MASB MALAYSIAN ACCOUNTING STANDARDS BOARD
LEMBAGA PIAWAIAN PERAKAUNAN MALAYSIA

16 November 2012

Mr Hans Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London, EC4M 6XH
United Kingdom

Dear Mr Hoogervorst

REQUEST FOR INFORMATION *POST-IMPLEMENTATION REVIEW: IFRS 8 OPERATING SEGMENTS*

The Malaysian Accounting Standards Board (MASB) welcomes the opportunity to provide comments on the IASB's Request for Information *Post-implementation Review: IFRS 8 Operating Segments*. We support the post-implementation review process and therefore welcome the publication of the Request for Information.

MASB is established under the Financial Reporting Act 1997 as an independent national standard-setter to develop and issue accounting and financial reporting standards in Malaysia. IFRS 8 was issued as FRS 8 by the MASB in 2008 and was effective on 1 July 2009. In November 2011, the MASB issued a new MFRS Framework, an IFRS-compliant Framework, as part of its commitment to full convergence with IFRS on 1 January 2012. MFRS 8, an equivalent to IFRS 8, was issued as part of the MFRS Framework and was effective on 1 January 2012.

The comments from our constituents on the effect of applying IFRS 8 are attached in the Appendix. Respondents generally find it difficult to identify the Chief Operating Decision Maker (CODM). They are also concerned that too much latitude is given to management resulting in a reduction in quality of segment information. Therefore, they recommended that the IASB should improve the determination of CODM in IFRS 8 and reduce the use of judgment by the management in disclosing segment information. Additionally, they recommended that more clarification should be provided by the CODM about the disclosures made in segment information.

If you need further clarification, please contact Ms. Tan Bee Leng at +603 2240 9200 or by email at beeleng@masb.org.my.

Thank you.

Yours sincerely,

MOHAMMAD FAIZ AZMI
Chairman

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Comments from our constituents consist of comments that answer the questions stated in the Request for Information and comments that are general in nature. The former is in Section A and the latter is in Section B as follows:

Section A: Specific comments

Your background and experience

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 is your current job title is;

(b) what your principal jurisdiction is; and

(c) whether your jurisdiction or company is a recent adopter of IFRSs.

Commentator 1	We are not an adopter of IFRSs but as an external auditor, our auditee adopted IFRSs in preparing their financial statements.
Commentator 2	Comparing IFRS 8 with IAS 14.
Commentator 3	External auditors.
Commentator 4	An executive director and chief financial officer of a public listed company.
Commentator 5	We are comparing IFRS 8 with IAS 14. (a) Financial accounting (b) Malaysia (c) Convergence in 2012
Commentator 6	External auditors.
Commentator 7	Regulator.

The use of the management perspective

Question 2: What is your experience of the effect of the IASB's decision to identify and report segments using the management perspective?

Commentator 1	Our comments are as other users. We are satisfied with the IFRS 8 that enables organisation to provide a more detailed and comprehensive results of the various segments of business within the statutory bodies. In our experience, we find that the disclosures of the financial statements provide more information on the operations.

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Commentator 2	From a commercial banking preparer point of view, we have not encountered much problem in using management perspective as this is very much align to the internal performance tracking/reporting of our business segments. As such there were no changes in the operating segments upon applying IFRS 8. The changes made to the operating segments was as a direct result of change in business environment i.e. acquisition of banks which has a new distinct business segment e.g. Investment Banking or disposal of subsidiaries with non-core banking business i.e. Insurance company.
Commentator 3	Preparers have, in the past, geared their financial reporting systems to provide geographical and business segments in accordance with IAS 14 and this remains the main method of reviewing segment results and performances up till today. Consequently, it is not surprising to notice that there is little change in the manner of segment reporting in accordance with IFRS 8. There are indeed at times, challenges within preparers in identifying the CODM as there could be more than 1 decision makers, all of whom are equally important as part of the entity's decision-making process of resource allocation.
Commentator 4	We have not found our shareholders raising any questions on the segment information which may indicate that they are less concern about the segments' performance versus the total performance of the company.
Commentator 5	Since we applied IFRS 8, we do not disclose segmental information for liabilities and other segment information as this information are not provided to the CODM. This has increased the efficiency of our reporting process and this has not affected our ability to communicate with investors.
Commentator 7	The reportable segments using the management perspective are disclosed based on the components of the entity that the CODM monitors in making decisions over the resource allocation and the performance assessment of the components. It may not reflect the actual financial position and financial performance of the reportable segments. For example, the expenses that incurred by corporate divisions such as group treasury, group human capital and others may not be allocated to respective segments although the respective segments utilise those resources. Therefore, the users are unable to compare the actual performance amongst segments within an entity and industries. We have reviewed the segmental information prepared by 50 companies listed on the Main Market of Bursa Malaysia. The companies were randomly selected from various sectors, including but not limited to finance, construction, consumer products and services.

