**Financial Statement Presentation**

Staff draft of an exposure draft

**Introduction**

The project on financial statement presentation is a joint project of the International Accounting Standards Board (IASB) and the US Financial Accounting Standards Board (FASB) to establish a common standard that would improve how information is organised and presented in the financial statements.

The IASB has implemented the decisions reached in the first phase of this project into IFRSs. Accordingly, a future FASB exposure draft will include improvements related to that phase as well as the matters the boards are currently discussing together. For the IASB, the project covers three main areas: (a) the replacement of IAS 1 *Presentation of Financial Statements* and IAS 7 *Statement of Cash Flows*; (b) the presentation of other comprehensive income (OCI) and (c) the presentation of discontinued operations.

In 2008 the boards published a discussion paper in which they set out the principles for presenting financial statements in a manner that portrays a cohesive financial picture of an entity’s activities, disaggregates information so that it is useful in predicting an entity’s future cash flows, and helps users to assess an entity’s liquidity and financial flexibility. The boards actively reconsidered the discussion paper proposals in the light of the comments received, the results of their other outreach activities with preparers and users, and academic research assessing the utility of certain proposals from a user perspective.

In July 2010 the staff of the IASB and the FASB posted on each board’s website a staff draft of an exposure draft that reflects the boards’ cumulative tentative decisions on financial statement presentation, concluding with their joint meeting in April 2010. All of those proposals have been reported as tentative decisions in IASB *Update* and FASB *Action Alert*. The proposals to change the presentation of OCI and discontinued operations are not covered in the staff draft as they are being addressed in separate projects.

The financial statement presentation project is an ongoing project. The boards decided to engage in additional outreach activities before finalising and publishing an exposure draft. Those activities will focus primarily on two areas: (1) the perceived benefits and costs of the proposals and (2) the implications of the proposals for financial reporting by financial services entities. In particular, the staff plan:

(a) to ask users of financial statements to evaluate how the proposed changes to the organisation of and information presented in financial statements would benefit their analysis and resource allocation decisions.

(b) to ask preparers of financial statements to evaluate the effort and cost involved in adopting these proposed changes in their unique circumstances.

(c) to meet preparers and users of the financial statements of financial services entities to discuss the proposed changes.

(d) to gather additional information about benefits and costs by doing more field work on the proposals in the staff draft, including additional field testing and/or experimental research.

After completing those outreach activities, the boards will consider whether to change any of their tentative decisions in response to the input received.

The following is a summary of the main proposals that would result from the boards’ tentative decisions. The summary and the proposals included in the staff draft have been made publicly...
available only for information as a basis for outreach activities. The boards are not formally inviting comments on the staff draft; however, they welcome input from interested parties. The boards expect to publish an exposure draft for public comment in early 2011.

Summary

Why are the IASB and FASB addressing financial statement presentation?

S1. How an entity presents information in its financial statements is vitally important because financial statements are a central feature of financial reporting—a principal means of communicating financial information to those outside the entity.

S2. The IASB and the FASB initiated the joint project on financial statement presentation to address users’ concerns that existing requirements permit too many alternative types of presentation and that information in financial statements is highly aggregated and inconsistently presented, making it difficult to understand fully the relationship between an entity’s financial statements and its financial results.

S3. The objective of the financial statement presentation project is to establish a global standard that will guide the organisation and presentation of information in the financial statements. The proposals developed in this project would directly affect how the management of an entity communicates financial statement information to the users of its financial statements, such as existing and potential equity investors, lenders and other creditors. The boards’ goal is to improve the usefulness of the information provided in an entity’s financial statements to help those users in their decision-making.

Information is not presented consistently in financial statements

S4. Transactions or events recognised in financial statements today are not described or classified in the same way in each of the statements. That makes it difficult for users to understand how the information in one statement relates to information in the other statements. For example, the boards’ standards on the statement of cash flows require a section for operating activities, but International Financial Reporting Standards (IFRSs) and US generally accepted accounting principles (GAAP) do not provide a section for operating activities in the statement of comprehensive income or the statement of financial position. That makes it difficult, for example, for users who want to compare operating income with operating cash flows—a comparison often made in assessing the degree to which an entity’s earnings are likely to recur and to reflect the underlying cash flows. Even though users can sometimes understand the relationship between items of information in the financial statements (eg the statement of cash flows is intended to explain the change in the cash account), users have asked for improved linkage among the different statements.

