# Accounting Standards Board

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Dear Denise

**Discussion Paper 'Preliminary Views on Financial Statement Presentation'**

This letter sets out the comments of the UK Accounting Standards Board (ASB) on the above IASB Discussion Paper (DP).

The ASB welcomes the publication of this discussion paper and supports the IASB's goal of improving the usefulness of the information provided in the financial statements. We also welcome the retention of net income as a key line item. However, in line with the original objective of the project, we would have liked to see the DP consider the presentation of the statement of comprehensive income in more detail and discuss a conceptual basis for the determination of net income.

The ASB's responses to the questions asked in the Invitation to Comment in the DP are set out in the Appendix to this letter. The ASB has a number of major concerns with the proposals, which are outlined below.

1. We are concerned that the way the DP proposes to apply the cohesiveness principle does not result in decision-useful information. In our view, the issue here is that many of the conclusions in the DP are based on the premise that information that is cohesive at a line item level is always more useful than information that is not. While this may be the case in some instances, there are a number of exceptions where cohesiveness at a line item level is difficult to achieve and trying to force the principle has not resulted in proposals that will make financial statements more useful. We agree that understanding how the financial statements link together is important and that this link should be made clear, when possible, and in a pragmatic way.

2. In our view, the DP does not make a compelling case for eliminating the option to prepare an indirect method cash flow statement. We feel that the costs of such a move would only be justified in the instance that there is a demonstrated need for direct method cash flow information from a large number of users. While there are some users groups who advocate direct method cash flow statements, it is our understanding that the majority of users prefer an indirect cash flow.

3. The proposed reconciliation schedule is a lengthy and cumbersome disclosure and in our view many of the numbers in the reconciliation are of little information value. We do not consider that reconciliation of every line item in the cash flow/ statement of comprehensive income is necessary or informative. We would support reconciliation of a limited number of balance sheet line items when there is a demonstrated user need for the reconciliation. For example, users have frequently requested a reconciliation of net debt.

4. We agree it is decision useful for users to be able to distinguish between business and financing activities. We also agree that, given every entity is unique, making this distinction will rely heavily on management judgements. However, we are concerned that:

    - primary financial statements may be more useful for providing quick, at-a-glance information if they are more comparable between entities than is likely under the proposals in the DP; and

    - classification at the reportable segment level may result in primary statements that appear fragmented and haphazard.

    As such, there may be a need to consider some practical guidelines that will balance the need for entity specific classifications with the need for comparability and a sensible organisation in the primary statements. Alternatively, much of the information the DP proposes to provide through reformatting the primary statements may be better conveyed through note disclosure. This would allow the primary statements to remain concise and present information at a highly aggregated level without looking too cluttered and hard to understand. In addition, a narrative disclosure may be better able to convey the fact that not all elements of the financial statements fit neatly into the operating, financing and investing categories.

Overall, the ASB considers that the proposals will require significant reworking before they will achieve the goal of improving the decision-usefulness of financial statement presentation. In our view, it is possible to make fewer, less radical changes than those proposed in the DP while still supplying the majority of the useful information. For example, by addressing user's requests for:

- a net debt reconciliation
- an operating earnings before remeasurements sub-total
- isolation of one-off gains and losses
- a more detailed segmental reporting note

If you would like to discuss these comments, please contact Melanie Kerr (020 7492 2428, m.kerr@frc-asb.org.uk) or me.

Yours sincerely

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**Appendix**

**Response to the Invitation to Comment**

***<u>Chapter 2: Objectives and principles of financial statement presentation</u>***

***Question 1***

*Would the **objectives of financial statement presentation** proposed in paragraphs 2.5–2.13 improve the usefulness of the information provided in an entity's financial statements and help users make better decisions in their capacity as capital providers? Why or why not? Should the boards consider any other objectives of financial statement presentation in addition to or instead of the objectives proposed in this discussion paper? If so, please describe and explain.*

1. We consider that the objective of financial statement presentation should be to provide information in a format that meets the objectives of financial reporting described in the IASB Exposure draft '*An improved Conceptual Framework for Financial Reporting – Chapter 1 The Objective of Financial Reporting, and Chapter 2 Qualitative Characteristics and Constraints of Decision-useful Financial Reporting Information*'. That is, financial reports should provide decision-useful information that allows capital providers to assess the cash flow prospects, resources, changes in resources and stewardship of an entity.

2. In our view, the objectives of financial statement presentation should not differ from the objectives of financial reports as a whole. The IASB should consider how to utilise the cohesiveness and disaggregation principles as tools for achieving a decision-useful report. We are concerned that in places the DP considers adherence to the cohesiveness and disaggregation principles more important than providing decision-useful information.