	Based on our observation, in their first application of IFRS 8, only 9 of the 50 listed companies have reported changes to the number of reportable segments, of which 7 reported an increase whilst the remaining 2 reported a reduction. The result of our observation, to a large extent, is consistent with the IASB's expected benefits in its Basis of Conclusion on ED 8 Operating Segments. There is no explicit requirement within IFRS 8 to disclose the CODM. Nonetheless, more than half of those being reviewed have such disclosure. 8 of those listed companies identified the Board of Directors as the CODM and 7 others identified the management team. However, no further details of who constitute the management team. We believe that the identity of the CODM is relevant and useful to the users of financial statements. Paragraph 12 of IFRS 8 states that operating segments often exhibit similar long-term financial performance if they have similar economic characteristics. IFRS 8 provides an example of 2 operating segments that would have similar economic characteristics if they have similar long term average gross margins. We believe further guidance on the definition of "similar economic characteristics" would be useful to determine the segments that can be aggregated into a single operating segment.

The measurement of reported line items on a basis consistent with amounts reported to the CODM

Question 3: How has the use of non-IFRS measurements affected the reporting of operating segments?

Commentator 1	Not applicable because as an external auditor, we only audit the financial statements.
Commentator 2	As per reply in Q2, we did not change measurement basis as it is consistent with our internal performance tracking.
Commentator 3	Our experience with preparers indicates that the preparers seldom use non-IFRS measurements.
Commentator 4	It is better to report segment's pre-tax profits instead of after tax profit.
Commentator 5	No measurement basis has changed for operating segment information on the application of IFRS 8.

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The reporting of only those line items regularly reviewed by the CODM

Question 4: How has the requirement to use internally-reported line items affected financial reporting?

Commentator 1	Not applicable because as an external auditor, we only audit the financial statements.
Commentator 2	As per reply in Q2, we did not change reporting line items as it is consistent with our internal performance tracking.
Commentator 3	Our experience with preparers indicates that they are generally happy with the requirement to report only line items that are regularly reviewed by the CODM.
Commentator 4	In reporting a segment's performance, certain line items such as income tax expense may be omitted.
Commentator 5	Since we applied IFRS 8, we do not disclose segmental information for liabilities and other segment information (such as, depreciation, amortisation, etc.) as this information are not provided to the CODM.
Commentator 7	We believe that financial information in respect of revenue, profit or loss, assets and liabilities for each reportable segment are useful to investors. Hence, these items should be disclosed regardless whether they are regularly reviewed by the CODM.

You and your role

Question 5: How have the disclosures required by IFRS 8 affected you in your role?

