

7 April 2009

International Accounting Standards Board  
 30 Cannon Street  
 London  
 EC4M 6XH  
 United Kingdom



LETTER OF COMMENT NO. 42

**Re: Discussion Paper Preliminary Views on Financial Statement Presentation**

Dear Sirs,

On behalf of software company Basware we are writing to comment on the IASB/FASB Phase B Financial Statement Presentation project discussion paper "Preliminary Views on Financial Statement Presentation". Our comment letter represents a software providers point of view.

Basware Financial Management builds software for IFRS Group Consolidation as well as operational planning, reporting and analyzing purposes. Our main market areas are currently in addition to Finland, the other Scandinavian countries as well as Russia.

Our IFRS Consolidation solution consists of the consolidation engine and a pre-built IFRS Package. The IFRS Package consists of our pre-built Group Chart of Accounts as well as a complete set of reports required for professional full IFRS reporting. The IFRS Chart of Accounts and the reports, input sheets, and interfaces to transaction based systems are continuously updated and kept in line with updates released by IASB. Upgrades to customer environments are launched on regular basis. This ensures that our customers at all times have an IFRS Group Consolidation Solution being in line with existing IFRS standards.

According to our experience all changes related to the presentation of financial statements are of fundamental importance, because these changes will affect all companies in different industries. In most cases extensive and costly changes are needed to sophisticated financial consolidation systems as well as transaction based ERP systems.

Based on our own experience of implementing recent changes of IFRSs into financial consolidation systems we can assure that it is very easy to underestimate the actual challenges, costs and risks related to the practical specification and implementation work. For example, the latest amendments to IAS 1, that were not considered very fundamental from the theoretical point of view, were finally pretty fundamental from the financial consolidation system's point of view. These changes affected some of the most complex areas in group accounting: calculation and presentation of translation differences and minority interests. Fortunately, our IFRS Group Chart of Accounts was already defined on a very detailed level and we managed to implement the changes in our fully automated IFRS consolidation and reporting solution for our customers.

On the other hand, there are always a lot of risks when companies have to update their existing IT solutions, because of the continuously changing IFRS compliance requirements. The problem is that the continuous changes increase the complexity of the whole solution, because everything has to be built phase-by-phase to keep in line with moving targets. The worrying issue related to the Discussion Paper is, that it can still be considered an intermediate step in improving the presentation. More changes will come along especially related to disclosure information, because these disclosure issues were not

7 April 2009

included in the project's scope. Nevertheless, life would be more straightforward if all foreseeable changes could be implemented simultaneously.

We would also recommend all companies that are planning to invest in a new ERP system or financial consolidation system in the near future to carefully consider the practical effects of the proposed discussion paper.

On the other hand, we foresee a lot of business opportunities for our ready-made IFRS Consolidation solution, because companies will need to make a lot of changes in their IT-systems or even replace existing IT-systems.

It should be considered that upgrades are not limited only to financial consolidation systems but also to underlying General Ledger/ERP systems. Updating these solutions has traditionally been extremely expensive and time consuming. ERP-/cash management -systems can be considered as bottlenecks for achieving a full automated direct cash flow statement. We are worried of the challenges related to direct cash flow statement as well as the new suggested reconciliation format, especially on the level of detail presented in the examples.

We think that the Discussion Paper contains many good ideas and we support much of what it says. However, we would like to comment on a few system-related issues:

#### **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.**

We strongly support the proposed main objectives of the discussion paper as long as they are applied on a reasonable way. However, we are a bit worried that the proposed disaggregation objectives might result in too detailed presentation of financial statements with too many sub-groupings and line items. This level of disaggregation might make it difficult to understand the "big picture" and the overall financial performance of an entity. It is important that the disaggregation principles should not always require the information to be provided on the face of the primary financial statements and that alternatively disclosures could be used. From our point of view only useful and meaningful information should be required.

#### **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?**

We agree that separating the business activities from how they are financed or funded is useful information. However, the separation would be more complicated for banks and other financial institutions.

7 April 2009

We are more worried about the separation of business activities into operating and investing activities in practice.

### 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?**

We believe that the equity should be kept separately from the financing section according to the same way it is done today. We do not see any benefits in mixing the non-owner and owner related financing together. In addition, the continuity of equity from one period to another is the most important check calculation in ensuring the correctness of the consolidated accounts and therefore it is important to keep it as it is today.

