity Y must explain how its line items have changed in the comparative periods as a result of applying IFRS 18 retrospectively. For the 3 months and 9 months ended statements of profit or loss for the periods ended 30 September 2026, Entity Y must reconcile the restated line items (e.g. the affected items of income and expense) to their revised presentation under IFRS 18 and how they were presented in previous condensed interim financial statements in accordance with IAS 1.

7.5 Considerations for the successful implementation of IFRS 18

7.5.1 IFRS 18 accounting considerations

In order to achieve a successful implementation of IFRS 18, entities should consider multiple factors. In general, IFRS 18 requires an entity to use judgement and to perform assessments to determine how to present and disclose information in such a manner that it fulfils the purpose of primary financial statements and the related notes (see section 4.1). IFRS 18 provides limited accounting policy choices. These accounting policy choices are often dependent on the capabilities of an entity's systems and processes to differentiate between income and expenses arising from various sources or business activities within the entity.

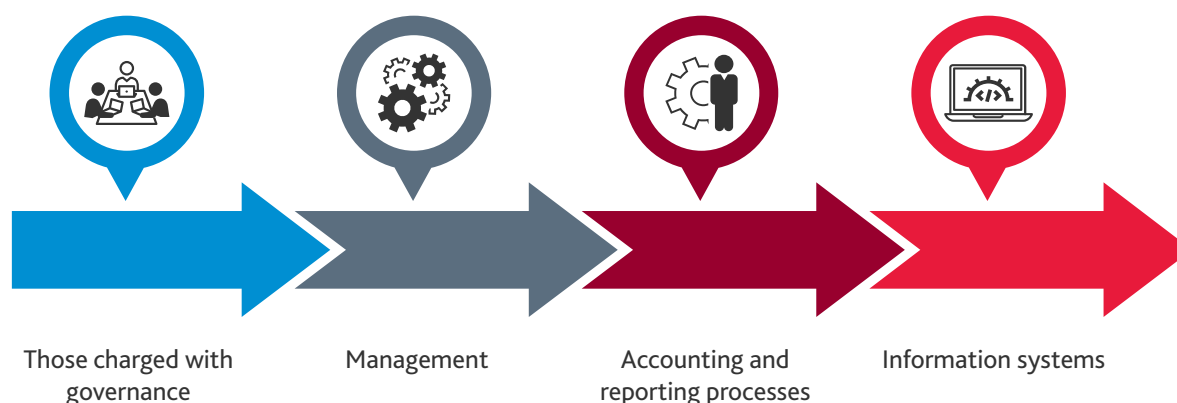
The following table is a non-exhaustive list of considerations (referenced to the related section in this publication or the IFRS Accounting Standard) to consider when implementing IFRS 18.

General presentation and disclosure - Presentation in financial statements vs. disclosure in notes 4.1 - Mandatory line items 4.3 - Mandatory totals and subtotals 5.1 - Additional line items and subtotals 5.2 - Aggregation vs. disaggregation 4.2 - Labels & descriptions (use of 'other') 4.5 - Material accounting policy information IAS 8.27	Specific to the statement of profit or loss and related notes - Assessment of specified main business activities 3.7 - Categorisation of income & expenses within five categories 3 - Accounting policy choices subject to system capabilities 3.8.2, 3.9.1, 3.9.3 - Presentation of operating expenses 4.4 - Operating expenses note 4.4 - Earnings per share 2.2	Management-defined performance measures (MPMs) - Identification of MPMs 6.1–6.2 - Disclosure in notes: 6.3 ▶ Labelling of information ▶ Reconciliation ▶ Income tax & non-controlling interest effect
		Specific to statement of cash flows - Mandatory interest and dividend classification IAS 7.33A – 7.34A - Accounting policy choice (specified main business activities) IAS 7.34B – 7.34D

7.5.2 Other IFRS 18 considerations

The adoption of IFRS 18 will not only have a significant impact on accounting and financial reporting but may also affect broader organisational processes, systems, and governance.

An entity should also consider the effect that IFRS 18 will have on:



Those charged with governance

IFRS 18 will affect how financial performance is communicated to stakeholders and creates the opportunity for entities to reassess the presentation and disclosures in their financial statements as a whole.