Commentator 1	From our auditing experience, we found that large organisations need to report segmental information to monitor their performance whereas it's a burdensome to small organisations because it is costly and time consuming.
Commentator 2	Disclosures required by IFRS 8 provide a good snap shot of the performance of the respective segment of the company as such it conveys concise information to investors and analyst. We do receive quite a number of talking points from analyst/investors on the IFRS 8 disclosure note and it proved that investors/analyst are making use of this information for their own review.
Commentator 3	Our experience with preparers also indicates that practical compliance with the disclosure requirements of IFRS 8 is less burdensome as compared to IAS 14 but there remains uncertainty over the understanding of the link between disclosures of segment

	information and entity-wide disclosures, especially in the context of preparers with diverse operations in multiple jurisdictions.
Commentator 4	Some simplification would be helpful. Operating versus Geography - option should be given to the reporting entity to elect the most appropriate segment. For example, entities whose business activities are primarily engaged in one geographical location (say 90% in Malaysia) should not be required to provide additional information based on the geographical location of customers and assets.
Commentator 5	Operating segment disclosures have become less burdensome as there are fewer disclosures and based on our own internal reporting requirements. However, the process in determining the reportable segments and aggregating and the need to reassess regularly is time consuming. The information presented now about operating segments conveys better information to investors and shareholders. There are no regular reports on any segment information in addition to that required by IFRS 8.

Your experience of implementing IFRS 8

Question 6: How were you affected by the implementation of IFRS 8?

Commentator 1	Not applicable because as an external auditor, we only audit the financial statements.
Commentator 2	There were no significant costs incurred from adopting IFRS 8. As IFSR 8 is largely driven by management perspective approach, most of our MIS are in place for reporting of the segments and the respective reporting lines.
Commentator 4	Depending on the nature and complexity of the entity's business, meeting the full requirements of the IFRS can be time consuming and tedious.
Commentator 5	No significant unexpected costs were incurred to comply with IFRS 8. The practical difficulty we encountered was with the identification of operating segments and the appropriateness of aggregating operating segments at first-time adoption of IFRS 8, as judgement is applied.

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Section B: General comments

Commentator 6:

Introduction

IFRS 8, replicates the FASB's SFAS 131, which is quite substantially different from the precursor (IAS 14) in respect of segment information identification, measurement and disclosure. This new standard has three main key features which are different from its precursor. First, IFRS 8 has a wider scope of application. Entities that hold assets in a fiduciary capacity are required to produce segment reports under the new standard, which is not required under IAS 14. Consequently, this standard should lead to an increase in the number of preparers than what it was under the IAS 14. This hopefully will result in greater corporate transparency pertaining to segment information. Second, "management approach' is used in identifying and measuring reportable segments. Under this approach, segments are identified based on the internal reporting system that is regularly reviewed by the entity's CODM as opposed to a risk and reward measurement approach. Finally, additional disclosure of segment information is required under the new standard.

Issues and challenges of IFRS 8

IFRS 8 has been dogged by controversy since its implementation in the beginning of 2009. Unlike many other IFRSs, IFRS 8 is not truly the IASB or European accounting standard. IFRS 8 replicates the SFAS 131 as part of the convergence effort between the IASB and the FASB. The extant academic research on SFAS 131 had some far revealed unfavorable findings against it.

In the UK, the Financial Reporting Review Panel (FRRP) had raised concerns over the application of IFRS 8 by undertaking a review on a sample of 2008 annual accounts and 2009 interim accounts. In their review, they found organizations with different divisions and significant operations in different countries reported only one operating segment. The titles and responsibilities of the executive team implied an organizational structure that was not reflected in the accounts segment figures.

In other cases, the Review Panel noted that the operating analysis set out in the narrative report differed from the operating segments in the financial statements. Further, in some incidents, the narrative commentaries focused on non-IFRS measures, while the segmental disclosures were based on IFRS amounts. The Review Panel noted that preparers have complained about the complexities and impracticalities of implementing the standard.

The Tax justice campaigners in UK, for example, Richard Murphy, are not too happy with IFRS 8 because the requirements under IAS 14 to disclose segmental data by geographic location have been sidelined under the new requirements. The segmental data by geographic location is the core principle for curbing transferring tax liabilities to lower rate jurisdictions. Murphy further argued it would be logical that segmental reporting standard, as in the case of former IAS 14, should be based on the same accounting standards as the main financial statements, but it is not case of IFRS 8. He concluded that segment data can offer a completely different view from the rest of the audited financial statements.

