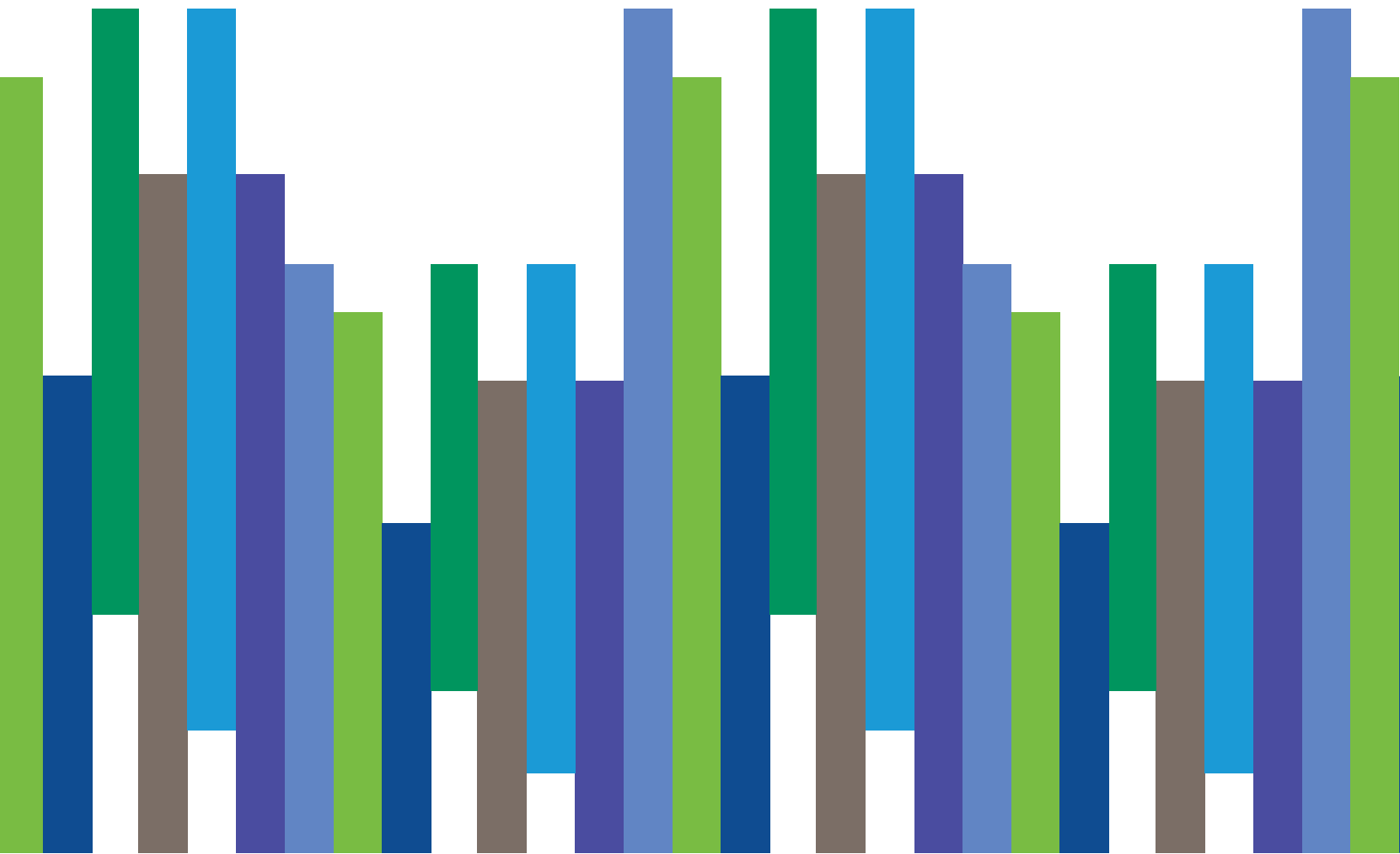




CFA Institute

SEGMENT DISCLOSURES: INVESTOR PERSPECTIVES



CFA Institute is the global association of investment professionals that sets the standard for professional excellence and credentials. The organization is a champion for ethical behavior in investment markets and a respected source of knowledge in the global financial community. The end goal: to create an environment where investors' interests come first, markets function at their best, and economies grow. CFA Institute has more than 155,000 members in 165 countries and territories, including 150,000 CFA® charterholders, and 148 member societies. For more information, visit www.cfainstitute.org.

CFA®, Chartered Financial Analyst®, AIMR-PPS®, and GIPS® are just a few of the trademarks owned by CFA Institute. To view a list of CFA Institute trademarks and the Guide for the Use of CFA Institute Marks, please visit our website at www.cfainstitute.org.

© 2018 CFA Institute. All rights reserved. No part of this publication may be reproduced, stored in a retrieval system, or transmitted, in any form or by any means, electronic, mechanical, photocopying, recording, or otherwise, without the prior written permission of the copyright holder. This publication is designed to provide accurate and authoritative information in regard to the subject matter covered. It is sold with the understanding that the publisher is not engaged in rendering legal, accounting, or other professional service. If legal advice or other expert assistance is required, the services of a competent professional should be sought.

ISBN: 978-1-942713-59-3

Contents

- BACKGROUND AND INTRODUCTION 1
 - INTRODUCTION 1
 - BACKGROUND..... 1
 - SEGMENT DISCLOSURES: 20 YEARS OLD AND STILL CHALLENGING..... 2
 - INVESTOR OBSERVATIONS 4
- SUMMARY OF RESULTS..... 6
- SURVEY QUESTIONS AND FINDINGS..... 13
 - GENERAL OBSERVATIONS 14
 - Importance of Segment Disclosures*..... 14
 - Satisfaction*..... 16
 - Critical Audit Matter* 17
 - Competitive Harm*..... 19
 - Technology*..... 20
 - Specific Elements of Disclosures*..... 21
 - Disaggregation*..... 23
 - Presentation*..... 23
 - Additional Disclosures*..... 23
 - Discussion of Results and Alternative Performance Measures* 24
 - Enforcement and Segment Changes*..... 24

CONSIDERATION OF SEGMENT DISCLOSURE REQUIREMENTS	26
<i>Management Approach</i>	26
<i>Presentation: Product/Service versus Region</i>	27
<i>Operating Segment: Revenues and/or Expenses</i>	28
<i>Chief Operating Decision Maker</i>	29
<i>Discrete Financial Information</i>	31
<i>Aggregation: Operating Segments into Reportable Segments</i>	33
<i>Aggregation: Qualitative Aggregation Criteria</i>	35
<i>Disaggregation: Quantitative Criteria</i>	38
<i>Qualitative versus Quantitative Criteria</i>	40
<i>Aggregation Criteria: Minimum Amount of Revenue Reported</i>	42
<i>Presentation: Improving the Presentation</i>	44
<i>Disclosures: Improving Disclosures</i>	46
ABOUT THE SURVEY	55

BACKGROUND AND INTRODUCTION

INTRODUCTION

Segment reporting information is critical to investors. Investors consider the information provided at the segment level to be just as important as information provided on an entity-wide basis. Many times, the segment footnote is the last footnote prepared with traditional accountants not fully trained in how investors' use segment information in the valuation process. Those running the business understand better the use of this information by the market and have regularly been seen to attempt to manage the level of disclosures. Segment disclosures complement the consolidated financial statements because they can shed light on differences in economic fundamentals, such as growth prospects, rates of profitability, degrees of risk, financing and financial structures, and differences in regulatory and tax regimes across business units.

Segment reporting formally began in 1997 under US GAAP with the issuance by the Financial Accounting Standards Board (FASB) of Statement of Financial Accounting Standard No. 131 (SFAS No. 131), "Disclosures about Segments of an Enterprise and Related Information." SFAS No. 131 became FASB Accounting Standards Codification (ASC) Topic 280.

We are pleased that the FASB has recently added a project to its agenda to undertake improvements to segment reporting with the objective of providing users with more decision-useful information about the reportable segments of public companies. The FASB indicated that the elements of Topic 280 under consideration by the FASB are the aggregation criteria and the disclosure package. We agree that targeted improvements in a number of areas are warranted. A review of International Financial Reporting Standard 8 (IFRS 8), "Operating Segments," should also be a project for the International Accounting Standards Board (IASB), given the similarity of the segment reporting requirements between the two reporting regimes.

We recently surveyed CFA Institute members, including portfolio managers and analysts. See the "About the Survey" section at the end of this document. We surveyed their level of satisfaction with existing segment disclosure requirements and solicited their views on areas for improvement. We surveyed general perceptions about segment disclosures as well as specific questions that correlate to the segment disclosure standards in Topic 280 so that we could provide the most useful information to accounting standard setters.

BACKGROUND

Current US GAAP and IFRS require that companies report segment information in a manner that is consistent with the way that management organizes the firm internally for making

operating decisions and assessing performance. This is referred to as the “management approach” to segment reporting.

In brief, companies first determine what constitutes an operating segment, which is defined as a component of a company that earns revenues and incurs expenses, whose operating results are reviewed by the company's chief operating decision maker (CODM), and for which discrete financial information is available. The CODM is the individual who both (1) allocates resources to, and (2) assesses the performance of the segments of a public entity. Discrete financial information generally consists of operating performance information, such as revenue and gross profit by product line; generally, a review of revenue-only data does not meet this requirement.

Operating segments are then aggregated into larger groups, or “reportable segments,” that must be reported in the financial statements. The aggregation criteria are based on both qualitative criteria, which are applied first and are based on economic characteristics, and then quantitative factors to ensure that the reportable segments meet certain reporting minimums based on revenues, profits, or assets.

Public companies are required to disclose certain specified components of segment profitability, as well as specific information regarding a reportable segment. Currently, segment disclosures are not required to be presented in any particular format by either US GAAP or IFRS.

What typically concerns professional investors is over aggregation, which clouds and reduces transparency around the mix and quality of the business and its related performance. Whether such aggregation is an intentional cloaking of results or required by Topic 280, investors see greater opportunity for reducing the “gaming” of the segment disclosures and increasing the clarity and transparency of these disclosures.

SEGMENT DISCLOSURES: 20 YEARS OLD AND STILL CHALLENGING

Despite having been issued over 20 years ago, Topic 280 on segment reporting always makes the top of the list when it comes to comments by the US Securities and Exchange Commission (SEC) calling out misapplication or questionable financial reporting practices. Specifically, elements of the standard, including identification of operating segments, aggregation of operating segments, and changes in reportable segments, are among the most frequently occurring comments provided to issuers. The SEC has publicly stated they will compare the financial statement disclosures to releases made by the company in other venues (e.g., press releases, websites, and speeches) to evaluate the application of the management approach. Comments from the 2016 and 2017 AICPA Conference on Current SEC and PCAOB Developments highlight the SEC’s focus on this topic.

2016 AICPA Conference on Current SEC and PCAOB Developments

Division of Corporation Finance Deputy Chief Accountant Nili Shah focused on two core aspects of this perennial staff accounting “hot button:” identification of operating segments and improper aggregation. Segment disclosures in the footnotes to the financial statements are based on a “management” approach,” with segment definition tied to how the CODM actually views and operates the business. A company should evaluate -- and disclose in the segment footnote-- all relevant data points regarding the enterprise when performing a segment analysis, including (but not limited to) the CODM report, the organization chart, compensation arrangements and the internal budgeting process. The staff generally will object to a company’s assertion that a business line or unit is not a separate operating segment because no shared operating costs are allocated to it, particularly where the availability of gross margins suggests that discrete financial information is available to the CODM to classify this unit as an operating segment.

With respect to aggregation of operating segments, Ms. Shah stressed the need for a holistic analysis of both quantitative and qualitative factors in light of the principles set forth in ASC Topic 280, to determine similarity of business activities across segments as a predicate to permissible aggregation. Just because there are quantitative similarities between operating segments does not mean that they are qualitatively similar business activities that should be combined; to the contrary, quantitative similarities may be merely “coincidental” and as such warrant more critical analysis of qualitative factors.

Another important point on segments was made by Mr. Kronforst, who cautioned companies to avoid “voluntarily expanding” their GAAP segment footnote to offer a “secondary” non-GAAP measure of profit or loss evaluated by the CODM. Since such disclosures are not mandated by GAAP, they fall within the scope of the SEC’s non-GAAP rules (in the case of the segment footnote to the financial statements, this means Item 10(e) of Regulation S-K as well as Regulation G).

Finally, the staff noted the recently settled SEC administrative proceeding brought against PowerSecure International, in which the SEC alleged that the company failed to accurately identify and report its segments as required by GAAP, thus violating Regulation S-X. This in turn led to the company’s failure to properly identify reporting units for purposes of goodwill impairment testing as required by other GAAP (ASC Topic 350). After discussions with the SEC staff, the company was permitted to use its fiscal 2015 Form 10-K to describe errors in prior period disclosures and revised its segment reporting disclosure to reflect corrected information for the affected fiscal years (2012-2014). The company also concluded in its 2015 Form 10-K that its disclosure controls and procedures for the three-

year period were not effective due to a material weakness in ICFR identified in 2015 relating to its misapplication of GAAP. The SEC's order instituted cease-and-desist proceedings under the financial reporting, internal accounting controls, and books-and-records provisions of the Exchange Act, and imposed a \$470,000 civil penalty.¹

2017 AICPA Conference on Current SEC and PCAOB Developments

A panel on SEC comment letters discussed the SEC staff's review of information disclosed in platforms other than the financial statements, including earnings releases, earnings calls, investor presentations, and registrant's websites. Comments are frequently issued on the consistency of this information with what is disclosed in the financial statements.

The panel also provided a list of the most frequent SEC staff comment focus areas, which was generally consistent with the topics communicated last year. The topic receiving the highest volume of comments this year was non-GAAP measures, but the volume is declining as companies continue to improve their non-GAAP disclosures. The staff will continue, however, to question misleading labelling and presentation of non-GAAP measures that have greater prominence than GAAP measures.

The other most common topics included MD&A, fair value disclosures, segments, and revenue recognition. Other areas generating frequent comments included business combinations, goodwill, intangible assets, and income taxes.²

INVESTOR OBSERVATIONS

Investors find segment disclosures as challenging as the SEC. Amazon—always criticized for their stingy disclosures—did not disclose the profitability of their Amazon Web Services business until 2015. And, as noted in a recent article by Bloomberg, "[Amazon Takes Secrecy to a Comic Extremes](#)," it changed the way analysts valued the company:

Mind you, Amazon has no problem blabbing about its financials when it's in the company's interests to do so. Amazon in 2015 started to disclose the revenue and segment operating profit of its cloud-computing business, Amazon Web Services, and it's not an exaggeration to say that the financial reveal boosted the company's stock market value by tens of billions of dollars. Analysts until then had been able to roughly estimate sales for AWS, but the company's transparent disclosure—especially about the surprising profit of the business—changed the way investors valued the company.³

When adopting the new revenue recognition disclosures—disclosures that were designed to provide more detail on revenue than required by the segment level disclosures—the disclosures were less informative than what investors expected. Amazon's and Google's (Alphabet Inc.) early adoption of the revenue recognition were disappointing, and the

¹https://www.weil.com/~media/publications/sec-disclosure-corporate-governance/2016/pcag_alert_dec_22_2016.pdf.

²<https://www.pwc.com/us/en/cfodirect/assets/pdf/in-depth/us2017-32-2017-aicpa-conference-sec-pcaob-developments.pdf>.

³<https://www.bloomberg.com/news/articles/2017-10-23/amazon-s-stinginess-with-disclosure-can-t-last-forever-gadfly>.

disclosures prompted comments from the SEC on their segments results—not just their revenue disclosures as highlighted in a Market Watch article, “[SEC: Tell Us More about All This Money; Amazon and Google: Nope.](https://www.marketwatch.com/story/sec-tell-us-more-about-all-this-money-2018-04-19)”

The SEC is apparently as curious as MarketWatch is about Google’s YouTube revenue, Amazon’s allocation of R&D spending and a few other matters related to the vast amounts of money coming and going from Big Tech’s corporate giants. Along with a back-and-forth with Microsoft Corp. MSFT, +0.38% that mostly involved that company’s early adoption of revenue-recognition rules, the SEC has disclosed correspondence with three of the world’s largest tech companies so far this year.

While the correspondence was only disclosed this year, it has actually been occurring for a while, as these tech companies became some of the most valuable and important in the world. The SEC engaged in lengthy correspondence with both Alphabet Inc. GOOG, +0.64% and Amazon.com Inc. AMZN, +1.17% AMZN, +1.17% in what ultimately turned out to be futile efforts to get more specifics from each company about certain items in their financial statements.

Specifically, the SEC seemed interested in parts of these companies that have grown into massive companies on their own, such as YouTube, Amazon Web Services and the Alexa line of intelligent speakers. Both Alphabet and Amazon avoid disclosing much about the performance or costs of those businesses, lumping them in to large buckets of money instead of fully breaking them out as segments of their much larger businesses.⁴

These examples highlight why improvements in segment disclosures, particularly aggregation and disaggregation, are necessary.

⁴<https://www.marketwatch.com/story/sec-tell-us-more-about-all-this-money-2018-04-19>

SUMMARY OF RESULTS

We sought to gain a general sense of how important and satisfied respondents were with the current state of segment disclosures. Accordingly, we asked several questions that were not directly tied to the manner in which segments are determined under the accounting guidance and then we asked questions directly related to the segment disclosure requirement set forth in Topic 280. The survey results are summarized below in that manner. Exhibits bolded have been reproduced in the summary. The remaining Exhibit and Table references are included in the detailed sections that follow the summary.

- Importance versus satisfaction**—For investors, 75% rate segment disclosures as very important to their analysis (see **Exhibit 1**, reproduced below from the full report). The respondents rate segment disclosures as equally, 58.7%, if not more important, 31.4%, for a total of 90.1%, than entity-wide disclosures (see **Exhibit 2**, reproduced below from the full report). That said, their satisfaction, 13.4%, with the segment disclosures is substantially less (see **Exhibit 3**, reproduced below from the full report) than their rating of the importance of segment disclosures. The implication for standard-setters is that there is substantial work to be done to meet segment disclosure investor needs.

Exhibit 1: Importance

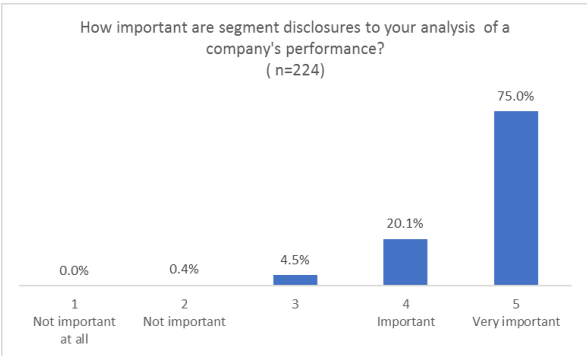


Exhibit 3: Satisfaction

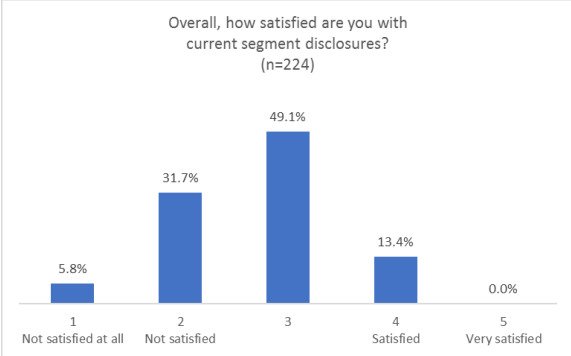
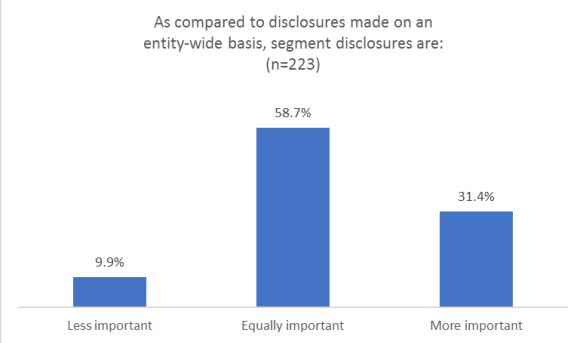


Exhibit 2: Importance Relative to Entity-Wide Disclosures



- **Critical audit matter**—Respondents strongly agreed (49.3%) or agreed (34.1%; for a total of 83.4%) that segments should be disclosed as a critical audit matter in the new auditor’s report (see Exhibit 4).
- **Competitive harm**—Respondents agreed or strongly agreed (67.8%) that competitive harm is overstated as a reason not to improve segment disclosures (see Exhibit 5).
- **Technology**—Respondents agreed or strongly agreed (86.6%) that technological improvements should, but have not, substantially improved segment disclosures (see Exhibit 6).
- **Enforcement**—Respondents (72.7%) agreed that regulators do not seem to enforce segment disclosure requirements effectively, but they did not feel as strongly (only 51.0%) that changing segments was a red flag. The question likely needed to be rephrased to ask if “frequent changing of segments were a red flag.” That said, respondents had insightful comments on this issue (see Exhibit 7 and Table 1).
- **Consistency of discussion results with segment disclosures**—A majority (61.8%) of respondents indicated that the public discussion of results was not necessarily consistent with segment results. Similarly, 74.8% of respondents agreed that non-GAAP measures are not, but should be, reconciled to segment results (see Exhibit 7 and Table 1).
- **Presentation**—We touched on the concept of presentation—specifically income statement presentation—in several questions. First, we queried satisfaction with presentation and then asked what improvements respondents perceived as most important. Respondents, 77.8%, noted that segment disclosures are not always presented clearly and reconciled to the basic financial statements and that presentation by product/service or by region—as currently allowed—made comparative analysis more difficult, 82.4% (see Exhibit 7 and Table 1).