3. We also have some comments that are specific to each of the objectives of financial statement presentation discussed in the DP.

<u>Cohesiveness</u>

4. The DP notes that the 'cohesiveness objective responds to the existing lack of consistency in the way information is presented in an entities financial statements'. In order to be more pragmatic in the approach to cohesiveness, we consider that the IASB should investigate what problems the inconsistency between statements causes and focus on making financial statements more cohesive in a way that will improve specific weaknesses in the current reporting model. We do not accept the implication made in a number of places in the DP that information that is cohesive at a line item level is always more decision useful than information that is not. We are also concerned that in several instances, applying the cohesiveness principle serves only to increase the complexity of the financial statements. For example:

- Arbitrary allocation of a gain/loss on a single transaction to different categories does not reflect the reality of the transaction
- Short-term liquid assets may no longer be grouped together in the same section of the balance sheet thus assessing the liquidity of a business is more cumbersome.
- Labour costs could conceivably need to be allocated to each of the operating, financing and investing categories and it may be more useful if these like costs were grouped together given the user preference for by-nature classification.
- Classifying the identical assets (ie. cash) in separate categories because they are used differently in different segments may make the statement of financial position appear fragmented.

5. We are particularly concerned with the application of the cohesiveness principle in the case of defined benefit pensions. Classifying the net plan asset/liability in the operating category of the statement of financial position and requiring that the associated items of profit and loss follow this classification does not result in a useful presentation. We consider that the most useful presentation is for the liability to be classified as financing, the expected return on plan assets as financing, the current service cost as operating and the interest cost as financing and would support efforts to achieve this outcome.

6. Overall, we are concerned that the approach to classification, which starts with the balance sheet and requires items of profit and loss to follow, may be flawed given the implications of this approach on the presentation of pension plans.

<u>Disaggregation</u>

7. The ASB agrees that an entity should disaggregate its financial statements in a manner that is useful. However, we disagree with the wording in the disaggregation objective, which says information in financial statements should be disaggregated in a manner that 'makes it useful **in assessing the amount, timing and uncertainty of its future cash flows'**. While assessing future cash flows is an important objective of financial reporting, we consider that financial statements should be appropriately disaggregated to provide information that is useful not only for assessing cash flow prospects but for meeting the other objectives of financial reporting outlined in the conceptual framework as well.

8. We support the discussion of disaggregation in paragraphs 2.8-2.11, particularly the need to report separately items with different economic characteristics while achieving a balance between too much and too little information. We consider that, in some instances, disclosure in the notes, as opposed to a requirement for disaggregation in the primary statement, may be the best way to achieve this balance.

Liquidity and financial flexibility

9. We consider that assessing 'liquidity and financial flexibility' is included under the banner of 'assessing cash flow prospects' in the Phase A conceptual framework exposure draft which says the following in paragraph OB10:

   *'.........the prospects for those cash flows depend on the entity's present cash resources and, of more importance, on its ability to generate enough cash to pay its employees and suppliers and satisfy its other operating needs, to meet its obligations when due, and to reinvest in operations'*

10. Financial statement presentation obviously needs to aim to be consistent with the principles in the conceptual framework. As such, we do not consider it necessary to re-articulate this objective again as a principle of financial statement presentation. If the IASB wishes to be more explicit about assessing liquidity as an objective of financial reporting, we consider it should be done at the conceptual framework level.

***Question 2***

*Would the **separation of business activities from financing activities** provide information that is more decision-useful than that provided in the financial statement formats used today (see paragraph 2.19)? Why or why not?*

11. We believe that the separation of business activities from financing activities does provide decision useful information, particularly in the statement of comprehensive income where users find it helpful to distinguish between the primary activities of the business and other activities.

12. That said, we do not necessarily support the proposal in paragraph 2.35, which requires assets and liabilities (and therefore items of income and expense) that cannot be clearly distinguished as operating, financing or investing to be classified as operating. We consider that operating income is one of the more useful sub-totals in the proposed financial statement formats and worry that the sub-total might be made less useful if it is used to 'dump' items that are hard to classify.

13. We are also concerned that the proposal to classify assets and liabilities in the statement of financial position has a number of negative implications for this statement. These include the lack of total assets and total liabilities sub-totals and the possibility that similar or identical assets and liabilities will not be presented in the same category. This is an example of where application of the cohesiveness principle may add to the complexity of the statement of financial position without making information more decision useful.

***Question 3***
*Should* ***equity*** *be presented as a section separate from the financing section or should it be included as a category in the financing section (see paragraphs 2.19(b), 2.36 and 2.52–2.55)? Why or why not?*

14. We consider it to be of relatively little consequence whether equity is shown separately as its own section or separately as a part of the financing section. However, it would be more familiar to users to show it as a separate section, and we see little benefit to making a change in this area.

