

IFRS 8 – OPERATING SEGMENTS

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Segment reporting in accordance with IFRS 8 will be mandatory for annual financial statements covering periods beginning on or after 1 January 2009. The standards replaces IAS 14, Segment Reporting, from that date.

The objective of IFRS 8 is to require public companies to disclose information about their business activities and the economic environments in which they operate on the same basis as it is used by management to make decisions about the allocation of the company’s resources and to assess the performance of the business.

The standard has been endorsed for use in the European Union; other jurisdictions may have similar legal constraints on the use of new IASB standards (these are not discussed here).

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Summary of main differences between IFRS 8 and IAS 14

The table below analyses the main differences between IFRS 8 Operating Segments and IAS 14 Segement Reposting, in terms of the identification of segments, the measurement of segment information, and disclosures

IFRS 8	IAS 14
<i>Identification of segments</i>	<i>Identification of segments</i>
Operating segments are identified based on the internal reporting of financial information to the chief operating decision maker. Operating segments can include those that sell exclusively to internal customers.	Primary and secondary segments are identified based on the dominant source and nature of an entity’s risk and return, which are either products/services, or geographical areas. Repostable segments are only those that generate a majority of revenues from external sales.
<i>Measurement of segment information</i>	<i>Measurement of segment information</i>
Operating segments are measured as reported to management. Requires explanations on how disclosure items were measured.	Segmental information is disclosed in accordance with the group’s accounting policies. Defines how to measure disclosure items, such as segment revenue and expenses, segment asset and liabilities.
<i>Disclosures</i>	<i>Disclosures</i>
Requires disclosure about factors used to	No similar requirement.

<p>identify the operating segments and explanations on the types of products or services from which the reportable segment derives its revenues.</p> <p>Disclosure of much of the segmental information is reviewed by the chief operating decision maker.</p> <p>Disclosure of interest income and expense is required, unless net interest is used by management as basis for decision making.</p> <p>All entities have to provide some geographical information and certain major customer details.</p>	<p>Disclosure of certain segmental information is mandatory.</p> <p>No similar requirement</p> <p>No entity-wide disclosure requirements, although some secondary reporting segment disclosures are mandated.</p>
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Scope

Not all entities are required to disclose segment information in accordance with IFRS 8. IFRS 8 applies to entities that are public or are in the process of going public. If the listed parent company financial statements are presented together with a group's financial statements, no separate segmental information is required for the parent.

The questions and answers below clarify which entities are required to present segment information, and the requirements for companies who choose to present segment information even when not required to do so by the standard.

Are segment disclosures only required in the consolidated financial statements of a group?

Paragraph 2 of IFRS 8, no, an entity whose debt or equity instruments are traded in a public market is required to present segment disclosures in its individual financial statements. Segment information is also required in the consolidated financial statements of a group, when the parent's debt or equity instruments are traded in a public market. If the parent's individual financial statements are presented together with the group's consolidated financial statements, separate segmental disclosures for the parent are not required.

Is an entity whose securities are not yet listed, but which contemplates a public offering of its debt or equity securities in the future, required to provide disclosures under IFRS 8?

Only entities or groups which file or are in the process of filing their individual or the group's financial statements with a regulatory body for the purpose of issuing to the public debt or equity instruments would need to comply with IFRS 8.

Can an entity that is not under the scope of IFRS 8 report segmental information?

Entities outside the scope will not need to comply with IFRS 8 – but may choose to do so. Information about segments that is produced on a voluntary basis but that is not compliant with IFRS 8 cannot be described as segment information.

Operating segments

Operating segments are basis of the reportable segments disclosed in the financial statements. This section also highlights the importance of the concept of the chief operating decision maker (CODM) for the identification of operating segments. An operating segment is defined in IFRS 8 as a component of an entity:

- that engages in business activities from which it may earn revenues and incur expenses (including revenues and expenses relating to transactions with other components of the same entity);

- whose operating results are regularly reviewed by the entity's CODM to make decision about resources to be allocated to the segment and assess its performance, and, for which discrete financial information is available.

IFRS 8 indicates that a component should have its own revenue streams as well as incur expenses. Corporate division which earn no or only incidental revenues would not be operating segments, such as head office cost centres.