When asked whether presentation by product/service and region should be required, 73.2% noted their preference for this alternative, as noted in Exhibit 9. Nearly all respondents believed that reconciliation of segment disclosures to the financial statements was a needed presentation improvement. Exhibit 18 notes that only 10.2% of respondents favored retaining the existing approach or not seeking any improvement. Overwhelmingly, respondents (88.7%) favored disclosures that reconciled to the financial statements—with 46.3% favoring reconciling the disclosure elements and 42.4% favoring a full income statement and balance sheet reconciliation. We believe the ordering of the response options may have impacted the response selection. With reconciliation of selected elements appearing first, we believe a quick read might have caused respondents not to discern the difference in options being the selection of elements of the financial statements and the full financial statements. Our

impression is supported by the responses to the question in Exhibit 19, where the results suggest that a minority, 31.0%, believed no improvement was needed in presentation of income statement components (i.e., where there are components that are not reconciled), while 65.0% believed companies should be required to disclose all segment income statement information—with 34.5% indicating it should be reviewed by the CODM and 30.5% indicating it should be provided regardless of whether it has been reviewed by the CODM.

When we asked respondents about whether segment disclosures should include a disclosure presenting all balance sheet items, a majority of respondents, 53.5% (Exhibit 20) agreed or strongly agreed that all balance sheet line items should be disclosed by segment regardless of whether they were allocated to the segment and reported to the CODM.

- **Disclosures**—Although all segment information is a disclosure, we queried investors’ satisfaction with, as well as the desired improvements needed in, the specific elements of disclosure. Improvement in disclosures is touched upon in several questions. The concepts of aggregation and disaggregation were queried broadly in the questions represented in Exhibit 7 and Table 1 as well as in the questions and responses displayed in Exhibits 13 through 17 related to the requirements in Topic 280. We discuss both items under the captions of aggregation and disaggregation that follow, but it is important to distinguish aggregation/disaggregation in financial statements captions from principles of aggregation/disaggregation used in the determination of reportable segments. This is a challenging difference to discern and communicate to investors, given that ultimately, the determination of reportable segments has, to some degree, a bearing on the aggregation/disaggregation in financial statements captions. As we prepared and evaluated the survey results, we found this an important distinction in the discussion with investors. The terms aggregation/disaggregation are used as a “term of art” when discussing the segment reporting (Topic 280) requirements and then used more broadly in gauging sentiment regarding sufficiency of detail with investors.

With regard to specific disclosures related to the balance sheet and statement of cash flows, as well as specific elements of disclosure, we describe our findings below:

- **Balance sheet**—As noted above under the section “Presentation,” when we asked respondents about whether segment disclosures should include a disclosure presenting all balance items, a majority of respondents, 53.5%, (Exhibit 20) agreed or strongly agreed that all balance sheet line items should be disclosed by segment regardless of whether they were allocated to the segment and reported to the CODM. We then queried respondents’ interest in specific balance sheet elements, as can be seen in Exhibit 21 and Table 2. Although all items were supported in the majority—consistent with the findings in Exhibit 20, somewhat surprisingly, the disclosure of cash, 58.3%, was not considered as important as the other disclosure elements, particularly total assets, which was considered the most important to include. Overall, liability disclosures (64.5% to 69.4%) were perceived as more

important than asset disclosures (58.3% to 73.4%) other than total assets (80.4%).

- Statement of cash flows—As can be seen in Exhibit 21 and Table 3, improvements in cash flow disclosures by segment were considered the most important (all were over 75% supported), with 93.9% of respondents indicating that the operating cash flow disclosures were important to include, followed by investing cash flows at 84.5%. This is not surprising given the desire to understand the operating and investing activities of the segments being valued.
- Other disclosures—Respondents noted in Exhibit 21 and Table 1 that they did not believe disclosures regarding segment allocations were sufficient (74.1%) and that segment disclosures could be improved (80.4%) by providing additional disclosures related to capital expenditures, depreciation and amortization, and goodwill. As noted in Exhibit 22 and Table 4, there was very strong support (72%–75%) for enhancements to geographic disclosures as well as improvements in what companies include in other segments versus corporate and other and what is included in corporate and other. Respondents also strongly supported improvements in disclosures regarding allocations (73.4%). They most strongly supported (81.1%) improvements in disclosures related to changes in segment measures of profitability. Surprisingly, although there was majority support (60.2%) for the inclusion of all segment information quarterly, it was less strongly supported than the aforementioned measures. As we note in the detailed discussion, this is due to very low support (30%) in the Europe, Middle East, and Africa (EMEA) region where quarterly reporting is less common. Other regions supported the improvements by approximately 70%.
- **Segment standard requirements**—We queried our members on specific elements of the segment disclosures requirements from Topic 280 to be able to provide a direct connection between respondent views and the elements of the accounting standard that the FASB is currently reconsidering. Our findings were as follows:
 - Management approach—Respondents agreed (40.1%) or strongly agreed (16.7%) with retaining the management approach—a slight majority at 56.8% in the aggregate (see Exhibit 8).
 - Definition of an operating segment:
 - CODM—We queried respondents on whether the current definition of chief operating decision maker was sufficient. Only 38.3% (Exhibit 11) thought no improvement was needed. The majority of respondents (61.7%) believed a change was necessary but differed in why or how a change was needed. Substantively, all improvements were related to lowering the level of the decision-making or tying it more directly to compensation.
 - Revenues and expenses—The current requirement is that an operating segment should include both revenues and expenses, with 48.3% of respondents—a

significant minority—agreeing with this definition (Exhibit 10). Few respondents believed a segment should only incur revenues or only incur expenses. A significant minority of respondents (30.7%) stated that they believe an operating segment can either earn revenues or incur expenses but does not have to do both. Overall, 50.2% of respondents believe that just earning revenues is sufficient to classify something as an operating segment.

- Discrete financial information—When asked about the definition of discrete financial information, respondents, over 60% believed that discrete financial information should include information provided to analysts and/or including non-GAAP measures (see Exhibit 12).
- Aggregation and disaggregation—As noted above under “Disclosures,” many of the questions related to disclosures are connected to the issue of aggregation and disaggregation. As we note previously, as we prepared and evaluated the survey results, we found this an important distinction in the discussion with investors. The terms aggregation/disaggregation are used as a “term of art” when discussing the segment reporting (Topic 280 requirements) and then used more broadly in gauging sentiment regarding sufficiency of detail with investors. The concepts of aggregation and disaggregation were queried broadly in the questions represented in Exhibit 7 and Table 1 as well as in the questions and responses displayed in Exhibits 13 through 17 related specifically to the requirements in Topic 280.

As noted in Table 1 and Exhibit 7, we queried satisfaction with elements of disaggregation related to income statement, balance sheet, and cash flow items, as well as items included within “other.” Overall, there was a view that disaggregation could be improved, which is why we also queried what specific elements of financial statements could be improved upon (68.5% to 80.6%). Our findings regarding general sentiments in Table 1 and Exhibit 7 are consistent with the results regarding the detailed improvements queried later.

As a part of these questions, we asked whether investors thought segments seemed to be aggregated (e.g., Topic 280 segment requirements) based upon dissimilar characteristics or whether the disaggregation was, in their view, sufficient for management to make resource allocations. Respondents did not feel as strongly (47.1% to 49.0%) that there were deficiencies in this area, but when asked about disclosure improvements to enhance transparency in these elements they viewed these as important. This may be suggestive of differences in satisfaction with aggregation/disaggregation in determination of segments—something which is less visible—than in satisfaction with the disaggregation provided once a determination of segments has been made.

Our findings related to aggregation and disaggregation as it relates to the principles within the accounting standard are as follows:

- Aggregation of operating segments to reportable segments—A majority of respondents (57.1%) agreed that companies should be able to aggregate operating segments into reportable segments. That said, they noted that additional information should be provided on such aggregation (e.g., number of segments, operating margin, range of revenues) (see Exhibit 13).
- Qualitative aggregation criteria—We asked respondents whether the current qualitative criteria for aggregating operating segments into reportable segments could be improved, asking them to check all the responses they thought were applicable. The most common response (63.5%) was the need to define more precisely the similar economic characteristics upon which segments may be aggregated, including a discussion of gross margins, sales growth, and operating margins. In a similar vein, the second most common response (40.4%) of respondents related to defining the “similar economic characteristics” that form the basis of aggregation in quantitative terms. Overall, better definitions with quantitative criteria seemed to be the improvement that standard-setters could make in terms of improving aggregation criteria (see Exhibit 14).
- Disaggregation: quantitative criteria—After aggregating by qualitative criteria, segment guidance requires that companies ascertain whether certain quantitative criteria have been met such that certain operating segments are disaggregated into reportable segments. There was little support, 16.0% (Exhibit 15), for removal of the quantitative criteria—consistent with the findings above to define aggregation criteria quantitatively. Of the respondents, 37.1% said no improvement was needed, while 31.4% supported reducing the threshold to 5% and 26.9% supported separate identification of the segments identified by management as growth areas. Overall, more saw the need for change than retaining the status quo.
- Quantitative versus qualitative aggregation criteria—Overall, 51.7% of respondents thought that applying the quantitative test first was a preferred solution, while 13.6% felt eliminating the qualitative aggregation criteria entirely was the best answer. Overall, 68.7% of respondents noted that some sort of change was necessary and that quantitative criteria had primacy (see Exhibit 16).
- Aggregation: minimum amount of revenue reported—We asked respondents whether the current requirement to disclose operating segments comprising 75% of revenue could be improved. Exhibit 17 shows that 37.7% of respondents indicated the threshold should be increased from 75% to 80%–90%, and 12.0% felt that adding a minimum net income requirement might be helpful. Of the respondents, 26.9% felt that no improvement was needed and, surprisingly, 25.7% felt that eliminating the requirement to disclose a minimum amount of revenue was the best response.

There are regional variations in the responses to each of the survey questions. We describe, or illustrate through regional charts, these regional differences in the detailed sections that follow. Broadly, respondents in the Americas region were closest to the overall averages noted above, while those in the Asia Pacific region more strongly favored improvements—particularly as it related to disaggregation and limiting management choice. Those in the EMEA region less strongly favored limiting management choice and were less strong—but most times, still in a majority—in making improvements to the disclosures in areas such as disaggregation. That said, the regional results should be evaluated by question.

SURVEY QUESTIONS AND FINDINGS

We sought to gain a general sense of how important and satisfied respondents were with the current state of segment disclosures. Accordingly, we asked several questions that were not directly tied to the manner in which segments are determined under the accounting guidance. This survey was also quite technical, longer, and more complex than we would normally ask our members to complete. The survey had 22 questions, and three questions had multiple parts, which provided us with 54 data points. The survey took respondents nearly 25 minutes to complete—longer than we had anticipated in the invitation to participate. We had approximately 225 respondents, a number that varied by question. We are appreciative to the members who took the time to complete the survey, demonstrating their commitment to helping us to improve segment disclosures on behalf of investors. See the About the Survey section for more details on the job description, region, and years in industry of respondents.

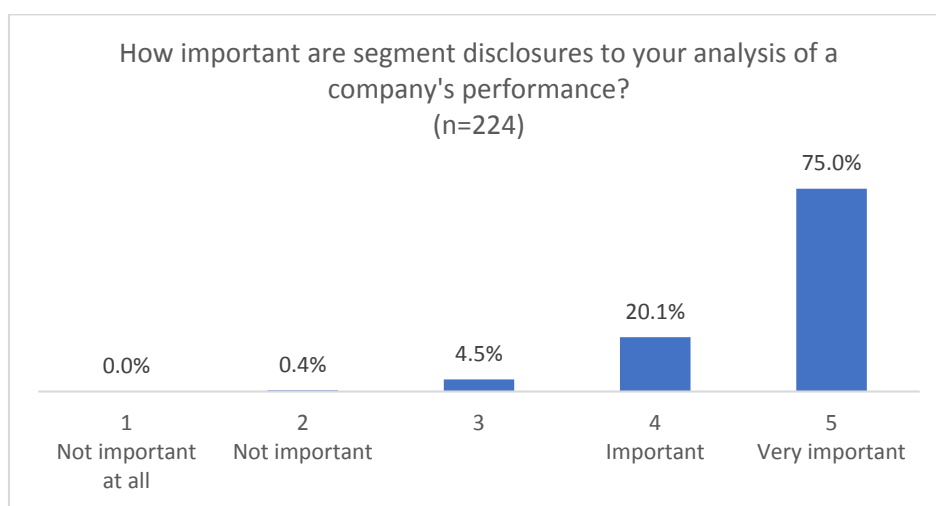
In addition to analyzing the overall survey results, we considered the responses by region. In the sections that follow, we highlight regional differences in descriptions below the exhibits presenting the overall results. Where the regional differences are more pronounced, or more challenging to describe, we have included additional charts that illustrate the regional differences.

GENERAL OBSERVATIONS

Importance of Segment Disclosures

We commenced our survey with two questions aimed at gaining a sense as to the importance of segment disclosures to CFA Institute members who are analysts and portfolio managers. **Exhibit 1** highlights that 75.0% of respondents view segments disclosures as very important with 20.1% viewing them as important. In total, 95.1% of respondents viewed segment disclosures as important. No respondents noted the disclosures were not important.

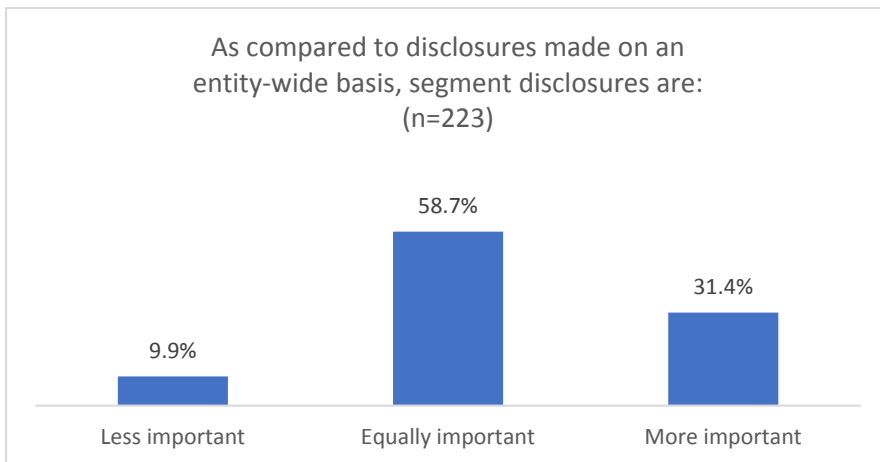
Exhibit 1: Importance of Segment Disclosures



Regionally, the results were similar with the exception of the Asia-Pacific (APAC) region where a higher percentage (80%) of respondents rated segment disclosures as very important rather than important.

We queried whether respondents perceived segment disclosures to be less, equally, or more important than entity-wide disclosures. **Exhibit 2** shows that 31.4% of respondents believe segment disclosures are more important than entity-wide disclosures, and 58.7% viewed segment disclosures as important as entity-wide disclosures. Overall, 90.1% of respondents viewed segment disclosures as at least as important as entity-wide disclosures. This is an important finding for standard-setters. As the FASB considers improvements to segment disclosures, the relative importance of segment disclosures to entity-wide results and disclosures should be a significant consideration. These are not just another set of disclosures, but disclosures that directly facilitate analysis and valuation.

Exhibit 2: Importance of Segment Disclosures Relative to Entity-Wide Disclosures

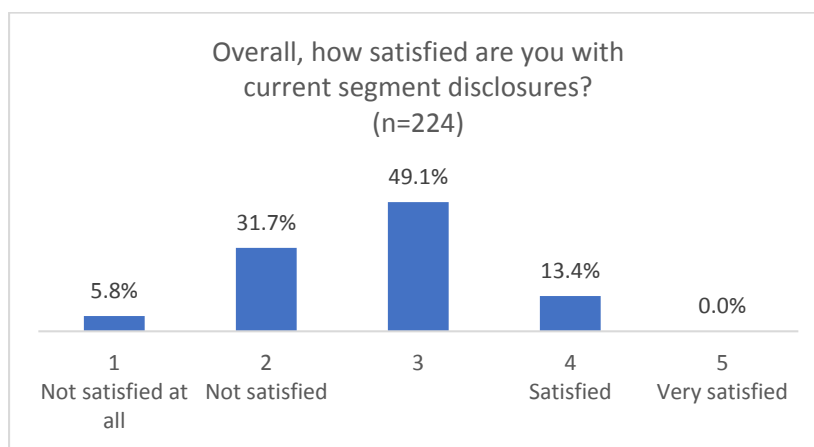


Regionally, the results were similar with the exception of the APAC region, where a higher percentage (63%) of respondents rated segment disclosures as equally important rather than more important, than entity-wide disclosures.

Satisfaction

We then queried our members’ satisfaction with current segment disclosures (**Exhibit 3**). The response was distributed significantly more toward the dissatisfied than satisfied spectrum of responses with no respondents indicating they were very satisfied with the disclosures. Only 13.4% of respondents were satisfied with segment disclosures. In contrast, 5.8% of respondents were very dissatisfied and 31.7% were dissatisfied with the segment disclosures. That is 13.4% on the satisfied end of the spectrum and 37.3% on the dissatisfied spectrum, with 49.1% having a neutral view on their satisfaction with the disclosures. Superimposing satisfaction with the disclosures (13.4%; Exhibit 3) on top of their importance (95.1%; Exhibit 1), there is substantial room for improvement in segment disclosures that investors view as particularly important.

Exhibit 3: Satisfaction with Segment Disclosures



Regionally, the results were similar with the exception of the EMEA region where respondent were substantially (approximately 10%) more dissatisfied with segment disclosures.

Critical Audit Matter

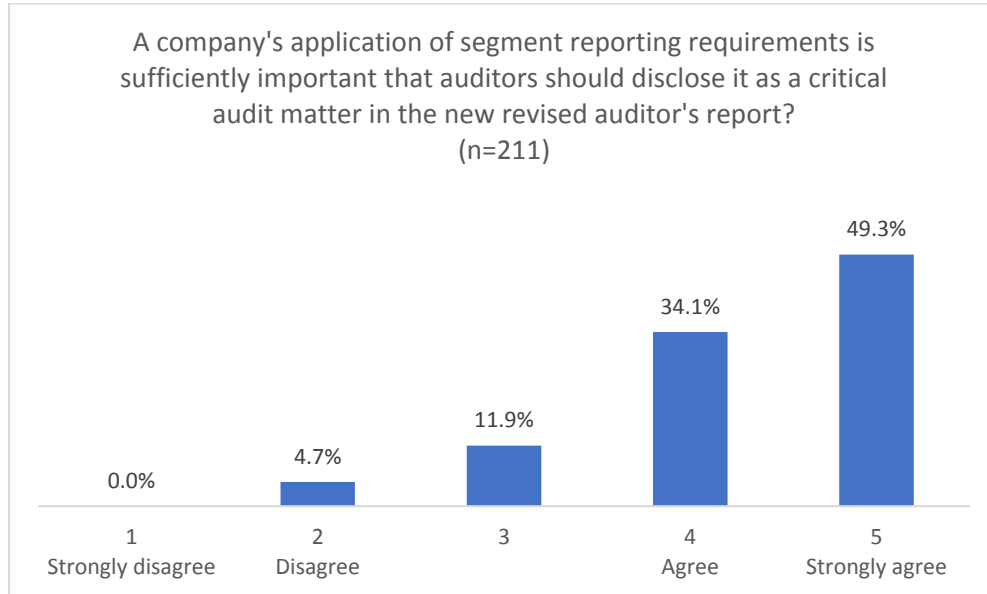
Beginning in 2019, auditors of US public companies will be required to provide a discussion of critical audit matters (CAMs)⁵ in their opinion on the financial statements. Many auditors think of these CAMs similar to critical estimates and have not necessarily considered how management has communicated segment results as a CAM. This decision is, however, a very important judgment and decision for management because they understand its importance to investors. Although this is a consideration of the auditors, it generally is not something that is always deeply analyzed—unless segments have changed. Because businesses can change without segments changing, this is something the auditors should always consider. With segment disclosures being seen by investors as equivalent in importance to that of entity-wide results, this is likely something the auditors should more closely consider as they prepare their CAM disclosures because it a key decision. Auditors are in a unique position to evaluate the internal systems; the reporting package received by management, the chief operating decision maker, and the board; and to ascertain if the external communications align with the internal narrative regarding results. Investors may question why auditors have or have not commented on segment disclosures in the auditor's report should the SEC ask questions regarding how these decisions are being made by management.

