

LETTER OF COMMENT NO. 142

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Financial Accounting Standards Board 401 Merritt 7 PO Box 5116 Norwalk, CT 06856-5116

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Discussion Paper Preliminary Views on Financial Statement Presentation

Johnson & Johnson would like to comment on the joint Financial Accounting Standards Board and International Accounting Standards Board Discussion Paper entitled "Preliminary Views on Financial Statement Presentation". In addition to our role as preparers of financial statements, we are also users of financial statements. Our participation in the field test afforded us a valuable insight into the practical considerations of reformatting our financial statements to comply with the guidance contained in the Discussion Paper. It is with these perspectives that we offer the following observations.

Objectives

Overall, we agree with the objectives of the proposed financial statements (cohesiveness, disaggregation, and ability to assess liquidity and cash flow). However, we believe the objectives could be met more appropriately through enhanced footnote disclosures rather than revamped financial statements. We believe the financial statements that result from the proposed reporting model are complex and confusing.

Cohesiveness: The cohesiveness approach is useful in understanding the relationship between items across the financial statements but may produce financial statements that are too detailed and complex for the majority of financial statement users.

Disaggegation: We felt the disaggregation objective was taken to an extreme. Currently, Johnson & Johnson's consolidated financial information is not sourced by nature, as we have previously determined it is not useful information. In addition, we believe that disaggregation by nature can be misleading when comparing across organizations or reporting periods. We agree that the financial statements should convey to users the ability of the entity to fulfill its financial commitments and demonstrate its financial flexibility. To the extent that more functional information (e.g.Selling/Marketing) is disclosed, we feel that would be insightful and useful; but not expenses by nature.

Classification

Johnson & Johnson agrees that an entity should classify its assets and liabilities using a management approach if we are to disaggregate our financial information into Operating, Investing and Financing activities. We feel management is in the best position to communicate the unique aspects of its business to users of its financial statements. However, we believe this approach may reduce comparability of financial statements and will require additional disclosures. The board should consider providing specific guidelines in areas that are applicable to all companies regardless of their industry (i.e., pensions).

Segment Disclosures

We feel that the classification of assets and liabilities on the reportable segment level may be useful when directly identifiable but may not be as useful when allocated on an indirect basis (e.g., asset and liabilities used in a shared service model).

Direct Cash Flow

Both the direct and indirect method presentations of operating cash flow provide decision-useful information. The direct method of cash flows would meet the cohesiveness and disaggregation objectives, however, we believe users of financial statements are primarily concerned with cash flows from operations and fail to see how the direct method provides more decision-useful information. The *indirect* method of cash flow provides a useful link between net income and cash flow from operations that is captured in one schedule and is easy for users to understand. We do not use a direct method to make decisions about the business and our systems do not capture data in this manner. The Board's proposal to provide a detailed direct method of cash flow in addition to a detailed reconciliation schedule that reconciles cash flow to comprehensive income would create an arduous burden to the preparer and may be too complex for users. We strongly believe that the substantial costs to implement a direct method of cash flow statement would far outweigh any potential benefits.

Reconciliation Schedule

We do not use much of the detailed transactional information needed to complete the Reconciliation of Cash Flows to Comprehensive Income schedule and we question why it would be useful to anyone else. We found this statement to be too lengthy and overly complex. Although remeasurements are not significant for our company, we anticipate further clarification would be necessary to explain what should be reflected in this schedule.

Implementation Costs

Johnson & Johnson is a global company operating on a decentralized approach that utilizes many general ledger systems that are not designed to capture information on a cash basis. The Board's proposed financial statements would require the development of new systems that would capture transactional data categorically by function, by nature, on both cash and accrual basis. The costs,

human resources and time necessary to transform our accounting systems, policies and procedures (including SOX, internal and external audit testing) to a system capable of being able to meet the proposed changes would be very hard to justify. These significant costs would outweigh any potential incremental benefits.

FPS

The discussion paper is unclear on the guidance for earnings per share calculation given the new financial statement format. EPS continues to be calculated on Net Income while the Statement of Comprehensive Income has subtotals for Total Business Income, Net Income, and Total Comprehensive Income. Our opinion is that EPS should follow net income to avoid misleading users that EPS is calculated on Total Comprehensive Income.

Other

The FASB needs to provide a clear road map on how the convergence with International Financial Accounting Standards and the proposed financial statements are aligned. Both projects will require significant resources and system transformation.

