



Email

Sir David Tweedie
Chairman
International Accounting Standards Board
30 Canon Street
UK – London, EC4M 6XH

Brussels, 7 April 2009

Subject: *EBF Comments on the Discussion Paper “Preliminary Views on Financial Statements Presentation”*

Dear Sir David,

The European Banking Federation¹ would like to thank you for the opportunity to comment on the Discussion Paper (DP) on financial statements presentation. While in general the EBF agrees on the overall objectives as set out in the paper, we are concerned that the proposals do not appear to meet the set objectives. We are sceptical about whether the information requirements proposed in the Discussion Paper are of benefit to users in respect of the financial statements of banks. As many of the requirements are not particularly relevant for banks, but nonetheless must be presented in the Primary Financial Statements (PFS), we would question whether it can be said that users will be placed in a position of better understanding. Information which is not useful should not be displayed. We encourage the Board to seek further comments from the users of banks' financial statements (e.g. banking analysts) and the treasury departments of banks regarding the usefulness of information provided in the proposed format as we are not convinced that presentation needs from a banking perspective were sufficiently discussed, analysed and is reflected in the discussion paper.

International Financial Reporting Standards should not be limited to an investor-oriented approach but serve multi-tier purposes in the framework of an integrated reporting system. In the case of a bank, users will be interested in other forms of reported information, including risk and liquidity figures.

We believe that accounting information should serve as a common basis and that the differences between financial and regulatory reporting should be limited to those areas where the different objectives of the two regimes necessitate a different approach. We also believe

¹ Set up in 1960, the European Banking Federation is the voice of the European banking sector (EU & EFTA countries). The EBF represents the interests of some 5000 European banks: large and small, wholesale and retail, local and cross-border financial institutions.

that the discussion paper should have taken the links to other IFRS standards into account to a greater extent. This is particularly true given that most of a bank's balance sheet will fall within the scope of IFRS 7.

We agree that trying to achieve a certain amount of cohesiveness within the principal statements will improve the usefulness of the information provided. An entity should also present information in its financial statement in a manner that faithfully portrays the financial picture of its activities. In this respect, we recognize that imposing a rigid classification of the various line items into categories may improve the comparability. However, we are concerned that it may not improve the users' understanding and may not reflect the way business is managed in certain industries. As most of the transactions on the financial services industry are of an operating nature, the relevance of the distinction between operating, investing and financing is very limited.

We consider many of the new requirements proposed in the discussion paper as restrictive, too detailed and too prescriptive. Requiring specific headings, subtotals and reconciliations may not give decision useful information for each industry. If information is not relevant, it should not be disclosed. In our opinion reporting should reflect the information that management uses for making operating decisions. As such, we believe that a management approach would provide a useful view of an entity to stakeholders as it allows the users to see how management applies the IFRS principles and permits performance to be assessed based on the way in which the business is managed.

One of the objectives of the presented discussion paper aims to provide decision-useful information in predicting an entity's future cash flows.

Providing decision-useful information is a key objective on which the discussion paper is funded to justify the requested information on primary financial statement and footnotes. We would appreciate that a definition of "decision-useful" is given, what would facilitate the exercise of judgment in appreciating the relevance of the prescription of accounting information to be disclosed and especially the statement of cash flows for the financial industry.

We do believe that the liquidity issue is currently one of the major challenges for the banking industry. When it comes to a bank, however the cash flow statements do not provide a particularly useful means of assessing its economic future. Future cash flows cannot be forecast only on the basis of accounting information as they result from the assets and liabilities that compose a balance sheet as of a specific date, but also from the future production of loans and its appropriate funding. The direct method statement of cash flows and the reconciliation schedule to the statement of comprehensive income is not relevant for banks. The cash flows statement provides historical information but gives little idea of banks' liquidity risk exposure. A cash flow statement is unlikely to provide information on banks' ability to manage its liquid resources.

The use of a direct method for presenting cash flows in the statement of cash flows for the banking industry will be very expensive and will give neither additional nor consistent information. If there are users who consider that direct or indirect method cash flow statements are relevant for their analyses on banks, then we would find it helpful if they could relate how they would use them. We suggest the IASB makes further enquiries in this regard.

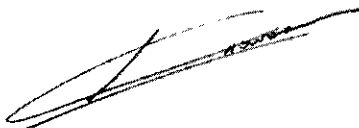
Last, but not least, we believe that comprehensive income and net income should be disclosed separately. The presentation of the components of comprehensive income under a single statement increases confusion for the reader since it may be read that comprehensive income represents the value created during the reporting period (especially when income per share is calculated on net income). We therefore suggest that the choice currently offered to entities to present the statement of comprehensive income under one or two statements should be retained.