***Question 4***
*In the proposed presentation model, an entity would present its* ***discontinued operations*** *in a separate section (see paragraphs 2.20, 2.37 and 2.71–2.73). Does this presentation provide decision-useful information? Instead of presenting this information in a separate section, should an entity present information about its discontinued operations in the relevant categories (operating, investing, financing assets and financing liabilities)? Why or why not?*

15. As noted in our response to the IASB's *Exposure Draft of proposed amendments to IFRS 5 'Discontinued Operations'* we consider that discontinued operations information is best presented in the notes to the financial statements. This allows discontinued assets and liabilities to continue to be presented in their relevant sections without cluttering the primary financial statements with a discontinued operations sub-total in each category. We recognise that a note disclosure only treatment is not consistent with the current requirements of IFRS 5 and we would support the IASB taking a longer look at this area.

16. Assuming the current requirements remain unchanged, we think it is preferable that this information be disclosed in a separate 'discontinued operations' section. Having a discontinued operations sub-section in each of the operating, investing and financing sections would add a large number of sub-totals to the primary financial statements and risk making the statements longer and less understandable.

***Question 5***
*The proposed presentation model relies on a* ***management approach*** *to classification of assets and liabilities and the related changes in those items in the sections and categories in order to reflect the way an item is used within the entity or its reportable segment (see paragraphs 2.27, 2.34 and 2.39–2.41).*

*(a) Would a management approach provide the most useful view of an entity to users of its financial statements?*

*(b) Would the potential for reduced comparability of financial statements resulting from a management approach to classification outweigh the benefits of that approach? Why or why not?*

17. (a) & (b) The ASB agrees in principle that an entity should classify its assets and liabilities using a management approach. We do consider that separating core and non-core information is decision-useful and that the only practical approach to classification of assets and liabilities into the operating, investing and financing categories is an approach that relies heavily on management judgement.

18. We acknowledge that the proposals in the DP will result in financial statements being less standardised between entities than is currently the case and there is a risk that this reduced standardisation will make the financial statements less useful, but overall we think that this would be outweighed by the benefits.

19. That said, there are several *rules* proposed in the DP which conflict with the proposed management approach. We support that there is a need for some detailed guidance to assist management in making classifications in order to achieve an acceptable level of comparability in the financial statements between different companies. However, we do not support the detailed *rules* that are proposed in an effort to be consistent with the cohesiveness principle, unless it is clear why this will make the financial statements more decisions useful.

20. For example, in the name of cohesiveness the DP proposes that defined benefit pension assets and liabilities will mostly likely be classified as operating and that all related items of income and expense should be classified in the operating section as well. As discussed in our response to question one, we consider that the more useful presentation is the liability classified as financing, the expected return on plan assets as financing, the current service cost as operating and the interest cost as financing and would support guidelines to achieve this outcome.

21. Also, we can see little benefit to, say, cash, being reported in several different categories in the financial statements and for different entities to classify cash in different sections. As such, we would support a requirement that cash be presented in a single section of the financial statements, regardless of how it is used at segment level. We also wonder whether a more useful presentation would classify all investments in associates as investing, as opposed splitting these investments into multiple sections as illustrated in the example financial statements in appendix A of the DP.

22. We consider that the management approach to classification of assets and liabilities requires high quality, transparent disclosures that clearly explain the reasons for classification decisions. We are therefore concerned because the example classification disclosures in the DP appear to be boilerplate.

23. Overall, each business will never fit neatly into the three categories; the reality is much more complex and dynamic than that. We think it is important that the balance sheet remain concise and it is worth investigating whether most information is better conveyed through note disclosure. This would allow the primary statements to remain comparable and present information at a highly aggregated level without looking too cluttered and hard to understand. In

addition, a narrative disclosure may be better able to convey the fact that not all elements of the financial statements fit neatly into the three categories.

***Question 6***

*Paragraph 2.27 proposes that both assets and liabilities should be presented in the business section and in the financing section of the **statement of financial position**. Would this change in presentation coupled with the separation of business and financing activities in the statements of comprehensive income and cash flows make it easier for users to calculate some key financial ratios for an entity's business activities or its financing activities? Why or why not?*

24. As noted in paragraph 2.51 of the DP, this proposal will be a significant change in the format of the statement of financial presentation and we are not sure that the benefits of this change are clear.

25. We consider that the statement of financial position should be presented in such a way that the total assets and total liabilities sub-totals are clear from the face of the statement as we consider the statement is more intuitive this way. In our view, disclosure of these sub-totals in the notes to the financial statements is not a good alternative to presentation on the face of the primary statement.

26. Presentation of both assets and liabilities in the same category will make it easier to calculate certain ratios and more difficult to calculate others.