Additional comments related to the issues that the FASB specifically requested comments on are contained in the attached Appendix.

Thank you very much for taking our comments into consideration.

Sincerely,

Stephen J. Cosgrove Vice President, Corporate Controller

Appendix

Chapter 2: Objectives and Principles of Financial Statement Presentation

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.

We agree that the objectives of financial statement presentation proposed in the discussion paper 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. However, the objectives of the financial statements should be aligned with the overall objective of financial reporting, which is to convey useful and comprehendible information that is helpful in assessing the amounts, timing, and uncertainty of prospective net cash flow to users. We believe rather than creating a lengthy and complex set of financial statements the most efficient manner to meet the Board's objectives is in the financial statement footnotes rather than on the face of the financial statements.

The cohesiveness approach is useful in understanding the relationship between items across the financial statements but may produce financial statements that are too detailed and complex for a broad range of financial statement users. We felt the disaggregation objective was taken to an extreme. Currently, Johnson & Johnson's consolidated financial information is not sourced by nature, as it is not viewed as vital information for senior management in the analysis and decision making process. The disaggregation of the proposed financial statements by function and nature fails to take into account the substantial complexity and costs to the preparer. In addition, we believe that disaggregation by nature can be misleading when comparing across organizations or reporting periods. We agree that the financial statements should convey to users' the ability of the entity to fulfill its financial commitments and demonstrate its financial flexibility. We feel that our current classified balance sheet, prepared in accordance with GAAP and related disclosures, allow the users to assess the entity's ability to meet its financial commitments and the wherewithal of the entity to invest in business building opportunities.

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 believe the separation of business activities from financing activities does provide decision-useful information. We believe users will gain insight by distinguishing

between the core activities of the business versus those activities intended to finance those activities.

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?

Johnson & Johnson supports the position of having the equity section separate from the financing activities. It follows the cohesiveness objective in the discussion paper and clearly distinguishes between owner sources and non-owner sources.

- 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 asset, and financing liabilities)? Why or why not?
- U.S. GAAP requires presenting discontinued operations on the Statement of Comprehensive Income and Cash Flows. The impact of discontinued operations on the statement of financial position is disclosed in the footnotes. We believe segregating discontinued operations on the statement of financial position will maintain the cohesiveness objective and provide decision-useful information regarding liquidity and future cash flows. Further disaggregation of discontinued operations into operating, investing, and financing sections would make the statements more complex and difficult for users to identify the effect of the discontinued operations.
- 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?
 - 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?

Johnson & Johnson agrees that an entity should classify its assets and liabilities using a management approach if we are to disaggregate our financial information into Operating, Investing and Financing activities. Johnson & Johnson feels management is in the best position to communicate the unique aspects of its business to users of its financial statements. However, this approach will most likely reduce comparability of financial statements and will require additional disclosures. The board should consider providing specific guidelines in areas that are applicable to all companies regardless of their industry (i.e., pensions).

6. Paragraph 2.27proposes 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?

Presentation of both assets and liabilities in the same category will make it easier to calculate certain ratios and more difficult to calculate others. The financial statement presentation would allow for operating activity analysis that is currently not available. We believe current assets and liabilities and their subtotals should continue to be included on the face of the Statement of Financial Position. This will allow for the calculation of certain ratios used to assess the liquidity and financial condition of a company (i.e., current and quick ratios).

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.

We feel in order for the Board to achieve the objectives of cohesiveness, disaggregation, and liquidity and financial flexibility the classifications of assets and liabilities would have to be at the reportable segment level. However, we feel that the classification of assets and liabilities on the reportable segment level will create confusing and lengthy financial statements and may not give the reader a succinct view of the resources and obligations at an entity level.

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.

We agree that different disclosures will be needed for consistency and reconciliation between the proposed financial statements and the segment information provided in the notes of the financial statements. However, the proposed financial statements and the Segment disclosures will most likely deviate from the information that is reviewed by the chief operating decision maker. The level of detail required to be disclosed may or may not be useful to readers of external financial statements, and may be cumbersome for an enterprise to present.

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 believe the business section and the operating and investing categories within the section are defined appropriately. The management approach to classification allows management to determine the transactions directly related to an entity's value-creating activities versus investing activities and those transactions that are related to financing the business or other 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 U.S. GAAP as proposed? Why or why not?

Overall, we like the Board's approach of giving management the flexibility in classifying its assets and liabilities according to how they are used within the entity. However, the financing assets and financing liabilities categories need further clarification in order to allow comparability among entities.