We are disappointed that the discussion paper has failed to provide a model suitable for use within the banking industry. We remain convinced, however, that such a model can be developed within the parameters of a single standard on presentation.

The Board may also care to consider whether progress towards the use of XBRL may enable the adoption of more than one approach to presentation without removing the ability of users to make cross-industry comparisons using a standardised analysis of non standardised formats. The EBF acknowledges the current involvement of the IASCF in XBRL and favours an increasing involvement of the IASCF and the IASB in this language.

You will find enclosed our answers to the questions raised in the Discussion Paper (*see D0124F-2009*). We hope you will find our contribution useful and will be happy to provide you with further details on any point raised in our response.

Yours faithfully,



Guido Ravoet

Enclosures: 1 + 2

ANSWERS TO THE QUESTIONS RAISED IN THE DISCUSSION PAPER

- 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.**

The objectives of general purpose financial reporting related to entities of any kind, including banking institutions, is to create a communication framework to assist users in making economic decisions, to assess the accountability of management for entrusted resources and to provide present and potential investors, creditors and other users with useful information about the entity’s financial performance and financial position, enabling them to evaluate the entity’s ability to generate cash flows. Such information includes indications about the timing and uncertainty of cash flow generation and the entity’s ability to make distributions under the legal framework in which it operates. In order to meet these objectives, this information has to be relevant, reliable, understandable and comparable.

The financial information shall have predictive value to enable users to forecast future cash flows. We have identified two types of information that may be required from users:

- (a) Information on the ability of the entity to generate cash flows in the future in order to produce a dividend stream, or to be in a position to reimburse debt or meet other liquidity commitments. This exercise requires providing information on historical and existing transactions, enabling users to make projections of the cash flow impacts of potential future transactions; and
- (b) Information on elements that will enable users to make their own estimates of the current value of the entity in order to make arbitrages.

Cohesiveness objective

We agree that a certain amount of cohesiveness between the PFS (principal financial statements) will improve the usefulness of the information provided. However, imposing a rigid disaggregation of the various line items will overly complicate the financial statements and will not improve the users understanding in particular when the line is not applicable or material. Information that is cohesive at a line item level is not always more decision useful than information that is not. Adherence to the cohesiveness and disaggregation principles should not be at the expense of the provision of decision useful information. In our view:

- The scope of the Discussion Paper (DP) should be limited to the PFS i.e. the three statements described in the DP.
- The principles of “faithful representation, relevance and materiality” which are described in the Framework should be applicable so that the future standard should remain principle-

a.i.s.b.l.

based. The cohesiveness principle should not be applied at the line level because it goes against the more fundamental principles of faithful representation, relevance and materiality.

- The financial statement presentation standard should be consistent with other disclosure requirements in existing standards, including especially IFRS 7.

Shareholders, investors, analysts, management, lenders, employees, state organisations, financial regulators and the public are interested to see overall performance to be able to judge how a bank has performed compared to its peer group as a basis for an investment decision.

In the banking industry, core operations can be divided between on-balance sheet activities and off-balance sheet activities, which represent a significant amount of the transactions. The off-balance sheet activities consist primarily of fee-based activities for services rendered on commitments that are not recognized on the statement of financial position. This type of activity therefore creates income and cash flows but rarely create an asset or a liability.

In this respect, we consider that the proposed presentation does not allow a cohesive and comprehensive financial picture since there is no clear relationship between items across the financial statements regarding some material off-balance sheet transactions. We are concerned that the specific activities of the financial sector would not be properly reflected in financial statements prepared on the basis of presentation proposed in the DP.

Disaggregation objective

We would like to make the following comments:

- We agree that an entity should disaggregate information in its financial statements in a manner that makes it useful to the users. Although we support the objective of disaggregation, we do not think that presenting more information on the face of the PFS (instead of in the notes) will be beneficial to the users' understanding.
- As we believe that the objective of financial statements are broader than merely assessing the entity's ability to generate net cash flows we are not comfortable with the proposal that the focus of the disaggregation objective should be limited to information that is useful in assessing future cash flows. We therefore suggest to reword paragraph 2.7 as follows:

"An entity should disaggregate information in its financial statements in a manner that makes it decision-useful to the users".

Liquidity and flexibility objective

We agree with the objective and have no further comments.