### 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?**

In our experience the presentation of discontinued operations in line with IFRS 5 requirements has so far been one of the most challenging parts in preparing the consolidated accounts in practice. The challenges have been both theoretical in interpreting the definitions in IFRS 5 as well as making the separation in IT-systems and converting the comparables.

Today there are also alternative ways for presenting the discontinued operations on the face of the statement of comprehensive income (net presentation or separate columns) which also affects the disclosure specifications. We also think that the presentation of discontinued operations should be in line with IFRS operating segments and no smaller categories should be required to be disclosed in the notes. We hope that the presentation of discontinued operations could be simplified one way or the other and there should be less alternative ways of presentation the discontinued operations.

### 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?**

In our opinion it is more challenging to build a standard pre-built IFRS consolidation tool for all potential customers from the management approach compared with more formal and standard guidance in the

7 April 2009

proposed standard. The management approach is likely to lead to a situation where each IT environment and the format of each final IFRS report package is slightly different from each other. This, of course, weakens the comparability between the companies and increases the costs of IT, because each environment needs to be customized to be in line with the company's way of managing the business. On the other hand, the management is more likely to change their opinion more frequently and there is also the possibility of re-organizations, that might affect the consistency from one period to another. This might lead to a situation where companies would continually adjust their classifications and make changes to their IT systems and restate their figures over and over again.

We expect that the classification of all assets and liabilities in new sections and categories will be a very challenging task especially for the very first time and a lot of management judgment will be required to keep this exercise on a reasonable and meaningful level. We would like to point out, that this kind of an approach is not a completely new one. This kind of classification approach of assets and liabilities has been widely used for building the statement of cash flows.

#### 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?**

In our opinion the biggest practical challenge with the proposed new format of statement of financial position is that it will take the IFRS accounting and presentation further away from the traditional statutory accounting, NGAAPs and local tax accounting point of views. This would be something new and extra, that is only required for the group reporting and for the consolidated IFRS accounts. We are not sure if companies would like to change the whole structure of their legal entity chart of accounts in the transaction based systems and ERPs because of the new IFRS presentation requirements. However, some changes (for example additional analytical dimensions) are also needed in the ERP:s in order to get the new management approach automatically out of the ERP systems. At this stage it is also too early to say, whether management would prefer the suggested new format for the management reporting purposes or they would rather rely on the traditional formats for their decision making. All this adds complexity for overall financial reporting processes and increases the costs of implementing the changes in practice.

The proposal will have significant effect on financial consolidation solutions and all old reports need to be replaced with the new formats. In addition, the classification rules need to be built for the group reporting purposes. It is also important to ensure correct handling of the changes in classified assets and liabilities on the statement of cash flows and statement of comprehensive income and therefore some additional checks and internal controls (including the audit trail) need to be built in the reporting system. In fact, this does not seem to be a minor issue in practice.

The first impression on the new proposed statement of financial position reports is that there seem to be much more lines than in the current presentation format. We also think that users and preparers will need some time to get used to the proposed format.

7 April 2009

We agree that the new presentation format would make the calculation of the key ratios much easier and add the transparency and improve the overall audit trail in that perspective.

#### 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.**

If management approach should be used for classifying assets and liabilities and as the management approach is also used for identifying reportable segments in accordance with IFRS 8, we cannot recommend any other better approach.

There are also some IT system related issues that should be considered related to the practical implementation of the proposed approach.

First of all, the classification should as a minimum be done separately for each legal entity belonging to the group. The complexity would in most cases be doubled if there are more than one reportable segment and if one legal entity can have operations than belong to several operating segments. In those cases it could mean that assets or liabilities on one General Ledger account might be allocated to different sections and categories on financial statements for different reportable segments. In these cases more features and dimensions are needed in the IT systems. Actually, the classification should be considered already in the general ledgers and transaction based systems. This would eventually increase the complexity and costs, because this kind of approach is currently not considered in the existing general ledger chart of accounts or analytical dimensions. In the financial consolidation systems more analytical dimensions are also required.

We would also recommend for those companies, that are planning to invest in a new ERP system or financial consolidation system in the near future to carefully consider the practical effects of the proposed discussion paper.

