LETTER OF COMMENT NO. 70

ACCA

International Accounting Standards Board
30 Cannon Street
London
EC4M 6XH

Our Ref: TECH-CDR-845

9 April 2009

Dear Sirs

Preliminary views on financial statement presentation

ACCA (Association of Chartered Certified Accountants) is pleased to have this opportunity to comment on the above discussion paper which was considered by ACCA's Financial Reporting Committee and I am writing to give you their views.

General observations

Our overall view is that while this is an interesting discussion paper (DP), the radical change envisaged is not likely to be justified by any benefits that would be gained.

The proposals would mark a major change to the presentation of the balance sheets (statements of financial position) of all entities. The primary segregation would no longer be between assets and liabilities, but a segregation between business assets and liabilities on the one hand and financing assets and liabilities on the other. The main change in the statement of cash flows would be to end the currently predominant indirect method in favour of the direct method and to change entirely the concept of investing cash flows. For the Statement of Comprehensive Income there would be a single statement instead of the current option for a two statement approach.

The main justification of the proposals is that presentation currently is too variable and that some (but perhaps not all) analysts would like to see a greater cohesiveness between the different financial statements.

We see the main disadvantages of these proposals being that they appear to be providing too rigid a format to deal with the variety of business entities using

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IFRS while the importing of large amounts of detail onto the principal statements could result in the overall position being obscured.

Nor does the discussion paper properly address two key issues that are significant for the progress of other IASB projects. Firstly, how to present appropriately fair value changes as compared to the main transactional cost based results and secondly, the principle which should govern what is shown in other comprehensive income (OCI) as compared to being included in profit for the period.

We would make the following other general points

- It is not clear how fixed and prescriptive certain aspects of the statements are intended to be, such as the names and headings or the order of items, as well as whether preparers would have the ability to add further items, columns or subtotals. We would favour there being some degree of flexibility in these respects, as with the current IAS1.
- The DP does not appear to cover a number of issues such as reclassifications from one category to another, changes of formats from period to period or the question of whether items might be recycled from one part of the SOCI to another
- The field testing of these proposals will be very important and should be widely based so that a variety of sectors and jurisdictions are included.
- The interaction with software such as XBRL is not explored. Our understanding was that this should make rigid formats and rules unnecessary as users can develop the presentation that suits them best, as long as the right building blocks are provided.

Draft responses to questions asked by IASB/FASB

1. Objectives of financial statement presentation

Generally we would agree with these objectives, but note that they should not be pursued too far, but need to be kept in balance. The more general qualitative characteristics in the conceptual framework should not be overlooked, such as the understandability of the accounts. The DP refers to information to estimate future cash flows. We would note that there are other objectives such as reporting by management on their stewardship of the company

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Cohesiveness – while we appreciate it does allow some 'read across', the different financial statements are trying to do different things. For example the cash flow statement might support the concept of 'free cash flow' by separating the operating cash flows from the results of all sorts of investing (PP&E, R&D, intangible assets). On grounds of cohesiveness with the other statements this will be lost and will be limited to the returns from and purchase of non-core investment stakes.

Disaggregation – there is a risk this could be extended such that the primary statements are filled with a great deal of detailed information much of which will be immaterial or insignificant.

Financial flexibility – while we agree with this we are not sure that accounts have attempted to reflect the ability to raise capital (paragraph 2.13).

2. The separation of business activities from financing activities

We accept that financial statements need to reflect this fundamental approach to the analysis of business performance and financial position. Companies might however, most naturally start with the distinction in the income statement rather than in the balance sheet as required in the DP's approach. We are less clear that this is an improvement to the balance sheet presentation. There are advantages in highlighting what the company sees as its sources of finance, but on the other hand the emphasis on the solvency position and the liquidity margin in the current approach would be lost. The information would be available, but with less prominence in the main statement.

3. Separate equity section

We agree that there should be a separate statement of equity.

4. Separate section for discontinued activities

We agree. There are significant implications for two important analytical measures – the estimation of future cash flows and of sustainable earnings – where the identification of discontinued activities is a vital input.

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5. *Management approach to classification as business or financing*

We agree with the management approach. The activities of companies are too diverse for one approach to fit all. The accounting policies should set out both the basis of the distinction as well as its rationale.

6. *Assets and liabilities to be presented section-by-section*

As noted above we are not clear that this is a significant improvement in presentation. An insufficient case for this change has been made.

We are concerned for example that some difficult cases have not been dealt with. For example pension scheme assets and liabilities should perhaps be divided up in the balance sheet between the obligations and the assets set aside to meet them which would therefore allow a similarly unbundled presentation in the income statement (as is done now). On the other hand the current net presentation in the balance sheet appears to be the most appropriate at least for certain kinds of pension arrangements (such as ring-fenced separately administered schemes). Some other long term provisions for decommissioning might be in a similar position when it comes to the income statement presentation.

7. *Operating/financing distinction should be at a segment level*

Only in rather diverse groups is this likely to be a significant issue otherwise we would expect that there might be consistent allocation of assets and liabilities between business/investing and operating/financing. The requirement will in diverse groups lead to more complex balance sheets with more line items and users may find it confusing to have apparently similar items appear in several places in the balance sheet. However we appreciate that this will allow for greater coherence between the consolidated statements and segment information.

8. *Changes to segment information requirements*

We note that the DP moves in a number of ways in making the operating segment information the fundamental building blocks of the financial

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statements. While we agree that this is right as it corresponds to many analytical approaches, there are implications for the segment information provided. It seems wrong for example for segment information to be based on different accounting principles than the consolidated numbers, or for the reconciliation of the segment numbers to the consolidated numbers to be as incomplete as in IFRS8. We agree that there should be a revision of IFRS8 as part of this project.