- 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 question whether such presentation will provide information that is more useful than the current presentation method for the statement of financial position used by most financial institutions. The separation of business and financing activities in the financial services industry would not be meaningful and we expect it would result in presenting almost all activities within the business activities (operating category), as by virtue of the character of the banking business, most of the transactions in the financial services industry are of an operating nature.

- 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 agree that the equity should be presented separately as proposed by the boards.

- 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?**

We agree on the proposal for presenting the discontinued operations in a separate section, as the information on discontinued operations is helpful to users when they are isolated from the entity's continuing operations. In our view, this will be in line with the management approach and will enable entities to faithfully present its operations.

Presenting the discontinued operations in a separate section will be consistent with the objective of IFRS 5, which is to provide users with information about the discontinued operations that have been part of the reporting entity but are not going to be part of the entity's continuing operations in the future.

- 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?**

Although we do not fully support the proposed presentation model due to its irrelevance for banks, we do believe that if a breakdown is to be made, the management approach would provide users with the best decision-useful view of the entity. Management approach is the best way to carry out the business model principle and to show the intention of the management in the PFS.

(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?

We do not believe that the management approach will necessarily lead to a decrease in comparability compared to the current situation. Comparable values would not give sensible and meaningful information if they do not reflect how the assets and liabilities are used in an entity's business model. The practical outcome of comparable information would be questioned if financial statements would not reflect the reality behind the business and the way entities are managed. The management approach should be seen as a strategy decided and followed by management in a consistent and transparent way in accordance with the rules set in internal and external documents of the entity. This should be made clear in an entity's accounting policy note in the notes to the financial statements which include the policies for classifying its assets and liabilities.

The management approach could even lead to an increase in comparable contents if not in comparable layouts.

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?

We do not believe that separating information into sections and categories will make it easier for users to calculate financial ratios in the banking industry. As far as we can see, a bank's activities would principally, if not exclusively, be found in one single section since banks would not have few if any activities in the financing section. The relevance of the division for banks is therefore limited and will not enhance the reader's understanding.

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.

Assets and liabilities should be classified at the level of the entity. This should be in relation with the management approach as assets and liabilities may be classified based on the

business model employed. We believe that segment reporting should be out of the scope of the DP since it is defined by another standard.

- 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.

Segment reporting is defined by IFRS 8 and should be kept at the disclosure level, not at the PFS level. The scope of this discussion paper should be limited to the presentation of PFS. We recommend that the Boards deal with the segment reporting disclosures in the framework of the relevant standard.

- 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 appreciate that the definitions were defined in line with the principle-based approach and we believe that by using the management approach, assets and liabilities can be classified properly in accordance with what the management considers as central operations of an entity. We expect that this will provide more useful information to users than a narrow or prescriptive definition of operating and investing categories.

We also agree on the view expressed in paragraph 2.64 that the operating and investing categories should be based on a notion of ‘core’ and ‘non-core’ activities.

- 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?**

We believe that the definition is not appropriately defined as it excludes non-financial assets and liabilities from being used in the financing category. It could be the case that financing is provided from liabilities which are not financial in nature or are outside of the scope of IAS 32 and 39, but management consider them as part of its financing activity.

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?

We expect banks would not present a classified statement of financial position. In respect of banks, presentation by order of liquidity provides better information in terms of liquidity risks and is in line with the way a bank manages its assets and liabilities. An arbitrary segregation of assets and liabilities into short term and long term would not add any useful information.

(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?

No. Most financial institutions currently present a statement of financial position in order of liquidity. This is not an area where more guidance is needed.

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?

Yes. Cash equivalents should be considered as financial assets.

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?

We believe that a relevant disaggregation for the financial industry would consist of classifying the balance sheet into financial instruments and non-financial instruments further disaggregated according to their classification and by the type of instruments taking into account the entity's business model.

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?

No. We do not agree with the concept of a single statement approach. An item of income needs to be kept disclosed separately from owner changes in equity both for accounting and

economic reasons. The information included in the statement of comprehensive income (net income or profit and loss) is different in nature from the components of other comprehensive income (OCI).

Aggregating non-owner changes in equity and net income in a single separate statement is confusing as some of the OCI will never become part of the profit and loss and OCI shows a potential benefit (or loss). Users may believe that the total is meaningful, while other non-owner components (cash-flow hedges and valuation reserve, for instance) have been specifically excluded from the income statement as they are not contributing to the measure of the entity's performance. Banks do not want to show a mixed result combining recurring and non-recurring items.