***Question 7***

*Paragraphs 2.27, 2.76 and 2.77 discuss classification of assets and liabilities by entities that have **more than one reportable segment for segment** reporting purposes. Should those entities classify assets and liabilities (and related changes) at the reportable segment level as proposed instead of at the entity level? Please explain.*

27. The statement of financial position currently provides an 'at a glance' view of the resources and obligations of an entity – we are concerned that this will no longer be the case if assets and liabilities are scattered across the different categories in a way that only becomes clear after reading the segmental disclosures note. For example, consider the following extract from paragraph 2.40 of the DP:

    *'For example, an entity may have three reportable segments: manufacturing, financial services and retail, each with a portfolio of financial instruments. In the manufacturing segment, the financial liabilities are used to fund ongoing operations and, therefore, are classified in the financing liability category. In the financial services segment, the main operation consists of earning a higher return on financial assets than is paid on financial liabilities and, therefore, the financial instruments are classified in the operating category. In the retail segment, the financial instruments provide a return, but are not used to fund the activities of the retail business and, therefore, are classified in the investing category. Thus, in this example, an entity's financial statements would present financial instruments in the financing liability, operating and investing*

*categories in a way that is consistent with how the entity uses those financial instruments in each reportable segment.'*

28. In the case described in this extract, the statement of financial position would appear haphazard until a reader understood the different segments of the business. As such, in the interests of the statement of financial position continuing to provide high-level aggregated information, we support efforts to achieve classification at the entity level.

***Question 8***

*The proposed presentation model introduces sections and categories in the statements of financial position, comprehensive income and cash flows. As discussed in paragraph 1.21(c), the boards will need to consider making* ***consequential amendments to existing segment disclosure requirements*** *as a result of the proposed classification scheme. For example, the boards may need to clarify which assets should be disclosed by segment: only total assets as required today or assets for each section or category within a section. What, if any, changes in segment disclosures should the boards consider to make segment information more useful in light of the proposed presentation model? Please explain.*

29. We consider that a useful segmental disclosure note needs to be reconciled to the key line items on the face of the financial statements – currently total assets, total liabilities, etc. Some of the line items required to be disclosed under IFRS 8 *Operating Segments* such as total assets and total liabilities may no longer be presented on the face of the primary financial statements under the new proposals. As such, a change in disclosure requirements under IFRS 8 may be needed. For example, presentation of net operating assets or other such subtotals that are available on the face of the financial statements. We also understand the users would find more cash flow information at the segmental level useful.

30. However, we feel this could be difficult to achieve because IFRS 8 is based on the fundamental principle that disclosure of information is only required if it is regularly reviewed by the chief operating decision maker. We consider that this principle may conflict with the proposals in the DP because a management approach to classification is not the same as using information management has already. This may mean that very few key lines in the financial statements will correspond to information provided to the chief operating decision maker.

***Question 9***

*Are the* ***business section*** *and the* ***operating and investing categories*** *within that section defined appropriately (see paragraphs 2.31–2.33 and 2.63–2.67)? Why or why not?*

31. Overall, we agree with the proposed definition of the business section as the 'value creating' activities of the enterprise and the further split into operating on the basis of 'primary' or 'central' value creating activities and investing as non-central value creating activities. Based on the proposed definitions we

agree with paragraph 2.66 that many entities will have very few assets and liabilities classified as investing.

32. We are concerned that the definition of investing in paragraph 2.33 mixes the idea of 'value creating activities unrelated to the central purpose' with the idea that the classification depends on the nature of returns that may be earned such as interest, dividends and capital gains. We consider that these are two fundamentally different ways of thinking about investing activities, which may be confusing to apply in practice. For example, an entity may consider the investment of excess cash in short-term securities operating because this cash will ultimately be used to settle invoices from suppliers. However, given the nature of returns, the definition also points to an investing classification. We wonder if the notion of working capital (short-term assets that may be used to generate cash for use in primary value creating activities) may be useful in distinguishing between true investment activities and interest-earning operating activities.

***Question 10***

*Are the **financing section** and the **financing assets and financing liabilities** categories within that section defined appropriately (see paragraphs 2.34 and 2.56–2.62)? Should the financing section be restricted to financial assets and financial liabilities as defined in IFRSs and US GAAP as proposed? Why or why not?*

33. While we consider that the majority of assets and liabilities classified in the financing section will be financial assets and financial liabilities (as defined by paragraph 11 of IAS 32) we do not necessary agree that there should be a rule that prohibits classification of non-financial assets and liabilities in this section. The primary justification for this rule in the DP is to 'add objectivity' to the classification process. However, we consider that the more difficult aspect of the classification will be deciding which financial liabilities are operating and which are financing. This rule will not result in this aspect of the judgement becoming more objective.

