To the IASB and FASB regarding Financial Statement Presentation:

Thank you for the opportunity to comment on the important work of the FASB and IASB on much needed guidance regarding financial statement presentation. I commend your efforts in this draft.

As an advisor to companies and boards who has worked with institutional investors and banks as well, I know that updates to reporting serve to benefit not only capital providers but also will benefit corporate managers (and boards) by helping to create a better understanding of their businesses, the investments those businesses make, and the risks and financing needs in those businesses.

Below are my responses to the Discussion questions you have raised in your October 16, 2008 document.

1. I agree that the objectives of financial statement presentation described in paragraphs 2.5 – 2.13 will improve the usefulness of the information. There are other objectives the Board should also consider as outlined in Appendix A of this letter with respect to disaggregation of the information. Each statement should have a narrow enough objective to be useful and provide specific information and enough information to meet its particular objective in the best manner possible.

2. Separating business from financing could be useful as a window into the thinking process of management. However, because the category approach opens up additional potential for managers to classify items differently in different time periods, there should be requirements for line item specificity and disclosures with respect to reclassifications and the identification of the reclassified items, including restatements of history. One concern I would have is related to management estimates which are carve outs of equity (for example, allowance for loan losses or bad debt). Making sure that those line items stand on their own is important in analyzing the statements in a cohesive way. (Managers often reclassify items and without sufficient disclosure, so guidance here is needed to meet the objectives of transparency.)

3. I think there is a danger in separating out equity from the other aspects of financing as suggested here. Because there is no stated “cost of equity” included on statements and many corporate managers are paid based on earnings, I have witnessed numerous examples of managers who are lulled into a belief that equity is free. That belief does not serve capital providers or, more broadly, the governance of the firm. By including equity as part of financing (not just as a separate “what’s leftover”), perhaps that illusion could be partially pierced.
Another issue that causes difficulties in separating equity from liabilities has to do with accounting changes which reclassify items from equity to liabilities. The reporting of equity is also important in terms of the manner, as a practical matter, equity is used in shortcuts such as ROE.

Per my comment on 2 above, it is important that carve outs of equity be clearly delineated. In some ways, it would be best if these carve outs could be presented in the same part of the statement as equity itself to reinforce their status. My recommendation would be to ensure that all non-owner changes in equity clearly identify on a line item basis the changes in equity due to business estimates.

4. It would be useful to present discontinued operations in a separate section utilizing the relevant categories (operating, investing...) within that section. Line items previously used for reporting those operations in the past should be used in reporting them in this section. If there are reclassifications of categories or line items, those should be noted and a reconciliation between previously reported and history on a restated basis should be included. Clearer definitions of discontinued operations would be helpful.

5. Definitional guidance would be helpful. Changes in classification between categories or line items should require specific disclosure and major components (90% is one suggestion) of totals by category should require line item specificity. A reconciliation between previously reported and history on a restated basis should be included.

6. If definitions are not strict, and instead this category approach provides insight into management’s views, recommending the use of these figures in ratios should be approached with caution.

7. The use should govern – and the reportable segments should determine the basis for entity reporting not vice versa. Many firms today have a large component of their business which is a financial business. It would be inaccurate to report the major results of that financial business in investing or financing (although other components of the business might) when, in fact, it is a matter of operations. Similarly, financial services firms often have a business line that is central to the business that specifically trades or invests the company’s assets. This would be properly classified as operations, not investing. Better definitional guidance should be provided so that statement preparers agree on the meaning of the term “central to the business”. This would be particularly important for certain industries: examples, insurance, hospitals. General standards or guidance by industry would be helpful.

8. Segment reporting is a primary way that capital providers can get a good understanding of the business. Further guidance should err on the side of too many line items. In addition, it is important to recognize that results can be obfuscated (as the potential exists in the new proposal of categories) due to reclassification of items every year. To help prevent the obfuscation and act as an incentive against unnecessary reclassifications, changes in classification between categories and line items should require specific disclosure. In addition, major components (90% is one suggestion) of totals by category should require line item specificity. Reconciliation between previously reported and history on the restated basis should be required.