In addition, the proposal to present a single statement of comprehensive income effectively eliminates the available-for-sale category. According to the standard, gains and losses arising from a change in the fair value of available-for-sale financial assets should be recognised directly in equity while gains and losses from the instruments designated at fair value through profit or loss are recognised in the statement of comprehensive income (net income or profit or loss). We believe that moving to a single statement will eliminate the distinction between market fluctuations recognised in equity and the results for the period. We believe that the option to present two separate statements should be maintained.

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 are not convinced that further disaggregation of other comprehensive income by category would be useful.

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 for 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?

We support disaggregation to the extent that it does not result in the primary financial statements becoming cluttered with information that is not useful or that can be disclosed in the notes to the financial statements. Any disaggregation should reflect the business model and the management view.

As explained by the IASB in paragraph 3.52 of the discussion paper, banks usually disaggregate income and expense items by nature only, as further disaggregation by function would not provide any decision-useful information but merely imposing an unnecessary extra workload. By disclosing performance information both by function and by nature would not

significantly improve the understanding of the entity's performance – especially that of a bank.

We believe that the current disclosure requirements under IFRS 7 provide useful information in predicting future cash flows arising from liabilities. From the point of view of financial institutions, these requirements result in the provision of better indicators of performance, i.e. in the provision of more useful information for users as capital providers.

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 do not support the allocation of income taxes to sections and categories. Income taxes should be maintained in a separate section as disaggregation will decrease the degree of comparability and cohesiveness as comparability is easier if the amounts exclude the income tax effect. Providing more details about the income taxes in the proposed statements would generate much more complexity in the figures as income taxes would have to be arbitrarily allocated into each of the sections. This is because income tax is not merely a sum of all the income taxes resulting from each transaction but is influenced by the verity of other factors. Disclosures provided on income taxes (IAS 12), especially within the reconciliation between expected and actual tax, already provide enough information on the discrepancies between theoretical and current tax expenses.

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 re-measurement into its functional currency, in the same section and category as the assets 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?

a) We do not think that it would provide decision useful information as it does not represent the way the FX risk is managed. For example, presenting foreign currency transactions gains and losses into the different sections and categories might lead to natural hedges being presented into separate sections or categories. As the transaction hedged and hedged items belong to the operating activity, the foreign transaction currency gains and losses will be in operating with the results of the structural exchange rate position possibly in financing. This may lead to a higher perceived volatility where there is only a presentation mismatch.

In addition, any allocations would be arbitrary and costly to implement. We believe that the current disclosures provided in the notes to the financial statements provide sufficient and adequate information. In line with our response to question 17, such additional details may make the financial statements more obscure rather than being more informative.

- b) - IT systems will have to be changed as currently the FX risk is managed and accounted for in different way
- Trainings to be provided, etc.

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?**

- a) A bank's performance is often based on its ability to manage the transformation of short term deposits into longer term credits. The cash flow statement gives information on the type of transactions that provide or use cash. It therefore presents a restrictive view of the processes that create value in banks since the proportion of transactions settled by cash or via current account of customers¹ is arbitrary between periods. Measuring banks' performance by means of the cash flow statement has little relevance and could be compared to measuring an industrial entity's performance with in- and outflows of inventory.

Cash flow statements in the banking industry do not provide the reader with the information on the entity's ability to generate future cash flows and anticipation of liquidity risks. Banks manage their liquidity risk on a day-to-day basis. The cash flow statement provides information on the current period but does not provide much perspective on the liquidity risks incurred by the reporting entity for the next period, which is the relevant information users are looking for. The IFRS 7 requirements related to liquidity risks already give adequate information about the future cash flows and liquidity risk in the banking industry.

¹ Cash often has broader meaning in the banking business when IFRS principles are applied in practice. Generally when IFRS standards mention cash flows banks also have to take into account settlements via the current account of customers. For example, IAS 39 defines effective interest rate as "the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument". Payments of loans are typically received from the current account of customers. Inconsistencies between cash flows and definition of cash across all the standards should be reviewed.

Generally, a cash flow statement – whether based on the direct method or the indirect method – is of no use for banks internally or externally. It is particularly the case that for the trading portfolio the direct method is not in line with the way the instruments especially derivatives are managed. Providing collateral in this business field often equals to cash payments.

As cash flow statements are not relevant for banks, we recommend that they be optional for them.