34. In addition, we consider that the financing section should include the net defined benefit pension asset/obligation and lease liabilities and support some guidelines to achieve this outcome.

***<u>Chapter 3: Implications of the objectives and principles for each financial statement</u>***

***Question 11***

*Paragraph 3.2 proposes that an entity should present a classified statement of financial position (short-term and long-term subcategories for assets and liabilities) except when a presentation of assets and liabilities in order of liquidity provides information that is more relevant.*

*(a) What types of entities would you expect not to present a classified statement of financial position? Why?*

*(b) Should there be more guidance for distinguishing which entities should present a statement of financial position in order of liquidity? If so, what additional guidance is needed?*

35. (a) We agree with the analysis in paragraph 3.6 that entities with a large number of financial instruments that mature within a relatively short time period may be able to provide more decision useful information by providing assets and liabilities in order of liquidity rather than using the arbitrary distinction of maturing in greater or less than one year (short-term and long-term categories).

36. On a related note, we are unclear how the definition of short-term and long-term based on greater or less than twelve months links in with the concept of a management approach to presentation.

37. (b) We consider that the guidance provided in the DP is sufficient.

***Question 12***
*Paragraph 3.14 proposes that cash equivalents should be presented and classified in a manner similar to other short-term investments, not as part of cash. Do you agree? Why or why not?*

38. We agree with the proposal to classify cash equivalents in a manner similar to other short-term investments, separately from cash.

39. We note that the financial statements may provide information that is more decision-useful for assessing liquidity if all short-term, liquid financial instruments were presented in a single category in the statement of financial position.

***Question 13***
*Paragraph 3.19 proposes that an entity should present its similar assets and liabilities that are measured on different bases on separate lines in the statement of financial position. Would this disaggregation provide information that is more decision-useful than a presentation that permits line items to include similar assets and liabilities measured on different bases? Why or why not?*

40. We agree that disaggregation of assets and liabilities that are measured on different bases provides more decision-useful information. However, we do not necessarily agree with paragraph 3.20 that 'providing that information in the statement of financial position is more straightforward and avoids making users go back and forth between the statement and the notes to find important information'. We believe that in most instances it will be appropriate to present disaggregation in the notes to the financial statements to avoid cluttering the statement of financial position. Disaggregation in the notes allows for highly aggregated information in the primary statements along with the ability to 'drill down' to detailed notes for those who are interested in the detail.

41. In addition, implementing this policy in practice will require clarification of what the IASB means by the term 'measurement bases'.

### *Question 14*

*Should an entity present comprehensive income and its components in a single statement of comprehensive income as proposed (see paragraphs 3.24–3.33)? Why or why not? If not, how should they be presented?*

42. As comprehensive income continues to be divided into net income and other comprehensive income components, we consider that it does not make sense at this stage to remove the option to report these two components using two statements. In our response to the 2007 *ED of Amendments to IAS 1 Presentation of Financial Statements: A Revised Presentation* we observed that many entities will see the two-statement presentation as more consistent with user expectations and general practice, given the current focus on net income as an important measure of performance. As such, we consider that the option to report comprehensive income using one or two statements should be retained.

43. In the DP the primary rationale for eliminating the choice to present comprehensive income in one or two statements is to improve comparability. In our view, the choice regarding one or two statements does not result in significant incomparability between entities. Many of the other proposals in the DP have a far more significant impact on comparability than this option.

### *Question 15*

*Paragraph 3.25 proposes that an entity should indicate the category to which items of other comprehensive income relate (except some foreign currency translation adjustments) (see paragraphs 3.37–3.41). Would that information be decision-useful? Why or why not?*

44. Disclosing the category to which items of other comprehensive income relate may be decision useful in some instances. In other instances, for example actuarial gains and losses on defined benefit pension plans, the category should be reasonably obvious after review of the financial statements. Again, if available-for-sale securities are only presented in a single category on the balance sheet (which we hope they are) then it will also be obvious.

### *Question 16*

*Paragraphs 3.42–3.48 propose that an entity should further disaggregate within each section and category in the statement of comprehensive income its revenues, expenses, gains and losses by their function, by their nature, or both if doing so will enhance the usefulness of the information in predicting the entity's future cash flows. Would this level of disaggregation provide information that is decision-useful to users in their capacity as capital providers? Why or why not?*

45. We consider that the deciding factor in the decision to disaggregate the statement of comprehensive income by nature or by function should be the usefulness of the resulting information. We do not support a preference for disaggregation by function in order to be consistent with the functional categories as proposed in the DP, especially since the DP notes a user preference for by nature. We are concerned the drafting of the DP, which first asks for disaggregation by function and then further by nature, may compel entities to make a disclosure by function even if they consider that a by-nature only presentation is most useful.

