International Accounting Standards Board
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Post-implementation Review: IFRS 8 Operating Segments

Grant Thornton International Ltd is pleased to comment on the International Accounting Standards Board's (the Board) Request for Information *Post-implementation Review: IFRS 8 Operating Segments* (the Request for Information). We strongly support the post-implementation review process and therefore welcome the publication of the Request for Information.

Six years ago we agreed with the Board's proposal to replace IAS 14 with a management approach to segment reporting (IFRS 8). We continue to support that decision today and believe that IFRS 8 is a fundamentally sound standard that requires no major changes. That said, IFRS 8 has perhaps proved more controversial than anticipated and the information provided may have fallen short of some users' expectations. This is unfortunate and the Board will no doubt pay close attention to users' concerns.

We note that the information reported in practice is particularly sensitive to judgements made about both the identification of the Chief Operating Decision Maker (CODM) and the application of the aggregation criteria. We suggest, therefore, that the Board should consider improving the definition of the CODM and providing additional guidance in order to encourage more appropriate judgements. We welcome the Board's proposal to require judgements made by management in applying the aggregation criteria. The Board might also usefully consider providing more guidance on the application of those criteria.

Our responses to the questions in the Request for Information's Invitation to Comment are set out in the Appendix.

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If you have any questions on our response, or wish us to amplify our comments, please contact our Executive Director of International Financial Reporting, Andrew Watchman (andrew.watchman@uk.gt.com or telephone + 44 207 391 9510).

Yours sincerely,

Kenneth C. Sharp

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Invitation to comment questions

Question 1

Are you comparing IFRS 8 with IAS 14 or with a different, earlier segment-reporting Standard that is specific to your jurisdiction?

In providing this information, please tell us:

(a) what your current job title is;
(b) what your principal jurisdiction is; and
(c) whether your jurisdiction or company is a recent adopter of IFRSs.

This letter is sent on behalf of Grant Thornton International - one of the world's leading organisations of independently owned and managed accounting and consulting firms. These firms provide assurance, tax and advisory services to privately held businesses and public interest entities. More than 2,500 partners and 30,000 staff provide clients with distinctive, high quality and personalised service in over 100 countries. We serve both publicly quoted entities and the privately-owned sector across the world. In many markets our publicly quoted clients are predominantly smaller listed entities for which issues of practical application of IFRSs are of particular concern.

Accordingly, this letter reflects the experience of Grant Thornton member firms in a number of different jurisdictions. These include jurisdictions in which IAS 14 was previously applied and jurisdictions that transitioned to IFRSs at a time when IFRS 8 was already effective.

Question 2

What is your experience of the effect of the IASB's decision to identify and report segments using the management perspective?

Our broad observation is that the adoption of a management perspective for reporting segment information has led to rather less extensive changes in practice than might have been expected. This reflects our observations that, in many cases:

- the number of reportable segments determined in accordance with IFRS 8 is the same or similar to the number of primary segments reported in accordance with IAS 14
- the segment profit measures reported are consistent with IFRS
- differences in how segments are described between the financial statements and management commentary (or equivalent) persist.

On the basis of these observations it is perhaps questionable whether IFRS 8 has succeeded in its aim of allowing investors and other users to see the company's operations 'through the eyes of management' and to understand better the risks the company faces and how they are managed. However, investors and other users are of course best placed to comment on the extent to which IFRS 8 has led to more useful information in practice.

The following paragraphs discuss some possible reasons why the management perspective may not have delivered the extent of change (and benefits) that the Board anticipated.

Interpretive issues and key judgements
The information reported in accordance with IFRS 8 is particularly sensitive to the judgements made about:

- identification of the CODM
- application of the aggregation criteria.

We observe that many companies identify their Board of Directors (which includes both executive and non-executive directors) as the CODM. Typically, this leads to the reported segment information being relatively high level (few operating segments and limited detail). Given that the function of the CODM is to allocate resources to and assess the performance of the operating segments, it is perhaps surprising that a body that includes non-executives is identified as often as seems to be the case. However, we find in practice that this is a judgement which auditors are not easily able to challenge on the basis of the definition and guidance in IFRS 8. We note that the European Securities and Market Authority's Report 'Review of European enforcers on the implementation of IFRS 8 – Operating Segments' (the ESMA Report) recommends giving consideration to amending the definition of the CODM, and adding more guidance. We agree with this recommendation. In addition, we recommend that the identity of the CODM should be disclosed.

IFRS 8 permits the aggregation of two or more operating segments if this is consistent with the core principle of this IFRS, the segments have similar economic characteristics and certain other criteria are satisfied. We note that the ESMA Report raises concerns as to the application of these criteria – particularly the 'similar economic characteristics' criterion. We share these concerns. We therefore welcome and support the Board's proposal (in ED/2012/1 'Annual Improvements to IFRSs 2010-2012 Cycle') to require additional disclosure about the judgements made by management in applying the aggregation criteria.

Other issues
IFRS 8's management approach is simple to apply and audit for a company in which a particular individual or function undertakes resource allocation and operating decisions using a clearly identifiable segment report that is prepared and reviewed regularly, and is largely consistent from one period to the next. However, many companies do not fit this description. For example:

- decision-making may be dispersed among various functions and levels
- reporting entities have many different management structures and supporting management information systems. At one end of the spectrum we observe entities that prepare segment information only on a somewhat ad hoc basis. These are usually smaller or less complex entities whose CEO has close day-to-day involvement with all the operations. At the opposite end of the spectrum some entities operate sophisticated enterprise reporting systems that provide information on a real-time basis and enable different reports to be generated for different purposes.

We believe these issues are inherent challenges for, or limitations to, the management approach. We do not therefore suggest specific changes to IFRS 8 in order to address them. However, providing clearer guidance in the determination of the identity of the CODM should help preparers with the identification of the data set that is used to make operating decisions and, therefore, the basis of determining the operating segments to be reported.

Questions 3 & 4

How has the use of non-IFRS measurements affected the reporting of operating segments?

How has the requirement to use internally-reported line items affected financial reporting?

As noted above we have observed that a majority of entities appear to report segment information using measurement bases that are consistent with IFRSs.

The main effect we observed is widespread reporting of what might be described as non-GAAP line items (such as EBITDA).

Questions 5 & 6

How have the disclosures required by IFRS 8 affected you in your role?

How were you affected by the implementation of IFRS 8?

Consistent with the introduction of any other major new standard, we invested time and resources in training our people and in developing guidance (internal and external) on the application of IFRS 8.

We do not consider IFRS 8 to be a particularly problematic standard from an audit perspective, other than the potential difficulty in challenging the identity of the CODM and, therefore, the data set used for reporting operating segments. Our global IFRS consultation service receives few questions relating to the interpretation or application of IFRS 8. That said, we note again that the information provided in accordance with IFRS 8 is highly sensitive to key judgements about:

- identifying the CODM
- application of IFRS 8's aggregation criteria.

We do observe that compliance issues relating to IFRS 8 are a fairly frequent source of audit adjustments (including during the 'hot review' stage of our audit process). This indicates an evident lack of attention to, and understanding of, the Standard on the part of some preparers. We also sometimes encounter resistance to the disclosure of 'internal information' in a few cases – including protestations that the information is commercially sensitive (as noted in the Request for Information).