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LETTER OF COMMENT NO. 58

Sir David Tweedie
Chairman
International Accounting Standards Board
30 Cannon Street
LONDON EC4M 6XH
UNITED KINGDOM

Dear Sir David

DISCUSSION PAPER: *PRELIMINARY VIEWS ON FINANCIAL STATEMENT PRESENTATION*

Thank you for the opportunity to comment on the International Accounting Standards Board's Discussion Paper *Preliminary Views on Financial Statement Presentation*. I am attaching for your information a copy of the Heads of Treasuries Accounting and Reporting Advisory Committee's comments on the Discussion Paper.

HoTARAC does not consider the issues of inconsistent, highly aggregated and alternative financial statement presentation requirements raised in the Discussion Paper to be of significance to the Australian public sector. This is because HoTARAC members ensure consistency within their jurisdiction by issuing accounting instructions to their entities. Further, the application of AASB 1049 *Whole of Government and General Government Sector Financial Reporting* ensures consistency at a whole-of-government level.

HoTARAC believes that the issues set out in the Discussion Paper will only address those issues identified by the IASB. The IASB will need to review optional treatments that exist within the Standards if they want to achieve full consistency between entities.

HoTARAC cannot see any benefit to the disaggregation approach raised in the Discussion Paper as it could potentially overload the financial statements. Minimum disclosure in the form of a single line item should be provided in the statements, and disaggregated amounts disclosed in the notes.

Please contact Peter Gibson from the Australian Department of Finance and Deregulation on 612 6215 3551 if you wish to discuss these matters further.

Yours sincerely

A handwritten signature in black ink, appearing to read 'D W Challen', written in a cursive style.

D W Challen

CHAIR

HEADS OF TREASURIES ACCOUNTING AND REPORTING ADVISORY COMMITTEE

7 April 2009

Encl

Contact: David Tadd
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Discussion Paper – Preliminary Views on Financial Statement Presentation

Chapter 2 – Objectives and principles of financial statement presentation

Question 1: Would the objectives of financial statement presentation proposed in paragraphs 2.5–2.13 improve the usefulness of 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.

The majority of HoTARAC members do not consider that the three proposed objectives will improve the usefulness of the information provided in an entity's financial statements as the objectives are aligned to the current qualitative characteristics. Cohesiveness and disaggregation would be aligned to the current qualitative characteristics of understandability and liquidity and financial flexibility would be aligned to relevance.

To improve information usefulness, the IASB should ensure that all information required to be presented or disclosed is aligned to the qualitative characteristics and financial statement objectives determined by the Conceptual Framework Project.

The Board should not consider any other objectives of financial statement presentation in addition to, or instead of, the objectives proposed in this Discussion Paper.

Question 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?

Separating business activities from financing activities may provide more decision-useful information by assisting users to assess the stewardship of management. It would also provide greater transparency over the activities of the entity.

Question 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?

Equity should be presented separately from the financing section. Equity has different characteristics to other sources of funding, in particular the way it is derived through owners or prior periods and the way accumulated results are not derived purely from financing activities. Presenting equity separately would satisfy the cohesiveness objective and would maintain the traditional approach whereby the Statement of Financial Position balances.

Question 4: In the proposed presentation model, an entity would present its discontinued operations in a separate section (see paragraphs 2.20, 2.37 and 2.71-2.73). Does this presentation provide decision-useful information? Instead of presenting this information in a separate section, should an entity present information about its discontinued operations in the relevant categories (operating, investing, financing assets and financing liabilities)? Why or why not?

The most decision-useful way to present information on discontinued operations is by separating this information from other sections of the Statement of Financial Position. This presentation method is superior as it clearly identifies those items which are not going to contribute to the entity's objectives in the future.

Question 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).

Part (a): Would a management approach provide the most useful view of an entity to users of its financial statements?

A management approach would ensure that assets and liabilities are classified in the way they are used by the entity. However, the subjectivity of this approach will, in HoTARAC's opinion, reduce the comparability between entities and increase incentives for management manipulation. Subsequently, this would make it difficult to question specific accounting classifications, as the response would be "this is management's view", although management must explain its classification policy in the accounting policy note. Conversely, restricting entities to a rigid rules-based format would promote consistency and comparability among entities, but the information might not be relevant and useful.

Therefore, HoTARAC considers that the Standard should include some guidance to assist management in their category selection. The Standard should also include disclosure requirements on the method of determining the category and establish principles to limit the changes allowed between categories from period to period. This guidance would help limit possible manipulation by management.

Part (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?

Refer to question 5(a).