46. We consider that the DP should ask entities to select the most useful of disaggregation by:

    (i) function;
    (ii) nature; or
    (iii) function and nature.

47. We think this change in drafting will better emphasise the importance of usefulness over the importance of disaggregation by function. We consider that, in practice, companies would not provide disaggregated information unless this information is being used internally and that this concept should be built into the exposure draft.

***Question 17***

*Paragraph 3.55 proposes that an entity should allocate and present income taxes within the statement of comprehensive income in accordance with existing requirements (see paragraphs 3.56–3.62). To which sections and categories, if any, should an entity allocate income taxes in order to provide information that is decision-useful to users? Please explain.*

48. Given the practical difficulties associated with allocating income taxes to the operating, financing and investing categories, we agree with the proposal not to extend allocation of income taxes beyond present requirements.

49. We note that the existing requirements to allocate income tax to each component of comprehensive income also have the potential to be very complex with costs that outweigh the benefits. Particularly where adjustments arise in different tax jurisdictions and where actual tax charges, rather than deferred tax, arise.

***Question 18***

*Paragraph 3.63 proposes that an entity should present foreign currency transaction gains and losses, including the components of any net gain or loss arising on remeasurement into its functional currency, in the same section and category as the assets and liabilities that gave rise to the gains or losses.*

*(a) Would this provide decision-useful information to users in their capacity as capital providers? Please explain why or why not and discuss any alternative methods of presenting this information.*

*(b) What costs should the boards consider related to presenting the components of net foreign currency transaction gains or losses for presentation in different sections and categories?*

50. (a)& (b) We do not support the proposal that gains or losses arising on remeasurements from foreign currency into functional currency be classified in the same section and category as the assets and liabilities that gave rise to the gains or losses. We agree with the DP that classification is not particularly onerous in the case of a single foreign currency transaction, however, allocation of the gain/loss on remeasurement of an entity's local currency financial statements into the functional currency is likely to be impractical and arbitrary. Because this information will be arbitrary, we do not consider it particularly decision-useful and therefore do not consider that an evaluation of the costs is necessary. We consider this another example of application of the cohesiveness principle being taken beyond what is useful and practical.

51. In our view the gain or loss on remeasurement should be presented in the category management considers best reflects the underlying activities being translated.

**Question 19**

*Paragraph 3.75 proposes that an entity should use a direct method of presenting cash flows in the statement of cash flows.*

*(a) Would a direct method of presenting operating cash flows provide information that is decision-useful?*

*(b) Is a direct method more consistent with the proposed cohesiveness and disaggregation objectives (see paragraphs 3.75–3.80) than an indirect method? Why or why not?*

*(c) Would the information currently provided using an indirect method to present operating cash flows be provided in the proposed reconciliation schedule (see paragraphs 4.19 and 4.45)? Why or why not?*

52. (a) Yes the direct method of presenting operating cash-flows does provide information that is decision-useful. However, we are concerned that this method of presentation does not provide information that is more decision-useful than the indirect method of presentation. The DP does not build a compelling case for requiring direct presentation as it relies on better cohesiveness rather than decision-usefulness as the primary argument.

53. (b) It is possible that the direct method is more consistent with the proposed cohesiveness principle than the indirect method. However, as discussed earlier, we do not wish to see the cohesiveness principle applied in such a way that cohesive presentation is prioritised over useful presentation.

54. We are concerned that the user group, as whole, prefers the indirect method of presentation and that a change in presentation to be consistent with the cohesiveness principle will not improve the utility of reports. In our view, any argument for a change in the current presentation needs to provide compelling evidence that direct presentation will improve the usefulness of financial statements for users. The DP provides, at best, mixed evidence that users want direct presentation.

55. In relation to the disaggregation objective, we do not understand the argument the paper provides at paragraph 378(b) for why the direct method is more consistent with this objective than the indirect method. We consider that both methods provide information for assessing future cash flows.

56. (c) The reconciliation schedule and the indirect method cash flow will provide similar but not identical information because the indirect method explains the difference between net income and cash through use of non-cash transactions and balance sheet movements. The reconciliation schedule does not contain a direct link into the balance sheet.

**Question 20**

*What costs should the boards consider related to using a direct method to present operating cash flows (see paragraphs 3.81–3.83)? Please distinguish between one-off or one-time implementation costs and ongoing application costs. How might those costs be reduced without reducing the benefits of presenting operating cash receipts and payments?*

57. To us the bigger issue is that costs will be incurred preparing information that is not necessarily more useful to the majority of users.

