SEGEMENT REPORTING

Operating segments- The Management Approach

The management approach to determining segments is based on the way management disaggregates the enterprise for making operating decisions. Disaggregates components are referred to as operating segments. An operating segment is a component of an enterprise if:

1. It engages in business activities from which it earns revenues and incurs expenses.
2. If its operating results are regularly reviewed by the Chief operating decision maker to assess performance and make resource allocation decisions.
3. Discrete financial information is available for it.

Not all parts of a company necessarily are included in an operating segment. After a company has identified its operating segments based on internal reporting system, management must choose which of these segments should be used.

After determining whether any segments are to be aggregated, management must determine which of its operating segments are significant enough to justify separate disclosure. An operating segment is considered significant if it meets any of the following test:   
1. Revenue test: segment revenues, both external and intersegment, are 10 per cent or more of the combined revenue, internal and external, of all reported operating segments.

2. Profit or loss test: Segment profit or loss is 10 per cent or higher of the combined reported profit of all profitable segments or the combined reported loss of all segments incurring a loss.

3. Asset test: segment assets are 10 per cent or more of the combined assets of all operating segment.

4. Overall size test: if the combined sales to unaffiliated customers of segments determined to be significant are less than 75 per cent of total company sales made to outsiders, additional segments must be disclosed separately to meet one of the quantitative threshold, until the 75% mark is reached. This test is to ensure that all entities present a sufficient level of information regarding their individual activities to ensure that users of the financial statements can make informed economic decisions.

What has to be reported?

IFRS8 requires the disclosure of general information, such as the type of products and services from which each reportable segment generates its revenue along with factors that have been used by management to identify its reportable segments. A measure of profit or loss and total should be disclosed for each reportable segment. A number of reconciliations should be provided in relation to the total of segment items corresponding in the financial statements.