Comments on Preliminary Views on Financial Statement Presentation (Discussion Paper October 2008)

From:

LETTER OF COMMENT NO. 7

1. NÜRNBERGER Beteiligungs-Aktiengesellschaft Department of Accountancy

Ostendstraße 100, D-90334 Nürnberg, Germany

2. SV SparkassenVersicherung Holding AG Department of Accountancy

Löwentorstr. 65, D-70376 Stuttgart, Germany

3. Wüstenrot & Württembergische AG Department of Accountancy

Gutenbergstr. 30, D-70163 Stuttgart, Germany

Please address all questions regarding this statement to mark.herrmann@nuernberger.de.

Focus on the Cash-Flow Statement Discussion:

Due to limited resources (manpower and time) we would only like to focus on the cash-flow statement discussion which is in our view currently too academically and not enough business practice orientated.

Discussion questions:

19 (a)

Would a direct method of presenting operating cash flows provide information that is decision-useful?

In our opinion is the question if the direct method of presenting operating cash flows provides more decision-useful information than the indirect method does.

Regarding the goal of the cash flow statement: transparency about entities cash flows. In our opinion is the result (sum of cash flows from operating/business activities) the most decision-useful information/number for an investor which indicates an entity's ability to pay all (financial) duties with its generated cash flows. The question which method is used to generate this figure is less important as long as all entities have to use similar rules and calculation models. In our opinion is the current status (and accepted benchmark) that almost all competitors and listed companies use the indirect method.

In comparison to the direct method the indirect method has the significant advantage that the required information can be drawn from the general ledger. In a very complex and diversified business modell/environment with various functions (as the insurance business) and a big number of diversified special ledgers data generation is the problem. IT systems need to be modified and adjusted. Just think of old systems which report only the balance but no movement/transaction type detail. And in some cases these IT systems might be old and not compatible and modifiable any more. If the venerable IASB insists on a cash flow statement per direct method we need very detailed information in the implementation and application guidance and an additional guidance on practice orientated aggregation rules which do not harm with the disaggregation goals of the IASB. Otherwise the application of the direct method can't be implemented because the required data generation is not available and implementable.

We are convinced that a direct method presenting operating cash flows does not provide more decision-useful information than the indirect method does. Furthermore special facilities for the data generation need to be suggested to help entities to achieve their reporting requirements.

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?

Using a direct method is **NOT more consistent** with the proposed cohesiveness and disaggregation objectives than an indirect method (argumentation as follows).

To help investors to understand how cash flows relate to the statements of comprehensive income and financial position the method used is not the critical issue. In our opinion the "accrual components" (see 19(c)) particularly the fair value changes and the valuation adjustments are critical items which help investors to understand how cash flow information relates to the statements of comprehensive income and financial position. The board took already care of that problem by expanding the profit and loss statement with the statement of recognised income and expenses to the new comprehensive income as an obligatory part of financial reporting (IAS 1(2007)).

In our opinion neither the indirect nor the direct method can predict future cash flows. Assessing future cash flows from current cash flows (direct method) does -in our view- not meet the reliability requirements of the framework. Detailed knowledge about the development of environmental changes would be necessary to make assumptions regarding the future "cash component" (see 19(c)). The subprime crises showed that environmental changes and future developments are unpredictable. Furthermore both methods come up with identical results, An entity's management, treasury department and capital expenditure department steer and manage the group liquidity. Using the direct method does not help investors to understand the liquidity planning/strategy of a group because it is too complex and detailed. Even if a company generates high cash flows from operating/business activities nobody can guarantee that this will happen in the next fiscal year again (Coming back to the subprime crises example: In the last two years a finance institute generated a lot of operating cash flows through interest income from bought debt obligations. In 2008 the finance institute had to sell these debt obligations half the price it were bought to generate liquidity.).

It might be possible that the group of assets and liabilities where cash flows relate to is easier to identify in the statement of financial positions by using the direct method. But without the knowledge of management's strategy and the future business development no decision-useful information is presented. And no reliable implications from the presented information can be drawn by the investors.

Summing up the arguments above the direct method does not present more consistent decision-useful information for investors than the indirect method. Besides that the direct method can not justify the tremendous effort which would be necessary to modify the IT architecture for data generation purposes (see 19 (a)) when the additional data does not add any recognisable (economic) value for the investors.

19 (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?

The information currently provided using the indirect method to present operating cash flows can almost be comprehensively provided in the proposed reconciliation schedule.

Only minor changes in paragraph 4.19 and 4.45 have to be made. In paragraph 4.45 Columns B and C should be merged. The combination of column B and C is the sum of the "cash component" supplemented by accruals and allocations (Column C: depreciation, etc.) not resulting from remeasurements. This sum equals the figure when using the indirect method. As stated above (see 19(b)) the split between the "cash component" and Column C does not provide any decision-useful information for investors. Therefore no decision-useful information will be lost if Column B and C are merged. As result the required disaggregation components in paragraph 4.19 should be shortened to a) plus b) as a sum and additionally into the components c) and d).

In our opinion facilities should be made when no decision-useful information for investors is lost. We are convinced that shortening paragraph 4.19 and merging the columns B and C in paragraph 4.45 (now six instead of seven columns) give investors the same quality and quantity of decision-useful information as the solutions in the Discussion Paper of the IASB do. With these suggested adjustments the **indirect** method to present operating cash flows could be retained and lots of money as well as other resources be saved by the enterprises.

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Cost-Estimate

The size and complex IT-structure of our group as well as the short comment period prevented to generate the required field studies and impact analysis for this purpose in time (Year-end closing 2008). Furthermore detailed guidance on implementation and application as theoretical basis is required for the identification of adjustment requirements and cost estimates (see 19(a)). We would like to inform the board that the employees in the accountancy department are incorporated in the year-end closing process from October (Fast Close) until April (Annual General Meeting). A more business requirements oriented comment period might have been a better solution for this topic and lead to a more detailed feedback.

Remark:

It is easy to assess that using the direct method to present operating cash flows is much more time consuming than using the indirect method. But due to several obligatory regulations (Corporate Governance in Germany, etc.) time is the most restricted resource in the year-end closing process.

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