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Dear Sir

<u>Comments on Discussion Paper - Preliminary Views on Financial Statements Presentation</u>

The Zambia Institute of Chartered Accountants welcomes the opportunity to comment on the International Accounting Standards Board (IASB)'s Discussion Paper – Preliminary Views on Financial Statements Presentation.

Our comments on the some of the questions on the exposure draft are as follows:

Chapter 2: Objectives and principles of financial statement presentation

Questions:

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.

Comment

The objectives would assist the understanding of an entity's financial statements. However, the paper should be mindful of the fact that forecasting tools have inherent limitations. This objective may be clouded by the seemingly detailed need to disaggregate in view of the *New reconciliation schedule* and the *accrual accounting* which at best is still a Framework ED.

2. Would the preparation 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?

Comment

The separation principle would entail that the business and financing activities be subjected to the *causative cash flow principle* and or *allocating, apportioning* and *eventual absorption* of the cash flow across the two activities. The end result may confuse the users, this being akin to follow the cash flow.

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?

Comment

The presentation of equity as a separate from the financing section should encouraged since this line item rarely changes and when it does the injection of the additional capital should stand out. A note must accompany the injection with the reasons disclosed.

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?

Comment

Discontinued operations must be disclosed with the associated cash flows. Not to follow this objective would defeat the other objectives as set out under paragraphs: 2.6, 2.7 and 2.12, the very bed rock of the Preliminary views on financial statement presentation.

- 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?

Comment

Yes. Provided the guidance given in the standard is sufficient, as it appears in this discussion paper

(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?

Comment

No. The management approach would result in considerable loss of comparability if it can be demonstrated that it would result in significantly different classification of an item within the **same industry**. (par 2.40) With sufficient sector guidance or knowledge, plus audits, the potential loss of comparability, even the one across industries, is apparently tolerable.

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?

Comment

Yes, to the extent that items (assets and liabilities) that are used similarly in an entity will be grouped under the same heading.

However there are ratios that are computed currently which may require re-aligning or further summing of figures. Liquidity ratios are a good example. e.g. where a manufacturing firm obtains an overdraft to finance its working capital needs, it is still meaningful to compare the level of, say, trade receivables (an operating item) with the outstanding overdraft (a financing item) - see examples in par 2.40

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 entity level? Please explain.

Comment

Reportable segment level is favoured. For purposes of consistency, ease and meaningful analysis of such a diversified entity as a whole, and the analysis of its individual segments, it is more informative to apply the same level of classification at the entity and segment levels

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 classify 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

Please explain.

Comment

Assets for each section is recommended. This may result in disclosing a lot of information but, for reasons advanced in question 7 above, this proposed level of disclosure is achievable and will be worthwhile.

Chapter 3: Implications of the objectives and principles for each financial statement

15. 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.

Comment

As regards the section in which Income taxes should appear within the statement of comprehensive income, it is our submission that the current requirements as elaborated in paragraph 3.55 of the discussion paper on Preliminary views on Financial Statement Presentation, Income taxes should appear in the relevant business and financing sections of the statement of comprehensive statement of income.

Our response is anchored on the premise that decision-usefulness in financial statements will be better served when taxes are allocated to sections most related to either the business or financing sections and most relevant categories in those sections. Such treatment will be most helpful in tax planning as users will see which sections are attracting what type and level of income taxation. Users can then ask leading questions that may help management practice their stewardship function better.

It is therefore necessary to maintain the status quo.

- 16. 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 liabilities that rise to the gains or losses.
 - (a) Would you 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.

Comment

I agree with the contents of paragraph 3.63 on foreign currency transaction gains and losses. I think the position in the said paragraph would help with presenting decision-useful financial statement to capital providers because it would be easier to interrogate the decisions leading to significant foreign currency transaction gains and losses that are appearing in either the business or financing sections of a relevant statement in the financial statements package.

One alternative presentation is to have a line in the comprehensive income statement showing a net position of gains and losses irrespective of whether they originate from business or financing activities with a note showing the break down or make-up of the net position in the stand alone line in the statement of comprehensive statement.

(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?

Comment:

No comment.

- 17. 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?

Comment

Yes, we agree with the proposal in paragraph 3.75 in the use of a direct method of presenting cash flows on account of the following points:

- It is more straight forward and easier to understand for non-accountants
- The specific recipients and payers of cash/cash equivalents are stated as suppliers, customers, employees or other
- The impact, cash flow-wise of the entity vis a vis its partners and contacts is clear for any intelligent layman to discern
- (b) Is a direct method more consistent with the proposed cohensiveness and disaggregation objectives (see paragraphs 3.75 -3.80) than an indirect method? Why or why not?

Comment

Yes, the direct method of presenting cash flows is more consistent with the cohesiveness and disaggregation objectives.

This is so because of the fact that the items consuming or generating cash are stated plainly as opposed to the aggregation you have in the indirect method especially in regard to the "working capital" elements changes.

(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?

Comment

Yes, some of the information currently required for use of the indirect method will be required e.g. depreciation and other accruals.

As an alternative, it may be necessary to have perhaps on an optional basis a requirement for reconciliation between net income and operating cash flows as is currently required using the indirect method of cash flow statement presentation. This would be for reconciliation purposes only as an additional detail under the Statement of Cash flows.

18. What costs should the board 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?

Comment

The initial cost of designing and changing huge accounting systems in order to make them respond to the ease with which to prepare cash flow statements on a direct method may be too colossal and cannot be over-emphasised. Apart from set –up costs continual re –orientation of accountancy school graduates to work with a system that favours the direct method may be a recurring cost!

The Institute will be ready to respond to any matters arising from above comments.

Yours faithfully

Modest Hamalabbi **Technical Officer**