- b) It could be argued that an advantage of the direct method is that cash flows generated within an entity are shown directly and without any adjustment in the cash flow statement. In this way, users would be provided with information on the entity's complete cash flows. However, such presentation is not suitable in every case for supplying decision-useful information that allows users to correctly interpret current cash flows and predict future cash flows. This is clearly illustrated by the cash flow statement presented by a bank. Because of the banks' payments processing function, a direct method cash flow statement would completely overstate cash flows. After all, processing payments for customers does not trigger any increase in a bank's own liquidity. Yet precisely this is what the direct method would suggest, so that it would plainly be at odds with the principles of decision-usefulness and fair presentation.

Appendix 1 (*see D0057A-2009*) sets an example of opening statement of financial position and a set of the most common transactions (excluding securities business) for a bank during a certain period of time. At the end of the period statements of comprehensive income, cash flows and financial position are prepared. This example shows that the information presented in the line items of the cash flow statement prepared using the direct method cannot be used for analysing bank's performance.

In business practice today, the presentation of a cash flow statement based on the indirect method is the norm for the operating segment. This is mainly because under this method cash flows can be derived from the accounting data already available. The indirect method therefore imposes much less of a workload in terms of data capture and data acquisition than would be the case with the direct method. Under the direct method, all gross receipts and payments would have to be reported as and when they occur; this would require the implementation of group-wide ancillary accounting, which would be extremely labour and cost-intensive. Whether introducing an obligation to use the direct method can actually produce additional benefits that would justify this enormous investment in terms of manpower and money appears very questionable.

Using the indirect method ensures a link between accrual accounting and cash-basis accounting. In addition, an indirect method cash flow statement is more suitable for showing connections with the other reporting tools for financial statement presentation and therefore also easier to check.

Overall, it may be concluded that the indirect method is superior to the direct method both from a cost-benefit angle and in terms of ability to provide decision-useful information.

We therefore believe that presentation of a cash flow statement based on the indirect method should remain an option preferably for the entities of all sectors, but at least for banks if a cash flow statement is still required. Even if the investing and financing categories are only of very minor importance for banks, we also believe that it would be advisable not to restrict use of the indirect method only to the presentation of operating cash flows. Instead, use of the indirect method should be permissible also for the investing and financing categories. This would allow uniform, consistent presentation of all three categories in a cash flow statement.

Considering the limited relevance of the cash flow statement in general we do not think that there is merit in the considerable additional effort to prepare direct cash flow information. In addition, the entities would not be able to use the high-level summary information. The indirect method serves its purpose to reconcile the balance sheet to the income statement.

- c) Because the cash flow statement is not relevant for banks, the reconciliation schedule to the statement of comprehensive income should also be optional. We do not support the reconciliation of the statement of financial position discussed in the appendix B, as this statement reconciles other statements to the direct method cash flow statement with which we disagree.

The statement of comprehensive income matrix discussed in the appendix B may be relevant when assessing persistence and subjectivity of income and expense items. However column C should include all income and expense items that have been settled either by means of cash or current accounts of customers. This is the way transactions are settled in banks and are not accrued anymore.

The example provided in the appendix to the DP is in our opinion too detailed for the average user.

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?

It is currently difficult to give a detailed estimate of the implementation costs involved. However, we consider that if we would implement all proposed changes in the DP, almost all of the total cost of these changes would be caused by the implementation of the direct method cash flow statement.

The most complex one off modification would relate to the allocation of income between realized and unrealized, in order to split out unrealized income. Banks' systems have not been developed to provide information splitting realized and unrealized income and expenses. We expect that there would be significant one-off costs related to IT changes, labelling or "tagging" all cash flow information to the accounting systems and the training costs. There

will be a need to change the data systems and the way to record the valuation of the instruments. As the statements are consolidated, banks need to adapt the collection process and the way to aggregate data. This may require an additional consolidation system, subject to its proper controls, checks and balances. This system would come on top of the existing consolidation system, whereas indirect method cash flow statements can be derived from existing information on financial flows and financial balances. Therefore, the cost of such a statement would become extremely high.

The ongoing costs would be related to the reconciliation of data and the large volume of details that would need to be tracked permanently. Therefore, additional resources as well as an increased number of employees would need to be involved in the process. This would represent only additional cost without any benefit.

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?

As the DP states, any allocation is arbitrary and costly to implement. We do not believe that allocation of basket transactions is in line with the DP's "management approach" as acquisitions and disposals are rarely done with individual assets and liabilities in mind but at the higher level of synergies and corporate strategies i.e. on portfolio basis. In addition, we consider that allocating the effects of a basket transaction to sections / categories will be impossible since the necessary information is seldom available. They could be on a specific line "non allocated" and disclosed to provide more information, but it implies a loss in the relevance of the primary financial statements.