S5. Both IFRSs and US GAAP permit alternatives for how an entity presents information in its financial statements. Permitted alternatives include (a) direct and indirect methods of presenting operating cash flows and (b) presentation of all items of income and expense in an overall statement of comprehensive income or in two statements. US GAAP permits a third alternative—presentation of other comprehensive income items in the statement of changes in equity rather than in a performance statement. Alternative presentations make it difficult for users to compare financial information across entities.

S6. IAS 1 Presentation of Financial Statements includes minimum presentation requirements for an entity applying IFRSs. Although US GAAP includes some requirements that focus on presentation of information in the financial statements (eg how information is to be classified in the statement of cash flows), those requirements were developed on a statement-by-statement basis and are not as comprehensive as IAS 1. In addition, the US Securities and Exchange Commission (SEC) requires particular presentation and disclosures for entities that file
financial statements in accordance with Regulation S-X. Thus, the existing presentation requirements in IFRSs and US GAAP provide opportunities for a wide spectrum of presentation formats that comply with the requirements but vary in detail and comparability. This is counter to the needs of users. Increased globalisation of capital markets and investment opportunities have led to a need for a common set of principles for presenting information in financial statements used by capital providers around the world. Even if entities’ financial statements use the same underlying recognition and measurement principles, different presentations of the resulting information make it difficult for users to compare the financial results of those entities.

**Information is not sufficiently disaggregated in financial statements**

S7. Even though IAS 1 and Regulation S-X address presentation issues, IFRSs and US GAAP provide little specific guidance on the presentation of line items in financial statements, such as the level of detail or number of line items that should be presented. The resulting variation and inconsistency in the amount of aggregation create difficulties for users who want to understand and analyse an entity’s activities. For example, some entities may disaggregate direct product costs (e.g., materials and labour) as well as general and administrative costs (e.g., rent and utilities) in their statements of comprehensive income. However, other entities may present both product costs and general and administrative costs in the aggregate. Such aggregation makes it difficult for users to study the relationship between revenue and costs for an entity’s principal activities as well as to perform a benchmark analysis of those activities across an industry.

S8. Insufficient disaggregation also makes it more difficult for users to understand how a line item in one financial statement relates to other information presented in the other financial statements. For example, a single line in the statement of comprehensive income for cost of goods sold makes it difficult for a user to understand how the cost of goods sold may affect future cash flows. This is because cost of goods sold usually comprises both cash and non-cash amounts as well as various expenses that respond differently to similar economic events.

S9. It is also common practice for users to analyse an entity’s financial performance independently of its capital structure. However, users say that this analysis is difficult because financial statements do not usually distinguish an entity’s financing activities (how it obtains capital) from its business activities (how it uses that capital to generate income).

S10. Users of financial statements often analyse the change in an asset or a liability caused by changes in market prices or rates (i.e., gains attributable to remeasurement of an asset) differently from other changes in an entity’s net assets. That is because those changes do not usually have the same implications for future cash flows as other amounts recognised in comprehensive income. However, amounts that are likely to have different implications for future cash flows are often aggregated in the statement of comprehensive income.

**Who would be affected by the proposals in this project?**

S11. The proposals in this project would affect all business entities that prepare financial statements in accordance with IFRSs or US GAAP except a benefit plan within the scope of IAS 26 Accounting and Reporting by Retirement Benefit Plans or within the scope of FASB Accounting Standards Codification™ Topics 960, Plan Accounting—Defined Benefit Pension Plans; 962, Plan Accounting—Defined Contribution Pension Plans; and 965, Plan Accounting—Health and Welfare Benefit Plans.

---

1 Regulation S-X sets out the form and content of and requirements for financial statements that are required to be filed by the Securities Act of 1933, the Securities Exchange Act of 1934, and the Investment Company Act of 1940.
What are the main proposals and how would they differ from current IFRSs and US GAAP?

Core principles

S12. There are two proposed core financial statement presentation principles—cohesiveness and disaggregation. Cohesiveness means that the relationship between items in the financial statements is clear and that an entity’s financial statements complement each other as much as possible. Disaggregation means separating resources by the activity in which they are used and by their economic characteristics. Together, the disaggregation and cohesiveness principles would enhance the understandability of an entity’s financial statement information.