Respondents to our survey overwhelmingly agreed (83.4%; **Exhibit 4**) that the new auditor's report should disclose what they have done to evaluate management's segment decision—as either important (34.1%) or very important (49.3%; Exhibit 4).

⁵The PCAOB Standard "The Auditor's Report on an Audit of Financial Statements When the Auditor Expresses an Unqualified Opinion and Related Amendments to PCAOB Standards," includes the following definition of a critical audit matter:

The repropoed standard defined a critical audit matter as any matter arising from the audit of the financial statements that was *communicated or required to be communicated to the audit committee* and that *relates to accounts or disclosures that are material to the financial statements and involved especially challenging, subjective, or complex auditor judgment*. For the reasons explained below, the Board is adopting the definition as repropoed.

Exhibit 4: Segments as Critical Audit Matter

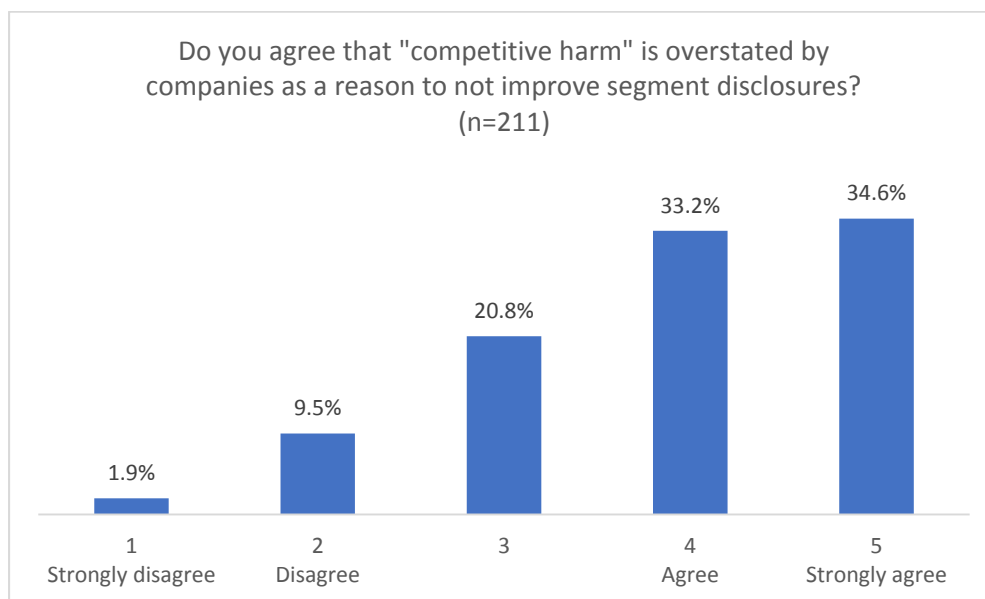


Regionally, the results were very similar with the exception of the EMEA region where there was a slight difference (5%) in the level of strong agreement with the inclusion of segments as a CAM. Respondents from the APAC and Americas regions more strongly agreed with segments being included as a CAM, while those from EMEA were slightly more neutral.

Competitive Harm

Many times, companies have more detailed segment information—especially given the aforementioned changes in technology—but do not want to disclose it, stating competitive harm as a reason (e.g., as can be seen from the aforementioned Amazon and Google examples). We asked respondents whether they—as investors who would bear the brunt of any competitive harm—believe this reason for not improving segment disclosures was overstated. Respondents agreed or strongly agreed (67.8%; **Exhibit 5**) with this statement, with only 11.4% of respondents disagreeing or strongly disagreeing with the statement.

Exhibit 5: Competitive Harm



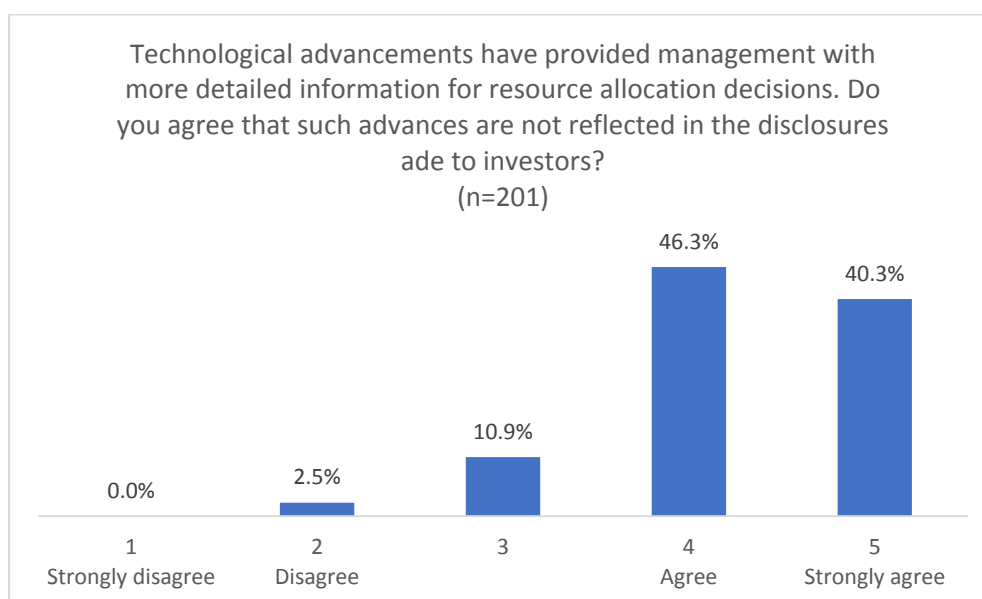
Regionally, respondents in the APAC region were in less agreement (by approximately 7%) that competitive harm was overused as a reason for not improving disclosures than were respondents in the Americas and EMEA regions.

Technology

We then asked respondents whether technological developments and the availability of information to managers have been reflected in improved segment disclosures. There was a resounding agreement (86.6%; **Exhibit 6**) that improvements in disclosures had not resulted from technological advancements.

We queried this issue because we believe policymakers must consider that technology has changed quite substantially since the creation of ASC Topic 280, formerly SFAS No. 131, in 1997. Our view is that the chief operating decision maker has substantially more information, and in a more timely manner, upon which they can make resource allocation decisions than when this standard was created over 20 years ago. The ability to have greater disaggregation of information and better presentation should, in our view, be guided by a significant shift in technology.

Exhibit 6: Technology's Influence on Disclosures



Regionally, the results showed a consistent level of agreement. That said, the respondents in the EMEA region strongly agreed—though they agreed in larger proportion—with the statement less often (by approximately 14%) than did those in the APAC region.

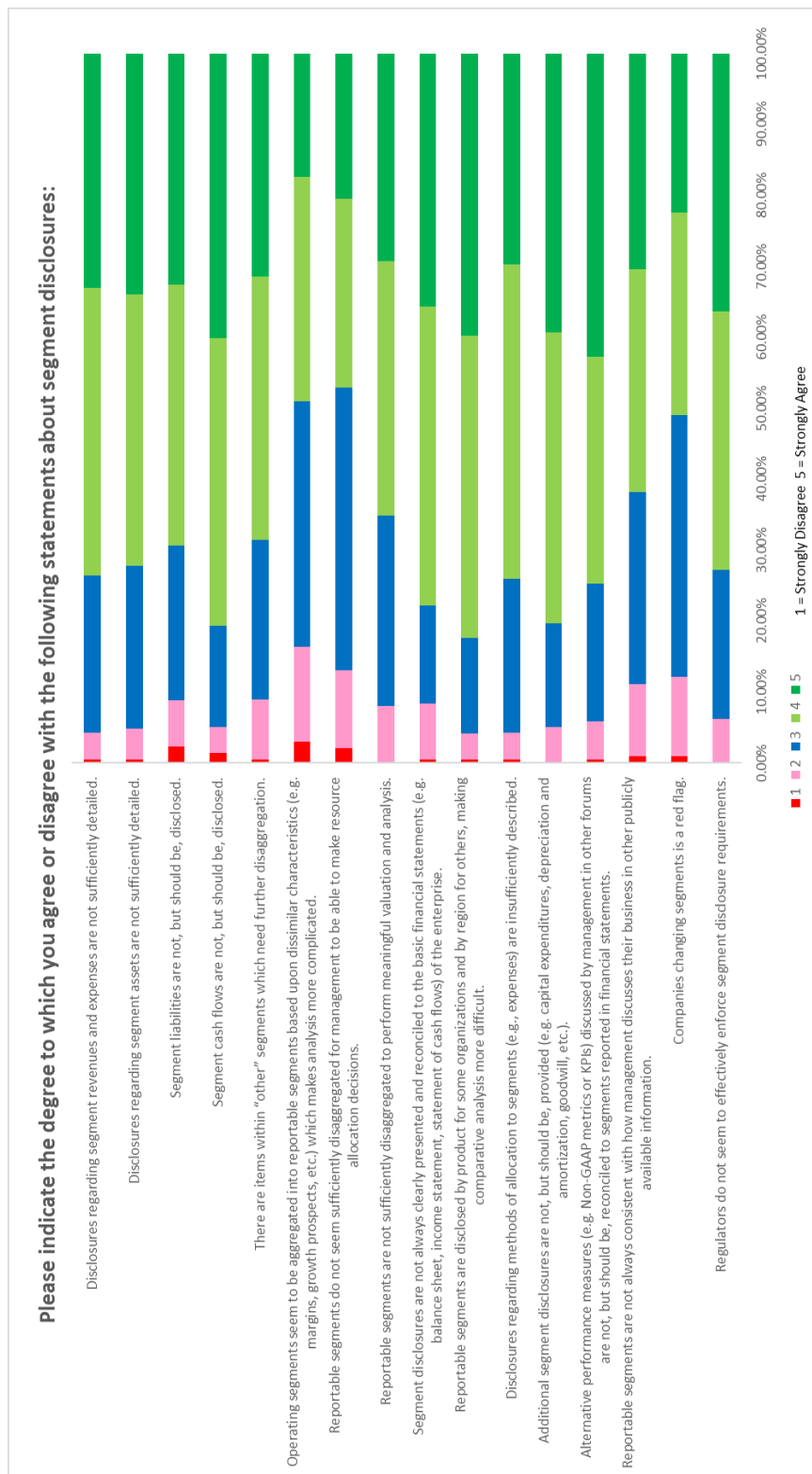
Specific Elements of Disclosures

We asked respondents to assess their agreement or disagreement with a series of 16 statements regarding segment disclosures. As a part of the survey, the statements were randomized. **Table 1** and **Exhibit 7** provide the results, with Table 1 highlighting the percentages visualized in Exhibit 7. Overall, the statements addressed elements of disaggregation, presentation, the need for additional disclosures, segment results relative to management's discussion of results in other venues, and alternative performance measures. Finally, we asked investors to provide their views on enforcement of segment disclosures.

Table 1: Satisfaction with Specific Elements of Disclosure Analysis

QUESTION	DISAGREE & STRONGLY DISAGREE	NEUTRAL	AGREE & STRONGLY AGREE
DISAGGREGATION			
Disclosures regarding segment revenues and expenses are not sufficiently detailed.	4.2%	22.2%	73.6%
Disclosures regarding segment assets are not sufficiently detailed.	4.8%	23.0%	72.2%
Segment liabilities are not, but should be, disclosed.	8.8%	21.9%	69.3%
Segment cash flows are not, but should be, disclosed.	5.1%	14.3%	80.6%
There are items within "other" segments which need further disaggregation.	8.9%	22.5%	68.5%
Reportable segments are not sufficiently disaggregated to perform meaningful valuation and analysis.	8.0%	26.9%	65.1%
Operating segments seem to be aggregated into reportable segments based upon dissimilar characteristics (e.g., margins, growth prospects, etc.) which makes analysis more complicated.	16.3%	34.7%	49.0%
Reportable segments do not seem sufficiently disaggregated for management to be able to make resource allocation decisions.	13.1%	39.8%	47.1%
PRESENTATION			
Segment disclosures are not always clearly presented and reconciled to the basic financial statements (e.g., balance sheet, income statement, statement of cash flows) of the enterprise.	8.3%	13.9%	77.8%
Reportable segments are disclosed by product for some organizations and by region for others, making comparative analysis more difficult.	4.2%	13.4%	82.4%
ADDITIONAL DISCLOSURES			
Disclosures regarding methods of allocation to segments (e.g., expenses) are insufficiently described.	4.2%	21.7%	74.1%
Additional segment disclosures are not, but should be, provided (e.g., capital expenditures, depreciation and amortization, goodwill, etc.).	5.0%	14.6%	80.4%
DISCUSSION OF RESULTS & ALTERNATIVE PERFORMANCE MEASURES			
Alternative performance measures (e.g., Non-GAAP metrics or KPIs) discussed by management in other forums are not, but should be, reconciled to segments reported in financial statements.	5.8%	19.4%	74.8%
Reportable segments are not always consistent with how management discusses their business in other publicly available information.	11.1%	27.1%	61.8%
ENFORCEMENT & SEGMENT CHANGES			
Companies changing segments is a red flag.	12.1%	36.9%	51.0%
Regulators do not seem to effectively enforce segment disclosure requirements.	6.3%	21.0%	72.7%

Exhibit 7: Satisfaction with Specific Elements of Disclosures



Disaggregation

Seeking to elicit respondent views on the sufficiency of disaggregation with segment disclosures, we queried the need for improvement in the area of revenue and expense, assets, liabilities, and cash flow disclosures. We found that respondents saw the need for improvement, especially in the area of disclosures related to presentation of segment cash flows, with 80.6% of respondents agreeing or strongly agreeing that such disclosures needed to be improved, followed by revenues and expenses (73.6%), assets (72.2%), and liabilities (69.3%). Disaggregation of cash flows was one of the areas in greatest need for improvement.

We also found that respondents sought improvement in items categorized within “other,” with 68.5% agreeing or strongly agreeing that there are items within other areas that require greater disaggregation.

Although 65.1% of respondents agreed or strongly agreed that reportable segments are not sufficiently disaggregated to perform meaningful valuation analysis, only 49.0% and 47.1%, respectively, believed that segments were aggregated based upon dissimilar characteristics or that reportable segments did not seem sufficiently disaggregated such that management would not be able to make resource allocation decisions. These figures were likely lower because the respondents were less likely to be able to comment on management’s ability to use the information than their own.

Presentation

When asked about the presentation of segment results, we found that 77.8% of respondents agreed or strongly agreed that segment results are not clearly presented and reconciled to the basic financial statements. Respondents agreed or strongly agreed (82.4%) that the option to present segment results by product/service or by region made comparison difficult. This question had the second-highest percentage of strong agreement after operating cash flows at 39.8%.

Additional Disclosures

Allocation Methods

We then asked respondents their views on whether the description of methods to allocate amounts to segments was sufficient. Respondents agreed or strongly agreed (74.1%) that allocation methods were insufficiently described.

Capital Expenditures, Depreciation, Amortization, and Goodwill

Respondents agreed or strongly agreed (80.4%) that additional disclosures such as capital expenditures, depreciation, amortization, and goodwill should be provided.

Discussion of Results and Alternative Performance Measures

We queried investors and members regarding whether segment results were consistent with how management discusses the business in other publicly venues and with the use of alternative performance measures. Respondents agreed or strongly agreed, 74.8%, that alternative performance measures (APMs) discussed by management should be, but are not, reconciled to segments reported in the financial statements. Respondents agreed or strongly agreed (61.8%) that there was a lack of consistency with the segment disclosures and how management discusses the business in other publicly available information.

Enforcement and Segment Changes

Respondents were fairly evenly split on whether a company changing segments is a red flag, with only 51.0% agreeing or strongly agreeing that such a change was a red flag. Of the respondents, 36.9% were neutral on the question. Possibly, the question should have been rephrased to indicate “frequent changes in segments” rather than simply “changing segments” because many investors perceive a frequent change in segments as a red flag, while a change in segment can simply be reflective of a change in the business. This is something we will validate via direct outreach. Interestingly, there was a significant regional difference in the response to this question, with 62% of EMEA region respondents, 51% of APAC region respondents, and only 46% of Americas region respondents indicating that a change in segments is a red flag. Only 16% strongly agreed that this was a red flag in the Americas region, which was half the percentage of that in EMEA and nearly half of that in the APAC region. There were clearly different views on this by region. Respondents noted:

- *Stipulate much stricter conditions around changes to reporting segments to significantly reduce the frequency with which these occur (should really never be more than once in a decade, unless a major acquisition or disposal is undertaken).*
- *Provide more historical data when segments are redefined.*

There was, however, strong sentiment that regulators could do more to improve enforcement of segment disclosure requirements, with 72.7% agreeing or strongly agreeing that regulators do not seem to enforce segment disclosures effectively.

Regional differences were most pronounced, as described in **Table 1A**.

Table 1A: Satisfaction with Specific Elements of Disclosure Analysis by Region

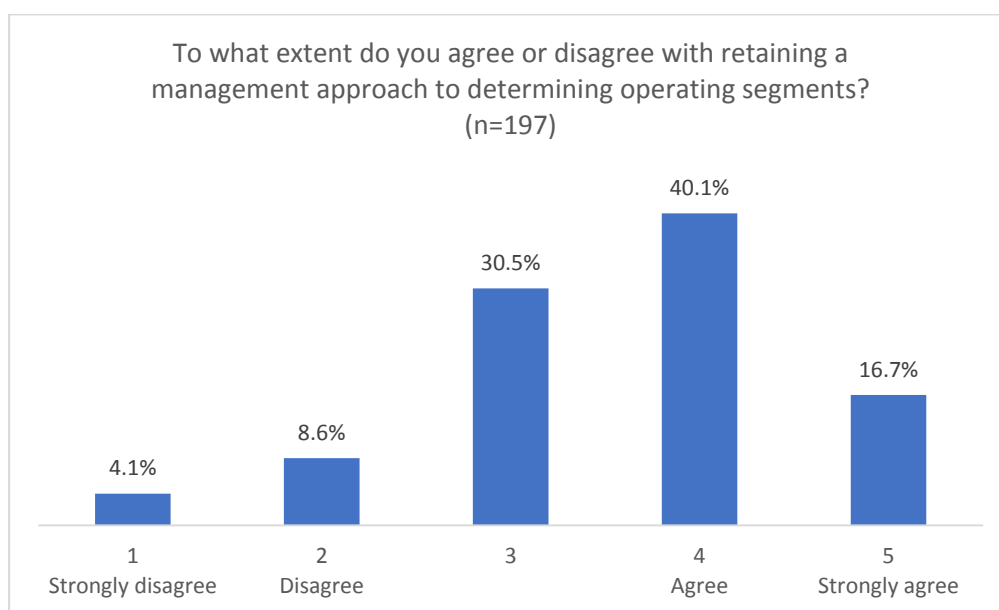
QUESTION	REGIONAL VARIATIONS
DISAGGREGATION	
Disclosures regarding segment revenues and expenses are not sufficiently detailed.	The regional differences in the disaggregation of the basic financial statement elements did not differ substantially other than in the desire for greater disaggregation of cash flows and in liabilities. Respondents in APAC felt less strongly, by approximately 10%, that cash flows should be more disaggregated and EMEA respondents felt less strongly, by approximately 10%, that there was a need for greater disaggregation of liabilities.
Disclosures regarding segment assets are not sufficiently detailed.	
Segment liabilities are not, but should be, disclosed.	
Segment cash flows are not, but should be, disclosed.	
There are items within "other" segments which need further disaggregation.	Respondents in APAC viewed the need for greater disaggregation of "other segments" as more important, by nearly 10%, than did respondents in the Americas or EMEA.
Reportable segments are not sufficiently disaggregated to perform meaningful valuation and analysis.	In APAC, respondents, by a margin of approximately 10% to the other regions, believed disaggregation for valuation and analysis and resource allocation were insufficient. Similarly, APAC respondents more strongly agreed, by 17%, that segments were aggregated by dissimilar characteristics.
Operating segments seem to be aggregated into reportable segments based upon dissimilar characteristics (e.g., margins, growth prospects, etc.) which makes analysis more complicated.	
Reportable segments do not seem sufficiently disaggregated for management to be able to make resource allocation decisions.	
PRESENTATION	
Segment disclosures are not always clearly presented and reconciled to the basic financial statements (e.g., balance sheet, income statement, statement of cash flows) of the enterprise.	Respondents in EMEA, by approximately 11%, felt less strongly about this inability to reconcile to the basic financial statements.
Reportable segments are disclosed by product for some organizations and by region for others, making comparative analysis more difficult.	Respondents in EMEA, by approximately 15%, felt less strongly about this lack of comparability.
ADDITIONAL DISCLOSURES	
Disclosures regarding methods of allocation to segments (e.g., expenses) are insufficiently described.	Regionally there were only slight variations with a slightly lower level of agreement, 3-5%, amongst EMEA respondents.
Additional segment disclosures are not, but should be, provided (e.g., capital expenditures, depreciation and amortization, goodwill, etc.).	Regionally, APAC respondents felt more strongly, by nearly 10%, that such disclosures needed to be provided.
DISCUSSION OF RESULTS & ALTERNATIVE PERFORMANCE MEASURES	
Alternative performance measures (e.g., Non-GAAP metrics or KPIs) discussed by management in other forums are not, but should be, reconciled to segments reported in financial statements.	The regional percentages were nearly identical in total with the APAC respondents not strongly agreeing, but agreeing, to the same degree as those in the Americas and EMEA by approximately 10%.
Reportable segments are not always consistent with how management discusses their business in other publicly available information.	APAC respondents more strongly agreed with this statement than did those in EMEA by approximately 10%.
ENFORCEMENT	
Companies changing segments is a red flag.	There was a significant regional difference in the response to this question with 62% of EMEA respondents, 51% of APAC respondents, and only 46% of Americas respondents agreeing that a change in segments is a red flag.
Regulators do not seem to effectively enforce segment disclosure requirements.	There were slight regional variances in this response with EMEA respondents more strongly agreeing, by 8%, as compared to those in the Americas and APAC that enforcement could be improved by regulators.

