



## **Comments on the Joint IASB/FASB Discussion Paper “Preliminary Views on Financial Statement Presentation” by the British Accounting Association Special Interest Group in Financial Accounting and Reporting**

The Financial Accounting and Reporting Special Interest Group (FARSIG) is a special interest group of the British Accounting Association. Its technical committee is charged with commenting on Exposure Drafts and Discussion Papers issued by standard setters on issues relating to financial accounting and reporting. Its views represent those of its members and not those of the BAA.

The British Accounting Association (BAA) is the representative body for UK accounting academics and others interested in the study of accounting and finance in the UK. The BAA Financial Accounting and Reporting Special Interest Group is the BAA's designated group specialising in issues relating to financial reporting. This response has been formulated by Mike Jones (Cardiff Business School) with detailed comments from Vivien Beattie, David Oldroyd and Pauline Weetman and has been approved by the Technical Committee of the Special Interest Group.

### ***General Remarks***

This discussion paper is a comprehensive revamping of the way in which financial items within the accounts are presented. As such it will involve a considerable amount of upheaval for those preparing and studying accounts, particularly for the users of the accounts. It is a daunting document which aims to make comparisons more valid. However, it significantly adds to the complexity of the statements. A key question, therefore, is whether the time and effort involved in this restructuring of the accounts will bring material added value to the user. In other words, is this a substantial improvement to the present situation? Or to put it another way is there a widespread dissatisfaction among present users of accounts that the present form of the income statement, balance sheet and cash flow statement are inadequate?

The short answer is that we believe that the case is not sufficiently made. Why is it important to substantially revamp the present financial presentation? Where is the weight of empirical evidence and academic research to support such a change? It is certainly not presented in this discussion paper. Has it been commissioned? Has it been published? The evidence which is presented in the discussion paper is scattered in various footnotes (such as 14, 19 and 20, 21, 22, 23 and 26). However, this is grossly inadequate and disconnected for such a major change. It deals with specific issues (such as accruals and cash flow) rather than taking a holistic overview. In addition, most of the studies are market-based ones not behavioural ones. Without more evidence, there appears to be no compelling reason to change the present situation. The introduction gives as a rationale of users' concerns that the financial statements are too aggregated, but they also complain the Annual Report is too long. The present prepared revisions will add length and complexity for dubious benefit. We would prefer consultation about present practices in presenting financial statements before proposing a radical, and perhaps unnecessary, new set of financial statements. It also seems strange to us that this project based on presentation and disclosure is proceeding at this time before there is agreement on the concepts. The current IASB work plan lists Phase E of the

Conceptual Framework, “Presentation and Disclosure” as an item for future consideration. Surely it would be more logical to agree on the concepts before proceeding to the specifics.

If we take the three “supposed” objectives underlying the proposed presentation model and compare it to the present model:

- a) Why does the present financial picture of an entity’s activities not portray a cohesive financial picture?
- b) In what way does the present financial picture not disaggregate information to predict an entity’s future cash flows? If it does not, why cannot the present financial statements be amended more simply? What extra information will be provided by the new financial statements and why can it not be incorporated into the present presentation?
- c) In what ways does the present presentation not help users assess an entity’s liquidity and financial position?

In short, what are the perceived advantages of the new presentational formats? They are not self-evident. Also, what are the additional disclosures of the new system and are they to be located in the new notes to accounts? We do, however, agree with more detail being presented on the face of the accounts.

A particular concern for FARSIG also is in the second objective underlying the proposed presentation model that the form of presentation adopted should be “useful in predicting an entity’s future cash flows” (S3, b). FARSIG does not accept that this is the sole criterion for assessing a business. It believes there is a stewardship function. When assessing this stewardship function, it is important to consider assets and liabilities. We believe that assessing an entity’s past performance should be an explicit objective under Stewardship.

A key aspect of the new system is its distinction between operating, investing and financing flows throughout the three statements. This overrides the more traditional classification of assets and liabilities. However, by including these distinctions it makes the statements very complex and unhelpful. If the aim is “to make it easier for users to calculate some key financial ratios for an entity’s business activities or its financing activities” (page 16), then would it not be considerably simpler to suggest certain ratios which might prove helpful and then ask companies to provide them? Obviously, many users, but not all, might wish to *supplement or modify these preparer supplied ratios.*

Turning to the Appendices and looking at the “main” statements, it is very helpful to have the examples of Toolco and Bank Corp. However, it would have been useful to include all the items in both (where appropriate of course). It is not clear which of the items in Toolco’s Statement of comprehensive income are mandated. Is it all, or are some of these for illustration?