The inclusion of MPMs in the financial statements and related disclosure requirements applicable to MPMs will require management to carefully consider what performance measures are publicly communicated, ensuring that these MPMs are aligned with management's view of an aspect of the financial performance of the entity as a whole. Entities may also need to develop financial reporting processes to identify public communications that fall within the scope of IFRS 18's MPM disclosure requirements.

Additionally, those charged with governance should also consider how the change of the determination of subtotals included in the statement of profit or loss (such as operating profit) could affect covenants, key performance indicators (KPIs), share-based payments and entity valuations. For example, traditional metrics like Earnings Before Interest, Tax, Depreciation and Amortisation (EBITDA) may be superseded by new measures such as Operating Profit Before Depreciation, Amortisation and Impairments within the scope of IAS 36 (OPDAI), which align with the classification requirements of IFRS 18. As a result, it is crucial for those charged with governance to anticipate and manage the broader implications of these changes within their entities.

To support a smooth transition to IFRS 18, those charged with governance may need to establish or update governance structures that oversee implementation. This process should foster effective collaboration across various departments, including finance, risk management, and IT, ensuring that all areas involved are coordinated and prepared for the new reporting landscape that IFRS 18 will bring.

Management

Management will generally lead the change set out by those charged with governance. This involves raising awareness, resource planning and arranging or providing training to affected employees. Management will most likely also be involved in redesigning the accounting and reporting process and related internal controls.

Financial reporting and closing processes

The accounting and financial reporting processes will have to be reviewed and where appropriate, updated.

The financial statements and notes will have to be updated to comply with the requirements of IFRS 18, such as the inclusion of mandatory subtotals, classifying income and expenses in one of five categories and presenting an MPM note.

Furthermore, data collection will require greater granularity. For example, an entity will need to disaggregate the movement in a provision between the unwinding of the discount (classified in the financing category) and other movements (operating category). MPMs will have to be carefully reconciled to a subtotal presented in the statement of profit or loss.

Groups with diverse operations may need to adjust existing consolidation processes to ensure that income and expenses are appropriately classified. In some cases, additional consolidation adjustments may be required to adjust the classification of income and expenses.

Internal controls relating to financial reporting should also be reviewed and updated to consider new risks arising from changes in presentation and disclosure. This includes controls over judgments related to classification of income and expenses, identification and disclosure of MPMs and the disclosure of operating expenses by nature.

Information systems

Although the information system needs may vary between different entities, each entity should assess if their current information system can support the new requirements of IFRS 18.

The information systems of entities may vary and be of differing levels of complexity and sophistication. Certain entities may utilise complex and highly automated information systems, whereas others may rely on less complex systems with minimal automation. Regardless of how sophisticated an entity's information system(s) is, each entity should assess if their current information system(s) can support the new requirements of IFRS 18.

IFRS 18 requires greater levels of data granularity. IFRS 18 may require an entity to differentiate between (non-exhaustive list):

- ▶ Income and expenses originating from different categories in the statement or profit or loss;
- ▶ Movements in liabilities that arise from transactions that do not involve only the raising of finance such as the unwinding of a discount, other movements and foreign exchange differences (see sections [3.3.3](#) and [3.9.3.1](#));
- ▶ Financing liabilities, cash and cash equivalents related to providing financing to customers and those not related to providing financing to customers (see sections [3.8.2.1](#) and [3.9.1](#));
- ▶ Foreign exchange differences related to transactions originating from different categories of the statement or profit or loss (see section [3.9.3.1](#)); and
- ▶ Different classification categories of income and expenses between the consolidated group and the individual financial statements.

An entity's information system may need to provide more granular data than has historically been required by IAS 1.



8. Examples of statements of profit or loss prepared in accordance with IFRS 18

The following examples use a common set of income and expenses and demonstrate how they would be presented under the following mutually exclusive scenarios:

- ▶ Scenario A: Entity S does not have any specified main business activities
- ▶ Scenario B: Entity S invests in financial assets as a main business activity
- ▶ Scenario C: Entity S provides financing to customers as a main business activity
- ▶ Scenario D: Entity S provides financing to customers as a main business activity and invests in investment property measured at fair value as a main business activity

These examples also include Scenario E, which is independent of the previous scenarios and illustrates how an insurance company that invests in financial assets as a main business activity may present its statement of profit or loss along with the line items and subtotals required by IFRS 17.