#### 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.**

According to our understanding the operating segment disclosures (in accordance with IFRS 8) should be in line with the method, how the data is currently reported to the chief operating decision maker. If these classifications are not currently used in internal management reporting, then maybe these disclosures should not be compulsory for all companies and if they are currently used, then they could also be disclosed by operating segments.

7 April 2009

Changes in segment reporting requirements are also big issues and we would very much appreciate if the timing and possible effective date for the changes in IFRS 8 could go hand in hand with this discussion paper. From the practical point of view it is easier to make fewer but more comprehensive changes to IT systems at once and avoid making minor changes all the time.

**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?**

We understand the logics in “core” and non-core” activities from the management point of view.

How should the companies handle those cases where the assets and liabilities are related to more than function in practice?

**Questions 10-13**

No comment.

**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?**

We think that the real issue is not really whether entities should present one single statement of comprehensive income or two separate statements. Both alternatives can easily be produced as long as the entity is able to produce the required line items for these statements information and then it is more of a technical issue where the “page break” should be put. On the other hand, we find it a little bit confusing that last time this issue was addressed (Amendments to IAS 1), it was decided to leave two alternatives for presenting the statement of comprehensive income, and now very soon after the effective date of that recent amendment, there seems to be a need for changing it again.

From our point of view the real issue related to the statement of comprehensive income is to clarify, whether items of other comprehensive income should continue to be presented in a manner different from all other non-owner related income and expense items. The basis for current classification rules in different standards could be more logical and easier to apply consistently for example for similar type of revaluation gains and losses (for example fair valuation gains of investment properties compared with fair valuation gains of available-for-sale financial instruments are currently handled differently). However, we understood that these kind of recognition and measurement issues were now beyond the scope of the current project.

7 April 2009

**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?**

We welcome the board's idea for not requiring the entities to make the proposed classification for foreign currency translation differences. Technically that would have been a real burdensome exercise.

In order to streamline and automate the whole information gathering and consolidation process, companies should technically consider classification of other OCI-items although it is initially considered to be a straightforward exercise. Typically some management judgment and some changes in information gathering are required in these kind of cases.

**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?**

It was interesting to read about the board's initial preference for presenting information in the statement of comprehensive income by function because it was assumed to give a better picture of entity's overall operations. According to our understanding many companies however increasingly prefer a disaggregation by nature to the one by function. In some countries, like in Finland, the majority of the companies in all different kind of industries have chosen the disaggregation by nature. If the disaggregation by function would become compulsory or the only allowed alternative, this would create a lot of additional IT system related costs for these companies. Maybe the management approach could also be useful here for selecting primary cost disaggregation basis for the statement of comprehensive income.

We understood that if the company has chosen the disaggregation by function, they should also disaggregate the items by nature on a far more detailed way that is currently required in IAS 1. Looking at the illustrative examples of the "Toolco company's" new statement of comprehensive income, we hope that this would not be the required level of details for all companies. Why should we report wages, salaries and benefits separately from the pension expenses? Why should we specify overhead costs into depreciation, transport and other on the very face of the statement of comprehensive income? Who will need the information on this detailed level? Furthermore, looking at the new proposed format of the statement of cash flows, it seems that we would also be required to produce the direct cash flows for these line items one way or another. From the financial consolidation systems point of view a lot of new accounts would be needed for producing this level of details on financial reports (Charts of Accounts in group consolidation solution are already now extremely long and complicated due to continuously increasing reporting demands).

A general concern we have of the proposals in the discussion paper is that they might result in too much data and not really value added compared with the existing formats. We do not see any point in making the primary financial statements excessively detailed or for requiring all companies to prepare disaggregation by function if that approach is not currently used for management reporting purposes.

7 April 2009

**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.**

We hope there will be no additional requirements for allocation of income taxes. The current requirement for disclosing tax effects for each component of other comprehensive income is already burdensome enough.

**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?**

According to our experience this approach would be very difficult and costly to do in practice and would most likely result into very arbitrary allocation. As mentioned earlier, even the existing requirements relating to the presentation translation differences are considered very challenging and we do not see enough benefits that would outweigh the related additional costs for this proposal.