#### ***Statement of Comprehensive Income***

- i) There is no particular problem with this – although it is not clear which items will be mandated.

ii) Other operating income appears to be a strange mixture of short-term and long-term items. Would not the long-term items be better split out and put into a separate category before other comprehensive income (e.g., disposables, goodwill, etc)? Is not share of profit of Associate A arguably an investing flow?

### ***Statement of Financial Position***

i) From a stewardship perspective, and also from the perspective of decision-making, the threefold division appears to lose in clarity what it might gain in cohesiveness. Users will probably assess a company primarily in terms of assets, liabilities and equity (as per the summary at the foot of the statement). Therefore, it makes more sense to us to retain these headings. We would prefer the categorisation at the foot of the statement to be incorporated into the main statement. Alternatively, we suggest including working capital as a separate item under “assets”. Reporting entities could if they wished have separate categories for investing and financing under the assets and liability headings.

ii) It seems somewhat unnecessary to have a separate heading for taxes.

### ***Statement of Cash Flows***

i) Under operating flows, the category “cash from other operating activities” appears to include both short-term and long-term items (Disposal of PPE and Investment in Associate A) which can be seen as investing flows.

ii) Discontinued operations would more logically occur under operating flows. Both the cash flow statement and the statement of comprehensive income do not make it clear whether “cash paid from discontinued operations” and “loss on discontinued operations” comprise capital as well as revenue items. Paragraph 2.37 suggests they do. If this is the case, including them together in a single figure represents an unhelpful aggregation of unlike items.

### ***Changes in Equity***

Seems reasonable

### ***Notes to the Financial Statements***

Seem reasonable apart from Toolco’s reconciliation of cash flows which is somewhat complicated and probably not very helpful. We cannot see who would want to use such a complex reconciliation. Certainly not the average investor and we suspect not the analyst.

### ***Answers to specific questions***

## ***Chapter 2: Objectives and principles of financial statement presentation***

***Q1. 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.**

It is undoubtedly true that cohesiveness is very important. However, it is not obvious that the revised statements are more understandable than the existing ones. Cohesiveness, we would argue is not as important as either simplicity or understandability. As noted above, assessing an entity's past performance should be included explicitly as an objective to be consistent with the stewardship function of accounts.

**Q2. 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?**

In theory, this would provide more information. However, the added complexity may be counter productive.

**Q3. 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?**

Equity represents the interests of present shareholders and for stewardship reasons should be included as a separate category.

**Q4. 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?**

Clarity and understandability would dictate that discontinued operations be shown separately from the continuing operations. However, we feel disaggregating them into separate sections would not help.

**Q5. 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?**

It provides an element of discretion which is probably undesirable. Part of the problem arises because of the enhanced disaggregation of the new 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?**

We think, given the history of impression management within financial reporting that it may well do.

**Q6. 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?**

No, not really. We think that those users who wish to calculate ratios will do so and vice versa. If ratios are thought to be an important driver then perhaps the companies should have to calculate them mandatorily.

**Q7. 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.**

At the entity level, preferably. To classify individual assets and liabilities by segment is problematic given the interrelatedness of activities particularly in large group structures. However, additional disclosures could be made by reportable segment as supplementary material. The problem is to avoid over-complexity.

**Q8. 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.**

If one accepts your prior assumptions, which we do not necessarily, we would advocate the minimum disclosure consistent with the new system. Separating out total assets is difficult enough, let alone further segmentation. As noted above, widening the disclosure of segment assets to individual sections or to categories within sections implies a degree of separateness which may not exist in practice. In a group context it would be less artificial if the holding company were obliged to include all of its subsidiaries' individual accounts in its annual report, not that we would wish to advocate that.

**Q9. 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?**

Probably, if you accept your prior assumptions, which we do not necessarily. It is desirable for the definitions to indicate clearly that the business section subsumes the operating and investing categories.

**Q10. 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?**

Again, yes if you accept the priors which we do not necessarily

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

**Q11. 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?**

Most entities will have a statement of financial position. However, we see no reason to split the statement into operating, investing and financing etc. This obfuscates the division between long term and short term assets and obscures the overall picture. We cannot see what would be the incentive for any company to present this additional information – analysing individual categories of short-term assets/liabilities by their maturity dates.

**(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?**

The discussion paper contains virtually no guidance at all. Therefore, if this proposal is retained more will be needed. Also, to allow companies the choice may reduce comparability and produce opportunities for impression management. An alternative might be to make this type of categorisation by liquidity compulsory for all companies where their working capital includes long-term items (> 12 months).