Common fact pattern for Examples A – D

Entity S has the following income and expenses:

- ▶ Revenue from contracts with customers
- ▶ Costs of goods sold
- ▶ Employee benefits not included in costs of goods sold
- ▶ Depreciation not included in costs of goods sold
- ▶ Expected credit losses on trade receivables
- ▶ Share of profit of associates and joint ventures (accounted for using the equity method)
- ▶ Fair value gains on equity instruments
- ▶ Fair value gains on investment property
- ▶ Interest expense on bank loans
- ▶ Interest income on contract assets
- ▶ Income tax expense
- ▶ Loss from discontinued operations

Entity S has applied the aggregation and disaggregation requirements of IFRS 18 and has determined that each of these classes of income and expense should be presented separately in the statement of profit or loss.

Entity S presents operating expenses by nature, except for the cost of goods sold line item, which is presented using a mixed presentation.

8.1 Example A – entity that does not have any specified main business activities

Scenario A: Entity S does not have any specified main business activities

The income and expenses described in the common fact pattern are classified as follows:

Income or expense	Classification	Explanation
Revenue from contracts with customers	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See section 3.4 .
Costs of goods sold	Operating	
Employee benefits not included in costs of goods sold	Operating	
Depreciation not included in costs of goods sold	Operating	
Expected credit losses on trade receivables	Operating	
Share of profit of associates and joint ventures (accounted for using the equity method)	Investing	Share of profit or loss from associates and joint ventures accounted for using the equity method is also classified in the investing category. See section 3.2 .
Fair value gains on equity instruments	Investing	Financial assets and investment property generate a return individually and largely independently of the entity's other resources (IFRS 18.53(c)), however, Entity S does not invest in those assets as main business activities, therefore, income and expenses are classified in the investing category. See sections 3.2 and 3.8.1 .
Fair value gains on investment property	Investing	
Interest expense on bank loans	Financing	Bank loans arise from transactions that involve only the raising of finance (IFRS 18.59(a)), and interest expense arises from the subsequent measurement of the liability (IFRS 18.60). As Entity S does not provide financing to customers as a main business activity, interest expense is classified in the financing category. See sections 3.3 and 3.8.2 .
Interest income on contract assets	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See section 3.4 .
Income tax expense	Income taxes	Income and expenses within the scope of IAS 12 are classified in the income taxes category. See section 3.5 .
Loss from discontinued operations	Discontinued operations	Income and expenses presented as a single line item in accordance with IFRS 5.33(a) are classified in the discontinued operations category. See section 3.6 .

Entity S considers the requirement in IFRS 18.24 to present additional subtotals beyond those that are mandatory (see section [5.1](#)) and concludes that it will present three additional subtotals:

Additional subtotal	Description
Gross profit	The difference between revenue and cost of goods sold.
Profit or loss before income taxes	All income and expenses other than those classified in the income taxes and discontinued operations categories.
Profit or loss from continuing operations	All income and expenses other than those classified in the discontinued operations category.

Entity S presents its statement of profit or loss for the year-ended 31 December 20x7 as follows

	31 December 20x7	31 December 20x6	Explanation
Revenue	xxx	xxx	
Cost of goods sold	<u>xxx</u>	<u>xxx</u>	
Gross profit	xxx	xxx	Additional subtotal: revenue less cost of goods sold
Employee benefits not included in costs of goods sold	xxx	xxx	
Depreciation not included in costs of goods sold	xxx	xxx	
Expected credit losses on trade receivables	xxx	xxx	
Interest income on contract assets	<u>xxx</u>	<u>xxx</u>	
Operating profit	xxx	xxx	Mandatory subtotal: The total of all income and expenses classified in the operating category.
Share of profit of associates and joint ventures	xxx	xxx	
Fair value gains on equity instruments	xxx	xxx	
Fair value gains on investment property	<u>xxx</u>	<u>xxx</u>	
Profit before financing and income taxes	xxx	xxx	Mandatory subtotal: The total of operating profit or loss and all income and expenses classified in the investing category.
Interest expense on bank loans	xxx	xxx	
Profit before income taxes	xxx	xxx	Additional subtotal: all income and expenses other than those classified in the income taxes and discontinued operations categories.
Income tax expense	<u>xxx</u>	<u>xxx</u>	
Profit from continuing operations	xxx	xxx	Additional subtotal: all income and expenses other than those classified in the discontinued operations category.
Loss from discontinued operations	<u>xxx</u>	<u>xxx</u>	
Profit	xxx	xxx	Mandatory total

8.2 Example B – entity that invests in financial assets as a main business activity

Scenario B: Entity S invests in financial assets as a main business activity

Differences from Example A are in red underlined text.