Classification and format

S13. The proposals in this project would establish a common structure for the statements of financial position, comprehensive income and cash flows in the form of required sections, categories or subcategory and related subtotals. The financial statements would display related information in the same sections, categories and subcategory in each statement so that the information is more easily associated.

S14. Separate presentation of business and financing activities would allow for better communication of an entity’s financial position and financial performance.

S15. The business section would include items that are part of an entity’s day-to-day and other income-generating activities and segregate them into operating and investing categories. Select liabilities directly related to operating activities, which some users view as an alternative source of financing (eg a pension obligation), would be classified in a subcategory within the operating category.

S16. The financing section would include items that are part of an entity’s activities to obtain (or repay) capital and segregate them into debt and equity categories.

S17. Discontinued operations and income taxes would be presented in their own separate sections.

S18. The statement of changes in equity would not include the sections and categories used in the other statements because that statement presents information solely about changes in items classified in the equity category in the statement of financial position.

S19. The following table illustrates the sections, categories and subcategory in each financial statement:
Statement of financial position

S20. In the statement of financial position, an entity would classify its assets and liabilities into the sections, categories and subcategory on the basis of how those items relate to its major activities or functions. Thus, unlike current practice, assets, liabilities and equity would not be presented in groups.

S21. Within each section, category and subcategory, an entity would choose one of the following formats: short-term assets and liabilities presented separately from long-term assets and liabilities or its assets and liabilities presented in order of liquidity. An entity would use the format that provides the most relevant information. An entity would present amounts for total assets and total liabilities and, if applicable, amounts for total short-term assets, total short-term liabilities, total long-term assets and total long-term liabilities in the statement of financial position.

S22. The classification of assets and liabilities into the required sections, categories and subcategory is a means of disaggregating assets and liabilities by function. Assets and liabilities also would be disaggregated in the statement of financial position by measurement basis and/or nature. Nature refers to the economic characteristics or attributes that distinguish assets and liabilities that do not respond similarly to similar events.

Statement of comprehensive income

S23. In the statement of comprehensive income, an entity would disaggregate its income and expenses by function (ie the primary activities in which the entity is engaged, such as selling goods, providing services, manufacturing, advertising, marketing, business development or administration). An entity would further disaggregate those functional amounts by nature and present that information in the statement of comprehensive income or in the notes to financial statements. Examples of disaggregation of income and expenses by nature include disaggregating revenues from selling goods into wholesale and retail components or
disaggregating total cost of sales into materials, labour, transport, depreciation and energy costs.

S24. An entity would not present its income and expenses disaggregated by function if that disaggregation is not useful in understanding the entity’s activities and the amounts, timing and uncertainty of future cash flows. An entity that does not present its income and expenses disaggregated by function would disaggregate and present its income and expenses by nature in the statement of comprehensive income.

S25. In US GAAP, entities that are required to provide a segment note would disaggregate in that note income and expenses by their nature for each reportable segment, with different by-nature disaggregation permitted for each reportable segment. Those entities would also disclose additional operating measures in the segment note. In IFRSs, all entities would disaggregate income and expenses by their nature on an entity basis (not by reportable segment) and present that information in the statement of comprehensive income or disclose that information in a separate note.

S26. As proposed in a separate joint project on presentation of other comprehensive income, the statement of comprehensive income would be segregated into two parts: profit or loss (net income) and other comprehensive income. In IFRSs, items of other comprehensive income would be grouped into those that in accordance with other IFRSs would be reclassified subsequently to profit or loss when specific conditions are met and those that would not be reclassified subsequently to profit or loss. Income taxes would continue to be allocated to items in other comprehensive income.

S27. In that separate joint project on presentation of other comprehensive income, the IASB decided to refer to the statement of comprehensive income as a ‘statement of profit or loss and other comprehensive income.’ However, an entity would not be required to use that title for the statement.

**Statement of cash flows**

S28. In the statement of cash flows, an entity would use a direct method to present cash flows in each of its sections and categories. For example, an entity would present separately the classes of its cash receipts and payments for its operating activities, such as cash collected from customers and cash paid to suppliers to acquire inventory. The disaggregation of cash flows in the statement of cash flows would be more limited than in the statement of comprehensive income. This is a change from the proposal in the discussion paper the boards published on this project in October 2008.