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?

No response

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?

We do not agree. Using our management approach we view cash equivalents should be classified in the same manner as Cash.

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 agree that disaggregating assets and liabilities that are measured on different basis provides information that is more decision-useful but feel this disaggregation is more appropriate in the notes to the financial statements rather than the face of the statements.

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?

Combining net income and other comprehensive income into one statement can be misleading to all but the most sophisticated users of financial statements. We do not support presenting net income and other comprehensive income in a single statement of comprehensive income given that the earnings per share continues to be calculated on net income. We believe the presentation of the earning per share after total comprehensive income may be misleading to the users of the financial statements.

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?

No response

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 in 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 do not believe the benefits of disaggregating the statement of comprehensive income by function, nature or both will outweigh the costs to prepare and audit the financial statements. The resulting disaggregation may confuse users with lengthy financial statements. Financial statement will also be less comparable between entities and may lead to incorrect conclusions by the users.

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.

Given the difficulties to disaggregate income taxes to operating, investing and financing categories we support the proposed presentation. The costs to track income tax by category would be burdensome and would result in arbitrary allocations that would not provide additional decision useful information.

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 and liabilities 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?

The benefits of presenting foreign currency transactions gains and losses into the appropriate sections or categories in the statement of comprehensive income may not justify the costs to track the individual transactions due to the fact that our systems are currently not designed to isolate this data. We do not feel this will provide additional decision-useful information and feel it is appropriate to include the transaction gains and losses in the operating section of the statement of comprehensive income.

19. Would a **direct method of presenting cash flows** in the statement of cash flows provide information that is more decision useful than an indirect method, and 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?

Both the direct and indirect method presentations of operating cash flow provide decision-useful information. The direct method of cash flows would meet the cohesiveness and disaggregation objectives, however, we believe users of financial statements are primarily concerned with cash flows from operations and fail to see how the direct method provides more decision-useful information. The indirect method of cash flow provides a useful link between net income and cash flow from operations that is captured in one schedule and is easy for users to understand. The Board's proposal to provide a detailed direct method of cash flow in addition to a detailed reconciliation schedule that reconciles cash flow to comprehensive income would create a tremendous burden to the preparer and may be too complex for the average user. We strongly believe that the costs to implement a direct method of cash flow statement would far outweigh the benefits.

- 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 onetime implementation costs and ongoing application costs.
 - a. How might those costs be reduced without reducing the benefits of presenting operating cash receipts and payments?
 - b. Are those costs incremental to the overall costs to adopt the proposed presentation model?

Johnson & Johnson is a global company operating on a decentralized approach that utilizes many general ledger systems that are not designed to capture information on a cash basis. The Board's proposed financial statements would require the development of systems that would capture transactional data categorically by function, by nature on both cash and accrual basis. The costs, human resources and time necessary to transform our accounting systems and policies would not be justified without the Board and the users of

financial statements providing substantial evidence that a direct presentation provides better decision-useful information.

21. Based on 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?

We do not believe that the effect of basket transactions should be allocated to the related section and categories in the statement of comprehensive income and the statement of cash flows to achieve cohesiveness. We believe that the effects of all acquisition or disposal transactions should be presented in the category that was the predominant source of these effects.

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?

No response

- 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 amounts, 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 mentioned above we believe the reconciliation schedule would be costly and a burden on the organization to prepare. If the objective of the Board is to highlight fair value changes and valuation adjustments we feel that the complex reconciliation schedule may not increase the users' understanding of the amount, timing and uncertainty of an entity's future cash flows. We feel that fair value changes and valuation adjustments should be addressed in existing or additional disclosures and the reconciliation schedule should not be a required disclosure.

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 believe disclosure of the changes in fair values of assets and liabilities should be addressed in additional disclosures to the financial statements and not in the proposed reconciliation schedule.

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?

See response to question 24

- 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. APB Opinion No. 30, Reporting the Results of Operations—Reporting the Effects of Disposal of a Segment of a Business, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions, 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?

We believe the disclosure of unusual and infrequent events is sufficiently addressed in existing pronouncements. Additional highlights in the reconciliation schedule are not necessary.

Question Specific to the FASB

No response

27. As noted in paragraph 1.18(c), the FASB has not yet considered the application of the proposed presentation model to nonpublic entities. What issues should the FASB consider about the application of the proposed presentation model to nonpublic entities? If you are a user of financial statements for a nonpublic 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.