The income and expenses described in the common fact pattern are classified as follows:

Income or expense	Classification	Explanation
Revenue from contracts with customers	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See section 3.4 .
Costs of goods sold	Operating	
Employee benefits not included in costs of goods sold	Operating	
Depreciation not included in costs of goods sold	Operating	
Expected credit losses on trade receivables	Operating	
Share of profit of associates and joint ventures (accounted for using the equity method)	Investing	Share of profit or loss from associates and joint ventures accounted for using the equity method is also classified in the investing category. See section 3.2 .
Fair value gains on equity instruments	Operating	<u>Financial assets such as equity instrument generate a return individually and largely independently of the entity's other resources (IFRS 18.53(c)). Entity S invests in financial assets as a main business activity; therefore, income and expenses are classified in the operating category (IFRS 18.58). See sections 3.3 and 3.8.1.</u>
Fair value gains on investment property	Investing	Investment property generates a return individually and largely independently of the entity's other resources (IFRS 18.53(c)), however, Entity S does not invest in investment property as main business activity, therefore, income and expenses are classified in the investing category. See sections 3.3 and 3.8.1 .
Interest expense on bank loans	Financing	Bank loans arise from transactions that involve only the raising of finance (IFRS 18.59(a)), and interest expense arises from the subsequent measurement of the liability (IFRS 18.60). As Entity S does not provide financing to customers as a main business activity, interest expense is classified in the financing category. See sections 3.3 and 3.8.2 .
Interest income on contract assets	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See section 3.4 .
Income tax expense	Income taxes	Income and expenses within the scope of IAS 12 are classified in the income taxes category. See section 3.5 .
Loss from discontinued operations	Discontinued operations	Income and expenses presented as a single line item in accordance with IFRS 5.33(a) are classified in the discontinued operations category. See section 3.6 .

Entity S considers the requirement in IFRS 18.24 to present additional subtotals beyond those that are mandatory (see section [5.1](#)) and concludes that it will present three additional subtotals:

Additional subtotal	Description
Gross profit	The difference between revenue and cost of goods sold.
Profit or loss before income taxes	All income and expenses other than those classified in the income taxes and discontinued operations categories.
Profit or loss from continuing operations	All income and expenses other than those classified in the discontinued operations category.

Entity S presents its statement of profit or loss for the year-ended 31 December 20x7 as follows.

	31 December 20x7	31 December 20x6	Explanation
Revenue	xxx	xxx	
Cost of goods sold	<u>xxx</u>	<u>xxx</u>	
Gross profit	xxx	xxx	Additional subtotal: revenue less cost of goods sold
Employee benefits not included in costs of goods sold	xxx	xxx	
Depreciation not included in costs of goods sold	xxx	xxx	
Expected credit losses on trade receivables	xxx	xxx	
Interest income on contract assets	xxx	xxx	
Fair value gains on equity instruments	<u>xxx</u>	<u>xxx</u>	
Operating profit	xxx	xxx	Mandatory subtotal: The total of all income and expenses classified in the operating category.
Share of profit of associates and joint ventures	xxx	xxx	
Fair value gains on investment property	<u>xxx</u>	<u>xxx</u>	
Profit before financing and income taxes	xxx	xxx	Mandatory subtotal: The total of operating profit or loss and all income and expenses classified in the investing category.
Interest expense on bank loans	<u>xxx</u>	<u>xxx</u>	
Profit before income taxes	xxx	xxx	Additional subtotal: all income and expenses other than those classified in the income taxes and discontinued operations categories.
Income tax expense	<u>xxx</u>	<u>xxx</u>	
Profit from continuing operations	xxx	xxx	Additional subtotal: all income and expenses other than those classified in the discontinued operations category.
Loss from discontinued operations	<u>xxx</u>	<u>xxx</u>	
Profit	xxx	xxx	Mandatory total

8.3 Example C – entity that provides financing to customers as a main business activity

Scenario C: Entity S provides financing to customers as a main business activity

Differences from Example A are in red underlined text.