**Q12. 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?**

No, seems logical to have them as part of cash

**Q13. 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?**

Neutral, about this proposed change, but see our doubts in introduction

**Q14. 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?**

A single comprehensive income statement is desirable. The present headings are reasonable.

**Q15. 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?**

If this new format is adopted, there is no harm to this. Perhaps the new totals could be shown as a note.

**Q16 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?**

Yes, possibly useful. Again there needs to be a balance between detail and complexity. It may be necessary to put excess detail in the notes.

**Q17. 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.**

Keep income taxes as a whole rather than a disaggregated item. Consequently, do not allocate them.

**Q18. 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.**

We do not really see how this categorisation could work in practice given that foreign exchange differences arising on consolidation are global figures, normally comprising a) the effect on the foreign subsidiary's net assets of the change in the rate of exchange between the start and end of the year, and b) the difference between the average rate applying to the income statement and the closing rate applying to the balance sheet.

***(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?***

We do not really understand this question. Presumably it is referring to the costs v. benefits of preparing and auditing the extra information, which have not been considered up until now.

***Q19. 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?***

Yes, we agree this would be an improvement on the indirect method in providing more useful information. However, this would involve more preparation/auditing costs and the loss of information on the effects on liquidity of changes in working capital. We need to recognise that accounting systems are currently designed for accruals accounting purposes. It would be a costly exercise to recode accounting systems to produce direct cash flow totals routinely. There needs to be a detailed survey of users to weigh up the advantages and disadvantages of the direct and indirect methods. Also the indirect method of reconciling cash flows to operating profits is easier to understand than the proposed reconciliation schedule of cash flows to comprehensive income.

***(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?***

Yes, it is more intuitively obvious than the indirect method. It is thus more likely to be understood by the average user.

***(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?***

If you are mandating the direct method, we see no reason to continue the indirect method except that the direct method does not as clearly highlight the effects on liquidity of changes in the components of working capital.

***Q20. 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?***

We think that most of the costs would be one-off implementation costs. It is not easy to see how these could be reduced. Moreover, there would also be ongoing auditing costs.

**Q21. 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?**

Given that any allocation of basket transactions would be subjective and arbitrary then their presentation as a single line item would probably be preferable.

#### **Chapter 4: Notes to financial statements**

**Q22. 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?**

In practice, this may be very complex. However, when practicable a simple classificational system could be adopted.

**Q23. 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.**

The examples presented are so complex that we doubt whether in practice most users would find these figures particularly useful or, indeed, understandable.

**(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.**

No – too complex and incomprehensible. Also it is unlikely to match the spreadsheets used by professional analysts and therefore will not help reduce their costs of information gathering.

**(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.**

No – too complex and incomprehensible

***(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 indicated above, the costs of such a statement to a company would appear to outweigh the benefits. The guidance is probably sufficient for a trained accountant with an understanding of double-entry bookkeeping but too complex for other users.

***Q24. 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?***

As per our previous submissions to prior exposure drafts, we have problems with fair value as a concept. As a result of the credit crunch it is currently the source of considerable discussion. However, in principle, sensible disaggregated information may help understanding.

***Q25. 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 B10–B22? 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?***

We are against such a reconciliation as we do not think it would add clarity to the appreciation of financial statements. The alternative reconciliation formats put forward are even less easy for non-specialist accountants to understand than the reconciliation of cash flows to comprehensive income, and they disclose less information.

***Q26. 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.***

The problem is that the reconciliation schedule is already too complex. Therefore, if unusual items were flagged up this would make it even more so.

***(a) Would this information be decision-useful to users in their capacity as capital providers? Why or why not?***

As explained above it is quite complex. It would not add anything to the current practice of highlighting exceptional items in the notes to the accounts.

***(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?***

The problem with all such definitions is that they are subject to managerial subjective interpretation and impression management. As such this subjectivity can soon be abused.

***(c) Should an entity have the option of presenting the information in narrative format only?***

Probably a good idea – as long as it has to present a quantified and controlled narrative

### **Question specific to the FASB**

***Q27. 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.***

We think this is a step too far at the moment. As stated throughout this response, we think there are several problems with the new formats. We urge caution. We do not think the present proposals have more benefits than costs when applied to limited companies let alone non-public entities.

Michael Jones  
Chair FARSIG  
[JonesM12@cardiff.ac.uk](mailto:JonesM12@cardiff.ac.uk)

David Oldroyd  
Chair FARSIG Technical Committee  
[David.oldroyd@ncl.ac.uk](mailto:David.oldroyd@ncl.ac.uk)