In terms of presentation, we would choose Alternative B, which consists in presenting in the category that reflects the activity that was the predominant source of those effects and seen as being in line with the management approach. However, as mentioned above, it is expected that in a bank most assets and liabilities would be categorised in the operating section (more in line with approach A).

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?

The information about the maturities of the short term contractual assets and liabilities may be useful information for some entities. For banks, this should not be linked to the presentation of the assets and liability in order of liquidity in the statement of financial position but rather it should be linked the liquidity risk management disclosures.

It is already customary for banks to adopt a contractual maturity breakdown based on the maturities listed in the discussion paper. Generally speaking, we are in favour of transparent

disclosure that provides information which is more decision-useful to the user. For this reason, we believe that the proposed changes are acceptable. The presentation could be based on IFRS 7.39 and IFRS 7.B11, respectively, which already require entities to indicate contractual maturity dates for financial liabilities when disclosing their liquidity risk.

Please also refer to answer for question 11 a).

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.

As, we reject the direct cash flow method we see no need for a schedule in the notes to financial statements reconciling cash flows to comprehensive income. The reconciliation of net income to cash flow achieved by the indirect method provides information on the differences between these two items that users can draw on also to predict future cash flows. While further disaggregation as called for in the discussion paper is technically possible we would question its decision-usefulness.

a) This creates an additional schedule that is not needed. We do not believe that it could increase the user's anticipation of the future cash flows and we are concerned that rather than increasing the users' understanding, the additional information provided in the proposed reconciliation schedule could have the opposite effect and make the financial statements less readable to the average user. Users might need to better understand the detail of the income. For that purpose, rather than a schedule of reconciliation, a more detailed statement of comprehensive income could give the required information.

We believe that the administrative burden to comply with the proposed requirements outweighs the benefits to the users of the financial statements.

b) Either the changes in the comprehensive income or the changes in the assets and liabilities could be disaggregated into the components described but not both. We do not see how this can be implemented in financial institutions with significant trading portfolios or why this would benefit the users understanding of the financial statements. It

would have an excessive cost to provide the same information twice and would be confusing for the users.

- c) As we believe it is not necessary to have a reconciliation schedule, this question is not applicable.

Please see also Appendix 2 (*D0252C-2009*).

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?

We see no need at present for any project to address further disaggregation of changes in fair value.

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?

As we do not believe that the direct cash flow method makes sense for banks, the proposed reconciliation to comprehensive income is unnecessary. We also disagree with the statement of financial position reconciliation, as discussed in Appendix B, paragraph 11. In addition to being complex, it constitutes reconciliation to the (direct) cash flow statement. The statement of comprehensive income matrix, which is also discussed in Appendix B, could be important for assessing the persistence and subjectivity of income and expense items. However, column C also calls for indication of cash flows, which appears problematic for the reasons already outlined.

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) Opinion 30 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?

- a) We believe the current requirements are sufficient.
 - b) Without further clarity of the definition of “unusual and infrequent” items, we would generally disagree with highlighting these events. It is better to have the choice of presenting or not the unusual or infrequent column. If empty it need not be shown.
 - c) This is already permitted under current IFRS. Companies decide which events are important to be communicated to users.
- 27) As noted in paragraph 1.18(c), the FASB has not yet considered the application of the proposed presentation model to non-public entities. What issues should the FASB consider about the application of the proposed presentation model to non-public entities? If you are a user of financial statements for a non-public entity, please explain which aspects of the proposed presentation model would and would not be beneficial to you in making decisions in your capacity as a capital provider and why.**

N/A

Statement of financial position at the beginning of the period

cash	10	deposits from customers	550
loans to customers	500	amounts due to banks	50
loans to banks	100		
fixed assets	20	equity	30
	630		630

Transactions during the year

Transactions connected with loans to customers

	DR	CR
new loans provided to customers via current accounts		deposits from cust.
in cash		cash
loans repaid - all settlement via current accounts	loans to cust.	loans to cust.
	loans to cust.	
	deposits from cust.	
interest income from loans to customers	loans to cust.	interest income
interest received from current accounts of customers	deposits from cust.	loans to cust.
interest received in cash	cash	loans to cust.
fees for servicing the loans received from current accounts	deposits from cust.	fee income
net impairment expense of loans to customers	impairment expense	loans to cust.

