

The LIAJ's Comments on the *Financial Statement Presentation* Staff draft of an exposure draft

1. We, The Life Insurance Association of Japan (LIAJ) thank the International Accounting Standards Board (IASB) for providing us with an opportunity to submit our comments on the *Financial Statement Presentation, Staff draft of an exposure draft*.
2. The LIAJ is a trade association comprised of all 47 life insurance companies currently operating in Japan. Its aim is to promote the sound development of the life insurance industry and maintain its reliability in Japan.

1. General Opinions

3. We submitted our comments on the IASB's discussion paper *Preliminary Views on Financial Statement Presentation* on 14 April 2009. On this occasion, we would like to comment on the *Financial Statement Presentation, Staff draft of an exposure draft*, recently published by staff of the IASB and the US Financial Accounting Standards Board (FASB), in light of 'benefit and cost' and 'financial reporting of financial services entities'. Having conducted a high level review of this draft, we would like the boards to deliberate some specific issues stated in these comments before the boards publish an exposure draft on financial statement presentation. We will not comment on particular issues described in the staff draft at this point, as we plan to submit our comments after reconsidering the final exposure draft when it is published by the boards for public comment.
4. Although it is likely that the structure of financial statements proposed in the staff draft will provide investors with decision-useful information, we believe it contains certain elements that need careful consideration in terms of costs and benefits, such as 'direct method statement of cash flows' and 'disaggregating information by function/nature.' With particular regard to the proposals on 'direct method statement of cash flows', we believe that the use of an indirect method in statement of cash flows should be allowed in terms of costs and benefits as the implementation of proposed direct method would impose excessive costs on preparers.
5. The boards did not debate which items should be presented in other comprehensive income (OCI) in the financial statement presentation project. Instead, they are being addressed in separate projects, including financial instruments, post-employment benefits and insurance contracts. In such cases as when the boards leave such considerations to individual projects, the presentation of OCI may be neglected on the grounds that such a conceptual principle does not exist. This may result in a lack of consistency among those projects. We therefore propose that the common nature of items to be presented in OCI should be considered across all projects.

2. Our comments on some specific issues in the staff draft.

<Structure of the financial statements>

6. With regard to the structure of the financial statements, this staff draft proposes that an entity's

business section comprises its operating activities and investing activities, which shall be presented separately. However, we think it would be difficult to clearly separate operating activity from investing activity using the same method as that of general business entities for financial services entities that invest in various types of financial instruments as part of their day-to-day operating activities. Therefore, we believe that the boards should develop a presentation format specific to financial services entities that would allow them to present operating activity and investing activity in a single category.

<Statement of financial position>

7. In the statement of financial position, an entity would be required to present short-term assets and liabilities separately from long-term assets and liabilities judged on the one year basis, or its assets and liabilities in order of liquidity. With regard to technical provision, which accounts for most of a life insurer's liabilities, classifying liabilities into short-term and long-term in each section on the face of financial statements, rather than in disclosed information, would be of little use in terms of costs and benefits. Instead, we believe that technical provision should be presented wholly rather than dividing it into short-term and long-term categories. Also, we find little value in classifying assets as short-term and long-term items as far as life insurers are concerned. Securities, which account for a substantial part of the total assets held by life insurers, include assets with a specified maturity, such as bonds and debentures, as well as assets with no specified maturity, such as common shares. We believe that such assets do not fit into the short-term or long-term categorisation and should therefore be presented wholly. Therefore, we take the view that entities should be able to choose presentation methods considering the relevance of financial statements according to the current IAS 1, *Presentation of Financial Statements* and this staff draft.

In addition, an entity is required to classify and present its assets and liabilities into the sections, categories and subcategories in the statement of financial position. We believe careful consideration is necessary, taking into account the cost the entity would incur in presenting them in this manner.

< Statement of comprehensive income>

8. In the statement of comprehensive income, an entity would be required to disaggregate its income and expenses by function and nature within each section and category. Although we do not deny the possibility of enhancing the usefulness of the information for users through disaggregation by function/nature, we do believe it necessary to consider carefully whether such efforts would impose excessive costs on the entity.