9. The definitions are too loose (see for example paragraph 2.66) and I believe, if this proposal of categories were to move forward on that basis, it would create less transparency instead of more. “Conversely an entity may decide...” is too open ended. What would be the basis for deciding an entire subsidiary, including its cost of goods sold, is not a part of operations? If the definitions are not made more explicit and if guidance is not provided for segment reporting, I think this idea will only serve to confuse, rather than inform. See also my comments in numbers 7 and 8 above.

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10. The definitions seem appropriate but I would recommend that they be more explicit. See comments in 7, 8, and 9 above.

11. More guidance is needed to ensure enough line item specificity. Those who produce statements based on maturities should disclose information about liquidity and vice versa. Also if there are reclassifications because of changes in liquidity, changes in classification between line items should require specific disclosure and reconciliation between previously reported and history on the restated basis should be required.

12. There could be benefits to the change. Line items within short-term investments should provide enough specificity to distinguish their risk characteristics.

13. See Appendix A. More disaggregation in statements themselves is better than less.

14. I strongly support the goal of all entities preparing the components of comprehensive income, in a similar manner, in the same financial statement. Per Appendix A, I think there should be multiple statements of comprehensive income, all prepared in the same way.

15. Yes, it would be decision useful.

16. Absolutely, it would be decision useful. Without that level of specificity it is difficult for the numbers to tell a useful story about what is really happening in the business. Without that level of specificity, reading text would work as well as a financial statement but not nearly as well as a disaggregated statement along the lines you describe. This is one of the most important recommendations that will provide benefits in all of what you have proposed.

17. Since I believe the categories in segment reporting should form the basis for the reporting at the entity level, I believe disaggregating the tax elements should be considered, so that capital providers can better understand where tax costs and benefits arise. More line item specificity on taxes should also be considered so that capital providers can better understand where tax costs and benefits arise and if there are reclassifications, changes in classification between line items should require specific disclosure and reconciliation between previously reported and history on the restated basis should be required.

18. I agree that the proposal would provide useful information and should be included in the appropriate category as a separate line item.

19. This is an important and useful recommendation. A direct method is more decision useful and keeping with the objectives and with transparency overall. More detail would be very useful and therefore is recommended (again not only for the benefit of capital providers but also for the benefit of managements and boards). I would need to study the reconciliation approach in more detail before commenting.

21. Yes, they should be allocated. Also, basket transactions are unusual or infrequent events. See the answer to 26.

22. Yes, they should disclose. See response to 11.

26. I think it is very important that, in the broadest meaning possible, unusual or infrequent events or transactions should be highlighted. Too often these items are buried in footnotes at best. It would be very
useful for them to be: (a) highlighted as separate line items on the statements and also (b) reflected in a memo on the reconciliation schedule, as suggested.

27. Most of my work is with public entities. However, in the work I’ve done with non-profit and private entities, they could also benefit from this presentation scheme. They need the discipline of it for their internal efforts and stewardship. It would help to emphasize their obligations to their capital providers and their obligations on the financing as well as the operational aspects of their work.

If you have any questions or I can be of help, please let me know (614-571-7020 or ebloxham@thevaluealliance.com).

Thank you again for the opportunity to comment.

With best regards,
Eleanor Bloxham
CEO, The Value Alliance and Corporate Governance Alliance
To the Financial Crisis Advisory Group:

Thank you for the opportunity to comment on the important work of the Financial Crisis Advisory Group (FCAG).

As I understand it, one of the major goals of the FCAG is to consider and provide recommendations regarding the standard-setting implications of the global financial crisis. I’d like to address that in light of my experience working with companies, boards, bankers and sophisticated investment managers and my particular experience and expertise with regard to analyzing the economics of financial institutions.

Regarding the questions raised, here is some context which may be helpful to FCAG in developing recommendations.