CONSIDERATION OF SEGMENT DISCLOSURE REQUIREMENTS

Management Approach

We asked respondents whether they agreed with retaining the management approach to determining operating segments. Only 16.7% (**Exhibit 8**) of respondents strongly agreed with this statement, though 40.1% agreed, for a total of 56.8%. That said, only 12.7% of respondents disagreed with retaining the management approach. Overall, it seems there is agreement—although not as strong agreement as with other queries—regarding retaining the management approach.

Exhibit 8: Management Approach



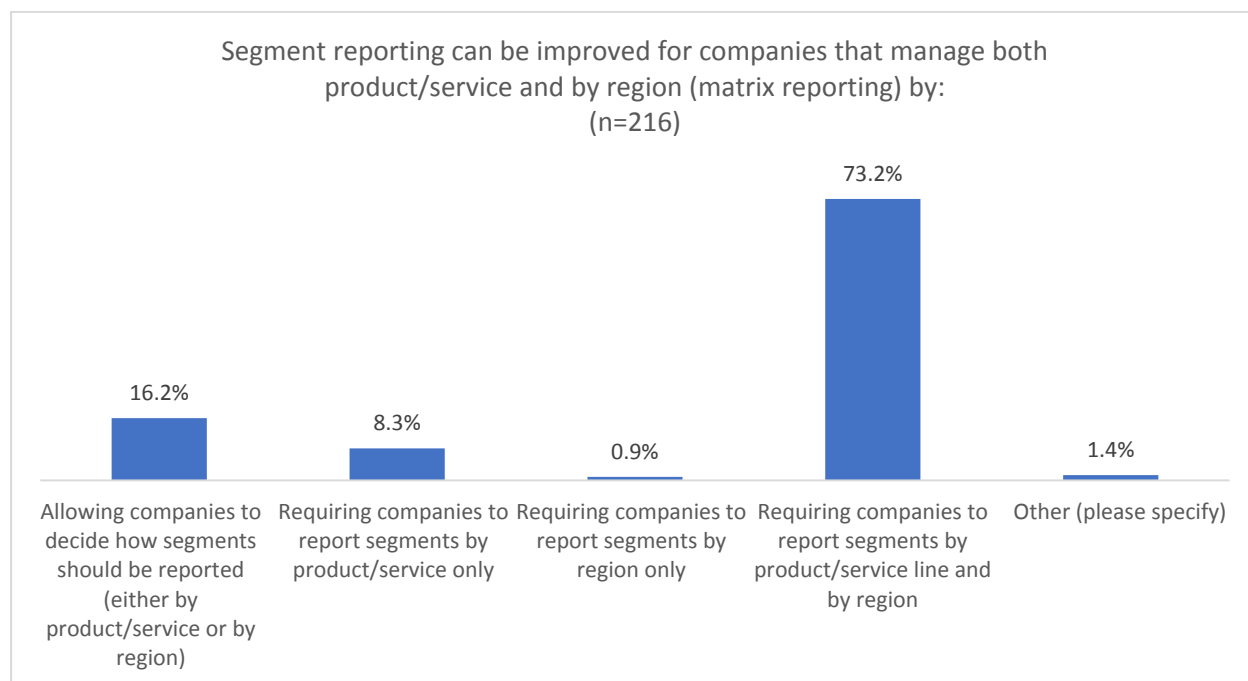
Regionally, respondents in the APAC region agreed more strongly (by nearly 12%) with retaining the management approach.

Presentation: Product/Service versus Region

We asked respondents whether they believed segment results should be presented by product/service or by region. Respondents agreed (73.2%; **Exhibit 9**) that companies should be required to present information by both product/service and region. There was virtually no support for requiring companies to do one or the other, and only minimal support (16.2%) for allowing companies to decide, which is the current approach. Analyzing companies by product/service allows for a better analysis of margins for a company's business, while analyzing regional results allows for better consideration of geographic and demographic trends. Respondents noted:

- *The full matrix should be provided, with any country/product or country/service combination that accounts for 5% or more of the group sales and group EBIT disclosed.*
- *Encouraging companies to report segments by product/service and region...or requiring it subject to exception by application to regulator.*

Exhibit 9: Product/Service vs. Regional Presentation

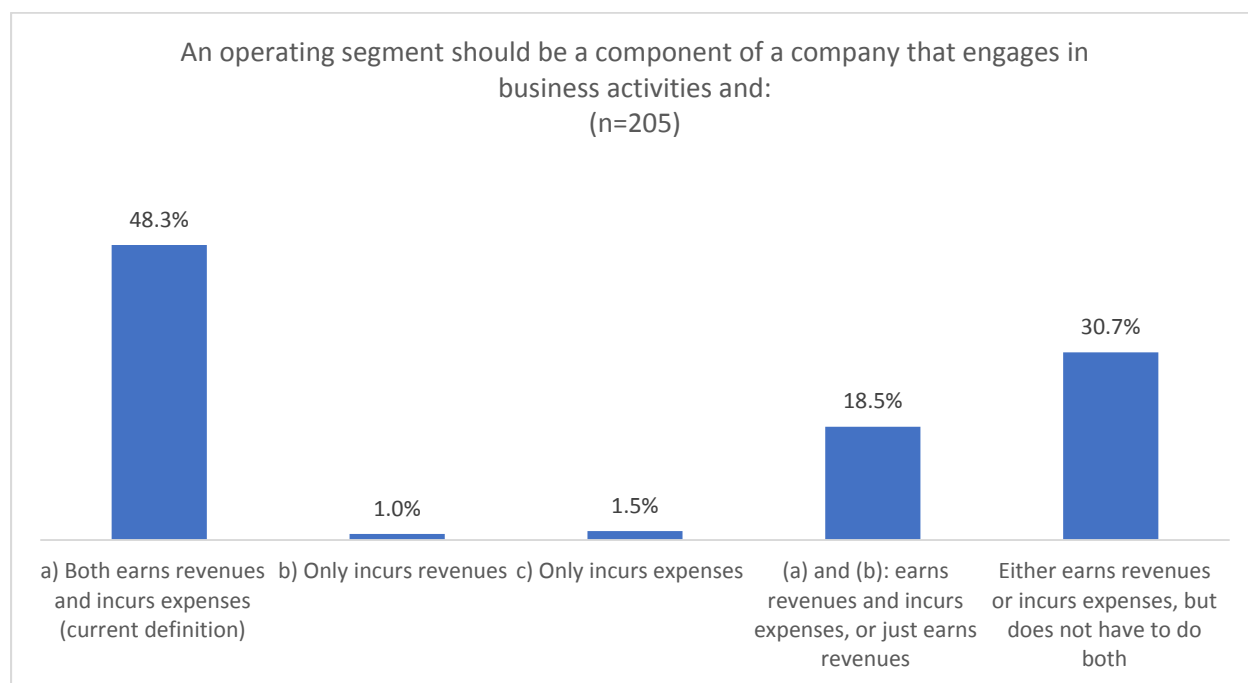


Regionally, 85% of respondents in the APAC region favored requiring disclosure by both product/service and by region over allowing companies to decide how segments should be reported (7%). In the EMEA region, 23% of respondents believed companies should be allowed to decide how segments should be reported, 72% favored requiring both by both product/service and by region, with only 4% of respondents selecting to require disclosure by product/service only.

Operating Segment: Revenues and/or Expenses

We asked respondents whether an operating segment must have both revenues and expenses to be an operating segment. The current requirement is that an operating segment should include both revenues and expenses, with 48.3% (**Exhibit 10**) of respondents agreeing with this definition. Few respondents believed a segment should only incur revenues or only incur expenses. A significant minority of respondents (30.7%) stated that they believe an operating segment can either earn revenues or incur expenses, but does not have to do both. A smaller number of respondents (18.5%) believed that an operating segment earns revenues and incurs expenses or just earns revenues. Overall, 50.2% of respondents believed that just earnings revenues is sufficient to classify something as an operating segment. Only 32.2% of respondents believed that just earning expenses is sufficient for classifying something as an operating segment.

Exhibit 10: Revenues and/or Expenses



Regionally, respondents' choices were very similar, with slightly more individuals in the EMEA region than the APAC region indicating that an operating segment should be defined as earning revenue and incurring expenses or just earn revenues.

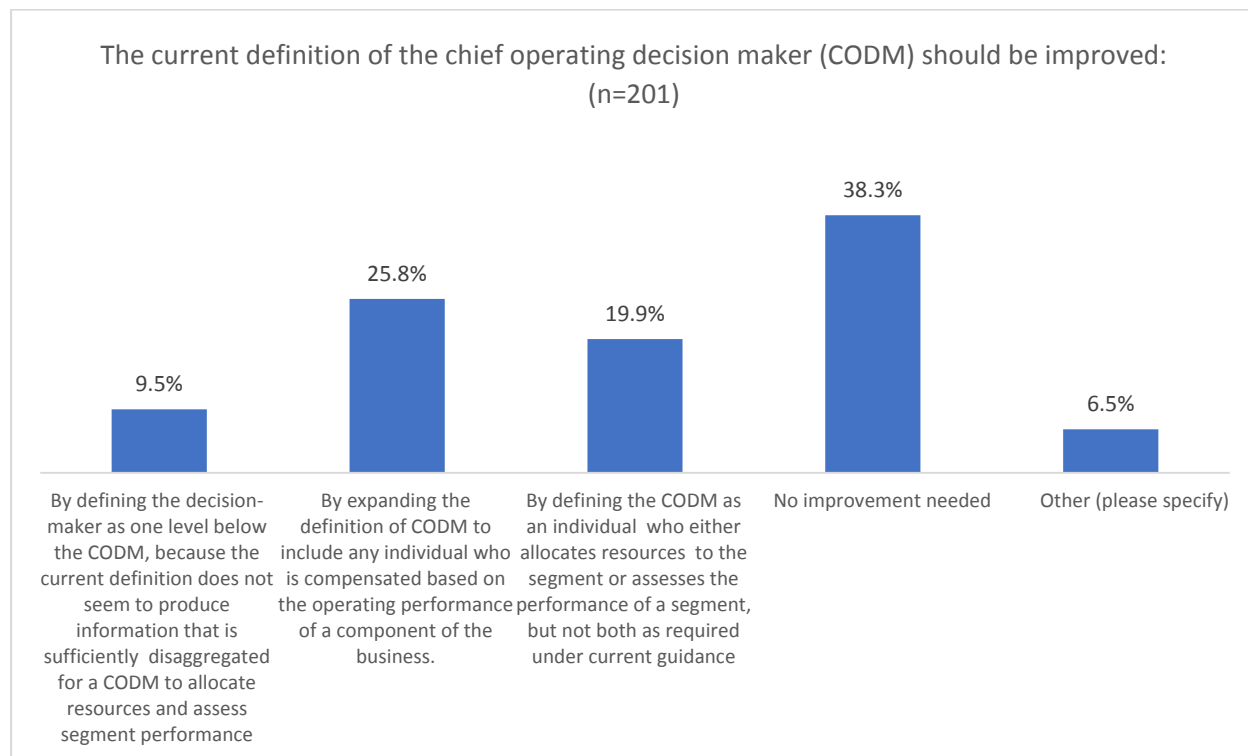
Chief Operating Decision Maker

We queried respondents on whether the current definition of chief operating decision maker was sufficient. Only 38.3% of respondents thought that no improvement was needed (**Exhibit 11**). The majority of respondents (61.7%) believed a change was necessary but differed in why or how a change was needed, as follows:

- 25.8%—definition should include any individual who is compensated based on the performance of the business
- 19.9%—definition should include any individual who allocates resources or assesses performance, but does not have to do both based on existing requirements
- 9.5%—definition should be refined because current disclosures aren't sufficient to allocate resources or assess performance
- 6.5%—most of the respondents responding “other” alluded to a definition that would improve disaggregation or auditing of the information

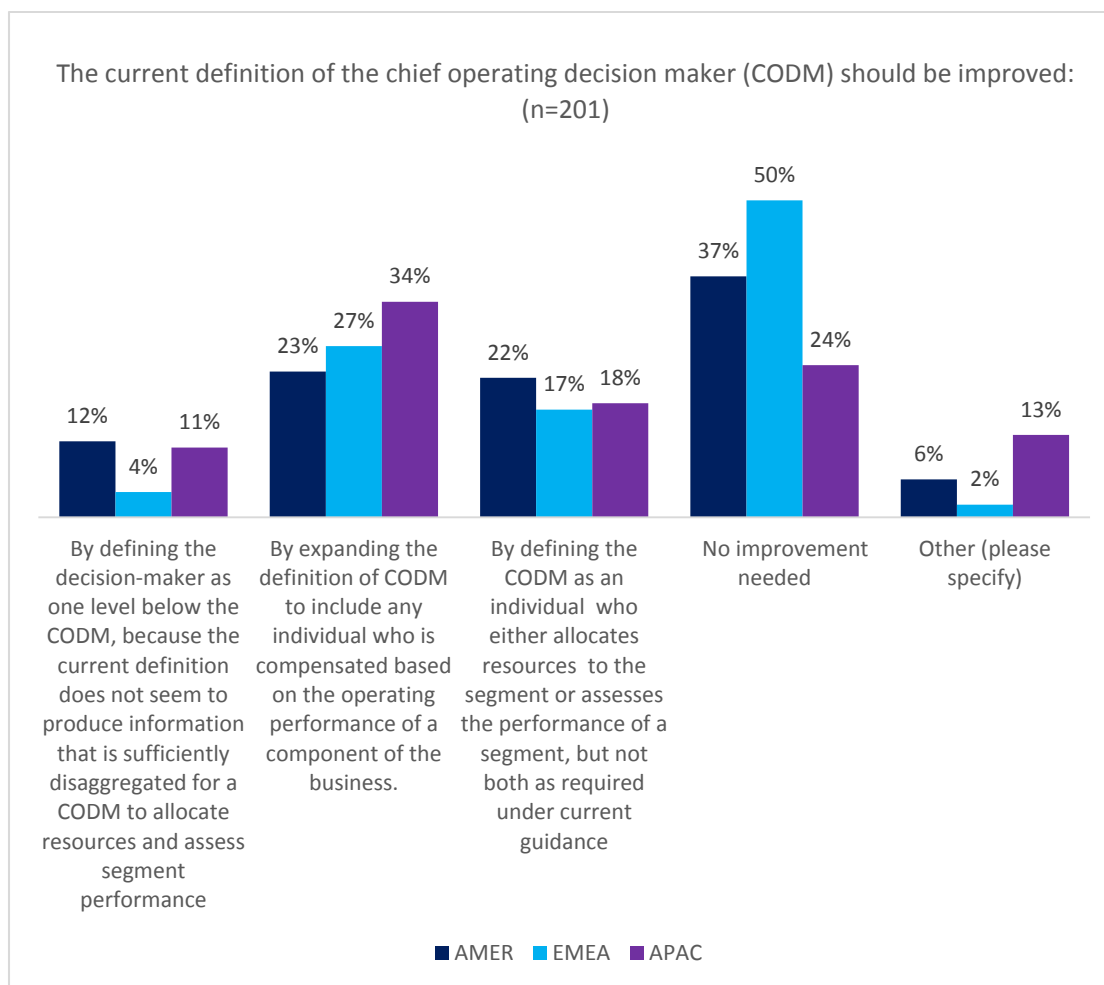
Overall, each of the alternatives for an improved definition of the CODM were about reducing the level in the organization where resource or performance allocation decisions were made—substantively, a disaggregation or more detailed assessment level—or simply increasingly the level of disaggregation.

Exhibit 11: Improvements to CODM Definition



Regionally, respondents saw this issue quite differently, as illustrated in **Exhibit 11A**.

Exhibit 11A: Improvements to CODM Definition by Region

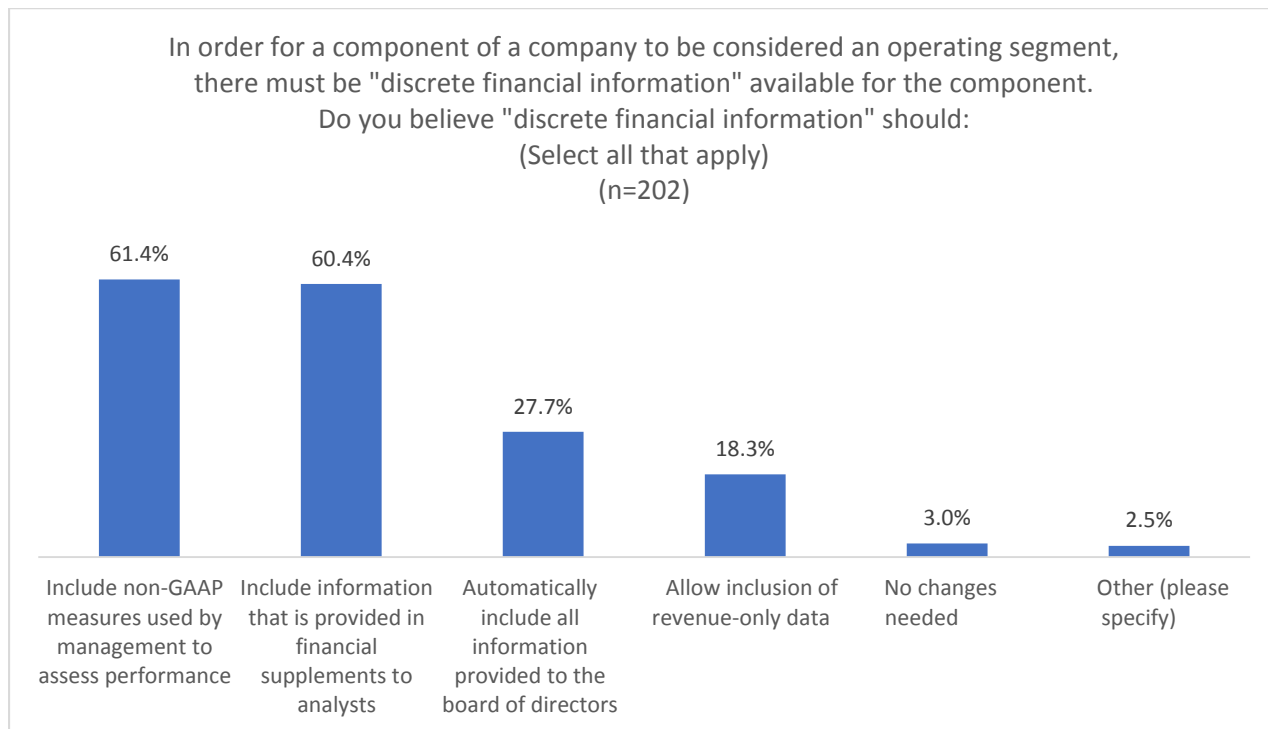


The most distinct difference was that 50% of respondents in the EMEA region indicated that no improvement was needed in the definition of the CODM. They did not respond to the same degree as other regions that responded to reduce the level of the CODM or change the definition to an individual who either allocates or assesses performance, but not both. In the APAC region, the result was much different, with only 24% of respondents indicating that no improvement was needed. These same respondents believed that expanding the definition to include any individual compensated based on the operating performance of the component of the business or some other method was appropriate to a greater degree than did those in the EMEA or the Americas regions.