The income and expenses described in the common fact pattern are classified as follows:

Income or expense	Classification	Explanation
Revenue from contracts with customers	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See section 3.4 .
Costs of goods sold	Operating	
Employee benefits not included in costs of goods sold	Operating	
Depreciation not included in costs of goods sold	Operating	
Expected credit losses on trade receivables	Operating	Share of profit or loss from associates and joint ventures accounted for using the equity method is also classified in the investing category. See section 3.2 .
Share of profit of associates and joint ventures (accounted for using the equity method)	Investing	
Fair value gains on equity instruments	Investing	
Fair value gains on investment property	Investing	Financial assets and investment property generate a return individually and largely independently of the entity's other resources (IFRS 18.53(c)), however, Entity S does not invest in those assets as main business activities, therefore, income and expenses are classified in the investing category. See sections 3.2 and 3.8.1 .
<u>Interest expense on bank loans</u>	Operating	<u>Bank loans arise from transactions that involve only the raising of finance (IFRS 18.59(a)), and interest expense arises from the subsequent measurement of the liability (IFRS 18.60). Entity S provides financing to customers as a main business activity, and Entity S concludes that the income and expenses arising from the bank loan is related to providing finance to customers (IFRS 18.65(a)(i)). Therefore, interest expense is classified in the operating category. See sections 3.3 and 3.8.2.</u>
Interest income on contract assets	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See section 3.4 .
Income tax expense	Income taxes	Income and expenses within the scope of IAS 12 are classified in the income taxes category. See section 3.5 .
Loss from discontinued operations	Discontinued operations	Income and expenses presented as a single line item in accordance with IFRS 5.33(a) are classified in the discontinued operations category. See section 3.6 .

Entity S considers the requirement in IFRS 18.24 to present additional subtotals beyond those that are mandatory (see section [5.1](#)) and concludes that it will present **four** additional subtotals:

Additional subtotal	Description
Gross profit	The difference between revenue and cost of goods sold.
Net interest income	The difference between interest income on contract assets and interest expense on bank loans.
Profit or loss before income taxes	All income and expenses other than those classified in the income taxes and discontinued operations categories.
Profit or loss from continuing operations	All income and expenses other than those classified in the discontinued operations category.

Entity S presents its statement of profit or loss for the year-ended 31 December 20x7 as follows.

	31 December 20x7	31 December 20x6	Explanation
Revenue	xxx	xxx	
Cost of goods sold	xxx	xxx	
Gross profit	xxx	xxx	Additional subtotal: revenue less cost of goods sold
Interest income on contract assets	xxx	xxx	
Interest expense on bank loans	xxx	xxx	
Net interest income	xxx	xxx	Additional subtotal: the difference between interest income on contract assets and interest expense on bank loans.
Employee benefits not included in costs of goods sold	xxx	xxx	
Depreciation not included in costs of goods sold	xxx	xxx	
Expected credit losses on trade receivables	xxx	xxx	
Operating profit	xxx	xxx	Mandatory subtotal: The total of all income and expenses classified in the operating category.
Share of profit of associates and joint ventures	xxx	xxx	
Fair value gains on equity instruments	xxx	xxx	
Fair value gains on investment property	xxx	xxx	
Profit before financing and income taxes	xxx	xxx	Mandatory subtotal: The total of operating profit or loss and all income and expenses classified in the investing category. <u>In this scenario, Entity S does not have any income and expenses classified in the financing category. However, IFRS 18.69(b) requires this subtotal to be presented for most entities (see 5.1.3 for explanation of situations where entities are forbidden from presenting this subtotal).</u>
Income tax expense	xxx	xxx	
Profit from continuing operations	xxx	xxx	Additional subtotal: all income and expenses other than those classified in the discontinued operations category.
Loss from discontinued operations	xxx	xxx	
Profit	xxx	xxx	Mandatory total

8.4 Example D – entity that provides financing to customers as a main business activity and invests in investment property measured at fair value as a main business activity

Scenario D: Entity S provides financing to customers as a main business activity and invests in investment property measured at fair value as a main business activity

Differences from Example A are in red underlined text.