9. Definition of business section and operating v investing categories

This is not a helpful distinction. It seems to be about non-core activities principally taking strategic stakes in businesses (associates or less). This would probably be unusual at best and perhaps a category no-one would want to use Other sorts of investments (government bonds etc.) might be hard to distinguish from financing assets. The labelling appears rather mismatched and the whole section would be better off called operating with subdivisions for core business and non-core (if this category is needed at all). This sort of distinction might be better covered in the management commentary than in the financial statements themselves.

The use of the title 'investing' then has detrimental knock-on effects for the cash flow statement where investing cash flows cannot then include buying businesses, new plant and equipment or development on grounds of cohesiveness.

We agree that the business section should be the default category.

10. Definition of financing section

We agree with the definitions and the management approach to categorisation.

While we would expect the vast majority of items here would be financial instruments, it seems possible that some non-financial liabilities such as pension obligations, long term decommissioning liabilities might be included by some entities as financing.

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11. Presentation of a classified balance sheet

We agree with these proposals for the short term and long term distinctions and would expect that the great majority of entities will be able to report on that basis. We deal with tax allocation under Q17 below but note here that there may be significant problems with identifying long and short term elements of deferred tax for example.

12. Cash equivalents will be reported separately from cash

We agree with these proposals. In UK standards separating cash from so-called cash equivalents has been a more helpful treatment for the cash flow statement for instance.

13. *Assets and liabilities measured on different bases should be shown separately*

While we would agree with this as a general objective the application needs to be within reasonable bounds. IFRS contains many slightly different measurement bases and so for these purposes different bases of measurement should be kept fairly broad. We would not expect for example that property plant and equipment measured at amortised cost would be distinguished on the face of the balance sheet from those that are impaired and so measured at either fair value less cost to sell or at value in use. In many cases items on different measurement bases can be distinguished in the notes to the financial statements. The DP's proposals in this and a number of instances, risk confusing the user and obscuring the picture given by the accounts with very extensive analysis provided on the face of the primary statements.

14. A single statement of comprehensive income

We agree that there should be a single statement to include all components of performance and we also support the retention of a profit for the year line within that.

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However the inherent limitations of one measure of performance needs to be acknowledged. Providing alternative measures including key performance indicators in the management commentary (MC) section of the report to shareholders is very important. Equivalent urgency needs to be given by IASB to advancing the MC project as to developing these proposals.

As noted among our general comments we would like to see more flexibility about the presentation than it appears in these proposals, especially with what is in the notes and what has to be on the face of the statement and the degree to which extra information can be added.

15. Categorise the components of OCI

We do not agree with these proposals. OCI is a specified category and items are included there and not under the other headings. There seems no reason to imply that they have been misallocated and should really be part of financing or business. Items such as actuarial gains and losses on defined benefit pension schemes will be difficult to allocate. As noted above among our general comments there is no principle being established as to what should be in OCI.

16. Disaggregation of income and expense by nature and by function

We can see merits for both disaggregation by function and by nature depending on the objectives. In terms of co-ordination with the cash flow statement and in the estimation of future cash flows a disaggregation by nature is likely to be more helpful, while co-ordination with segment analysis will be aided by a functional analysis. We therefore agree with these proposals, but would prefer if some of this was provided in the notes to the financial statement and not on the face of the statement of comprehensive income (SOCI).

17. Presentation of income taxes in SOCI continue as now

We agree with the proposals. Allocation of tax to elements of income and expense can be difficult and arbitrary. Dividing tax effects between operating and financing sections is not needed. The separate estimation of tax on discontinuing operations is important for the estimation of sustainable earnings and likewise for elements in OCI given that some of these may not be recurring.

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18. Allocation of currency gains and losses among different categories and sections

Any analysis of gains and losses can be improved by a full rational allocation of items to their proper category. However as with tax, the allocation of foreign currency gains and losses is not commonly done at present and so this new requirement would involve significant costs to preparers. We are not convinced that users would gain significant extra benefits from the process, given that to a large extent the allocations might be arbitrary.

19. Use the direct method of presenting cash flows

The current option should be left as it is. While the direct method does appear to provide more information and be more cohesive with the SOCI, it may not always be more useful for analysts etc. and may entail more costs to prepare

20. Costs of the changeover to direct method

Any costs we would expect to be primarily one off conversion costs.

21. Treatment of "basket transactions" in SOCI and Statement of cash flows (SOCF)

The most likely sort of basket transaction is an acquisition or disposal of a business. The best treatment would be a one line approach, with appropriate breakdown in the notes to the financial statements. This would be simpler and will communicate the effects more clearly. We prefer alternative C.

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22. *Disclosure of maturities of short term contractual assets and liabilities*

We agree with the proposals in principle, but note that IFRS7 already covers this area and are not sure that any changes are needed here. We would like any requirements of different standards properly integrated without duplication.

23. *The proposed reconciliation schedule*

This is going to be a very extensive and complex disclosure and we doubt that much of the information included in it will be sufficiently useful to justify the costs of its preparation.

There is information here that it is important here, particularly the fair value re-measurements and any unusual and infrequent events. However these will be given too little emphasis by being included among so much else.

24. *Disaggregating changes in fair values*

We agree that this will need to be addressed. The mixture of fair value and historical costs is considered a major issue and so improving users' understanding the effects of fair value is vital.

25. *Alternative reconciliation formats*

We are not yet convinced of the need for either the proposed reconciliation format or either of the alternatives.

26. *Unusual or infrequent events*

Unusual or infrequent events are often highly relevant information for any analysis of future earnings or cash flows. We would prefer to see the flexibility in the format of the SOCI and SOCF to allow unusual items to be given greater prominence in the financial statements than a memo column in the reconciliation schedule suggested in the DP.

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Yours sincerely

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