Discrete Financial Information

We asked respondents whether discrete financial information, used in determining an operating segment, should also include a list of additional information. Respondents were asked to select all that apply. The most commonly occurring responses were related to including information provided to analysts and non-GAAP measures within the definition of discrete financial information (see **Exhibit 12**).

Exhibit 12: Discrete Financial Information

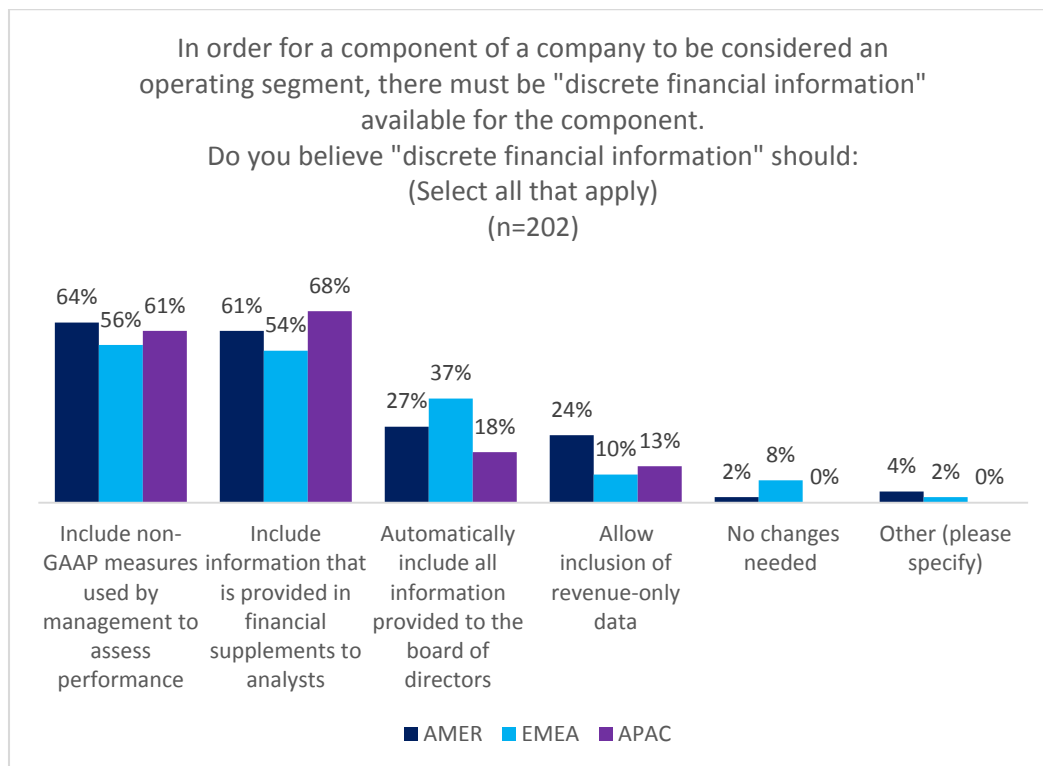


One respondent noted:

- *The definition of discrete financial information should be such that management can't hide behind it as an excuse to aggregate information, when disaggregation would be much more meaningful and useful.*

Regionally, respondents saw this issue quite differently, as illustrated in **Exhibit 12A**.

Exhibit 12A: Discrete Financial Information by Region



Respondents in the APAC region more strongly favored including non-GAAP measures and information provided to analysts in the consideration of what constitutes discrete financial information. Their support for including all information provided to the board of directors was significantly weaker than in other regions, particularly EMEA region respondents who had the opposite view. EMEA region respondents supported information provided to the board of directors over non-GAAP measures and information provided to analysts. In the Americas region, the ability to allow revenue-only data in the determination of segments was significantly more pronounced than in other regions.

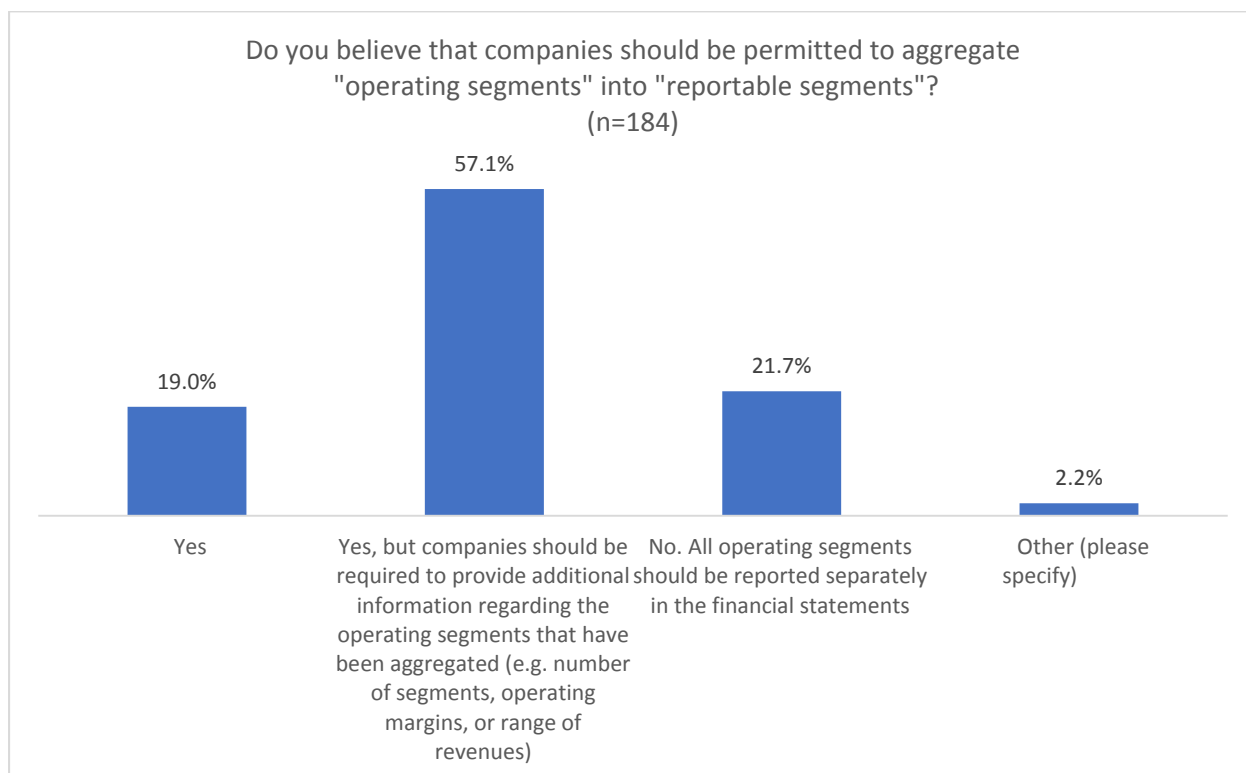
Aggregation: Operating Segments into Reportable Segments

We asked respondents whether companies should be permitted to aggregate reportable segments into operating segments, and found that only 21.7% of respondents said all operating segments should be reportable segments (**Exhibit 13**). Of the respondents, 19.0% agreed to aggregation and the majority (57.1%) agreed to aggregation but only if companies are required to provide additional information such as the number of segments aggregated, their operating margins, and the range of revenue. Respondents noted:

- *Aggregation should be permitted to an extent, but currently companies abuse this, and overaggregate, which is cause of major frustration for investors.*
- *I think there should be some threshold for materiality. Once an operating segment is greater than say 5% of revenue, expenses, EBITDA, EBIT, or net operating assets, it should be reported.*

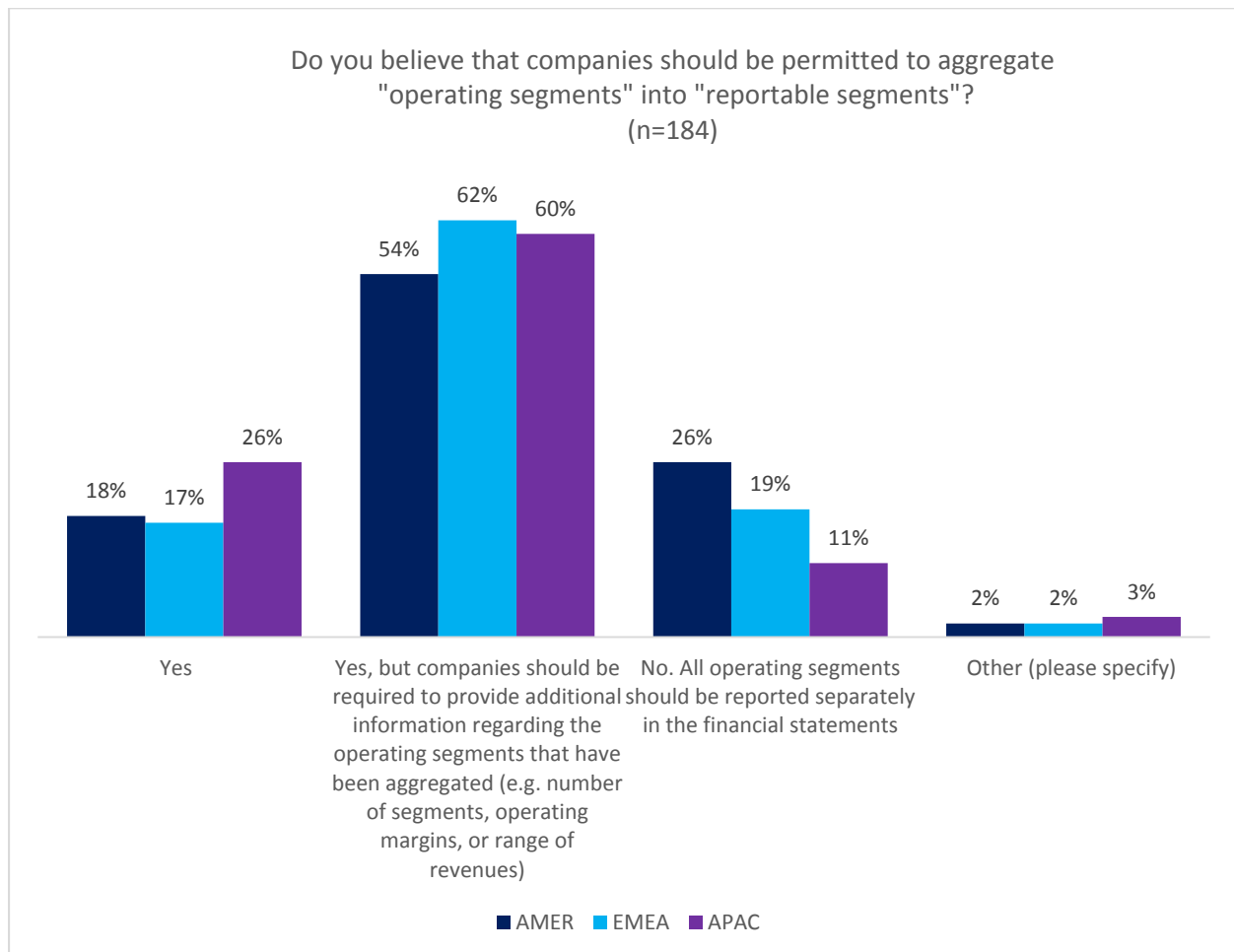
As the FASB evaluates the aggregation criteria, we believe this finding is important information. Investors support aggregation but want additional information on how it is being done.

Exhibit 13: Aggregating Operating Segments into Reportable Segments



Regionally, as noted in **Exhibit 13A**, respondents saw this issue quite differently, with those in the APAC region believing more strongly in the ability to aggregate than those in the Americas region who disagreed (26%) with the concept of aggregation.

Exhibit 13A: Aggregating Operating Segments into Reportable Segments by Region



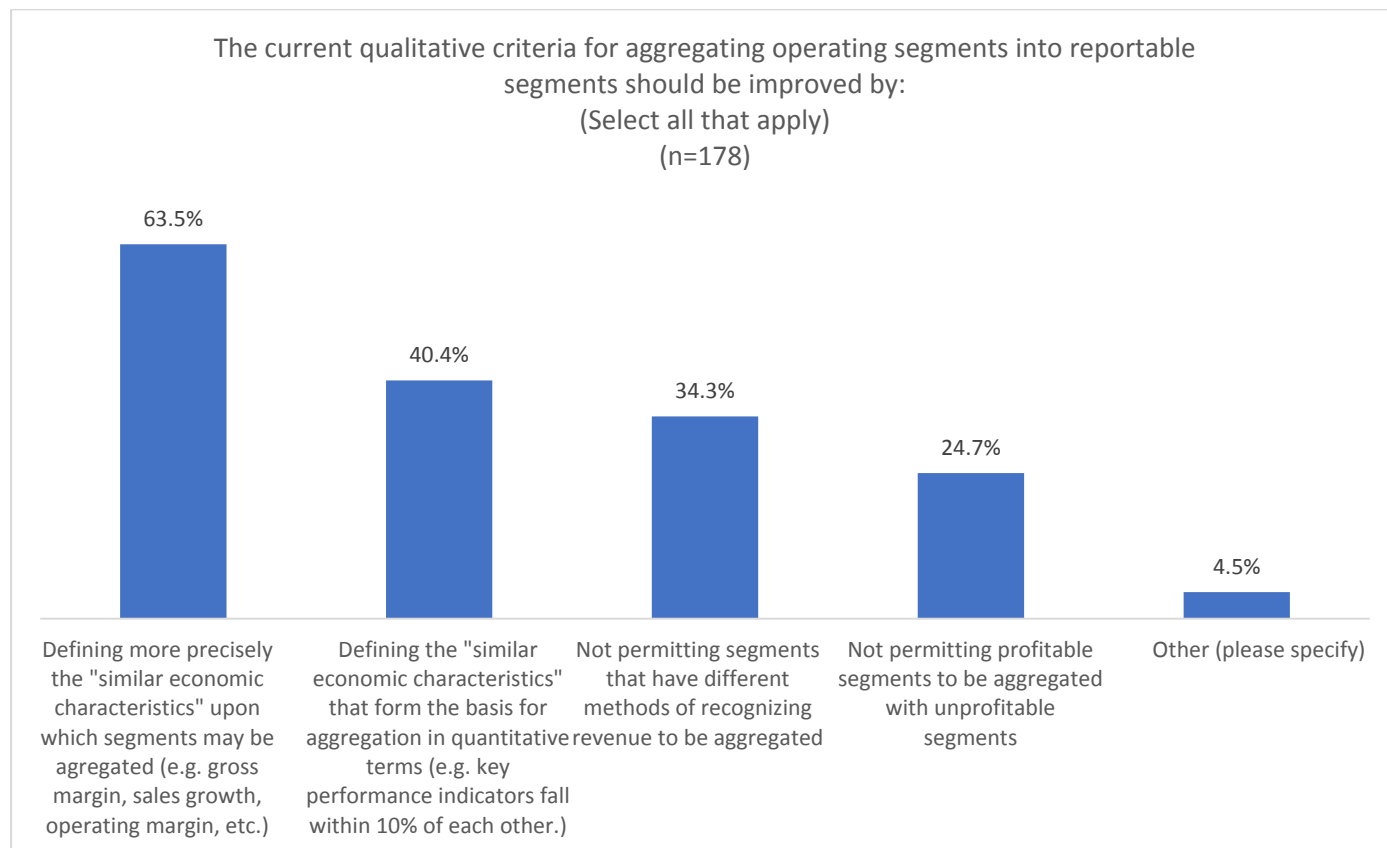
Aggregation: Qualitative Aggregation Criteria

We asked respondents whether the current qualitative criteria for aggregating operating segments into reportable segments could be improved, asking them to check all the responses they thought were applicable. The most common response (63.5%; **Exhibit 14**) was the need to define more precisely the similar economic characteristics upon which segments may be aggregated, including a discussion of gross margins, sales growth, and operating margins. In a similar vein, the second most common response of respondents (40.4%) related to defining the “similar economic characteristics” that form the basis of aggregation in quantitative terms. Overall, better definitions with quantitative criteria seemed to be the improvement that standard-setters could make in terms of improving aggregation criteria.

Also noteworthy was the view that entities should not be permitted to aggregate segments with different methods of recognizing revenue (34.3%) and not permit the aggregation of profitable and unprofitable segments (24.7%). A respondent noted:

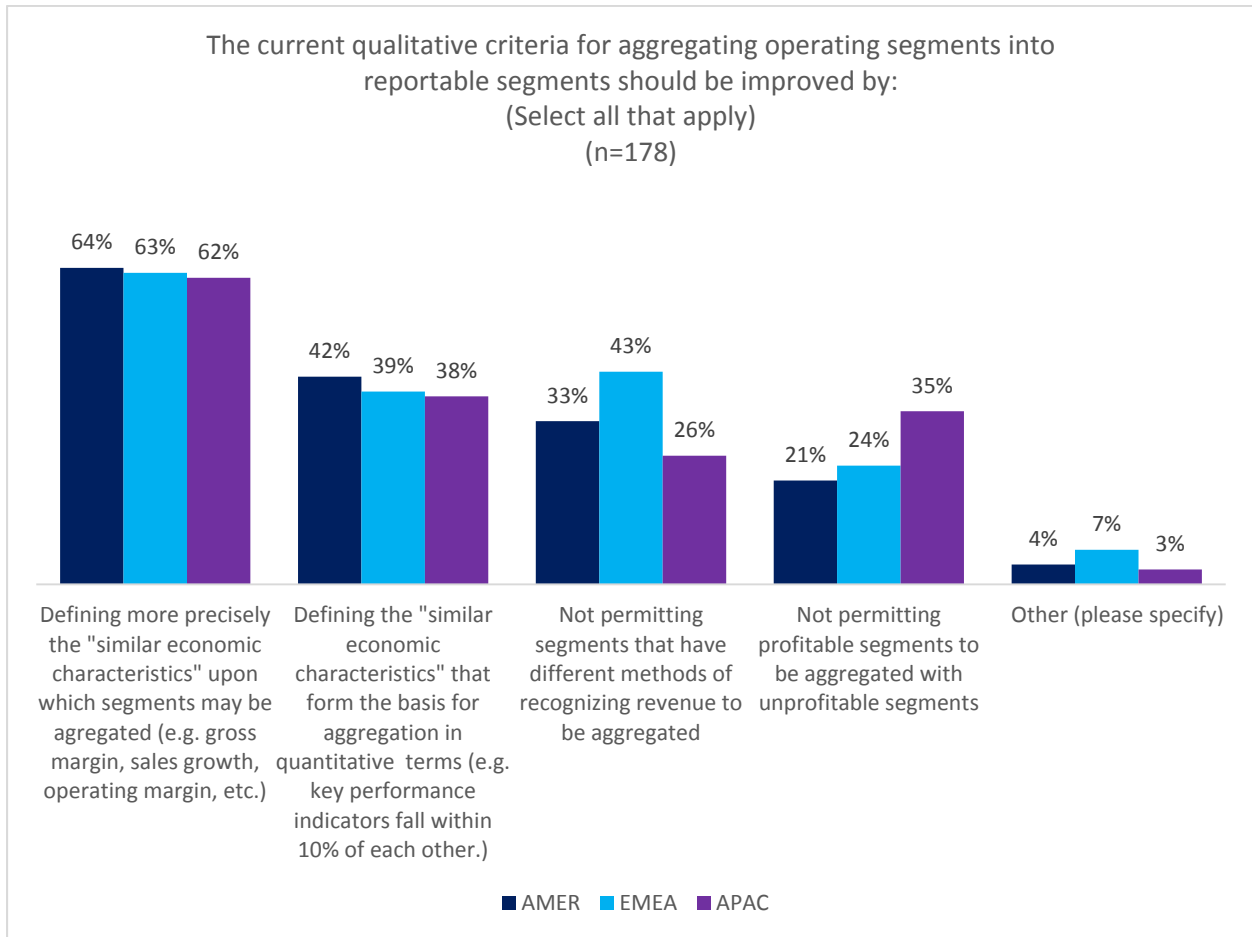
- *I think the qualitative aggregation test is sometimes far too liberally applied....So to summarize, I think there are three tests for aggregation: (1) is the business function sufficiently similar; (2) are the economic attributes sufficiently similar; and (3) is the component which is aggregated into the reportable segment material to the business (i.e., more than 5% of revenue, expenses, EBITDA, EBIT or operating assets).*

Exhibit 14: Qualitative Aggregation Criteria



Regionally, as noted in Exhibit 14A, respondents saw this issue slightly differently, with those in the EMEA region believing more strongly in limiting the ability to aggregate segments with different revenue recognition and those in the APAC region more strongly indicating that profitable and unprofitable segments should not be aggregated.

