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31 March 2009



LETTER OF COMMENT NO. 28

Sir David Tweedie
Chairman
The International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear David

DISCUSSION PAPER Preliminary Views on Financial Statement Presentation

The Financial Reporting Standards Board (FRSB) of the New Zealand Institute of Chartered Accountants (the Institute) is pleased to submit its comments on the IASB Discussion Paper *Preliminary Views on Financial Statement Presentation* (the Discussion Paper). The FRSB also sought the views of New Zealand constituents on the proposals in the Discussion Paper. Two New Zealand companies have been involved in field testing the proposals and some of the FRSB's comments reflect feedback from these companies.

Having considered the IASB's proposals, the FRSB has a significant concern about the level of detail proposed.

The Discussion Paper is proposing that a high level of detail be provided in the individual financial statements. This is highlighted in the illustrative financial statements for ToolCo with the statement of comprehensive income, the statement of cash flows and the statement of financial position each taking up two pages. In order to provide the level of detail proposed within each financial statement, entities will either need to use small fonts or extend statements over two pages.

The FRSB does not consider that this level of detail is appropriate within the individual financial statements. The FRSB notes that some users prefer statements with a generous amount of white space which allows them to focus on the key items within a statement and the relationship(s) between key components of the statements. A simplified layout is also likely to be more accessible to a wider range of user groups. The FRSB considers that entities should have some flexibility in whether they provide certain information in the individual statements or in the notes to the financial statements. We urge the IASB to permit entities to present visually accessible individual financial statements.

The FRSB notes that the level of detail proposed in the individual statements may be in response to assertions that some commentators, particularly in the US, do not read the notes to the financial statements. We do not consider that transferring information from the notes to the individual statements is an appropriate response to this problem.

The FRSB also considers that the overall level of information proposed to be disclosed, both in the individual financial statements and the notes, is excessive and will make the financial statements less accessible to a range of users. Our concerns stem from comments that many users are already finding existing IFRSs statements too detailed and difficult to use.

The FRSB notes that a number of the proposals in the Discussion Paper, including the proposed level of detail to be provided in the statements, appear to be aimed more at meeting the needs of analysts of listed companies than other user groups. The FRSB accepts that analysts are a key user group for listed entities, but queries the emphasis given to the needs of analysts compared to other user groups.

One of the objectives of the IASC Foundation (as expressed in the Constitution) is "to develop, in the public interest, a single set of high quality, understandable and enforceable global accounting standards that require high quality, transparent and comparable information in financial statements and other financial reporting to help participants in the world's capital markets and other users make economic decisions" [emphasis added].

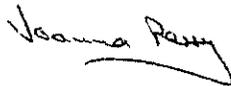
In New Zealand IFRSs are applied by a wide range of entities, including many companies that are not publicly traded. The FRSB accepts that analysts may support the provision of more detailed information in financial statements but is concerned that the level of detail proposed in the Discussion Paper may make financial statements less accessible for other user groups.

As a result of the significant increase in the level of detail proposed, the FRSB believes that there will be a corresponding significant increase in the cost of preparing financial statements.

The FRSB has considered whether it is possible to address the conflict between the high level of detail implied by the IASB's proposals and the FRSB's strongly held view that financial statements must remain accessible to a range of users. The FRSB has identified three alternative approaches that could be considered by the IASB. The first is to mandate the proposed level of detail only in respect of entities which have listed securities. The second is for the IASB to develop a standard on summary financial statements and encourage entities to produce summary financial statements. The FRSB notes that a number of entities in New Zealand produce audited summary financial statements and that these are well received by a range of user groups. The third approach is to require the presentation of simplified financial statements in the same report as the detailed financial statements proposed by the IASB.

Our responses to the specific questions in the Discussion Paper are attached as an Appendix to this letter. If you have any queries or require clarification of any matters in this submission, please contact Joanne Scott (jscott@ts.co.nz) in the first instance, or me.

Yours sincerely



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Appendix: Response to Questions in the Discussion Paper

Chapter 2: Objectives and principles of financial statement presentation

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| 1 | Would the objectives for financial statement presentation described 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. |
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General comment

The FRSB is generally supportive of the proposed objectives and acknowledges that they will have been useful in considering the merits of proposals in the Discussion Paper.