**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?**

In our opinion the requirement for all companies to present direct cash flow statements would probably be the most challenging and costly part of the whole proposed discussion paper. The practical challenges would probably be doubled if the proposed "reconciliation schedule" for reconciling the statement of cash flows to the statement of comprehensive income on a line item level would be required

7 April 2009

simultaneously. We hope the board will carefully reconsider this issue before drawing any final conclusions.

In many countries, like in Finland, the large majority of the companies have chosen the indirect presentation format. Moving into the direct presentation format would be a big technical challenge. On the other hand, if the management does not require the direct cash flow information for operational decision making, why should an entity provide it for third parties? Maybe the board could also here consider the management approach as a general guideline for companies choosing the between the direct and indirect method for presenting their cash flows related to operational activities.

We also understand that the board considers the direct method to be more informative than the indirect method. Looking again at the illustrative example of the discussion paper and "the Toolco statement of cash flows" we at least hope that this would not be the required level of details for the new direct cash flow statements. Who will need this level of details for example: how much did we pay cash for transport expenses or labour pensions related to cost of sales activities? From our opinion the first line of the direct cash flow is probably the most informative one, because it indicates how much cash receipts an entity actually received from its customers. This information is useful and it would help the users of the financial statements to evaluate the credit risks better.

In principle the direct cash flow can theoretically be produced either

1. directly from the accounting records of the entity (essentially based on an analysis of the cash book items by "tagging" the cash receipts and payment to the corresponding cash flow items )
2. by adjusting the accrual based sales and cost of sales of comprehensive income by changes during the period in inventories and operating receivables and payables and other non-cash items

Currently most of the companies use the second method. The direct cash flow statements are calculated on the basis of accrual based financial statements and with help of some additional specifications. A standard process typically starts from legal entity cash flows and after they reconcile, the effects of non-cash based consolidation adjustments (for example deferred taxes, minority interests, equity method etc.) and business combinations are adjusted separately. Making as detailed direct cash flow statements as shown in the illustrative examples of the discussion paper, would be a big effort. A lot of new accounts would be needed on the statement of financial position in order to convert the accrual based items on statement of comprehensive income into cash-based items. We think this would add unnecessary complexity to this already very demanding exercise. If required a rougher level direct cash flow statement would be much easier and cheaper to produce. This would mean that only cash receipts from customers and cash paid to suppliers and employees would be reported separately.

The additional costs related to the second indirect approach are very much related to the entity's current way of producing the cash flow statements. If Excel spreadsheets are used, more professional database solutions that are tightly linked to the other parts of financial consolidated accounts would be recommended in order to cope with the new proposed requirements. The costs of modifying the existing cash flow models can also be remarkable depending on the flexibility of current IT solution. According to our assumptions, the additional costs would be from tens of thousands of euros up to one hundred thousand euros. The costs could be kept on a more reasonable level, if there would not be too many changes compared with the current report formats. For example, if the handling of business combinations (so called basket transaction) is changed simultaneously, the costs of implementing the changes will increase.

7 April 2009

According to our understanding hardly any companies use the first alternative for generating the cash flows directly from the cash book or from cash management system. If this alternative is chosen, a lot of IT investments would be required because very few transaction based systems support this kind of automatic "tagging" of cash flows directly from the entity's bank statement. The whole processes of handling the purchase and customer invoices and payments in debtors' and creditors' should also be reviewed and modified. This can turn out to be very expensive up to several hundreds of thousand euros. The costs may be slightly reduced, if the final cash flow report does not have to be on a very detailed level and if companies would not need to split down the creditor payments into too small line items on the face of the direct cash flow.

#### **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?**

This question was answered together with question 19.

#### **Questions 21-22**

No comments

#### **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.**

The proposed reconciliation schedule is a very interesting idea. However we are very concerned with the practical implementation issues related to this new proposed disclosure report. The strict line-by-line reconciliation of the statement of cash flows into the statement of other comprehensive income would really be challenging to do and automate. The information related to the changes in assets and liabilities (categorized into a) accruals, allocations and other, b) recurring fair value changes and c) all other)

7 April 2009

would also be very difficult to capture and more data should be gathered from reporting entities in order to produce this level of analysis on the consolidated group level. Is all this level of detail really necessary and who will have time to study all these disclosures? We do not see that the benefits related to this new report would exceed the costs related to practical implementation.

**Questions 24-26**

No comments

We are happy to discuss these practical issues on a more detailed level, if the need arises.

Best Regards,

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