The income and expenses described in the common fact pattern are classified as follows:

Income or expense	Classification	Explanation
Revenue from contracts with customers	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See section 3.4 .
Costs of goods sold	Operating	
Employee benefits not included in costs of goods sold	Operating	
Depreciation not included in costs of goods sold	Operating	
Expected credit losses on trade receivables	Operating	
Share of profit of associates and joint ventures (accounted for using the equity method)	Investing	Share of profit or loss from associates and joint ventures accounted for using the equity method is also classified in the investing category. See section 3.2 .
Fair value gains on equity instruments	Investing	Assets generate a return individually and largely independently of the entity's other resources (IFRS 18.53(c)), however, Entity S does not invest in those assets as a main business activity, therefore, income and expenses are classified in the investing category. See sections 3.3 and 3.8.1 .
<u>Fair value gains on investment property</u>	Operating	<u>Financial assets such as investment property generate a return individually and largely independently of the entity's other resources (IFRS 18.53(c)). Entity S invests in investment property as a main business activity; therefore, income and expenses are classified in the operating category (IFRS 18.58). See sections 3.2 and 3.8.1.</u>
<u>Interest expense on bank loans</u>	Operating	<u>Bank loans arise from transactions that involve only the raising of finance (IFRS 18.59(a)), and interest expense arises from the subsequent measurement of the liability (IFRS 18.60). Entity S provides financing to customers as a main business activity, and Entity S concludes that the income and expenses arising from the bank loan is related to providing finance to customers (IFRS 18.65(a)(i)). Therefore, interest expense is classified in the operating category. See sections 3.3 and 3.8.2.</u>
Interest income on contract assets	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See section 3.4 .
Income tax expense	Income taxes	Income and expenses within the scope of IAS 12 are classified in the income taxes category. See section 3.5 .
Loss from discontinued operations	Discontinued operations	Income and expenses presented as a single line item in accordance with IFRS 5.33(a) are classified in the discontinued operations category. See section 3.6 .

Entity S considers the requirement in IFRS 18.24 to present additional subtotals beyond those that are mandatory (see section [5.1](#)) and concludes that it will present four additional subtotals:

Additional subtotal	Description
Gross profit	The difference between revenue and cost of goods sold.
Net interest income	The difference between interest income on contract assets and interest expense on bank loans.
Profit or loss before income taxes	All income and expenses other than those classified in the income taxes and discontinued operations categories.
Profit or loss from continuing operations	All income and expenses other than those classified in the discontinued operations category.

Entity S presents its statement of profit or loss for the year-ended 31 December 20x7 as follows.



	31 December 20x7	31 December 20x6	Explanation
Revenue	xxx	xxx	
Cost of goods sold	xxx	xxx	
Gross profit	xxx	xxx	Additional subtotal: revenue less cost of goods sold
Interest income on contract assets	xxx	xxx	
Interest expense on bank loans	xxx	xxx	
Net interest income	xxx	xxx	Additional subtotal: the difference between interest income on contract assets and interest expense on bank loans.
Fair value gains on investment property	xxx	xxx	
Employee benefits not included in costs of goods sold	xxx	xxx	
Depreciation not included in costs of goods sold	xxx	xxx	
Expected credit losses on trade receivables	xxx	xxx	
Operating profit	xxx	xxx	Mandatory subtotal: The total of all income and expenses classified in the operating category.
Share of profit of associates and joint ventures	xxx	xxx	
Fair value gains on equity instruments	xxx	xxx	
Profit before financing and income taxes	xxx	xxx	Mandatory subtotal: The total of operating profit or loss and all income and expenses classified in the investing category. <u>In this scenario, Entity S does not have any income and expenses classified in the financing category. However, IFRS 18.69(b) requires this subtotal to be presented for most entities (see 5.1.3 for explanation of situations where entities are forbidden from presenting this subtotal).</u>
Profit before income taxes	xxx	xxx	Additional subtotal: all income and expenses other than those classified in the income taxes and discontinued operations categories.
Income tax expense	xxx	xxx	
Profit from continuing operations	xxx	xxx	Additional subtotal: all income and expenses other than those classified in the discontinued operations category.
Loss from discontinued operations	xxx	xxx	
Profit	xxx	xxx	Mandatory total

8.5 Example E – insurance company that invests in financial assets as a main business activity

Scenario E: insurance company that invests in financial assets as a main business activity

Fact pattern

Scenario E is independent of Scenarios A – D.