The FRSB's main concern is that the Discussion Paper does not explicitly address the relationship between the proposed objectives and the IASB's Conceptual Framework project. The Discussion Paper refers to the objectives of financial reporting identified in Phase A of that project but it does not consider whether any of the qualitative characteristics could also be used as objectives of financial statement presentation or how they could guide the selection of such objectives. Nor does it consider whether the proposed objectives of financial statement presentation should be incorporated into the *Framework*. The FRSB suggests that if the proposed objectives are sufficiently important to guide the development of proposals for financial statement presentation that they should be integrated into the discussion of the objectives of financial statements in the *Framework*.

The FRSB supports the continued use of the proposed objectives, but cautions that they should not be regarded as being comprehensive.

Cohesiveness objective

The FRSB considers that clearer linking of the impact of transactions and events in the financial statements, in accordance with the cohesiveness objective, has the potential to make financial statements more accessible and useful.

However, the FRSB considers that the way in which the concept has been applied in some statements is unnecessarily prescriptive. This is discussed further in our comments on question 6.

Disaggregation objective

The disaggregation objective (paragraph 2.7) states that "An entity should disaggregate information in its financial statements in a manner that makes it useful in assessing the amount, timing and uncertainty of its future cash flows."

The FRSB agrees that capital providers are interested in an entity's future cash flows but it has two concerns about this objective. First, the FRSB is of the view that the IASB should take a broader approach in developing these objectives and focus on information that would be useful in assessing future performance rather than merely focussing on cash flows. Secondly, the FRSB considers that prospective financial statements are more useful than historical financial statements in providing information on future cash flows. The FRSB suggests that any future discussion of the disaggregation objective acknowledge that, *in conjunction with prospective financial statements and other forward-looking information*, historical financial statements may be used in forming opinions in future cash flows. We note that prospective information, including forecasts, will be considered in Phase E of the Conceptual Framework project.

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?

The FRSB generally supports the separation of business activities from financing activities as it considers that it will more appropriately reflect the distinction between the creation of wealth and the distribution of that wealth. However, the FRSB notes that an entity's classification of assets and liabilities into such activities may change over time. The Discussion Paper does not discuss how such changes in classification would be presented.

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?

The FRSB supports the presentation of equity as a category within the financing section on the grounds that the distinction between debt and equity instruments has become increasingly blurred, leading to a spectrum of financing instruments. That is, the FRSB agrees with the arguments outlined in paragraph 2.53 of the Discussion Paper. The FRSB also considers that this argument could be taken further and could be used to support the presentation, in the statement of financial position, of equity and debt (in a combined financing section) by expected maturity.

If equity and debt are regarded as interchangeable, this could have a number of implications for other statements, including:

- dividends and interest would both be regarded as financing expenses in the statement of comprehensive income;
- the usefulness of the statement of movements in equity would diminish – note disclosure of movements in capital would suffice; and
- dividends paid and interest paid would both be classified in the financing section of the statement of cash flows.

This approach would be consistent with the adoption of the entity perspective in the IASB's ED *Conceptual Framework for Financial Reporting: The Objective of Financial Reporting and Qualitative Characteristics and Constraints of Decision-Useful Financial Reporting Information*.

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?

The FRSB does not support the presentation of discontinued operations in the statement of comprehensive income either as a separate section or within the relevant categories. Instead the FRSB considers that note disclosure of discontinued operations is sufficient.

The FRSB does not consider that separate presentation in the statement of comprehensive income is warranted for two reasons:

- if an entity's segments have been appropriately identified the disclosures required by IFRS 8 *Operating Segments* would provide an overview of the impact of discontinued operations; and
- the separate presentation of discontinued operations in the statement of comprehensive income reduces comparability between periods. Generally discontinued operations occur due to sale with the proceeds of sale mostly being used to purchase additional assets or reduce liabilities. The return on these new assets or the impact of reduced debt shows up in the continuing

activities in the following period. The FRSB considers that users are better able to compare financial performance over the two periods if the figures for the first year include the discontinued activity and the figures for the second year include the impact of the change in activities.