Transactions connected with deposits from customers

deposits paid in cash or transferred to other banks	deposits from cust.	cash
deposits received in cash or transferred from other banks	cash	deposits from cust.
transfers between deposits within bank	deposits from cust.	deposits from cust.
interest expense from deposits	interest expense	deposits from cust.
interest credited directly to deposits	deposits from cust.	deposits from cust.
interest paid in cash	deposits from cust.	cash

Transactions connected with amounts due from and to banks

(all transactions are made in nostro accounts in central bank or other banks = cash, usually very short term => high turnover)

loans provided to banks	loans to banks	cash
receipts of payments of loans provided to banks	cash	loans to banks

For CF statement purposes:				
offset due to short term nature of assets (DP3.73)	240			
cash outflows after offset	60			
cash inflows after offset	40			
interest income on loans to banks	5	loans to banks	interest income	
interest received	6	cash	loans to banks	
deposits received from other banks	394	cash	amounts due to banks	
payments of deposits received from other banks	380	amounts due to banks	cash	
For CF statement purposes:				
offset due to short term nature of assets (DP3.73)	300			
cash inflows after offset	94			
cash outflows after offset	80			
interest expense on deposits	6	interest expense	amounts due to banks	
payments of interest	7	amounts due to banks	cash	
<i>Other transactions</i>				
depreciation expense	2	depreciation expense	fixed assets	
acquisition of fixed assets, payment to current account	4	fixed assets	deposits from cust.	
salaries to employees paid on current accounts	5	administrative expense	deposits from cust.	
services purchased, payments in cash	2	administrative expense	cash	
services purchased, payments on current accounts	1	administrative expense	deposits from cust.	
Statement of comprehensive income				
Interest income from loans to customers	40			
Interest income from loans to banks	5			
Interest income	45			
Interest expenses on deposits from customers	-20			
Interest expenses on amounts due to banks	-6			

Interest expenses	-26
Interest margin	19
Net impairment expense	-5
Fee income	3
Depreciation expenses	-2
Administrative expenses	-8
PL	7
Cash flow statement (direct method)	
Loans provided to customers	-10
Interest received from loans to customers	2
Deposits of customers paid or transferred	-200
Deposits of customers received	220
Interest from deposits of customers paid in cash	-1
Loans provided to banks	-60
Receipts of payments of loans loans provided to banks	40
Interest from loans to banks	6
Deposits received from other banks	94
Payments of deposits received from other banks	-80

Interest paid on deposits from other banks	-7
Services purchased	-2
Increase of cash during the year	2

Statement of financial position at the end of the period

cash	12	deposits from customers	571
loans to customers	518	amounts due to banks	63
loans to banks	119		
fixed assets	<u>22</u>	equity	<u>37</u>
	671		671

Postings on the accounts

loans to customers		loans to banks		fixed assets	
DR	CR	DR	CR	DR	CR
500		100		20	
100		300			2
10			280	4	
	90	5			6
40					
	35				
	2				
	5				
650		405		24	
	132		286		2
	518		119		22

depo from customers		am. due to banks		equity	
DR	CR	DR	CR	DR	CR
	550		50		30
	100		394		7
90		380			
35			6		
3		7			

200									
330	220								
17	330								
1	20								
	17								
	1								
	4								
	5								
	1								
676	1247	387	450	37					
571		63							

Appendix 2

Interest income or expense from instruments with initial discount / premium

Paragraph 4.31 defines how items of comprehensive income should be disaggregated into cash and accrual component. Interest income can have cash flows other than contractual interest. (When mentioning cash we refer to different kinds of settlements mentioned above.) This is relevant for cases of debt instruments with origination fees, transaction costs or interests paid in advance or which are purchased or issued with market discount / premium. Should such cash be considered to flow in advance or be just part of net acquisition amount? The issue is illustrated by example.

Debt financial instrument with initial carrying amount, principal 100, 3-year maturity, yearly contractual interest payments at a rate 10% per year. paid on principal 100

- contractual interest income = yearly 10
- interest income from amortisation = yearly 0.9 1.0 1.1
- total interest income calculated by effective interest method = yearly 10.9 11.0 11.1

It is acquired at the start of 1st period and repaid with one principal payment at the end of 3rd period.

The initial discount 3 can come from

- a) origination fee (settled in advance) or
- b) market discount (settled when principal is repaid).

Should such instruments with different sources of initial discount be treated equally in both cases?

In the statement of financial position and statement of comprehensive income they are treated like the same. However the question remains for cash flow statement and thus also for the split of interest income into cash and accrual component.