Entity T is an insurance company and has the following income and expenses:

- ▶ Insurance revenue
- ▶ Insurance service expenses
- ▶ Net expense from reinsurance contracts
- ▶ Finance expense from insurance contracts
- ▶ Finance income from reinsurance contracts
- ▶ Employee benefits
- ▶ Depreciation
- ▶ Changes in fair value from investment in associates and joint ventures (measured at fair value through profit or loss in accordance with IAS 28.18⁵)
- ▶ Interest expense on bank loans
- ▶ Interest revenue calculated using the effective interest rate method
- ▶ Fair value gains on equity instruments
- ▶ Income tax expense
- ▶ Loss from discontinued operations

Entity T has applied the aggregation and disaggregation requirements of IFRS 18 and has determined that each of these classes of income and expense should be presented separately in the statement of profit or loss. Entity T has also considered the requirements of IFRS 18.75(c) to present separate line items for income and expenses related to insurance contracts (see section 4.3).

Entity T presents operating expenses by nature.

Analysis

The income and expenses are classified as follows:

Income or expense	Classification	Explanation
Insurance revenue	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See section 3.4.
Insurance service expenses	Operating	
Net expense from reinsurance contracts	Operating	
Finance expense from insurance contracts	Operating	IFRS 18.64(b) requires insurance finance income and expenses to be classified in the operating category. See section 3.3.
Finance income from reinsurance contracts	Operating	
Employee benefits	Operating	
Depreciation	Operating	Income and expenses from assets that do not generate a return individually and largely independently of the entity's other resources (IFRS 18.B48). See section 3.4.

⁵ IAS 28.18 provides an entity an irrevocable election to measure certain investments in associates and joint ventures at fair value through profit or loss. This includes investment-linked insurance funds.

Change in fair value from investments in associates and joint ventures	Operating	The associates and joint ventures are not accounted for using the equity method; therefore, it is necessary to assess whether Entity T invests in associates and joint ventures as a main business Activity. Entity T concludes that it does, therefore, income and expenses are classified in the operating category. See section 3.8.1 .
Interest expense on bank loans	Financing	Bank loans arise from transactions that involve only the raising of finance (IFRS 18.59(a)), and interest expense arises from the subsequent measurement of the liability (IFRS 18.60). As Entity T does not provide financing to customers as a main business activity, interest expense is classified in the financing category. See sections 3.3 and 3.8.2 .
Interest revenue calculated using the effective interest rate method	Operating	Financial assets such as equity instrument and financial assets at amortised cost generate returns individually and largely independently of the entity's other resources (IFRS 18.53(c)). Entity T invests in financial assets as a main business activity; therefore, income and expenses are classified in the operating category (IFRS 18.58). See sections 3.2 and 3.8.1 .
Fair value gains on equity instruments	Operating	
Income tax expense	Income taxes	Income and expenses within the scope of IAS 12 are classified in the income taxes category. See section 3.5 .
Loss from discontinued operations	Discontinued operations	Income and expenses presented as a single line item in accordance with IFRS 5.33(a) are classified in the discontinued operations category. See section 3.6 .

Entity T considers the requirement in IFRS 18.24 to present additional subtotals beyond those that are mandatory (see section [5.1](#)) and concludes that it will present four additional subtotals:

Additional subtotal	Description
Total investment income	All income and expenses relating to financial assets classified in the operating category. This subtotal is presented as Entity T invests in financial assets as a main business activity, so a sum of those activities is considered useful to users.
Profit or loss before income taxes	All income and expenses other than those classified in the income taxes and discontinued operations categories.
Profit or loss from continuing operations	All income and expenses other than those classified in the discontinued operations category.

Entity also considers the requirements of IFRS 17 to disaggregate information, resulting in these additional subtotals:

Additional subtotal	Description
Insurance service result	Comprises insurance revenue and insurance service expenses, including the net expense from reinsurance contracts (IFRS 17.80(a)).
Net insurance financial result	Comprises insurance finance income from reinsurance contracts and insurance finance expense from insurance contracts (IFRS 17.80(b)), 82).

Entity T presents its statement of profit or loss for the year-ended 31 December 20x7 as follows.