The FRSB also considers that the separate presentation of discontinued operations on the face of the statement of comprehensive income contributes to the problem of excessive detail on the face of the statements.

- 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 best reflect the way an item is used within the entity or its reportable segment (see paragraphs 2.27, 2.34 and 2.39–2.41).
- (a) Would a management approach provide the most useful view of an entity to users of its financial statements?
 - (b) Would the potential for reduced comparability of financial statements resulting from a management approach to classification outweigh the benefits of that approach? Why or why not?

The FRSB acknowledges the increasing use of the management approach in a range of standards and is supportive of this approach being applied to the classification of assets and liabilities.

The FRSB considers that if the management approach is adopted, management should be able to exercise judgement in classifying assets and liabilities, without being constrained by some of the more detailed proposals in the Discussion Paper. For example, the FRSB considers that some entities may manage certain non-financial liabilities as financing activities and that they should be able to classify them in this way. This approach would align with the management approach in IFRS 8 *Segment Reporting* which permits disclosures to be based on information presented to management.

The adoption of the management approach would mean that there could be differences in classification between entities engaged in similar activities. However, if this difference in classification reflects the way the entities are managed then the FRSB considers that it is appropriate.

- 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?

The FRSB supports the concept of separate disclosure of assets and liabilities using the business and financing classifications. However, the FRSB does not agree with the proposal that this information be required to be provided in the statement of financial position.

The FRSB has received strong feedback that many users are likely to prefer a simpler layout for this statement which highlights total current and non-current assets and liabilities, with more detailed information such as the classification into business and financing sections being provided in the notes. As discussed in the covering letter, the FRSB considers that the IASB has a number of options which would allow it require a high level of detail about the items in the financial statements whilst maintaining the accessibility of the financial statements to a range of users. These options include:

- increasing use of summary financial statements (and a standard to guide their presentation);
- encouraging the provision of summary information within the financial statements and providing guidance on the presentation of such information; and

- requiring application of the proposals in this Discussion Paper to a limited range of entities, such as entities with instruments are traded in a public market.

The FRSB notes that XBRL is increasingly being used by regulators world-wide. For example the New Zealand Government is currently investigating the suitability of XBRL in the government environment with the aim of reducing compliance costs for businesses. If XBRL becomes widely used for regulatory reporting, it would allow analysts to select the form of presentation that they prefer and financial reporting standards could address the information needs of other users.

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 consolidated entity level? Please explain.

The FRSB does not support the proposal that entities with more than one reportable segment for segment reporting purposes should classify assets and liabilities at the reportable segment level. The FRSB is concerned this would result in unnecessary detail.

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 the light of the proposed presentation model? Please explain.

The FRSB considers that existing reconciliations required by IFRS 8 paragraph 28 are sufficient and does not recommend additional segment disclosures or associated reconciliations as a result of the proposals in the Discussion Paper.

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?

The FRSB supports the descriptions of the business section and the operating and investing categories within that section.

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?

The FRSB does not agree that the financing section should be limited to financial assets and financial liabilities. Although this is likely to be appropriate for many entities, the FRSB considers that some entities may regard certain non-financial assets and liabilities as being part of their financing activities and manage those assets and liabilities accordingly. For example, the New Zealand Government pre-funds a portion of its future New Zealand Superannuation expenses (a universal benefit paid to New Zealanders once they reach the qualifying age) by making contributions to an investment fund - the New Zealand Superannuation Fund (NZS Fund). Although the majority of the assets held by the NZS Fund are financial assets, it also holds other assets, including a portfolio of forest investments. The NZS

Fund is an important component of the Government's fiscal strategy in that the Fund's assets provide the means for the Government to partially pre-fund future fiscal pressures. Although this is a public sector example, we can easily envisage this type of situation occurring in private sector entities. In such cases the FRSB considers that the entity should be able to classify those assets and liabilities within the financing section.

The FRSB does not consider that mandating the classification of non-financial assets is consistent with a management approach to classification.

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

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?
 - (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?

In New Zealand, financial institutions typically present assets and liabilities in order of liquidity.

The consolidated financial statements of the Government of New Zealand are also presented in order of liquidity but the individual entities within that reporting entity, such as departments and local authorities, generally present a classified statement of financial position.