1. In the US certainly, earnings statements receive an over-weighted emphasis by internal managements in running their businesses. They also receive an over-weighted emphasis by sophisticated investors, traders, and bankers.
   For example:
   a. Even internally inside firms, not only at the top but at divisional levels, CEOs and boards, reinforced by financial consultants, can believe that a change in the accounting represents a change in economics (and I’ve witnessed a sale of a business on that basis alone).
   b. Even investment managers of billion dollar funds have difficulty sorting out the economics of major institutions – and over-rely on earnings statements.
   c. Despite no change in economics of the business, because of the over emphasis on earnings statements by banks, credit markets can be impacted by accounting changes as companies can be in violation of bank covenants simply because of accounting changes.

2. As a result of the over-emphasis on earnings, despite no change in economics of the business, market prices for equity securities often change when accounting changes are made. The implication of this is important for a number of reasons.
   a. Because market price changes may have no relationship to the economics of the underlying security, “fair value” (which I will put in quotes because the title itself suggests something that I think it is unfair to expect accounting standard setting to address) is mislabeled and suggests that the result is more than it is or can be.
   b. Since market prices change despite no change in economics, then using market prices in earnings statements should be approached very cautiously because market values, while they may be good measures of current liquidation/trading values, they may not represent longer term economic values as well.

3. Financial services firms’ statements are easy to manipulate and provide other distortions. Not only are provisions easy to manipulate, so too are earnings easy to manipulate by disposal of assets. Sales of traded securities is one example. Another one, fundamental to business operations, is the move away...
from “acquire and hold loans” to “securitize and sell”. Despite the negative impact on long run economics, from experience I can say that bankers were seduced to move toward “securitize and sell” leading up to this crisis because of the boost provided to short term earnings. Banks became traders because the earnings statements provided an incentive to do so. In that way, more broadly, accounting statements had an impact in fueling non-economic outcomes.

a. For example, one major institution I analyzed a few years ago tanked its earnings in the first year of a new CEO by cutting back on securitizations. Gradually after that, the major firm re-introduced securitization and increased its level of securitization each year thereafter which increased earnings year on year. This was something that most if not all sophisticated investors missed. Better line item disclosure would be helpful.

b. Off-balance sheet items confuse and confound managements, boards, investors and others. Items should not be off balance sheet if there is economic recourse/liability. (Substance in accounting reporting should trump form.)

c. In addition, reporting around trading activities is currently inadequate in terms of emphasizing risk exposures, particularly on derivative and hedging books. While shown on the books on a net basis where they may appear a minor part of the business, these books may at some firms represent over $1 trillion in outstanding contracts and represent real risk in a time of crisis. More disclosure should be required.

As a result of the above, my other recommendations would be:

1. A move by standard setters away from one major statement on which management, boards, investors and creditors overly depend.
   a. One statement (that of the going concern) should show market values only for assets to be liquidated near term (i.e. available for sale). A firm’s liabilities which are not readily saleable or intended for resale would not be marked.
   b. If investors demand it, another statement should be provided with market values on a traded/liquidation basis.
   c. If management would like to provide it, they should provide a statement with their estimates of the long run economic values (of assets and/or liabilities).

2. Because provisions are manipulated (my book, Economic Value Management, part of the Wiley finance series, shows how one bank even raised and lowered its provisions each quarter to achieve a very interesting effect), and because, in substance, the allowance for credit losses is simply nothing more than an equity carve-out, regarding question two, I would recommend any additional allowance be included either as an equity carve out (choice 3) or in a footnote (choice 4).

3. Because of the above, I believe standard setters should not act in crisis mode at all. I think that the impact of accounting is more than it should be. (And the impact of true changes in businesses, often too little.) Thus standard setters should approach changes to accounting standards, especially those that impact the over-emphasized statements, with caution and actively reach out to more diverse groups for input before proceeding.

If you have any questions or I can be of help, please let me know (614-571-7020 or ebloxham@thevaluealliance.com).

Thank you again for the opportunity to comment.

With best regards,

Eleanor Bloxham
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