



Preliminary Views on Financial Statement Presentation

The ABI's Response to the IASB's Discussion Paper

Introduction

- 1. The ABI is the voice of the insurance and investment industry. Its members constitute over 90 per cent of the insurance market in the UK and 20 per cent across the EU. They control assets equivalent to a quarter of the UK's capital. They are the risk managers of the UK's economy and society. Through the ABI their voice is heard in Government and in public debate on insurance, savings, and investment matters.
- 2. Our Association is pleased to have the opportunity to respond to this discussion paper. The appropriate presentation of financial statements is of critical importance, both as regards the information that is being presented and which can be accessed by the experienced user as well as the manner in which this is done so as to make accounts as accessible as reasonably possible to the spread of potential users. As preparers of accounts our views are also being conveyed to you through the joint response of the CEA and the CFO Forum. However, our members also have a very important interest in this subject as institutional investors and therefore as users of accounts. Our comments in this response to the discussion paper therefore reflect particularly, but by no means exclusively, matters of relevance or concern to users.

General comments

- 3. We are not of the view that presentation of financial statements is currently something that is broken and which therefore requires fixing. The one area where progress would have been helpful is the presentation of income, expenses, gains and losses that are currently split across two primary statements, the Profit and Loss Statement and that which reports other comprehensive income (OCI). The proposal in the discussion paper for a single statement does not seem to us to represent any form of breakthrough to this challenge of providing a comprehensive statement and the paper is therefore a disappointment on this score. We do not consider that the current proposal represents an appropriate basis for mandating a single comprehensive income statement.
- 4. The proposed design of the Financial Statements is much influenced by the IASB's stated objective of promoting 'cohesiveness'. This may be a theoretically desirable aim but we see considerable difficulties in actually achieving this in practice. Neither do we believe that users of accounts encounter material difficulties in obtaining the necessary access to accounting information at present as a result of any lack of cohesiveness. We are therefore of the view that the cohesiveness objective should not be allowed to drive changes in the architecture of financial statement

- presentation but that if there are informational issues these be addressed by improved Notes to the financial statements.
- 5. Cohesiveness between the Income Statement(s) and the Cash Flow Statement is the area where this would be most helpful in that it will permit ready comparison across what are the dynamic statements. However, even here it is clear that this objective will not be achieved. For example the treatment of associates differs in that the Paper proposes that these be treated within Operating activities within the Income Statement but as an Investing activity within the Cash Flow Statement. (This feature would have been made more apparent in the worked example of Toolco on pages 106 to 111 had the associate distributed some or all of its profits by way of dividend payments.)
- 6. We do, however, consider that the objective of enhanced disaggregation of information to be a worthwhile objective as this should provide users with additional information permitting improved analysis and insight, more confidence in their understanding of the entity that is the subject of the financial reporting, and better investment decisions to be made.
- 7. The specific proposal for a reconciliation schedule between Cash Flow and Income Statements could be helpful to users. Preparers of accounts are concerned at the potential complexity and quantity of information and explanation to be provided. In practice the debate is about where the right balance lies as to level of disaggregation of information, and where it is best located, and we think that more work would need to be done in this regard.
- 8. The amount of material to be carried on the face of the Income Statement appears to make for an unwieldy presentation. We envisage that some of this information will need instead to be carried in the Notes.
- 9. The presentation of eps data within the new Income Statement is potentially misleading. Its positioning needs to reflect its derivation from Net Profit and not total gains and losses. It is inevitable that a comprehensive Income Statement will need to have Net Profit as an intermediate number within it rather than at the bottom line. It is therefore inappropriate to continue to report eps as if it related to the new bottom line figure. Perhaps all eps and other per share data such as dividend per share should instead be displayed as a block elsewhere within the Financial Statements.
- 10. We do not consider that a strong case has been made for the proposal to change from the so-called 'indirect' to 'direct' cash flow method for drawing up the Cash Flow Statement. Some of our members would specifically support continuation of the current 'indirect' method. In any event it is apparent that, as it would have to be applied by many entities, the 'direct' approach is something of a misnomer.
- 11. It is in the Statement of Financial Position that the most radical change is proposed. We believe there is a loss of coherence within the statement that most users of accounts would prefer to continue to understand as the balance sheet. We consider

that a presentation running from long-term assets through short-term assets to short-term liabilities to long-term liabilities, the net position shown as balancing shareholder funds remains the most meaningful for most entities. We do not consider that the operating/ investing/ financing sub-division is of particular importance to the static view. The division of those elements of short-term assets and liabilities that constitute 'working capital' and their allocation to different parts of the statement does not reflect the reality of business organisation. The allocation of goodwill to operational activities similarly does not reflect the reality of business in that goodwill is not employed within a business but is recognised as an artifact of past transactions that have much more to do with investment and financing. We are also concerned at the presentation entirely within operating activities of pension scheme assets, liabilities, income and expenses.

12. In conclusion, we suggest that an early decision be taken on the priority to be given to this project and the opportunity taken to consider whether it actually represents the best means at this time of looking to improve the effectiveness of financial reporting in communicating relevant information to accounts users.

Questions for Consultation

We provide responses on some other more detailed aspects as per specific consultation questions:

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?

Yes. Transactions with owners in their capacity as such are qualitatively different, do not in themselves create gains and losses and should therefore not be accounted for as a category in the financing section within the Income Statement. Presentation within a Statement of Changes in Equity will provide the appropriate presentation within the dynamic statements completing the reconciliation of changes in the Statement of Financial Position over the reporting period.

- 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?

Investors value financial reporting that conveys information in a way that provides insight into the way management organises the business of the company. However, they harbour some reservations as to reliance on the management approach in that it can cut across accountability to shareholders as well as reducing comparability between reporting entities. To the extent that the management approach is being promoted as a palliative to concerns about the practical application of cohesiveness we see this as a weakness of the cohesiveness objective.

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