The FRSB considers that the current level of guidance on when an entity may present assets and liabilities in order of liquidity is sufficient.

- 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?

The FRSB supports this proposal. The FRSB notes that previous NZ GAAP limited the types of investments that could be presented as cash to highly liquid investments where there was a ready market to convert unconditionally the investment to notes and coins at the investor's option *within no more than two working days*.

However, constituents did not comment on this difference at the time that New Zealand adopted the requirements of IAS 7 *Statement of Cash Flows* (as part of NZ IAS 7 *Statement of Cash Flows*). This suggests that the changed presentation of cash equivalents under NZ IFRS was not regarded as a significant issue by New Zealand constituents.

- 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?

The FRSB does not support the proposal to require presentation of assets and liabilities measured on different bases on separate lines in the statement of financial position. Further, the FRSB does not

support the justification for this approach in paragraph 3.20 as the FRSB does not consider that such disclosures are unlikely to impose undue costs or are the primary reason why "users go back and forth between the statement and the notes". Further, the FRSB notes that a number of existing standards already require disclosure of assets and liabilities measured on different bases (for example, IFRS 7 *Financial Instruments: Disclosures* and IAS 16 *Property, Plant and Equipment*). The FRSB considers that note disclosure of this type of information is appropriate and sufficient.

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?

The FRSB strongly agrees with the proposal that all components of recognised income and expense should be presented in a single statement. This position is consistent with the FRSB's previous comments in relation to the Exposure Draft of Proposed Amendments to IAS 1 *Presentation of Financial Statements—A Revised Presentation* (2006) and our more recent comments on the Discussion Paper *Reducing Complexity in Reporting Financial Instruments* (2008).

Much of the current complexity in financial reporting revolves around the presentation of gains or losses within or outside earnings. If all gains and losses were presented in a single comprehensive income statement the need for rules regarding classification of gains and losses would be reduced or eliminated.

The FRSB further notes, in accordance with its view in question 3 above, that inclusion of equity within the financing section will have 'flow on' impacts in the statement of comprehensive income. In particular, it would follow that dividends and other movements in equity would appear within the statement of comprehensive income rather than in the statement of movements in equity.

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?

The FRSB does not agree that there should be a separate category for other comprehensive income and regards the proposals in relation to other comprehensive income as a less than desirable compromise.

Revenue and expenses have traditionally been included in other comprehensive income when standard setters have met conceptual or practical difficulties in including them within profit or loss. Such treatment has generally not been consistent with the conceptual frameworks applying at the time requirements were developed. The FRSB encourages the IASB to remove the category of other comprehensive income as soon as solutions can be reached for items presently classified there. While income and expenses continue to be classified as other comprehensive income, the category to which they belong should be indicated. Categorisation is only useful if it is applied to all income and expenses.

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?

The FRSB supports the disclosure of information on nature or function of expenses. However it disagrees with a number of the proposals in the Discussion Paper as it considers that the costs of the extensive additional information disclosed is likely to outweigh any benefits that might result from the additional disclosures. In particular:

- The FRSB does not support the proposal to require income items to be disaggregated by nature as well as function under certain circumstances because it is not clear what disclosures would result from this requirement.
- The FRSB does not support the proposal in paragraph 3.44 that entities disaggregating expenses by function should also be required to further disaggregate by nature within those functions "to the extent that this will enhance the usefulness of the information in predicting the entity's future cash flows". The FRSB does not consider that the reference to such information enhancing "the usefulness of the information for predicting the entity's future cash flows" will lead to this additional disclosure. If the IASB considers that it is critical for certain items to be disclosed then the FRSB considers that the IASB should mandate disclosure of these items.
- The FRSB considers that in some cases the disclosure of expenses by nature is not particularly useful. For example, IAS 41 *Agriculture* does not explicitly prescribe how to account for subsequent expenditure related to biological assets. An entity which capitalises subsequent expenditure on bearer assets would disclose quite different amounts compared to an entity which expenses such expenditure. The FRSB does not consider that the objective of the disclosure can be met if different entities can disclose non-comparable amounts. The alternative would be to require disclosure of the total amount of expenditure on an item (both the amount expended directly and the amount capitalised). However, the FRSB considers that any proposal to require disclosure of total costs as opposed to total expenses should be publicly debated.