Exhibit 14A: Qualitative Aggregation Criteria by Region

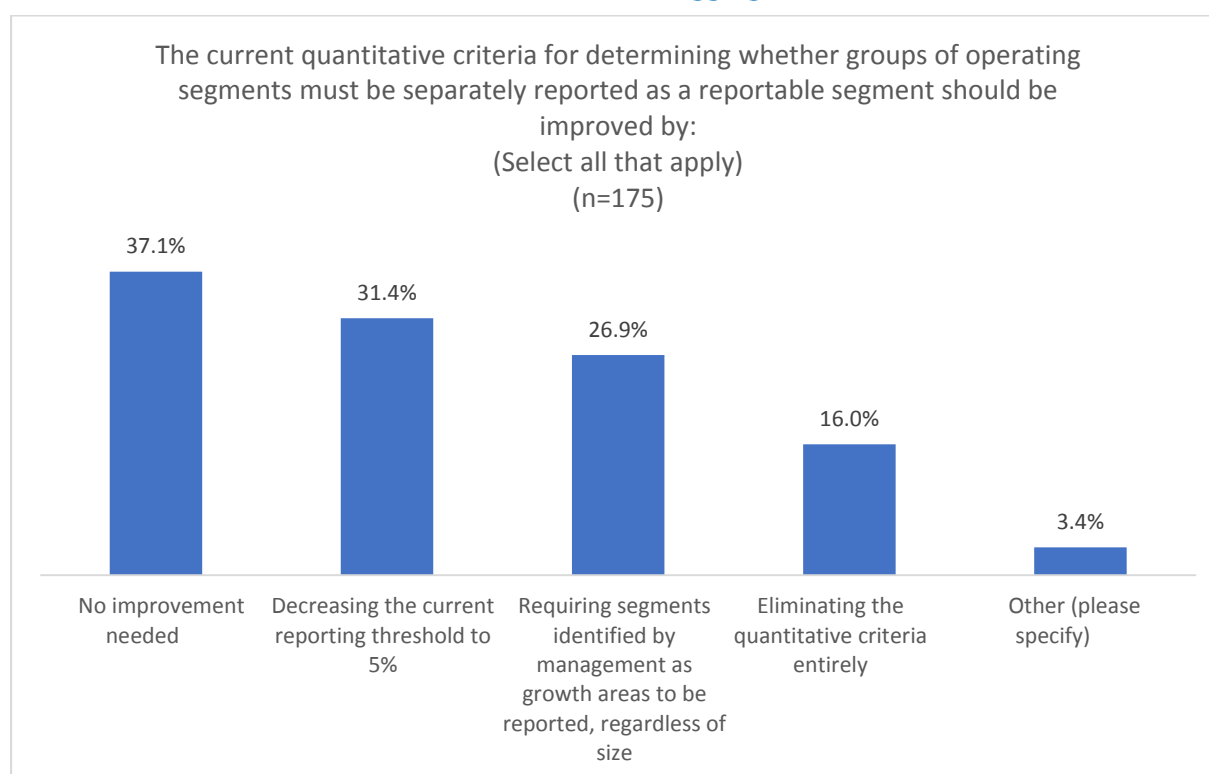


Disaggregation: Quantitative Criteria

After aggregating by qualitative criteria, segment guidance requires that companies ascertain whether certain quantitative criteria have been met such that certain operating segments are disaggregated into reportable segments. There was little support 16.0%; **Exhibit 15**) for removal of the quantitative criteria—consistent with the findings above to define aggregation criteria quantitatively. That said, 37.1%, a minority, said no improvement was needed but 31.4% of respondents believed decreasing the threshold to 5% would be useful. Further, 26.9%, nearly a fourth of respondents, believed requiring growth segments to be disclosed separately is appropriate. Overall, more saw a need for change than retaining the status quo. One respondent noted:

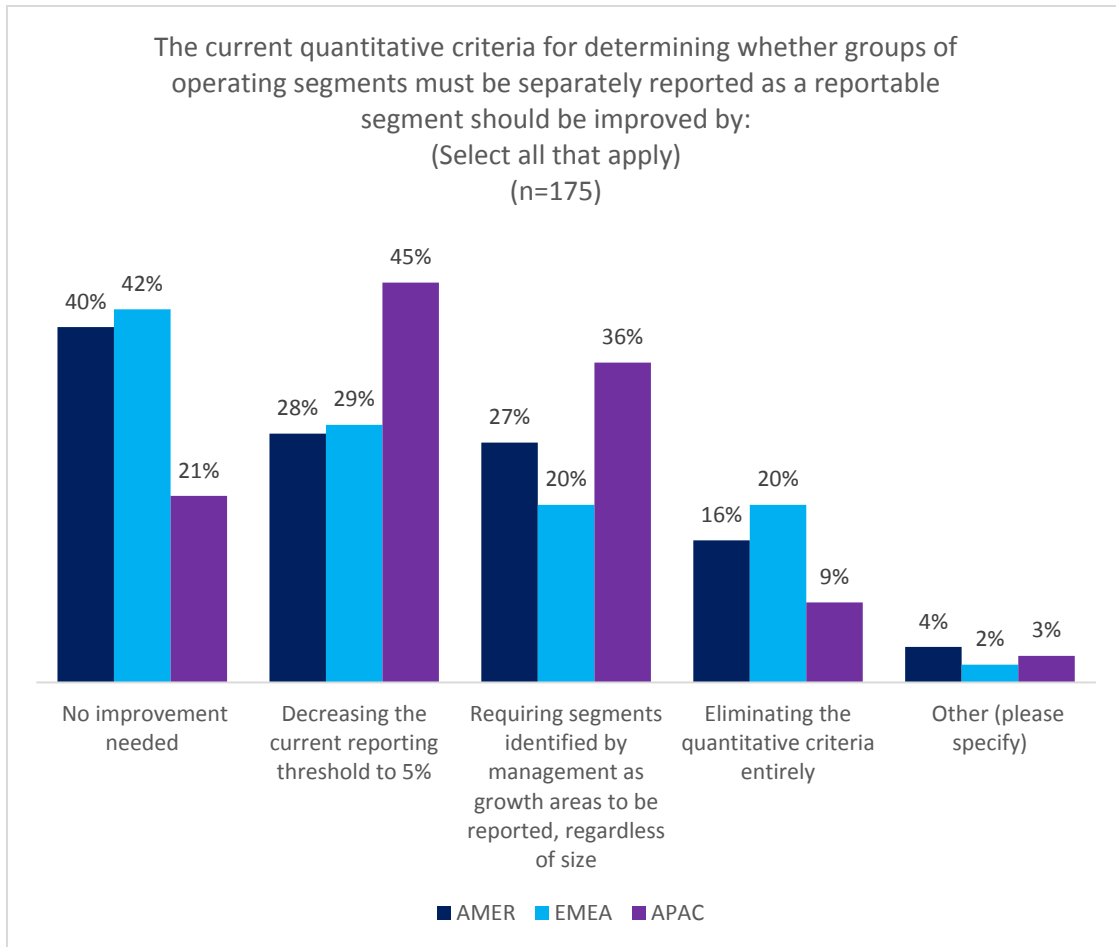
- *The problem is that the 10% (or even 5%) threshold is meaningless. Investors are extrapolating even 1%–2% changes in revenues/earnings to make long-term decisions.*

Exhibit 15: Quantitative Disaggregation Criteria



Regionally, as noted in **Exhibit 15A**, respondents saw this quite differently, with those in the APAC region strongly in favor of decreasing the disaggregation criteria to 5% as well as requiring segments that are growth areas to be reported regardless of size. Those in the EMEA region were most strongly in favor of eliminating the quantitative criteria.

Exhibit 15A: Quantitative Disaggregation Criteria by Region



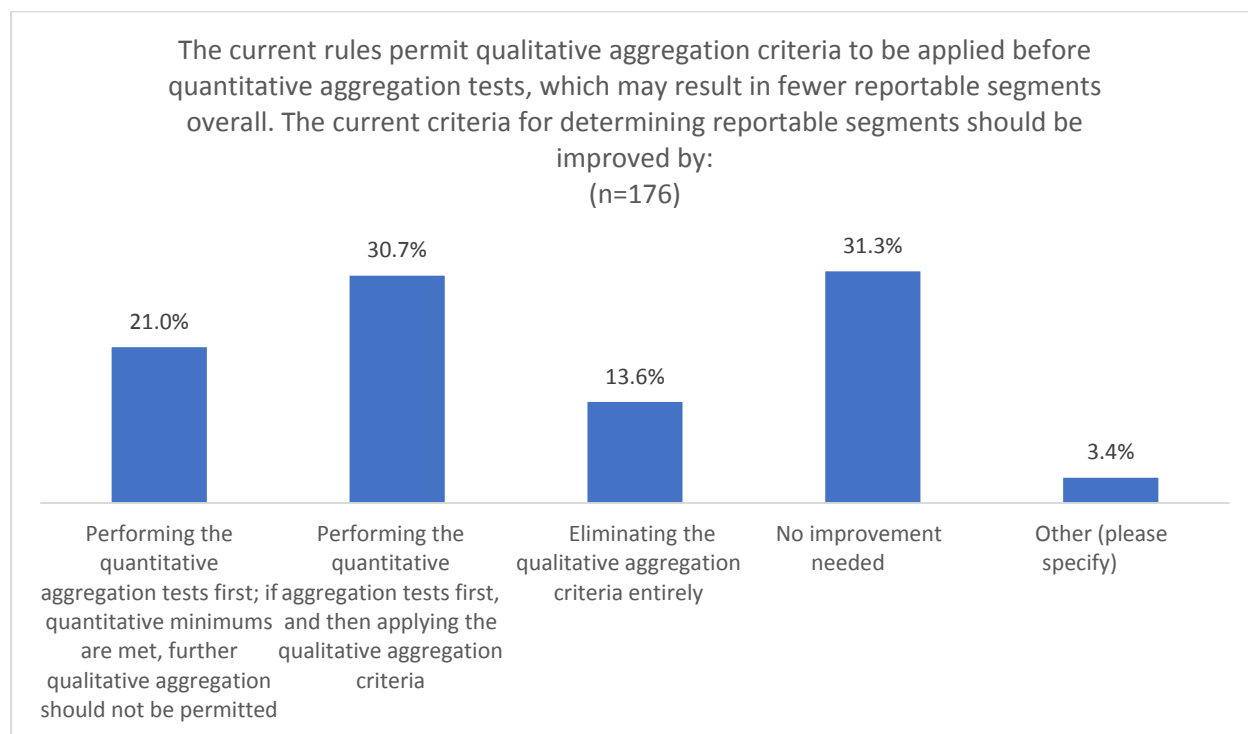
Qualitative versus Quantitative Criteria

After asking respondents about the qualitative and quantitative criteria separately, we then asked whether the quantitative criteria should be applied before the qualitative criteria. As shown in **Exhibit 16**, 31.3% of respondents indicated no improvement was needed, while 30.7% of respondents noted that applying the quantitative criteria first and then applying the qualitative criteria was important. Of the respondents, 21.0% noted that performance of the quantitative aggregation tests should first be performed, and then if met, skip the qualitative aggregation. Overall, 51.7% of respondents thought that applying the quantitative test first was a preferred solution, while 13.6% felt eliminating the qualitative aggregation criteria entirely was the best answer.

Overall, 68.7% of respondents noted that some sort of change was necessary and that quantitative criteria had primacy. A comment from one respondent was noted as follows:

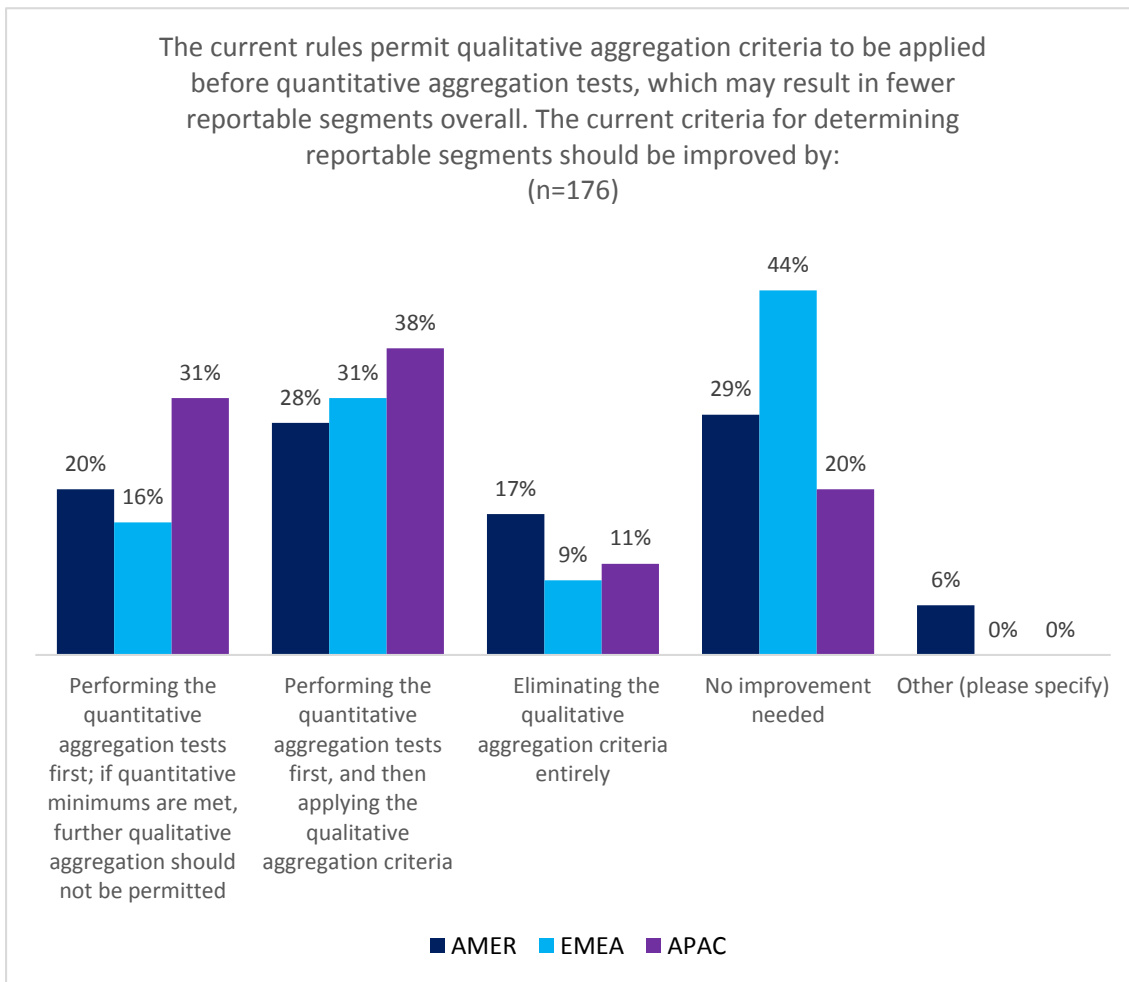
- *Regardless of whether the quantitative or qualitative criteria are applied first, the opportunities for management to aggregate must be reduced as they are currently abused to hide useful information that investors want and need.*

Exhibit 16: Qualitative vs. Quantitative Criteria



The regional differences were remarkably different, as noted in **Exhibit 16A**. Respondents in the EMEA region thought that no improvement was needed to a greater degree than any other region—particularly relative to respondents in the APAC region who were more in favor of apply the quantitative criteria first (69%).

Exhibit 16A: Qualitative vs. Quantitative Criteria by Region

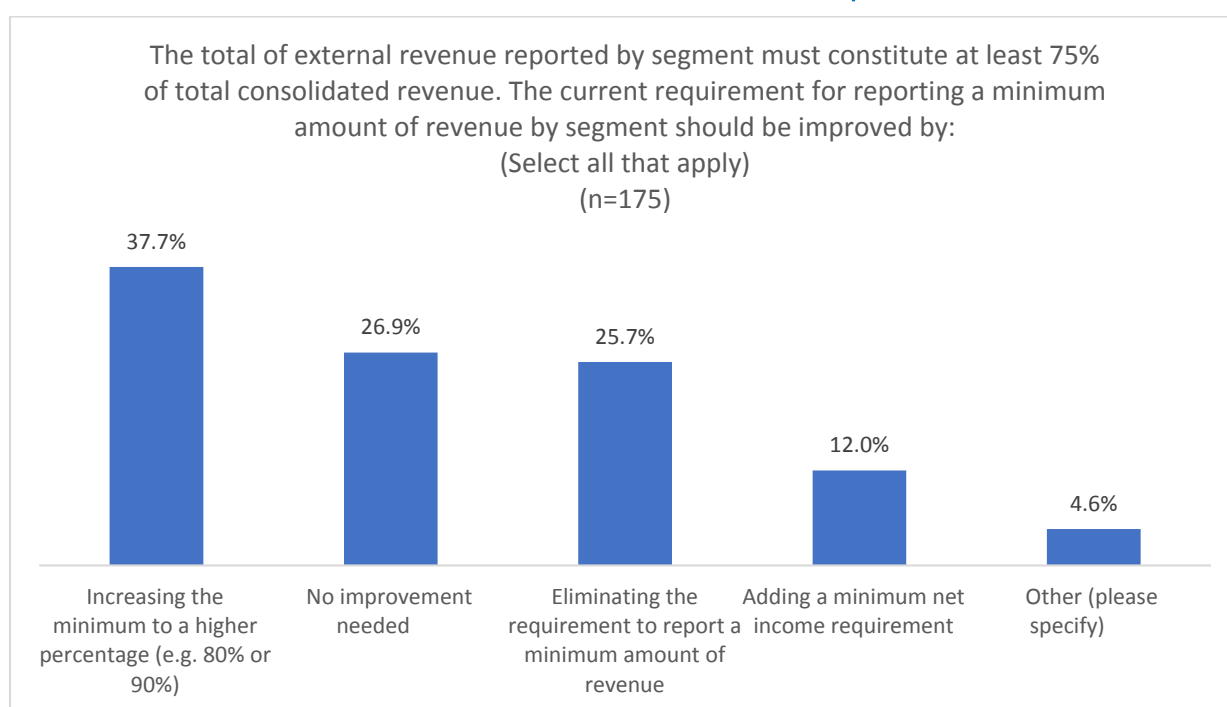


Aggregation Criteria: Minimum Amount of Revenue Reported

We then asked respondents whether the current requirement to disclose operating segments comprising 75% of revenue could be improved. **Exhibit 17** shows that 37.7% of respondents indicate the threshold should be increased from 75% to 80–90% and 12.0% felt that adding a minimum net income requirement might be helpful. 26.9% of respondents felt that no improvement was needed and, surprisingly, 25.7% felt eliminating the requirement to disclose a minimum amount of revenue was the best response. One respondent noted:

- *I think a minimum of total assets, EBIT, and EBITDA would be useful, too.*

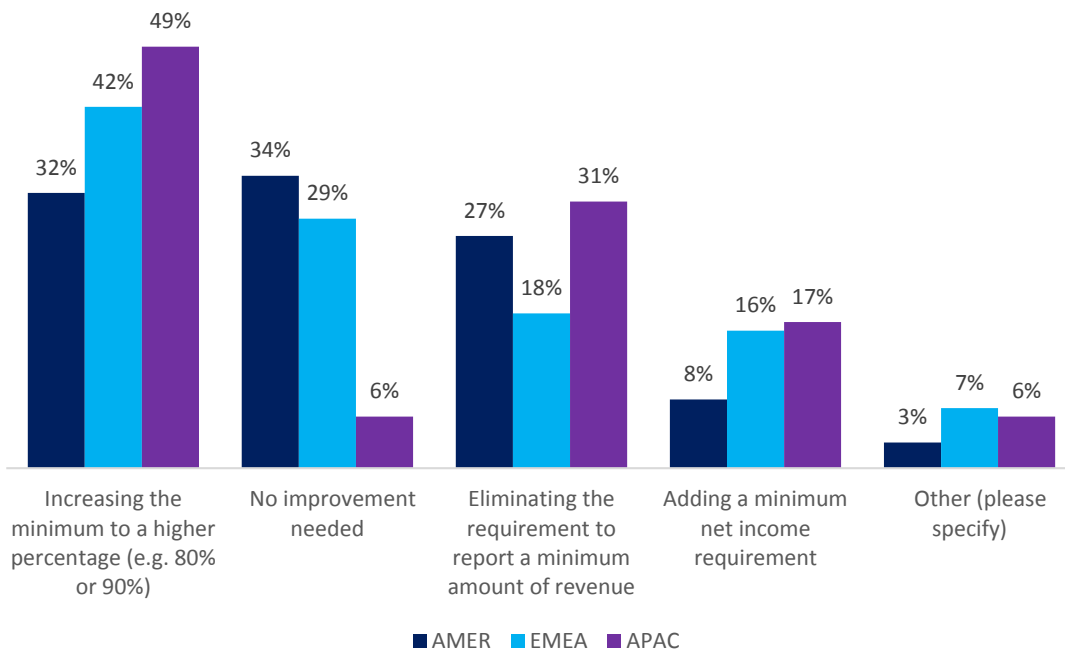
Exhibit 17: Minimum Amount of Revenue Reported



The regional differences were remarkably different as noted in **Exhibit 17A**. Respondents in the EMEA region (42%) and APAC region (49%) thought that increasing the percentage to 80-90% was substantially more important than did those in the Americas. In the APAC region, a very small percentage, only 6%, believed no improvement was needed in the requirement but a higher percentage (31%) than other regions thought eliminating the requirement to report a minimum amount of revenue was a preferred alternative, as was adding a minimum net income requirement (17%). Overall, in the APAC region, respondents had stronger views toward increasing the requirements or eliminating them.