Question 6: Paragraph 2.27 proposes that both assets and liabilities should be presented in the business section and in the financing section of the Statement of Financial Position. Would this change in presentation coupled with the separation of business and financing activities in the statements of comprehensive income and cash flows, make it easier for users to calculate some key financial ratios for an entity's business activities or its financing activities? Why or why not?

For individual entities, the proposals may make it easier to carry out ratio analysis by making it easier to find information about different categories (operating, investing and financing). However, the inclusion of items within these categories could be viewed as subjective, which could impair ratio comparisons between similar entities. This is discussed further in the answer to question 5 (above).

With regard to the effectiveness of the proposed layout, the totals of each of the elements (assets, liabilities, equity, revenue and expenses) should be provided on the face of the statements. The proposed layout is quite different to the current separation of assets and liabilities. This may take some time to get used to, as it appears overcrowded, as a result of the extra categories and the mix of assets and liabilities within these categories.

Question 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.

The Australian public sector does not apply IFRS 8. However, there is merit in classifying assets and liabilities at the reportable segment level as opposed to the entity level. Regarding the proposed management approach, reporting at reportable segment level would best reflect the activities of the entity in terms of classifying assets and liabilities as operating, investing or financing. This could in practice become quite a complex task for large, diverse organisations with matrix organisational structures. Therefore, HoTARAC would not like to see any mandatory requirements introduced.

Question 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.

The majority of HoTARAC members believe that changes need to be made to the existing segment disclosure requirements under the proposed presentation model. Given the proposed categorisation of assets and liabilities, it might be beneficial to report total figures at the section level (business, financing etc) or, if material, the categories within the sections (operating, investing, financing). The current system of reporting at the element level would be at too high a level under the proposed model due to the proposed focus on cohesiveness and disaggregation.

Question 9: Are the business section and the operating and investing categories within that section defined appropriately (see paragraphs 2.31–2.33 and 2.63–2.67)? Why or why not?

The business section definition and title is not appropriate for the public sector. The definitions are appropriate for other entities.

Question 10: Are the financing section and the financing assets and financing liabilities categories within that section defined appropriately (see paragraphs 2.34 and 2.56–2.62)? Should the financing section be restricted to financial assets and financial liabilities as defined in IFRSs and US GAAP as proposed? Why or why not?

The definitions seem appropriate. The financing section should only include financial instruments as stated. However, financial instruments should not be restricted to this category. For some entities, financial instruments will fall under the business activity section or the investing section.

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

Question 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.

Part (a): What types of entities would you expect not to present a classified Statement of Financial Position? Why?

The liquidity approach is adopted in Australian public sector as it aligns with the Government Finance Statistics presentation approach.

Part (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?

There should not be any more guidance issued. Whether a liquidity presentation would provide reliable and more relevant information to users would be determined by management. Management would be aware of whether the liquidity presentation is appropriate.

Question 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?

Cash equivalents should be a part of cash and not classified in a manner similar to other short-term investments. Cash and cash equivalents could continue to be disaggregated in the notes. HoTARAC considers that the management approach and the arguments provided in paragraphs 3.17-3.18 do not sufficiently justify the introduction of separate line items of cash and cash equivalents.

HoTARAC considers this proposal to be purely cosmetic as it does not enhance the liquidity and financial flexibility objective as suggested. This is because cash and cash equivalents are already disaggregated in the notes and the financial statements should be read in conjunction with the notes. Additionally, the accounting policy note will provide information on how management determines its cash equivalents (e.g. specifically mentioning the cut-off maturity date for classifying an investment as a cash equivalent). This is sufficient information to meet user needs. If the money can, and is intended to be used as an equivalent for cash, it is clearly not an investment.

Question 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?

This level of disaggregation might be beneficial in providing information about assets and liabilities that were measured differently. However, it could also double the number of line items within the Statement of Financial Position, making it harder to locate important information. In HoTARAC's opinion, the reasoning provided in the Discussion Paper does not justify disclosure in the statements. Minimum disclosure in the form of a single line item should be provided in the statements, with details of the differing measurement bases of similar assets and liabilities disclosed in the notes.

Question 14: Should an entity present comprehensive income and its components in a single Statement of Comprehensive Income as proposed (see paragraphs 3.24–3.33)? Why or why not? If not, how should they be presented?

The option of a separate Income Statement should continue as there is little justification for the elimination of the choice of two separate statements. Having the option of two separate statements does not reduce comparability or usefulness. However, a minority of HoTARAC members believe a single statement is superior to two statements as the separating of information confuses users.

Question 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?