Murphy suggested that, in one of the FRRP's findings, it appears that there was evidence that companies are overlooking new standard's provisions, or using them as a smokescreen to deter prying eyes.

The FRRP statement urged company directors to test initial segment reports by with a number of questions:

- What are the key operating decisions made in running the business?
- Who are the segment managers (as defined in the standard) and who do they report to?
- How are the group's activities reported in the information used by management to review performance and make resource allocation decisions between segments?
- Have the reported segment amounts been reconciled to the IFRS aggregate amounts?
- Do the accounts describe the factors used to identify the reportable segments including the basis on which the company is organized?

Murphy cited a few research studies which seemed to indicate that US organizations which adopt SFAS 131 would exploit the ability to abandon geographic disclosure to make it harder for shareholders to monitor managers' decisions related to foreign operations.

At this juncture, we shared with Murphy's view that unless the above issues, including geographical revenues, are accurately reported, IFRS 8 will be potentially bad for shareholders.

<u>Identification of the Chief Operating Decisions Maker (CODM)</u>

The term, CODM identifies a function, not necessarily a manager with specific title. The function is to allocate resources to and assess the performance of the operating segment of an entity. Thus, such function involves making operating decisions and may also be involved in strategic decisions. It is quite common in practice that allocating resources and assessing performance are not carried out by the same person(s) or using the similar set of information. This could potentially create a confusing picture as to who is/are CODM/CODMs. For example, the CODM could be identified as the board of directors which consists of both executive and independent non-executive directors. As a result, the operating segment disclosures could be based on less detailed information. Another issue we have is in relation to corporate governance responsibilities. The non-executive directors are identified as CODMs appears to be inconsistent with their role under the corporate governance appointment. **We therefore urge the Board to clarify the definition of CODM further to avoid unnecessary confusion and inconsistent application.**

This problem is exacerbated by non-disclosure of the identity of CODM. A Report on the usefulness of IFRS 8 published by the Research Committee of the Institute of Chartered Accountants of Scotland (ICAS) found that many FTSE 100 companies do not disclose the identity of CODM. Unfortunately a similar practice is noted in Malaysia. Thus readers of financial statements do not know who is reviewing the information which they are provided with. Although not mandatory to disclose, they are of the view that this information appears to be lost opportunities for companies to provide useful information to their stakeholders.

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We concur with ICAS's view on this as this is the key principle in the Conceptual Framework.

The use of management approach

We believe the intention of the management approach is good and its primary objective is to enhance the quality of the segment information, whose usefulness and relevance would increase. However, this approach provides too much leeway for the management to decide on what information goes into the report. This could lead to selective disclosures which would result in less objective and thus less relevant information. This can lead to inappropriate or wrong economic decisions. For example, because IFRS 8 allows non-IFRS based information for external reporting without requiring a full reconciliation to IFRS on a segment basis, a non-profit making activity can be easily be hidden using this provision.

The Bruegel Institute has published a research report on IFRS 8. This report argues that IFRS 8 runs the risk of decreasing the quality of information available to investors to assess companies' performance and value because IFRS 8 fails to impose consistent operating segment's format by allowing restrictions in geographical information (The Global Accounting Experiment, by Nicolas Veron, Bruegel Institute, blueprint series, April 2007).

In sum, the famous agency theory has manifested in the management approach which impinges upon the potentiality of management marginalizing the interest of shareholders.

Conclusion

The above comments and discussions have highlighted our concerns on IFRS 8. However, our principal concerns are not about comparability and consistency as these are enhancing qualitative information. But the core concerns are the reduction in quality of information and selective disclosures encouraged by the management approach. Both have negative effect on transparency and effectiveness of corporate governance of entities. The good old IAS 14 could do a better job than IFRS 8, in our view. The ultimate question is why throw away IAS 14 while its whatever defects, can be fixed without going to the great length of replacing it with a new standard which is of lower quality. In this regard, we are not making any progress towards a high quality financial reporting regime but instead, a regressive financial reporting regime which does not serve well to all stakeholders concerned, including the auditors.