If they should be treated the same, we would look at the instruments in both cases as if they were effectively the same and acquired in the amount 97 and at maturity 100 would be received. Cash component of interest income coming from the initial discount appears at maturity.

If they should not be treated the same, in case a) asset would be acquired at amount 100 with immediate cash component of interest income 3 (like for deferred income) and in case b) cash component 3 comes at maturity.

Differences in the amounts disclosed are the following:

a) s. b) "Table of split of interest income into cash component and accrual component"

initial discount cash component received in advance

year	interest income	cash component	accrual component
1	10.9	13	-2.1
2	11.0	10	1.0
3	11.1	10	1.1

initial discount cash component received at maturity

year	interest income	cash component	accrual component
1	10.9	10	0.9
2	11.0	10	1.0
3	11.1	13	-1.9

- When we consider opposite situation and initial carrying amount in the example would be 103 (=initial premium) and all other terms are the same as above
 - contractual interest income = yearly 10
 - interest income from amortisation = yearly -0.9 -1.0 -1.1
 - total interest income calculated by effective interest method = yearly 9.1 9.0 8.9

The initial premium 3 can come from

- a) transaction costs (settled in advance) or
- b) market premium (settled also in advance).

In both cases the result is the same because effectively such instrument was acquired at 103 and principal 100 is received at maturity. Cash component always appears at the beginning. So here the question does not arise.

initial premium cash component paid in advance

year	interest income	cash component	accrual component
1	9.1	7	2.1
2	9.0	10	-1.0
3	8.9	10	-1.1

•Such split should then also be provided on the face of the statement of comprehensive income. Such requirement would go too much into detail. Furthermore IAS 39 asks to calculate only the total interest income by effective interest method. It aggregates contractual interest income and the part of interest income (may be negative) from the difference between initial carrying amount and principal. Separation of the 2 components may require a material system changes for many entities.

- Similar issues arise for interest expense from financial liabilities.

- When the principal of the instrument is repaid gradually it is more difficult to follow what is the cash component that is included in the payments of principal. This is relevant for initial discount on financial assets and financial liabilities. (Initial premium both on financial assets and liabilities has cash component at the beginning.) These issues are shown on an example of financial asset which is repaid gradually during its life.

Initial carrying amount = 970 000

Payment schedule

Effective interest rate		11.4599%			
year	principal outstanding	payment of principal	payment of interest	payment total	discounted payment
0	1,000,000				
1	900,000	100,000	100,000	200,000	179,437
2	600,000	300,000	90,000	390,000	313,926
3	0	600,000	60,000	660,000	476,637
					970,000

Split of interest income into contractual and amortisation of discount part

	carrying amount	interest income total	Split of interest income	
			contractual interest	amort. of discount
0	970,000			
1	881,161	111,161	100,000	11,161
2	592,141	100,980	90,000	10,980
3	0	67,859	60,000	7,859
				30,000

The question is what is the cash component of interest income coming from amortisation of discount. The cash component is embodied in the payments of principal with total amount 1 000 000 which are higher than initial carrying amount 970 000. Such difference 30 000 might be allocated proportionately to all the payments.

difference between principal and initial carrying amount = 30,000
proportion to the principal = 3.00%

payments of principal	proportion of the payments = cash comp.	int. income from discount	cash component	accrual component
100,000	3,000	11,161	3,000	8,161
300,000	9,000	10,980	9,000	1,980
600,000	18,000	7,859	18,000	-10,141
1,000,000	30,000	30,000	30,000	0

The general question is whether it is feasible to track in the accounting system accrual and cash components from initial discount / premium determined by correct principles. As shown in the example, problems arise especially in the area of initial discounts which are repaid by principal payments during the life of the instruments.

Interest income from impaired financial assets

Other questions arise in the area of interest income from impaired financial assets. It is difficult to distinguish between cash and accrual component of the interest income determined under IAS 39.AG93. When impaired financial assets are repaid it is impossible to distinguish between cash flows that should be applied to the interest income part. Customer systems of the banks have rules how payments are applied – some banks cover principal, some interest receivable first (depending also on national legal system). But this is used to calculate the whole (nonimpaired) amount of receivable from the client. Therefore it is not usable for IFRS purposes because the amount of impaired receivable is quite different to legal amount of receivable.

So the question remains – should be payments received from impaired loans used to cover

- first interest income part and then the remaining impaired receivable,
- last interest income and the remaining impaired receivable or
- proportionately interest part and remaining receivable part?

Proportionate way would probably be the best.

Even when we find the answer the question remains whether it is possible to apply it in the accounting system.