The CODM is not meant to be title, but identifies a function. The CODM allocates the resources to and assesses the performance of the operating segments of the entity or the group. The CODM would generally be the most senior level of management in the entity, such as the chief executive officer, chief operating officer or a group of executive officers, such as the board.

In the UK, the CODM will often be the board of directors collectively, but could be a sub-set of the board or an individual.

If multiple sets of segment data are reviewed by the CODM, factors such as the nature of the business activities of the components, the existence of managers allocated to the components or the basis of the presentation of the information to the board should be considered to determine what the operating segments are. If none of these provides a conclusive answer, the analysis of segments that provides the most useful information in respect of the nature and financial effects of the business activities should be the basis for identification of the operating segments.

Under IAS 14 the primary reporting segment format is identified based on an entity's internal organisational and management structure and its system of internal financial reporting to key management personnel. The primary reporting segment is either based on product/services or geographical areas. Under IFRS 8 the operating segments are identified based on the reporting of divisional results to the CODM. The principles of identification under IAS 14 and IFRS 8 are thus similar, but an analysis to determine the operating segments under IFRS 8 is still required, and these may well be different from the IAS 14 segments.

Reportable segments

Operating segments are identified based on the internal reporting of financial information to the CODM. Reportable segments are those actually disclosed in the financial statements. Operating and reportable segments are not always identical. The following questions and answers look at when operating segments can be aggregated or combined for reporting in the financial statements. The question is, when may operating segments be aggregated?

Two or more operating segments may be aggregated if certain conditions are met:

- The segment have similar economic characteristics, such as similar long-term average gross margins;
- Aggregation allows the users of financial statements to evaluate the nature and financial effects of the business activities;
- and segments are similar in each of the following respects: the nature of the products and services, the nature of the production processes, the type or class of customer for their products and services, the methods used to distribute their products or provide their services, and if applicable, the nature of the regulatory environment, for example, banking, insurance or public utilities. The fact that operating segments have been aggregated should be disclosed. Operating segment information needs to be disclosed separately for each operating segment, including each aggregated operating segment, if they exceed certain quantitative thresholds.

However an entity should ensure that all operating segments have been appropriately identified and the aggregation criteria have been met. The entity-wide disclosures, in accordance with paragraphs 32 to 34 of IFRS 8, are still required. It is important to ensure that the segments selected for reporting purposes are consistent with other reported information included in the annual report such as KIPs. Differences between narrative reporting and segmental financial reporting may confuse users of the financial statements. IFRS 8 does not prescribe a minimum or

maximum number of segments an entity should report as this is dependent on the individual entity's circumstances. Reporting too many segments may however not be practical or helpful to users. Reportable segments may change as a result of: an entity changing its internal organization or reporting structure, an operating segment increasing in importance and meeting the significance test, or an operating segment no longer meeting the significance test. When reporting segments change because of a change in the internal organization or reporting structure, the comparative information for prior periods has to be restated to reflect the new reporting segments, unless the necessary information is not available and the cost to develop it would be excessive. If prior periods cannot be restated, then in the year of change the current period needs to be disclosed based on the new and old reportable segment bases, unless the information is not available and the cost to develop it would be excessive.

Measurement and disclosure

Under IFRS 8, reportable segments are measured as they are reported to the CODM, and they therefore do not necessarily comply with IFRS generally. Similarly, disclosures required by IFRS 8 are generally based on the information reported to de CODM. One of the main differences between IAS 14 and IFRS 8 is that under IFRS 8 the segment results are disclosed in the financial statements as they are used by the CODM for the purposes of making decisions about allocating resources to the segment and assessing performance. Similarly only those assets and liabilities that are included in the measures of the segment's assets and segment's liabilities that are used by the CODM shall be reported for that segment. Reconciliations from the segment results and segments assets and liabilities to the entity's results and entity's assets and liabilities respectively need to be presented. The reported measures to be disclosed should be those that management believes are determined in accordance with the measurement principles most consistent with those used in measuring the corresponding amounts in the entity's financial statements.

If the CODM does not review a measure of liabilities no such measure needs to be disclosed. A measure of assets is required, however this would only reflect the amounts that are used by the CODM. If no asset information is reviewed by the CODM, the measure would be nil, and hence non-disclosure is deemed to be compliant with IFRS 8.