	31 December 20x7	31 December 20x6	Explanation
Insurance revenue	xxx	xxx	
Insurance service expenses	xxx	xxx	
Net expense from reinsurance contracts	<u>xxx</u>	<u>xxx</u>	
Insurance service result	xxx	xxx	Additional subtotal: comprises insurance revenue and insurance service expenses, including the net expense from reinsurance contracts (IFRS 17.80(a)).
Interest revenue calculated using the effective interest rate method	xxx	xxx	
Change in fair value from investments in associates and joint ventures	xxx	xxx	
Fair value gains on equity instruments	<u>xxx</u>	<u>xxx</u>	
Total investment income	xxx	xxx	Additional subtotal: all income and expenses relating to financial assets classified in the operating category.
Finance expense from insurance contracts	<u>xxx</u>	<u>xxx</u>	
Finance income from reinsurance contracts	xxx	xxx	
Net insurance financial result	xxx	xxx	Additional subtotal: comprises insurance finance income from reinsurance contracts and insurance finance expense from insurance contracts (IFRS 17.80(b)), 82).
Employee benefits	xxx	xxx	
Depreciation	<u>xxx</u>	<u>xxx</u>	
Operating profit and profit before financing and income taxes	xxx	xxx	Mandatory subtotal: The total of all income and expenses classified in the operating category. Mandatory subtotal: The total of operating profit or loss and all income and expenses classified in the investing category. Entity T does not have any income and expenses classified in the investing category; therefore, these subtotals are equal to one another.
Interest expense on bank loans	<u>xxx</u>	<u>xxx</u>	
Profit before income taxes	xxx	xxx	Additional subtotal: all income and expenses other than those classified in the income taxes and discontinued operations categories.
Income tax expense	<u>xxx</u>	<u>xxx</u>	

Profit from continuing operations	xxx	xxx	Additional subtotal: all income and expenses other than those classified in the discontinued operations category.
Loss from discontinued operations	<u>xxx</u>	<u>xxx</u>	
Profit	xxx	xxx	Mandatory total



Appendices

Appendix 1 – Defined terms

Appendix 1 includes terms defined in IFRS 18 that are used in this publication. See Appendix A to IFRS 18 for a complete list of defined terms in IFRS 18.

Defined term	Definition
aggregation	The adding together of assets, liabilities, equity, income, expenses or cash flows that share characteristics and are included in the same classification.
classification	The sorting of assets, liabilities, equity, income, expenses and cash flows based on shared characteristics.
disaggregation	The separation of an item into component parts that have characteristics that are not shared.
IFRS Accounting Standards	Accounting standards issued by the International Accounting Standards Board. They comprise: (a) International Financial Reporting Standards; (b) International Accounting Standards; (c) IFRIC Interpretations; and (d) SIC Interpretations. IFRS Accounting Standards were previously known as International Financial Reporting Standards, IFRS, IFRSs and IFRS Standards.
management-defined performance measure	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 of IFRS 18, or specifically required to be presented or disclosed by IFRS Accounting Standards.
material information	Information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity.
notes	Information in financial statements provided in addition to that presented in the primary financial statements.
operating profit or loss	The total of all income and expenses classified in the operating category.
other comprehensive income	Items of income and expense (including reclassification adjustments) that are recognised outside profit or loss as required or permitted by other IFRS Accounting Standards.
primary financial statements	The statement(s) of financial performance, the statement of financial position, the statement of changes in equity and the statement of cash flows.
profit or loss	The total of income less expenses included in the statement of profit or loss.
profit or loss before financing and income taxes reclassification adjustments	The total of operating profit or loss and all income and expenses classified in the investing category. Amounts reclassified to profit or loss in the current reporting period that were included in other comprehensive income in the current or prior periods.

total comprehensive income	The change in equity during a reporting period resulting from transactions and other events, other than those changes resulting from transactions with owners in their capacity as owners.
useful structured summary	A structured summary provided in a primary financial statement of a reporting entity's recognised assets, liabilities, equity, income, expenses and cash flows that is useful for: (a) obtaining an understandable overview of the entity's recognised assets, liabilities, equity, income, expenses and cash flows; (b) making comparisons between entities, and between reporting periods for the same entity; and (c) identifying items or areas about which users of financial statements may wish to seek additional information in the notes.



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