On the basis of the proposed categorisation of operating, investing, and financing, the proposal in paragraph 3.25 has merit and may enhance decision-usefulness. The proposal would make the other comprehensive income section more consistent and comparable with other proposed disclosures on the face of the financial statements. HoTARAC agrees with the Discussion Paper's comments that the level of disclosure could help users to understand:

- (a) the relationship between the Statement of Comprehensive Income and the Statement of Financial Position; and
- (b) the section or category in which potential future reclassification adjustments will be presented in profit or loss or net income in future Statements of Comprehensive Income (paragraph 3.37).

Where an item of other comprehensive income relates to an asset or liability that is classified in more than one category, this could be disaggregated in the notes. Otherwise, if the relationships to the different categories are material, then the items of other comprehensive income should be disaggregated on the face of the statements.

Question 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?

Disaggregating by function, nature, or both, as in current practice with IFRS, would provide decision-useful information but only if the appropriate method is chosen. However, further disaggregation could provide information overload and reduce understandability and subsequently decision-usefulness. Therefore, the current levels of disaggregation and guidance (i.e. method chosen on the basis of whether it provides reliable and more relevant information) should be retained and minimum disclosure maintained.

Question 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.

Allocation into the categories is relevant for the for-profit sector and would provide useful information to users.

Question 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.

Part (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.

Presenting foreign currency transaction gains and losses in the same section and category as the assets and liabilities that gave rise to the gains or losses may be decision-useful and would also achieve the cohesiveness objective. However, this might not be feasible or realistic.

Part (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?

A cost the Board should consider is the increased time required to undertake this process.

Question 19: Paragraph 3.75 proposes that an entity should use a direct method of presenting cash flows in the Statement of Cash Flows.

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

The direct method is appropriate and would provide information that is more decision-useful than the indirect method. In Australia, AASB 107 paragraph 19 encourages the use of the direct method as it provides information which may be useful in estimating future cash flows. This information is not available under the indirect method. This use of the direct method is already supported in the Australian public sector as it provides reliable and relevant information.

Part (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?

The direct method properly categorises items into cash inflows and outflows. The indirect method works backwards to reconcile the figure, without actually disclosing the operating cash receipts and payments. Therefore, the direct method provides more relevant information that aids in the cohesiveness and disaggregation objectives. Although the direct method is not linked to the other statements, it would still aid cohesiveness due to the proposed presentation for the statements being categorised into operating, investing and financing. Cohesiveness is also promoted by the direct method Statement of Cash Flows in part providing the operating inflows and outflows of cash to compare, rather than the reconciliation which provides non-cash items.

Part (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 proposed approach appears to be the reverse of the current reconciliation (i.e. comprehensive income to cash flows relating to operating activities only). It still provides the same information, but with increased disaggregation of amounts through the columnar approach. It includes the proposed Statement of Cash Flows before the equity section and the proposed Statement of Comprehensive Income.

The proposed schedule would provide superior information on non-cash expenses as it would reconcile each line item in the Statement of Cash Flows to the line items in the Statement of Comprehensive Income.

HoTARAC agrees with the discussion in paragraph 4.46 that the proposed approach of cash flows to comprehensive income would be easier to understand in terms of the use of positive and negative signs for items and how they affect comprehensive income.

Question 20: What costs should the boards consider related to using a direct method to present operating cash flows (see paragraphs 3.81–3.83)? Please distinguish between one-off or one-time implementation costs and ongoing application costs. How might those costs be reduced without reducing the benefits of presenting operating cash receipts and payments?

Likely costs of an entity moving from an indirect to a direct method of presenting operating cash flows:

Implementation costs:

- amending accounting systems to capture information about gross operating cash receipts and payments; and
- personnel training.

Ongoing application costs:

- system updates to include new cash receipts and payments as they occur; and
- data storage.

Question 21: On the basis of the discussion in paragraphs 3.88–3.95, should the effects of basket transactions be allocated to the related sections and categories in the Statement of Comprehensive Income and the Statement of Cash Flows to achieve cohesiveness? If not, in which section or category should those effects be presented?

Allocating the effects of basket transactions to the related sections and categories has merit where the allocation is not costly to implement and results in decision-useful information. Allocation guidance should be provided to promote consistency within and between entities.

Allocations across categories should not occur when the cost involved outweighs the benefits. Instead, the basket transaction should be presented in either the category that reflects the activity that was the predominant source of those effects (Alternative B) or in a separate section (Alternative C). HoTARAC considers that Alternative A (presenting in the operating category) is not a suitable method. Although this method is simple, it might not properly reflect the items contained in the basket transaction, which would impair decision-usefulness.

Chapter 4 – Notes to financial statements

Question 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?

