Tel: +44 20 7893 3300
Fax: +44 20 7487 3686
@: abuchanan@bdoifra.com
www.bdointernational.com

BDO IFR Advisory Limited
Contact: Andrew Buchanan
55 Baker Street
London W1U 7EU
United Kingdom

IFRS Interpretations Committee
Columbus Building
7 Westferry Circus
Canary Wharf
London
E14 4HD

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Dear Sir

Tentative IFRS Interpretations Committee Agenda Decision: Management-defined Performance Measures – Hypothetical Income and Expenses (IFRS 18)

We are pleased to comment on the above noted Tentative Agenda Decision (TAD) of the IFRS Interpretations Committee (the Committee). Following consultation with the BDO network[1], this letter summarises views of member firms that provided comments on the TAD.

We strongly disagree with the Committee's technical analysis in the TAD applying the requirements of IFRS 18 *Presentation and Disclosure in Financial Statements*. In our view, the technical analysis does not fully comply with the requirements of IFRS 18 and, additionally, we have significant concerns about the practical consequences of the TAD if it were finalised as drafted. These concerns include the inability for certain hypothetical adjustments, which are not based on any actual financial performance or observable data to be verified, whether by management, assurance providers or regulators.

In paragraph 7 of the submission received by the Committee, three scenarios are identified. Of these, we agree that those in subparagraphs 1 and 3 could represent management's view of an aspect of the financial performance of the entity as a whole because they are based on actual transactions and observable data. In contrast, the scenario outlined in subparagraph 2 (presenting net profit as if a major crisis or geopolitical event had not happened) would result in amounts being presented that have no basis in reality; they would be fictitious 'hope value' amounts which would be incapable of representing anyone's view (let alone management's view) of an aspect of the financial performance of the entity as a whole. This is because no element of what would essentially be 'make believe' financial performance measures, would be capable of being reconciled or based on any actual transactions and events which took place during the reporting period.

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Technical analysis

As noted in the TAD, IFRS 18.117 sets out three criteria that all must be met in order for a subtotal of income and expenses to meet the definition of a management-defined performance measure (MPM). IFRS 18.117(b) requires such a subtotal of income and expenses to be used 'to communicate to users of financial statements management's view of an aspect of the financial performance of the entity as a whole' (subsequently, we refer to this requirement as 'management view' for brevity).

The TAD does not include any examples of hypothetical income and expenses, but indirectly defines them as 'income and expenses that an entity has not recognised and will never recognise in its statement of financial performance applying IFRS Accounting Standards.'

The TAD concludes that IFRS 18.117 does not restrict the types of income and expenses that may be included in an MPM and, therefore, that management's view may be on any basis decided by management. As stated in the TAD, the only obligations on management are to 'faithfully represent' the characteristics of the MPM by using labels and descriptions of the measure (IFRS 18.B134(a)).

We do not agree with this technical analysis. If it is accepted, we do not understand why the criterion in IFRS 18.117(b) exists, because it would result in there being no restrictions whatsoever on what may be considered an MPM. This would make the criterion redundant.

As explained in IFRS 18.B124-B131, we understand that IFRS 18.117(b) may not be met because of the reason for disclosing the subtotal of income and expenses. For example, this may be the case if the subtotal is disclosed outside the financial statements only because of a law or regulation (IFRS 18.B129(a)). Put another way, a subtotal of income and expenses disclosed solely because of regulation may not represent management's view.

However, we do not believe it is appropriate to conclude that this is the only reason for concluding that a subtotal of income and expenses may fail to communicate management's view. 'View' is not defined in IFRS Accounting Standards, but we understand it to mean an opinion or judgement, and financial performance is the change in economic resources and claims other than by obtaining additional resources directly from investors and creditors (Conceptual Framework – 1.18). Therefore, a subtotal of income and expenses that meets IFRS 18.117(b) must represent a valid opinion or judgement about changes in economic resources.

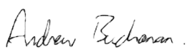
We do not believe that hypothetical income and expenses that are unrelated to historic events (e.g. profit if a specified event had not occurred) can be purported to represent management's view (or indeed, anyone's view) because they are not related to any element of actual financial performance, that is, changes in economic resources. We also do not consider it possible for disclosures made by an entity in accordance with IFRS 18.123 to faithfully represent the characteristics of such measures, because such hypothetical income and expenses require seemingly unending consideration of what would have occurred if events had transpired differently. For example, if an entity disclosed 'profit if COVID-19 had not occurred', we do not believe such a measure meets IFRS 18.117(b), and it would also not be possible for such a measure to be reconciled in accordance with IFRS 18.123(c) because no labels or descriptions could adequately explain the assumptions made by management.

For clarity, and as noted above, we do not believe that it is impossible for any hypothetical income and expenses to meet IFRS 18.117(b). For example, entities may disclose an adjusted measure of profit or loss using a constant foreign exchange rate, or on the basis that a business combination had occurred at the beginning of the year. In both of these cases, the subtotals of income and expenses can be tied to actual financial performance or actual observable data and provide useful predictive information to users of financial statements. Similarly, annualised property rental income (as set out in subparagraph 1 of paragraph 7 of the submission), or annualised rental income based on the final month of an annual reporting period can be directly linked to observable data, meaning that they can genuinely be considered to represent management's view.

Therefore, we believe the TAD should be adjusted to acknowledge that IFRS 18.117(b) contains a requirement for entities to consider whether the manner in which a subtotal of income and expenses is calculated is capable of representing a view (including management's view) of an aspect of the financial performance of the entity as a whole.

We hope that you will find our comments and observations helpful. If you would like to discuss any of them, please contact me at +44 (0)7776 215267 or by email at abuchanan@bdoifra.com.

Yours faithfully



Andrew Buchanan

Global Head of IFRS and Corporate Reporting