The FRSB notes that the Discussion Paper (paragraph 3.46) acknowledges that presenting by-function subcategories and by-nature information within those subcategories may result in too much information in the statement and suggests that note disclosure may be permitted. The FRSB considers that all entities should be permitted to disclose by-function or by-nature information in the notes.

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.
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The FRSB does not support requirements to allocate income taxes other than between profit or loss and other comprehensive income. This allocation is generally not affected by the vagaries of taxation legislation. However, any requirement to allocate income taxes by category will require guidance on the appropriate method of allocating income tax adjustments, such as subsidies for employing particular categories of workers, that are not related to any specific income or expense or category.

- 18 Paragraph 3.63 proposes that an entity should present **foreign currency transaction gains and losses**, including the components of any net gain or loss arising on remeasurement into its functional currency, in the same section and category as the assets that gave rise to the gains and 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 relating to presenting the components of net foreign currency transaction gains or losses for presentation in different sections and categories?

The FRSB does not consider that the benefits of such presentation would generally outweigh the costs.

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?

Response to (a)

The FRSB supports the direct method of presenting cash flows and notes that this method of presenting cash flows has been applied in New Zealand without significant difficulty for over twenty years. However, the FRSB does not support the level of disaggregation of cash flows proposed in the Discussion Paper.

The FRSB puts forward the following factors in support of the direct method of presenting cash flows:

- it best reflects the gross inflows and outflows of cash from operating activities;
- it provides additional and important information that is not otherwise available to users of financial statements;
- it is the best approach to provide meaningful information to enable a full analysis of an entity's financial activity and enables the full explanation of why the composition of the balance sheet changes from year to year;
- several empirical studies show that the direct cash flow statement is easier to understand and provides more information than the indirect method. IASB staff have been forwarded a summary of research on this topic. The studies include:
 - Clinch, G., B. Sidhu and S. Sin (2002). The Usefulness of Direct and Indirect Cash Flow Disclosures. *Review of Accounting Studies* 7: 383-404.
 - Ding, Y., T. Jeanjean and H. Stolowy (2006). *The Usefulness of Disclosing both Direct and Indirect Cash Flows: An Empirical Study*. Working paper, Centre National de la Recherche Scientifique.
 - Gahlon, J.M. and R.L. Vigeland (1988). Early Warning Signs of Bankruptcy Using Cash Flow Analysis. *Journal of Commercial Bank Lending* 71: 4-15.
 - Klammer, T.P. and S.A. Reed (1990). Operating Cash Flow Formats: Does Format Influence Decisions? *Journal of Accounting and Public Policy* 9: 217-235.
 - Krishnan, G.V. and J.A. Largay III (2000). The Predictive Ability of Direct Method Cash Flow Information. *Journal of Business, Finance & Accounting* 27: 215-245.

The FRSB does not support the level of disaggregation of cash flows proposed in the Discussion Paper and does not consider that it would provide information that is useful. In addition, the FRSB believes

that in order to provide the level of detail proposed, most entities would need to make very broad assumptions regarding the allocation of certain expenses to the cash flow line items, particularly the breakdown of accounts payable. Such assumptions would reduce the accuracy of the information provided. The FRSB also believes that the level of detail proposed would add significantly to the cost of preparing a statement of cash flows.

Response to (b)

The FRSB considers that the direct method of presentation is consistent with the cohesiveness objective because it allows users to understand the relationship between individual income and expense items and their associated cash flows.

Response to (c)

We agree.

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?

The cost of presenting cash flows using the direct method depend upon how that information is prepared and the level of detail proposed (refer also to our comments on question 19). The FRSB notes that information on direct cash flows may be prepared directly, or indirectly, by reversing the effect of accruals from the income statement using information on the changes in assets and liabilities. Generally the latter approach is most commonly used and would be the most efficient method. However, using this method, most entities would be able to provide the level of detail proposed in the Discussion Paper only with the use of very broad assumptions. The FRSB has received feedback that even with the use of such assumptions, the level of detail proposed would involve significant additional preparation costs.