S29. In current practice, most entities choose to present their operating cash flows indirectly in the statement of cash flows by reconciling profit or loss or net income to net operating cash flows rather than present those cash flows using a direct method. Existing IFRSs and US GAAP require all entities to use a direct method to present their investing and financing cash flows.

S30. An entity would also be required to reconcile operating income to operating cash flows as part of the statement of cash flows.

S31. The definitions of operating, investing and financing cash flows are different from the definitions in IAS 7 Statement of Cash Flows and Topic 230 Statement of Cash Flows. For example, cash flows related to capital expenditures are currently presented in the investing category. An entity would most likely present those cash flows in the operating category using the proposed definitions. Aligning the definitions across statements and disaggregating operating cash flows would help users relate information about operating assets and liabilities and operating income and expenses to operating cash receipts and payments.

**Notes to financial statements**

S32. The notes to financial statements would include new or additional disclosure requirements. In the notes to financial statements, an entity would be required to provide an analysis of the
changes between the opening balance and the closing balance of asset and liability line items that are important for understanding the current period change in the entity’s financial position. As part of that analysis, an entity would present separately the change related to cash transactions, non-cash transactions (eg reclassifications), accounting allocations (eg depreciation), write-downs or impairment losses, acquisitions or dispositions, and other remeasurements (eg fair value changes).

S33. [IASB only] As part of the analyses of changes in assets and liabilities, an entity would be required to present in a single note disclosure an analysis of changes in cash, short-term investments, finance leases and all line items in the debt category.

S34. The notes to financial statements also would include a note that discloses the remeasurement amounts recognised in the statement of comprehensive income and a narrative description as necessary to place the remeasurement information in context.

S35. [FASB only] In addition to providing other information in its segment note, an entity would provide a measure of operating profit or loss, operating assets, operating liabilities and operating cash flows for each reportable segment. An entity would reconcile the totals of each of those operating measures to the corresponding consolidated totals.

**Complete set of financial statements and comparative information [FASB only]**

S36. The FASB plans to propose some additional changes for US GAAP that are already required by IAS 1 (and thus also will be included in the IASB’s proposal).

S37. The definition of and the requirements for a complete set of financial statements would become authoritative in US GAAP. Currently, a complete set of financial statements for the period is defined only in the FASB Concepts Statements. The FASB’s proposal would require an entity to present one period of comparative information. Thus, a complete set of financial statements would consist of, at a minimum, statements of financial position, comprehensive income, cash flows and changes in equity, and notes to financial statements for two periods (the current period and the previous period). An entity would present each of its financial statements with equal prominence.

S38. Currently, US GAAP encourages an entity to present comparative information but does not require it. The FASB proposal differs from SEC Regulation S-X, which requires two statements of financial position for the two most recent years and three statements of income and cash flows for the three years preceding the most recent statement of financial position.

S39. The form and content of the statement of changes in equity would be similar to what many entities in the United States provide in their financial statements today relating to changes in shareholders’ equity. However, that information is usually presented in the notes to financial statements in accordance with Regulation S-X.

S40. An opening statement of financial position would be part of a complete set of financial statements if an entity applies an accounting principle retrospectively, restates its financial statements or reclassifies items in the financial statements.

**How are the main proposals an improvement in IFRSs and US GAAP?**

S41. The proposals in this project would improve the comparability and understandability of information presented in financial statements by imposing some degree of standardisation for the way information is presented in the financial statements, particularly regarding how information is classified and the degree to which it is disaggregated.

S42. The business section would depict how an entity uses its assets and liabilities to generate income and the financing section would provide greater transparency about an entity’s capital structure. Because the structure of the financial statements would separate the functional activities of an entity, it would assist users of financial statements who commonly analyse an entity’s performance independently of its capital structure.
S43. The presentation of assets and liabilities in the business section would clearly communicate the net assets that management uses in its income-generating (business) activities. Operating activities and investing activities would be classified and presented separately in the business section. Those changes in presentation coupled with the similar classification in the statements of comprehensive income and cash flows should make it easier for users to calculate financial ratios related to an entity’s operating activities.