Exhibit 17A: Minimum Amount of Revenue Reported by Region

The total of external revenue reported by segment must constitute at least 75% of total consolidated revenue. The current requirement for reporting a minimum amount of revenue by segment should be improved by:
 (Select all that apply)
 (n=175)

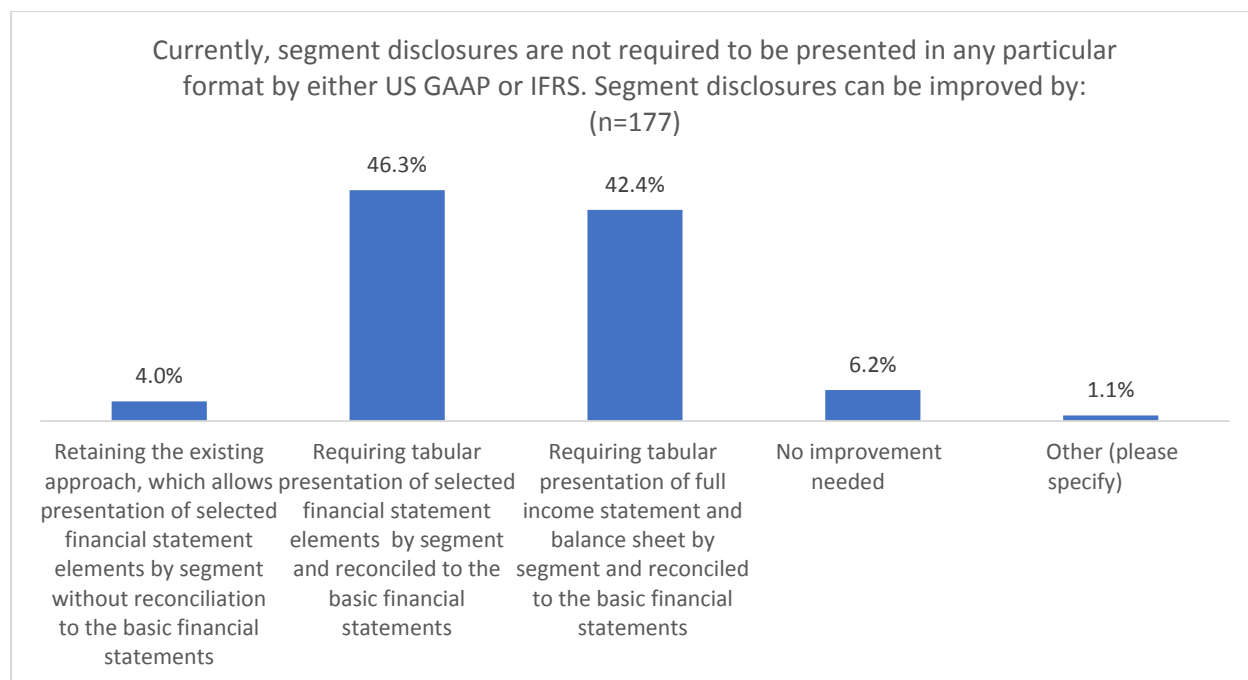


Presentation: Improving the Presentation

We then asked whether the presentation of the segment disclosures could be improved. **Exhibit 18** notes that only 4% of respondents favored retaining the existing approach. Overwhelmingly, respondents (88.7%) favored disclosures that reconciled to the financial statements—with 46.3% favoring reconciling the disclosure elements and 42.4% favoring a full income statement and balance sheet reconciliation. We believe the ordering of the response options may have impacted the response selection. With reconciliation of selected elements appearing first, we believe a quick read might have caused respondents not to discern the difference in options being the selection of elements of the financial statements and the full financial statements. We note later in Exhibit 19 the support for all income statement caption—whether or not reviewed by the CODM—is supported in the majority. As we extend this survey with direct outreach to investors and members over the next year, we will clarify the responses here. One respondent noted:

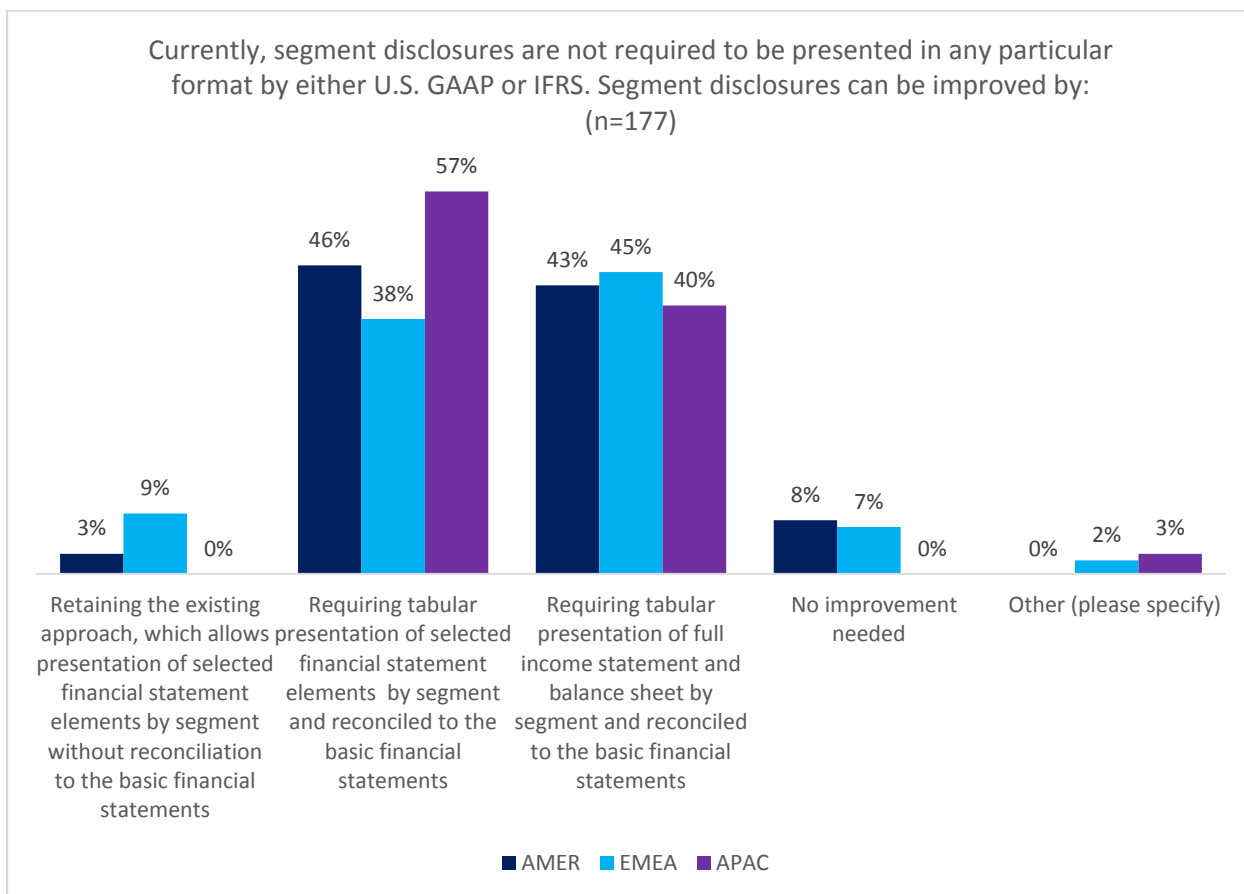
- *Elements—albeit including some which are not currently disclosed—being reconciled would be particularly useful.*

Exhibit 18: Presentation



The regional differences in **Exhibit 18A** again showed the APAC region respondents with stronger views toward adding a reconciliation. The APAC region respondents strongly believed in a greater need for reconciliation, with 57% and 40%—a total of 97%—for reconciliation of disclosure elements or the full income statement and balance sheet, respectively. No APAC region respondents agreed with retaining the existing approach, and a smaller percentage responded that no improvement was needed.

Exhibit 18A: Presentation by Region



Disclosures: Improving Disclosures

Income Statement

We asked about improvements to segment income statement disclosures. As noted in **Exhibit 19**, the results suggest that a minority (31.0%) believed that no improvement was needed, while 65.0% believed companies should be required to disclose all segment income statement information—with 34.5% indicating it should be reviewed by the CODM and 30.5% indicating it should be provided regardless of whether it was reviewed by the CODM or not. These results suggest that a majority of respondents agreed that all income statement information should be disclosed, whether reviewed by the CODM or not.

Exhibit 19: Income Statement Improvements

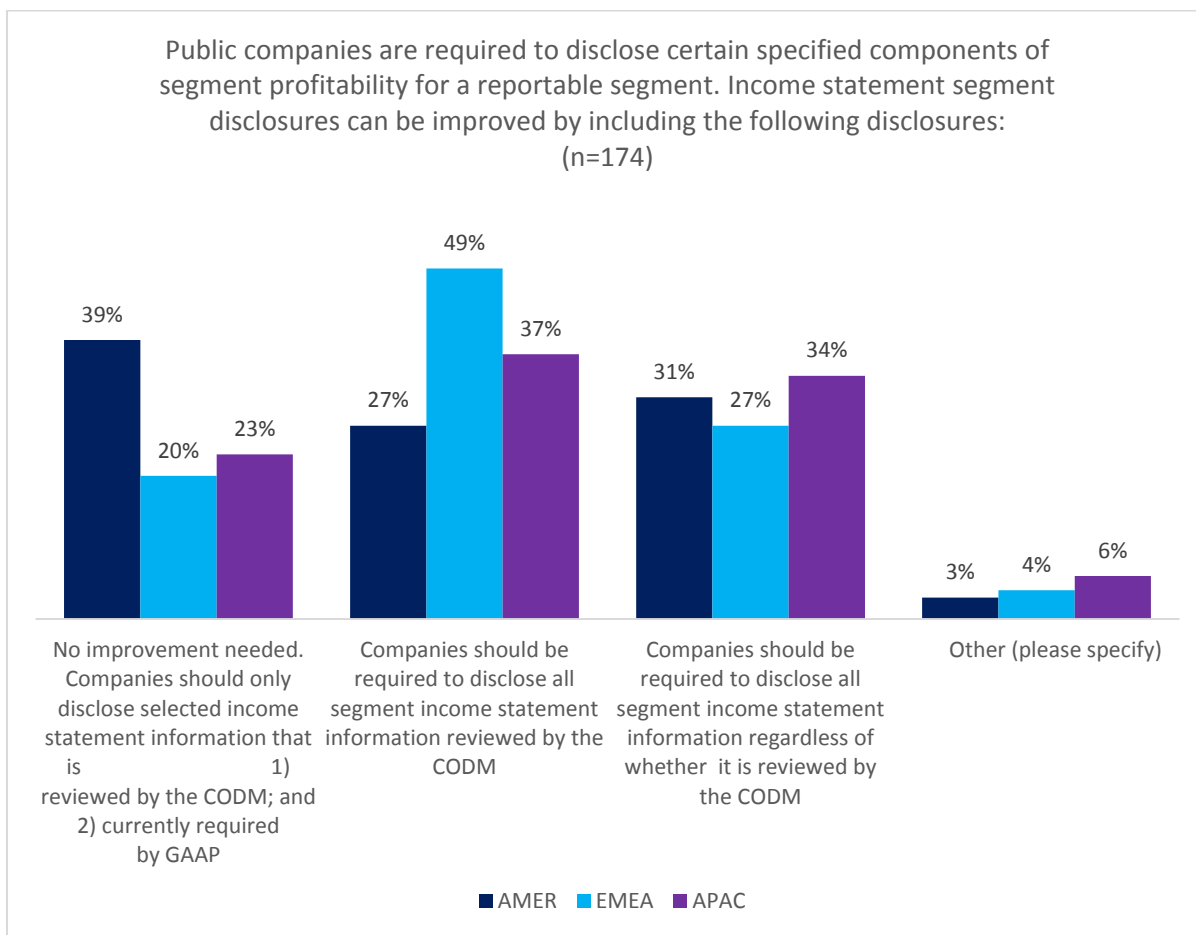


One respondent noted:

- *It is really important that more full financial statements be disclosed by segment so investors can calculate things such as segmental ROE, ROA, ROIC [return on invested capital], interest coverage, leverage ratios, et cetera. None of this is currently possible.*

The regional differences in **Exhibit 19A** showed differences in preferences most prominently among those in the EMEA region, with much higher support for disclosure of all income statement information reviewed by the CODM (49%). Respondents in the Americas region, on the other hand, more strongly—though still a minority—believed no improvement was needed.

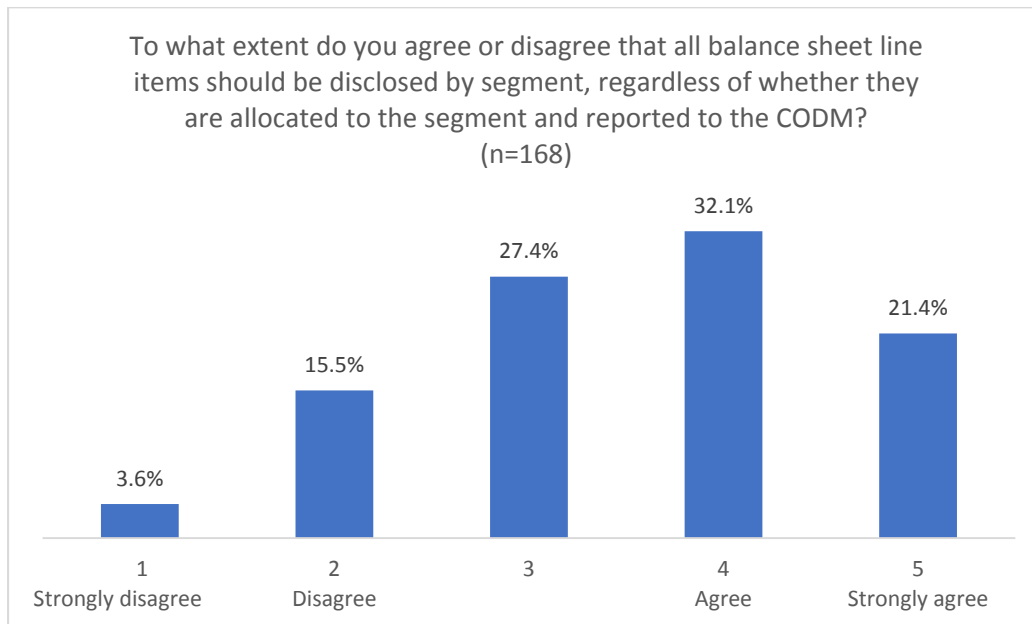
Exhibit 19A: Income Statement Improvements by Region



Balance Sheet

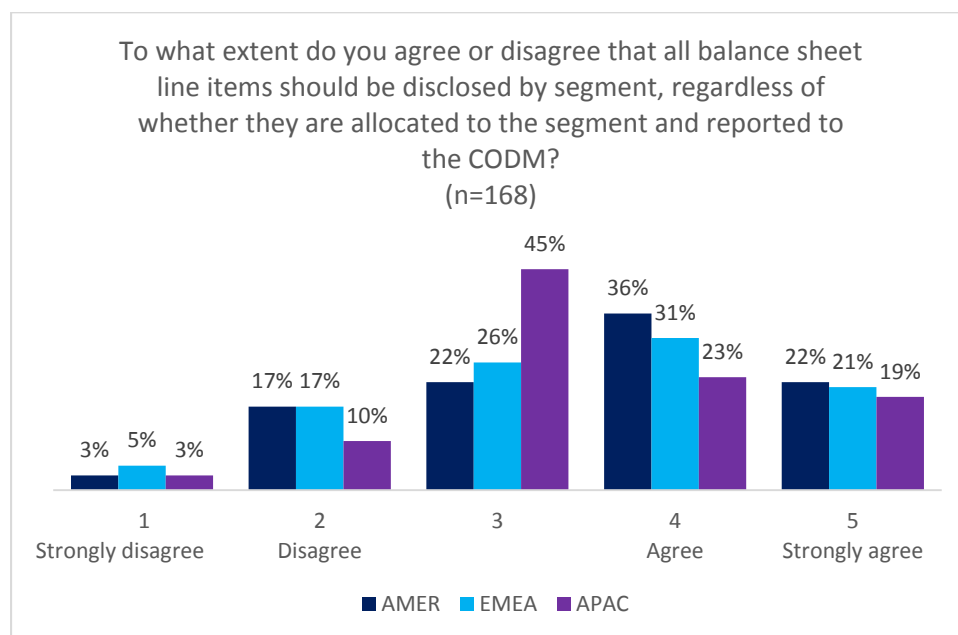
When we asked respondents about whether segment disclosures should include a disclosure of all balance items, a majority of respondents, 53.5%; **Exhibit 20**) agreed or strongly agreed that all balance sheet line items should be disclosed by segment regardless of whether they were allocated to the segment and reported to the CODM. Respondents disagreed or strongly disagreed (19.1%) with that perspective, while 27.4% of respondents were neutral.

Exhibit 20: Balance Sheet Improvements



The regional differences in **Exhibit 20A** showed differences in preferences. Most prominently among those was the fact that the APAC region respondents were more neutral about including all balance sheet captions as disclosures.

Exhibit 20A: Balance Sheet Improvements by Region



Additional Disclosures: Balance Sheet and Statement of Cash Flows

We inquired of respondents regarding their desire for improved balance sheet and statement of cash flows disclosures—related to items not currently disclosed—to gauge investor interest in certain key balance sheet items we understand are important to investors. **Exhibit 21** and **Tables 2** and **3** provide the results, with Tables 2 and 3 highlighting the percentages visualized in Exhibit 21.