58. The costs of providing direct method presentation of cash flows are highly dependant on whether cash flows are captured directly or calculated based on movements in asset and liability balances.

59. We understand that in other countries, such as Australia, where the direct presentation is used that this presentation is achieved primarily through reworking the indirect cash flow to achieve a direct cash flow presentation.

Using this type of calculated approach would not result in significant costs or system changes. However, as many users find the indirect method more useful, this direct method calculation is, in our view, best provided as a note disclosure.

60. Direct capture of cash flows may required significant changes to the way some organisations capture data. In organisations with many subsidiaries operating in multiple currencies and with multiple different accounting systems, these changes could be significant and difficult to implement. Any system changes will result in training costs and could add complexity to certain data entry processes. System changes and training are one-time costs, although for some organisations it may take several years to iron out problems. Increasing the complexity of the data entry process will result in ongoing costs.

**Question 21**

*On the basis of the discussion in paragraphs 3.88–3.95, should the effects of basket transactions be allocated to the related sections and categories in the statement of comprehensive income and the statement of cash flows to achieve cohesiveness? If not, in which section or category should those effects be presented?*

61. We consider that the effects of each basket transaction should be presented in a single category in the statement of comprehensive income and the statement of cash flows because we do not consider that arbitrary and theoretical allocations of the effects of basket transactions to different categories will provide useful information. Again, we do not wish to see cohesiveness given priority over usefulness.

62. We are concerned about the term 'basket transaction' as it is defined in the paper as '*a single acquisition or disposal transaction that recognises or derecognises assets and liabilities that are classified in more than one section or category*.' Introducing this term into IFRS adds undue complexity by creating a second set of requirements for the presentation of acquisitions and disposals that affect multiple categories as opposed to those that affect only a single category.

63. We believe that the effects of all acquisition or disposal transactions should be presented in the category that was the predominant source of these effects. This concept can be applied to both 'basket transactions' and acquisitions and disposals that affect only a single category.

64. We do not support a rule that requires the effects of acquisition and disposal transactions to be presented in the operating category. Users consider operating income to be important because it often has higher predictive value than other categories. As such, this makes operating income a poor place to 'dump' the effects of transactions that are difficult to categorise in accordance with the cohesiveness principle.

***Chapter 4: Notes to financial statements***

**Question 22**

*Should an entity that presents assets and liabilities in order of liquidity in its statement of financial position disclose information about the maturities of its short-term contractual assets and liabilities in the notes to financial statements as proposed in paragraph 4.7? Should all entities present this information? Why or why not?*

65. The example disclosure referred to at paragraph 4.9 visualises disclosure of short-term maturities in three categories: (a) on demand, (b) three months or less and (c) three to 12 months. We do not understand the justification for requiring entities that present assets and liabilities in order of liquidity to provide more disaggregation of the short-term category than is required for other entities. If users need further disaggregation of the short-term category, it should be required for all entities.

66. However, we have a serious concern about the development of disclosures regarding contractual materiality of assets and liabilities as part of this project. We note that the recent *Exposure Draft of proposed amendments to IFRS 7 'Financial Instruments: Disclosures'* includes a requirement for contractual maturity analysis of financial liabilities, which we supported in our response to that ED. We consider that there will be substantial overlap between the proposals in the DP and the latest thinking on IFRS 7 and would like to see an integrated approach to further development of these requirements.

**Question 23**

*Paragraph 4.19 proposes that an entity should present a schedule in the notes to financial statements that reconciles cash flows to comprehensive income and disaggregates comprehensive income into four components: (a) cash received or paid other than in transactions with owners, (b) accruals other than remeasurements, (c) remeasurements that are recurring fair value changes or valuation adjustments, and (d) remeasurements that are not recurring fair value changes or valuation adjustments.*

*(a) Would the proposed reconciliation schedule increase users' understanding of the amount, timing and uncertainty of an entity's future cash flows? Why or why not? Please include a discussion of the costs and benefits of providing the reconciliation schedule.*

*(b) Should changes in assets and liabilities be disaggregated into the components described in paragraph 4.19? Please explain your rationale for any component you would either add or omit.*

*(c) Is the guidance provided in paragraphs 4.31, 4.41 and 4.44–4.46 clear and sufficient to prepare the reconciliation schedule? If not, please explain how the guidance should be modified.*

67. (a) The proposed reconciliation schedule will result in a lengthy and time-consuming note disclosure and we are concerned that this disclosure will clutter the financial statements without adding significantly to their information value.

68. In the example reconciliation schedule in the appendix to the DP most of the reconciling items are in the 'accruals, allocations and other' category, which is by the DP's definition just a balancing figure. As such, it is unclear why users would find the majority of the line items in the reconciliation useful.