The alternative would be for an entity to establish systems to analyse its cash flows. System changes might reduce the ongoing costs of preparing a detailed cash flow statement but would involve significant up front investment.

Some would argue that it is possible to estimate direct cash flows using information provided in the financial statements, and therefore there is no need to mandate the provision of this information in financial statements. However the FRSB notes that research suggests mechanical procedures for estimating cash flow data provide poor estimates of reported cash flow numbers.¹

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?

Conceptually, the FRSB acknowledges the desirability of allocating the effects of basket transactions to the related sections and categories in the statement of comprehensive income. However the FRSB considers that there would be a number of practical difficulties in making such allocations.

Some of the difficulties relate to business combinations and disposals. For example:

¹ Austin, L. and M.E. Bradbury (1995). The Accuracy of Cash Flow Estimates. *Accounting and Finance* May: 73-86

- should the basket transaction include all items that make up the transaction, or only those aspects of the transaction that are accounted for as part of the business combination in accordance with IFRS 3 *Business Combinations*;
- if there is a mixture of consideration, how would the cash element of the consideration be allocated to the various components of the acquisition; and
- the information required to perform the allocation will not generally be available in relation to a business disposal.

The FRSB therefore concludes that the benefits of such allocations are likely to be outweighed by the costs and recommends that the effects of basket transactions be allocated to the category in which the major impact falls.

Chapter 4: Notes to financial statements

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 FRSB does not support this proposal. The current version of IFRS 7 *Financial Instruments: Disclosures* requires the disclosure of a maturity analysis of financial liabilities based on the remaining contractual maturities. The FRSB considers that the maturity disclosures required by IFRS 7 are sufficient and should not be extended.

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 liabilities and assets 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.

Response to (a)

The FRSB considers that the proposed reconciliation schedule could assist users in understanding the nature and amount of an entity's current cash flows, and that this may be helpful to users in making decisions about whether to continue hold investments, their assessments of management's performance and their assessment of the risks facing the entity. However, the FRSB does not consider that the proposed schedule would necessarily increase understanding of future cash flows and does not consider that it should be a mandatory component of financial statements for all entities.

The FRSB considers that the focus on future cash flows in this section of the Discussion Paper underscores the IASB's focus on analysts rather than on the information needs of other groups of users. In making this observation the FRSB notes that there appears to be support for this reconciliation from US analysts. If this statement does not have broad support from analysts in a number of jurisdictions

and from a broad range of users, it may be appropriate for it to be a FASB only requirement. Alternatively, the detailed reconciliation could be limited to certain types of entities.

New Zealand entities applying NZ IAS 7 are currently required to prepare a reconciliation of profit (loss) with the net cash flow from operating activities. The reconciliation required by NZ IAS 7 results in entities providing some of the information in column C, but does not provide a link between each line item of the respective statements.

The FRSB notes that much of the information to be presented in the proposed reconciliation could be obtained from analysing financial statements presented in accordance with existing requirements. This does raise the question of whether the limited additional information that would be presented justifies the preparation of the schedule. On a more positive note, by requiring cash flows to be reconciled to the amounts in the statement of comprehensive income, the reconciliation schedule could improve the quality of information presented in the statement of cash flows.

Response to (b)

The FRSB disagrees with the level of detail proposed to be required in respect of working capital movements on the grounds that it considers this would be a time consuming exercise.

Response to (c)

No comment.

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?
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The FRSB considers that further disaggregation of changes in fair value should be considered as part of the review of IFRS 7 *Financial Instruments: Disclosures*.

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 B.10–B.22? 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?
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No. The FRSB concurs with the arguments set out in paragraphs B20 and B21.

- 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?

The FRSB does not support the FASB preliminary view. It regards the FASB's proposal as being a step towards the reinstatement of extraordinary items, with the well-known problems that these created.

Question specific to the FASB

- 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.

With the potential for a standard arising from this project to be applied by both public and non-public entities, the FRSB would support research into the specific information needs of users of non-public entity financial statements and why and how these differ from the needs of users of public entity financial statements.

The FRSB considers that if the comments in paragraph 1.18 regarding not-for-profit entities were merely intended to scope out US not-for-profit entities then this should have been made clearer in the paper.