S44. The statement of comprehensive income and related notes would include more subtotals than are currently presented in an income statement or a statement of comprehensive income. Those additional subtotals would allow for the comparison of effects across the financial statements. For example, users would be better able to assess how operating assets and liabilities generate operating income and cash flows.

S45. The statement of comprehensive income and related notes would also include more line items than are required today because of the disaggregation of dissimilar items (ie income and expenses by function and by nature) that were previously aggregated. Providing entities with the flexibility to present the disaggregated by-nature information in the notes to financial statements should improve the understandability of the statement of comprehensive income.

S46. The proposals in the boards’ exposure drafts on the presentation of other comprehensive income along with the presentation proposals in this project would improve the understandability of comprehensive income and the relationships between changes in the statement of financial position, components of other comprehensive income and components of profit or loss or net income for each period.

S47. A direct method of presenting cash flow information would make the statement of cash flows more intuitive and understandable to a broad range of users of financial statements, improve the ability to predict future cash flows and provide insight into an entity’s cash conversion cycle. It also would provide insight into the relationship between (a) revenues and expenses presented in the statement of comprehensive income and (b) cash flows presented in the statement of cash flows.

S48. The proposed requirement to reconcile operating income to operating cash flows as an integral part of the statement of cash flows would make the relationships of changes in operating assets and liabilities clearer to users of financial statements.

S49. The proposed requirement to disclose an analysis of the changes between the opening and closing balances of asset and liability line items that management regards as important for understanding the change in an entity’s financial position should result in useful information. This is because a change in an asset or liability line item is the result of numerous transactions or events that differ in their ability to help users predict future cash flows and assess the likelihood that earnings levels are sustainable or likely to recur.

S50. The proposed requirement to disclose remeasurement amounts recognised in comprehensive income should provide users with information they do not currently have that will help them assess the amount, timing and uncertainty of future cash flows.

S51. The [FASB only] proposal to disclose disaggregated by-function and by-nature income and expense information in the segment note puts that information in the most decision-useful context. Disclosing a measure of operating assets, liabilities, profit or loss, and cash flows by reportable segment would bridge the presentation differences between the proposed structure of the related statements and an entity’s segment note.

S52. [FASB only] Convergence with the IASB on the form and labelling of financial statements will enhance comparability among entities from different jurisdictions.
How do the boards’ tentative decisions differ?

S53. The boards’ tentative decisions differ in the following ways:

(a) The IASB proposes retaining the minimum line item requirements for the statement of financial position. The FASB does not propose including these requirements because the disaggregation principle provides guidance on how an entity should determine the line items to present in that statement.

The FASB does not expect this difference to result in a significant difference in practice.

(b) The FASB proposes that an entity with more than one reportable segment should be required to present by-nature income and expense information in its segment note because that note provides the most decision-useful context for that information. To make that information more decision-useful, the FASB proposes that the by-nature disaggregation may vary across segments and that some additional operating measures should be disclosed in the segment note.

The IASB proposes that by-nature income and expense information on an entity basis (not by reportable segment) should be disclosed either in the statement of comprehensive income or in a separate note. There would be no variation by reportable segment in the presentation of that by-nature information. The IASB proposal differs from that of the FASB because the IASB does not want to amend IFRS 8 *Operating Segments* in advance of its planned review of that standard. The IASB will undertake a post-implementation review of its segment reporting requirements after 2011. In that review, the IASB will consider whether to align those requirements with the changes the FASB proposes.

This difference is expected to lead to significant differences in segment reporting practice between financial statements prepared according to US GAAP and those using IFRSs.

(c) The IASB proposes that information about the changes in asset and liability line items that normally constitute net debt should be disclosed together as a single note. The FASB does not propose a similar disclosure because users of US GAAP financial statements have not requested that information.

The FASB does not expect this to be a significant difference in practice because many of the amounts included in the net debt analysis will be included in the analyses of changes in asset and liability line items provided by preparers of US GAAP financial statements. Therefore, users of those statements will be able to incorporate that information into their individual analyses as desired.

[For ease of understanding the differences in the boards’ tentative decisions, the IASB staff draft includes paragraphs that would be proposed by the FASB but not the IASB and the FASB staff draft includes paragraphs that would be proposed by the IASB but not the FASB.]