The amount of each segment item reported should be the measure reported to the CODM for the purpose of making decision about the allocation of resources and the assessment of performance. When reported to the CODM allocations of costs, revenues, assets and liabilities should be included in these measures. Allocations should be made on a reasonable basis. An entity should report its measure of profit or loss for each reportable segment. The following items should also be disclosed, if reviewed by or regularly provided to the CODM, whether or not they are included in the measure of the segments results: external revenues, intra-segment revenues, gross interest revenue and expense, depreciation and amortization, material items of income and expense as disclosed under paragraph 97 of IAS 1, the entity's interest in associates and joint ventures accounted for by the equity method, income tax expense or income, and other material non-cash items.

IFRS 8 also contains disclosure requirements applicable to all entities, regardless of whether, or in what format, the information is reported to the CODM. The information needs to be presented in accordance with the entity's accounting policies.

Interaction of IFRS 8 with other standards

There are important interactions between IFRS 8 and IFRS 5 Discontinued Operations and Assets Held for Sale and IAS 36 Impairment of Assets. Segmental reporting is also a requirement under IAS 34 Interim Financial Reporting, although less detail is required.

The components identified as discontinued operations in accordance with IFRS 5 may either qualify as a segment under IFRS 8 or may be included within an operating segment also containing continuing operations. The information to be disclosed under IFRS 8 will mainly depend on whether the information for discontinued operations is separately reported to and

reviewed by the CODM, within its own operating segment. An entity has to present a reconciliation from the segments results to the entity's profit or loss before discontinued operations, unless the results of discontinued operations were allocated to the segment. In accordance with IFRS 5, the reporting segment which included the discontinued operation should be identified and disclosed.

Although to a lesser degree of detail and only by entities which are under the scope of IFRS 8 for their annual reporting. The following disclosures are required: amounts of revenues from external customers and intra-segment revenues, if included in the measure of segment profit or loss reviewed by the chief operating decision maker or otherwise regularly provided to the chief operating decision maker, amount of the measure of segment profit or loss, amount of total assets for which there has been a material change from the amount disclosed in the last annual financial statements in the basis of segmentation or in the basis of measurement of segment profit or loss.

On publication of IFRS 8, IAS 36 was amended to state that the cash generating unit, or group of such units, to which goodwill is allocated for the purpose of the goodwill impairment test cannot be larger than an operating segment identified under IFRS 8. Prior to the issuance of IFRS 8, the equivalent requirement in IAS 36 stated that the cash generating unit or group of such units, to which goodwill is allocated, cannot be larger than a segment based on the entity's primary or secondary reporting format determined under IAS 14 and the operating segments identified under IFRS 8 pre-aggregation may therefore require the reallocations of goodwill for impairment test purposes on adoption of IFRS 8. IAS 36 provides guidance on the reallocation of goodwill resulting from a change in the composition of cash generating units.

IAS 36 also contains additional disclosure requirements for entities within the scope of IFRS 8: The amount of impairment losses or reversed impairment losses recognized in profit or loss and in other comprehensive income by segment; for each material impairment loss or reversal of impairment loss, the segment to which the relevant asset or cash generating unit belongs.

Transition

IFRS 8 is effective for annual financial statements for periods beginning on or after 1 January 2009. Early application is permitted and since IFRS 8 has been endorsed for use in the European Union, UK based entities can adopt this standard early for their financial reporting. If an entity provides segmental disclosures under IFRS 8, the fact should be disclosed.

If an entity applies IFRS 8 from its effective date, that is to annual periods beginning on or after 1 January 2009, the entity's first IFRS 8 compliant segmental data is provided in its interim financial report in accordance with IAS 34 Interim Financial Reporting.

The proposed improvement by the IASB, Issue 3, in the exposure draft, Proposed Improvements to IFRS, published by the IASB in October 2008, is a clarification regarding the disclosure of a measure of segments assets, if such a measure is not reviewed by the CODM. The proposal is that if the measure is not reviewed by the CODM, non-disclosure is compliant with IFRS 8. The proposed amendment would not change the IFRS, but only the basis of conclusion. The proposed improvement would become effective from 1 January 2010, although earlier application would be permitted.

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