Exhibit 21: Additional Disclosures

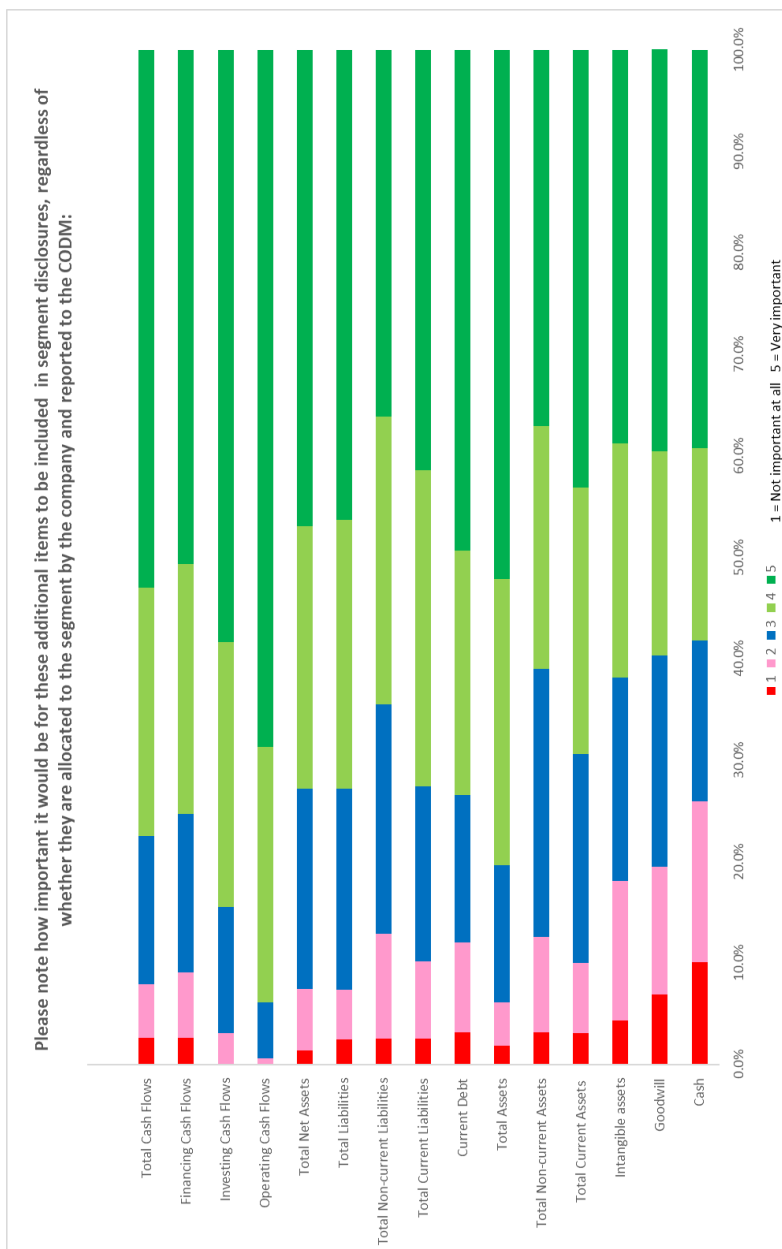


Table 2: Balance Sheet Disclosures Analysis

	NOT IMPORTANT & NOT IMPORTANT AT ALL	NEUTRAL	IMPORTANT & VERY IMPORTANT
Cash	25.9%	15.8%	58.3%
Goodwill	19.5%	20.8%	59.7%
Intangible Assets	18.1%	20.0%	61.9%
Current Assets	10.0%	20.6%	69.4%
Non-Current Assets	12.6%	26.4%	61.0%
Total Assets	6.1%	13.5%	80.4%
Current Debt	12.0%	14.6%	73.4%
Total Current Liabilities	10.2%	17.2%	72.6%
Total Non-Current Liabilities	12.9%	22.6%	64.5%
Total Liabilities	7.4%	19.8%	72.8%
Total Net Assets	7.5%	19.7%	72.8%

Somewhat surprisingly, the disclosure of cash, 58.3%, was not considered as important as the other disclosure elements, particularly total assets which was considered the most important to include. Overall, liability disclosures (64.5% to 69.4%) were perceived as more important than asset disclosures (58.3% to 73.4%) other than total assets (80.4%).

Regional differences were most pronounced, as described in **Table 2A**.

Table 2A: Balance Sheet Disclosures Analysis by Region

BALANCE SHEET ITEMS	REGIONAL VARIATIONS
Cash	Significantly fewer, approximately 20%, of EMEA region respondents believed disclosure of cash by segment was important than those in other regions.
Goodwill	Significantly fewer, approximately 10%, of EMEA region respondents believed disclosure of goodwill by segment was important. Americas region respondents believed it was of greater importance by approximately 5%.
Intangible assets	EMEA region respondents were substantially less neutral than other regions on this topic, with a greater percentage, approximately 10%, viewing the inclusion intangible disclosures as not important.
Current assets	Americas region respondents were substantially less neutral than other regions on this topic, with a greater percentage viewing as not important and a greater percentage viewing such disclosures as important.
Noncurrent assets	Americas region respondents viewed including noncurrent assets disclosures substantially (approximately 10%) more important than the average.
Total assets	All respondents in the APAC region believed total asset disclosures should be made, while those in the EMEA region were less supportive by approximately 10% regarding the need for these disclosures.
Current debt	Approximately 10% more respondents than average in the APAC region thought disclosure of current debt was important. A similar percentage of respondents in the EMEA region thought it was less important than average.
Total current liabilities	Approximately 5% fewer respondents than average in the EMEA region thought disclosures of current liabilities was less important than the average.
Total noncurrent liabilities	Approximately 10% fewer respondents than average in the EMEA region thought disclosures of noncurrent liabilities was important.
Total liabilities	Approximately 15% fewer respondents in EMEA thought disclosures of total liabilities was important.
Total net assets	Approximately 10% fewer respondents than average in the EMEA region and 10% more respondents in APAC thought disclosures of total net assets was important than did respondents from the Americas region.

Overall, respondents in the EMEA region had less strong views on the importance of balance sheet disclosures, especially with respect to liabilities, than did respondents in the APAC region.

Cash Flows

Not surprisingly, disclosure of operating cash flows was considered the most important disclosure to be made relative to the other cash flows (Table 3) as well as all balance sheet measures. Investing cash flows were second highest—even more important than total assets. The financing cash flows were rated more important than the disclosures of the liabilities to which they relate. Regional differences were most pronounced, as described in **Table 3A**.

Table 3: Cash Flow Disclosures Analysis

	NOT IMPORTANT & NOT IMPORTANT AT ALL	NEUTRAL	IMPORTANT & VERY IMPORTANT
Operating Cash Flows	0.6%	5.5%	93.9%
Investing Cash Flows	3.1%	12.4%	84.5%
Financing Cash Flows	9.1%	15.6%	75.3%
Total Cash Flows	7.9%	14.6%	77.5%

Table 3A: Cash Flow Disclosures Analysis by Region

CASH FLOW ITEMS	REGIONAL VARIATIONS
Operating cash flows	There was overwhelming support from all regions with respect to adding operating cash flows by segment.
Investing cash flows	There was overwhelming support from all regions with respect to adding investing cash flows by segment.
Financing cash flows	Only 59% of EMEA region respondents believed financing cash flow disclosures were important compared to 84% in the Americas region and 73% in the APAC region. This could be due to net debt disclosures popular in Europe.
Total cash flows	Only 71% of EMEA region respondents believed total cash flows were important compared to 85% in the Americas and 68% in the APAC regions.

Regionally, there was strong support for operating and investing cash flows, but very different views by region regarding financing and total cash flows.

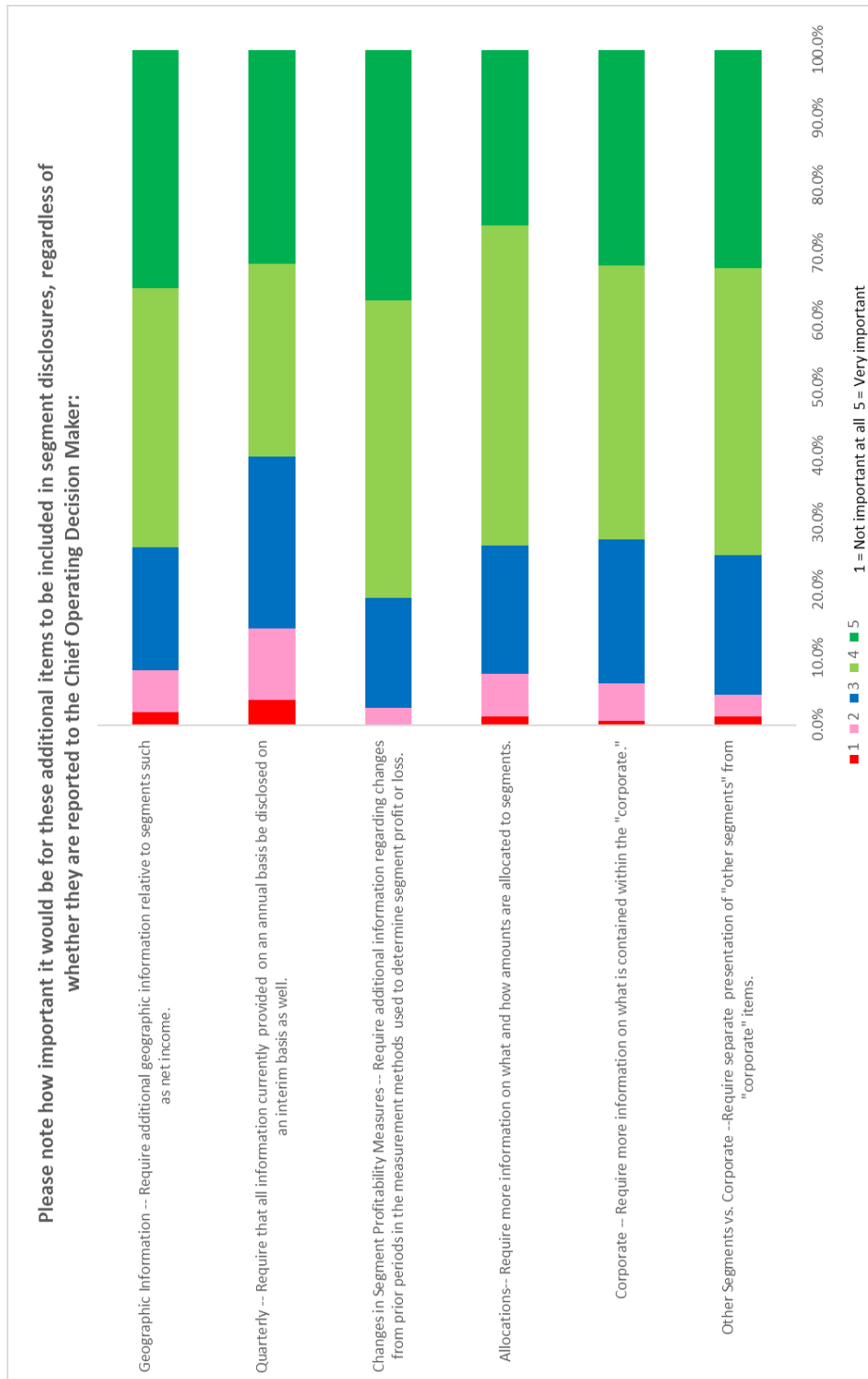
Other Disclosures

We then inquired of respondents as to whether additional disclosures related to geographic information, quarterly disclosures, changes in segment profitability measures, allocations, corporate only and corporate vs. other segment disclosures were important to add. **Table 4** and **Exhibit 22** provide the results, with Table 4 highlighting the percentages visualized in Exhibit 22. All were supported in the majority, with disclosures regarding changes in segment profitability perceived to be the most important supported and those requiring all segment disclosures to be provided quarterly were perceived as less important—but still important by a majority.

Table 4: Other Disclosures Analysis

	NOT IMPORTANT & NOT IMPORTANT AT ALL	NEUTRAL	IMPORTANT & VERY IMPORTANT
Geographic	8.2%	18.2%	73.6%
Other Segments vs. Corporate	4.5%	20.6%	74.9%
Corporate	6.3%	21.3%	72.4%
Allocations	7.6%	19.0%	73.4%
Changes in Segment Profitability Measures	2.5%	16.4%	81.1%
Quarterly	14.3%	25.5%	60.2%

Exhibit 22: Other Disclosures



Regional differences were most pronounced, as described in **Table 4A**.

Table 4A: Other Disclosures Analysis by Region

OTHER DISCLOSURES	REGIONAL VARIATIONS
Geographic	APAC region respondents (86%) thought that including additional disclosures on geographic information important, whereas only 68% of Americas region respondents saw additional geographic disclosures necessary. EMEA region respondents were more in line with the average.
Other segments vs. corporate	Americas region respondents (80%) thought that including additional disclosures on other segments vs. corporate and other information was necessary, whereas only 64% of EMEA region respondents saw additional disclosures of this nature necessary. APAC region respondents were more in line with the average.
corporate	EMEA region respondents (66%) thought that including additional disclosures on corporate information important, which was substantially different from those in APAC and the Americas regions at 74% each.
Allocations	Respondents across the regions thought that disclosure of allocations was important in similar magnitude, with those in the Americas region seeing the disclosures as very important in greater percentages, approximately 10%.
Changes in segment profitability measures	Respondents across the regions thought that changes in segment profitability measures were important in similar magnitude.
Quarterly	Only 30% of EMEA region respondents believed all the segment disclosures should be required quarterly compared with nearly 70% of respondents in the Americas and APAC regions. The EMEA region results substantially decreased the average and result in the differences from the other disclosures. This is likely because of the reduced level of quarterly reporting in the EMEA region and the narrative (empirically demonstrated to be false) that quarterly reporting results in short-termism.

ABOUT THE SURVEY

The survey was sent to a random global sample of 20,000 CFA Institute members in portfolio management and research analyst roles. The survey was sent out on 6 June 2018 and closed on 22 June 2018, with 224 responses received for a response rate of 1% and a margin of error of $\pm 6.5\%$.

This survey was also quite technical, longer, and more complex than we would normally ask our members to complete. The survey had 22 questions and three questions had multiple parts, which provided us with 54 data points. The survey took respondents nearly 25 minutes to complete—longer than we had anticipated in the invitation to participate. The number of respondents varied by question. We are appreciative to the members who took the time to complete the survey, demonstrating their commitment to helping us to improve segment disclosures on behalf of investors. The breakdown of respondents by region, job function, and years in industry is as follows (**Exhibits 23, 24, and 25**):

Exhibit 23: Respondents by Region

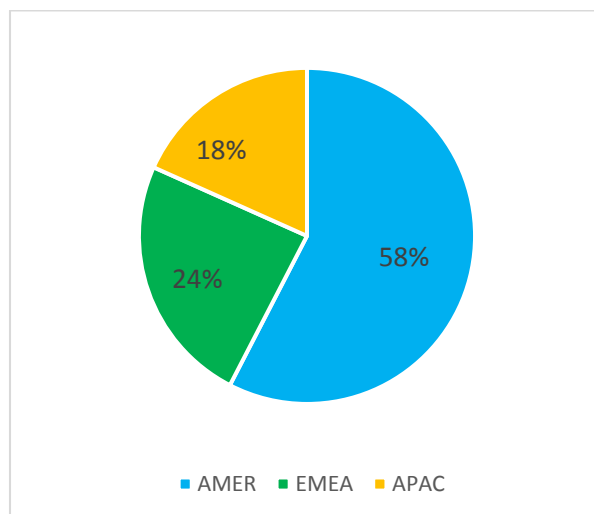


Exhibit 24: Respondents by Function

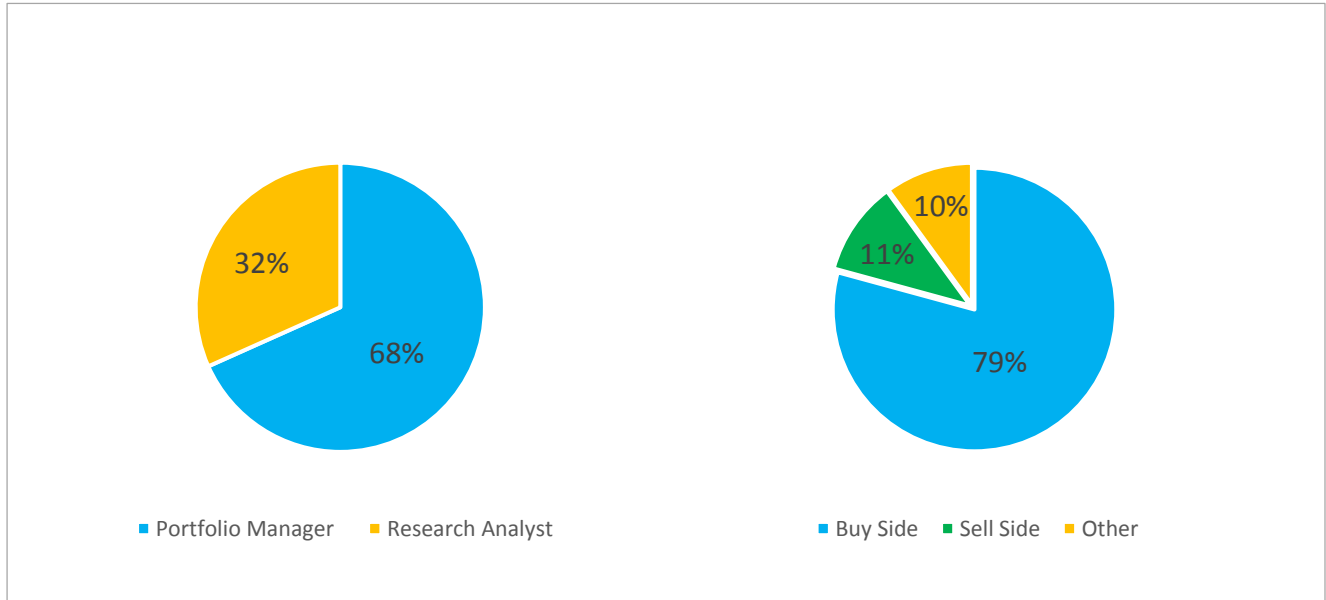
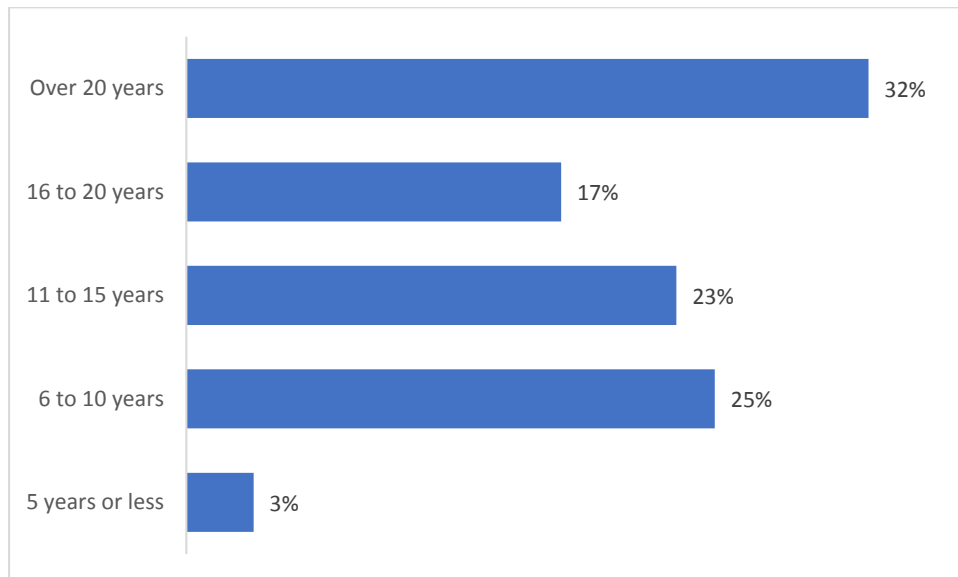


Exhibit 25: Respondents by Years in Industry





CFA Institute

Author

Sandy Peters, CPA, CFA
Head, Financial Reporting Policy Group
CFA Institute



THE AMERICAS

(800) 247 8132 PHONE (USA and Canada)
+1 (434) 951 5499 PHONE
+1 (434) 951 5262 FAX

915 East High Street
Charlottesville, VA 22902
USA

477 Madison Avenue
21st Floor
New York, NY 10022
USA

ASIA PACIFIC

+852 2868 2700 PHONE
+852 2868 9912 FAX

23/F, Man Yee Building
68 Des Voeux Road
Central, Hong Kong SAR

Si Wei Beijing Enterprise Management Consulting Company Limited
Unit 7, Level 12, Office Tower C1, The Towers, Oriental Plaza
No 1 East Chang An Avenue, Dong Cheng District Beijing, 100738, China

CFA Institute India Private Limited
Naman Centre, Unit No. 103
1st Floor, Bandra-Kurla Complex, G Block, Bandra (East)
Mumbai 400 051, India

EUROPE, MIDDLE EAST, AND AFRICA

+44 (0) 20 7330 9500 PHONE
+44 (0) 20 7330 9501 FAX

131 Finsbury Pavement
7th Floor
London EC2A 1NT
United Kingdom

Rue du Champ de Mars 23 1050
Brussels, Belgium



9 781942 713593 >



CFA Institute

www.cfainstitute.org
info@cfainstitute.org