69. We consider that it is unclear what the IASB is hoping to achieve with the reconciliation schedule as each of the formats under consideration provide slightly different information. We understand that users sometimes find the financial statements confusing in instances when statement of financial position movements cannot be explained through examination of the statement of comprehensive income and statement of cash flow[1]. If plugging this gap is indeed the objective of the reconciliation, then we consider it may be more useful to use a format that reconciles statement of financial position movements.

70. For example, we are aware that user groups in the UK have specifically requested that a reconciliation of net debt be required in the financial statements and we consider the best format for this reconciliation would start with the statement of financial position rather than the statement of cash flow. A definition of net debt for the purposes of this reconciliation could be tied into the concept of financing category liabilities (less the net defined benefit pension obligation). We note the example reconciliation schedule in appendix A of the DP provides enough information to reconcile net debt only because it is a simplified example without foreign exchange movements in debt or acquisitions of debt in a business combination.

71. In our view, the reconciliation schedule should hone in on specific instances where reconciliation of a line item in the statement of financial position is useful. For example, when there are significant non-cash transactions and other remeasurements, which obscure the articulation between the balance sheet movement and the other primary financial statements.

72. (b) As noted above our preference is to reconcile only a limited number of line items in the statement of financial position. As such, we consider that it may be more decision-useful to consider having companies describe the individual reconciling items or groups of reconciling items as opposed to completing a reconciliation with a number of pre-defined categories. We are concerned that allocating items to a category called 'accruals, allocations and other' provides very little information on a particular movement.

73. (c)We consider the guidance is sufficient to prepare the reconciliation schedule.

[1] For example, in its paper 'A comprehensive Business Reporting Model: Financial reporting for Investors' the CFA Centre for Financial Market Integrity proposes the reconciliation on the basis that the articulation between the balance sheet and other primary statements is obscured.

**Question 24**

*Should the boards address further disaggregation of changes in fair value in a future project (see paragraphs 4.42 and 4.43)? Why or why not?*

74. We are concerned that a requirement to disaggregate 'a change in the fair value of an interest-bearing instrument into….interest accrual, other interest rate changes, credit risk changes, foreign currency changes and other changes' and present these changes separately in the statement of comprehensive income may result in material, decision-useful information only for a small number of entities. We would therefore need more information on how many users need this information and for what types of entities before forming an opinion on whether we support this as a future project.

75. Overall, we consider that a project on further disaggregation of fair value may be skipping a step because there has been no evaluation of how fair value changes in general should be presented in the statement of comprehensive income, beyond the current requirement to present some changes in net income and others in other comprehensive income.

**Question 25**

*Should the boards consider other alternative reconciliation formats for disaggregating information in the financial statements, such as the statement of financial position reconciliation and the statement of comprehensive income matrix described in Appendix B, paragraphs B10–B22? For example, should entities that primarily manage assets and liabilities rather than cash flows (for example, entities in the financial services industries) be required to use the statement of financial position reconciliation format rather than the proposed format that reconciles cash flows to comprehensive income? Why or why not?*

76. We consider that the IASB should clearly outline the objectives of the reconciliation schedule and then select the reconciliation schedule that best meets these objectives. As discussed above in our response to question 23, we consider that a reconciliation of the balance sheet movements for a small number of line items corresponds best with our understanding of the objectives of the reconciliation schedule.

**Question 26**

*The FASB's preliminary view is that a memo column in the reconciliation schedule could provide a way for management to draw users' attention to unusual or infrequent events or transactions that are often presented as special items in earnings reports (see paragraphs 4.48–4.52). As noted in paragraph 4.53, the IASB is not supportive of including information in the reconciliation schedule about unusual or infrequent events or transactions.*
*(a) Would this information be decision-useful to users in their capacity as capital providers? Why or why not?*

*(b) APB Opinion No. 30 Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions, contains definitions of unusual and infrequent (repeated in paragraph 4.51). Are those definitions too restrictive? If so, what type of restrictions, if any, should be placed on information presented in this column?*

*(c) Should an entity have the option of presenting the information in narrative format only?*

77. (a)Users of financial statements are interested in the predictive value of various items in making their assessments of the cash flow prospects of an entity. As unusual or infrequent items by definition have relatively lower predictive value, it is decision-useful for these items to be highlighted. However, as we do not support the proposed reconciliation schedule we do not support that this information be provided as an additional column in the reconciliation.

78. (b) We support the definitions outlined in paragraph 4.51.

79. (c) It is difficult to require management to highlight infrequent or unusual items in a way that is objective. However, these items could be described in the notes to the financial statements in order to give users an understanding of why each item has been considered unusual or infrequent. In the case of transparent narrative disclosure, there is little chance of investors being mislead. As such, we support a narrative disclosure only proposal.