An entity that uses the liquidity format for the Statement of Financial Position should disclose elements of the classified format, such as the maturities of its short-term contracted assets and liabilities. The liquidity format alone would not disclose such information which might be useful in decision-making. In addition, presenting this information is a requirement of IFRS 7 *Financial Instruments: Disclosures* in regards to the disclosure of financial liabilities. Providing information on short-term contractual maturities will help the user assess the entity's liquidity.

Question 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.

Part (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.

The proposed reconciliation schedule would increase users' understanding of the amount, timing and uncertainty of an entity's future cash flows. However, there is an overload of disclosure on the proposed reconciliation schedule due to the columnar approach and the addition of non-operating activities. As reflected in HoTARAC's comments on the Conceptual Framework Exposure Draft, there is too much emphasis given to the assessment of cash flows.

Part (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.

The proposed columns D (remeasurements that are recurring fair value changes or recurring valuation adjustments) and E (all other remeasurements) could be aggregated into a single column. Disaggregating the remeasurements into two columns does not provide any extra information for users because the line items themselves indicate whether or not they are recurring remeasurements. HoTARAC believes the other columns are suitable.

Part (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.

The guidance provided for preparing the reconciliation schedule is clear and sufficient. However, in reference to paragraph 4.45(b), HoTARAC believes it would be simpler to add that the cash components are the amounts extracted from the Statement of Cash Flows. This is consistent with the guidance provided in paragraph 4.45(f) on the Statement of Comprehensive Income.

Question 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?

Further disaggregation in the Statement of Comprehensive Income regarding changes in fair value should be considered in the Fair Value Project being undertaken by the IASB. HoTARAC members will not support a proposal that overloads the financial statements with information that could otherwise be provided in the notes.

Question 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 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?

The majority of HoTARAC members can see merit in considering alternative reconciliation formats. However, the alternative reconciliation formats presented in Appendix B of the Discussion Paper should not be considered for the reasons provided below.

The Statement of Financial Position reconciliation is excessive. The inclusion of three of the financial statements in their entirety plus the reconciling columns on the one schedule increases the size and complexity of the information, which may inhibit users from finding the information the proposed reconciliation is supposed to provide. For entities that primarily manage assets and liabilities rather than cash flows (e.g. the financial services industries that the reconciliation was intended to assist), the reconciliation would be of little use. Although the Statement of Financial Position reconciliation appears to provide the information currently provided using an indirect method to present operating cash flows (as asked in question 19© with regards to the proposed reconciliation schedule), the Statement of Financial Position reconciliation provides the information in a way that it is obscured by all the other information.

The Statement of Comprehensive Income matrix appears to be similar to the proposed reconciliation schedule, but the layout and amounts that are recorded in the “changes in assets and liabilities not from remeasurements” columns are different. This is because the matrix format does not clearly link with the Statement of Cash Flows due to line items in the Statement of Cash Flows not corresponding with line items in the Statement of Comprehensive Income. This results in the proposed layout having no place to fit some items of cash flow, meaning that the matrix does not achieve the proposed cohesiveness objective. For example, the matrix excludes information about how much cash was spent to maintain or increase capital assets, yet includes the depreciation which relates to these assets. Further, the matrix would not provide the information currently provided using an indirect method to present operating cash flows (as asked in question 19(c) with regards to the reconciliation schedule).

The minority of HoTARAC members believe that no other alternate reconciliation formats should be considered and that the reasons for rejecting the alternate formats given by the Board are valid. Members in the minority see that for some entities (e.g. the financial services industry), the Statement of Financial Position reconciliation might provide more useful information than the Statement of Cash Flows reconciliation, as pointed out in paragraph B22 of the Discussion Paper. However, entities should not be required to use the Statement of Financial Position reconciliation format. If there is more than one reconciliation statement (HoTARAC believes there should not be), the choice of which statement to use should be a management decision. The Board’s advisory groups considered that the schedule would be too detailed, complex and costly to prepare (paragraph B21(b)).

Question 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.

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

Information provided in the proposed memo column would be no more useful than if it were provided in narrative form. Providing the memo column could draw users’ attention away from the usual and frequent events or transactions which are more likely to be helpful in providing decision-useful information.

Part (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 definitions provided in APB Opinion No. 30 are not too restrictive and appear to be suitable. However, the definitions also equate to what used to be termed abnormal or extraordinary items. Currently, IFRSs do not permit these items to be disclosed.

As per the response to part (a) of this question, the inclusion of a memo column is not supported by HoTARAC. The inclusion of such information on the proposed reconciliation schedule would vastly increase the already large amount of disclosure provided on the proposed schedule, and would draw users' attention away from other information.

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

Given the nature of these items, a memo column might not be useful for some entities. Therefore, having the option of presenting information in narrative format makes sense. This option also makes it distinct from the reconciliation schedule so users are not confused with usual or frequent events or transactions.