< To present a direct method statement of cash flows >

9. The staff draft proposes to eliminate the presentation of an indirect method statement of cash flows and requires all entities to present a direct method statement of cash flows. We do not deny the possibility that presenting cash flows using a direct method by some types of industries would be helpful in providing users of financial statements with information on the entity's ability to generate cash flows.

Meanwhile, for financial services entities that enter into many and various cash transactions on a day-to-day basis, hold a large amount of high liquidity financial instruments and trade those financial assets as part of their business activities, we are afraid that the cash flow information would not necessarily be as useful as the entities' financial performance. Even if the information

is regarded as useful, we could not consider that the total amount of cash flows and the figures in each item based on cash relate to the entities' ability to generate cash flows, thus, the benefit in presenting a direct method cash flows statement by financial services entities is likely to be more limited.

In addition, if the direct method is implemented, financial services entities may be required in practice to incur significant costs in order to establish new administration and systems to recognise transactions on a cash basis; therefore, we are concerned that financial services entities would incur greater costs compared to other types of industries.

Accordingly, we are of the view that the additional cost of preparing a direct method statement of cash flows would outweigh the benefit the users of financial statements might enjoy.

Furthermore, an indirect method statement of cash flows has not always been considered beneficial for users of financial statements because the sections displayed in the income statement and cash flows statement currently do not provide consistent presentation. We think the presentation by an indirect method or presenting information stated in paragraph 172 of this draft, i.e. a reconciliation of profit or loss from operating activities to net cash flows from operating activities, would meet the needs of the users when the sections displayed in both statements are unified.

Based on this, we believe that the boards should retain the alternatives in the new standard that leave the entities to select either a direct method or an indirect method depending on their business profile. This is because the indirect method would be more relevant for the objective of preparing financial statements in some types of industries. Although we are aware that the boards considered how a financial services entity should present cash flow information in the statement of cash flows at their board meeting in February 2010, we do not observe that the boards have fully discussed those issues. Therefore, we urge the boards to make the necessary amendment to the staff draft before publishing it as an exposure draft on financial statement presentation, following further discussion with constituents.

<The definition of cash flows in a statement of cash flows>

10. The definition of cash flows that are presented in a statement of cash flows, previously described as the 'changes in cash and cash equivalents of an entity', is amended to the 'changes in cash' (only including demand deposit) (according to the paragraph 169 (see paragraphs 117 and 118) of this staff draft.) We suggest that the boards retain the current definition of cash flows (i.e. the definition set out in the current IAS 7), or allow the entity to select the definition depending on its cash management practice according to either the current definition at the highest level or the proposed definition in the staff draft at the lowest level. Our reasoning for this is that the above mentioned amendment is not consistent with the objective 'to provide a meaningful depiction of how the entity generates and uses cash', which is considered one of the key objectives of a statement of cash flows.

We would also like to suggest that the boards amend the presentation requirement in the statement of financial position, when necessary, as the definition of cash flows in the statement of cash flows is intended to refer to the definition in the statement of financial position. This would ensure consistency of presentation in both statements.

For many entities, 'cash' is comprised of cash and cash equivalents. Both of these are managed together, and the ratio of cash and cash equivalents to the total 'cash' is determined contingently. In the following situation, for example, while the resulting cash flow is nil under the current IAS 7, it is 100 under the proposal in the staff draft. We are concerned that this result might

mislead users of the statement of cash flows when the entity does not generate any substantial 'cash.'

Opening balance: cash 100CU, cash equivalents 100CU

Closing balance: cash 200CU, cash equivalents 0CU

Cash flows presented in a statement of cash flows under current IAS 7: 0

Cash flows calculated under the proposal in the staff draft: 100

<Notes to financial statements>

11. Under the proposal in the staff draft, an entity would be required to disclose analyses of the changes between the opening balance and closing balance of asset and liability line items that management regards as important in the notes to financial statements. As noted above, we believe that the use of an indirect method in statement of cash flows should be allowed. Although information provided in the indirect method statement of cash flows will include fewer items, we believe that it represents adequate alternative information in the proposed analyses of the changes in asset and liability line items. In order to disclose the proposed analyses of those changes, preparers will need to incur costs for a system that would enable them to obtain detailed data to be used as components for the reconciliation schedule and for the establishment of relevant administrative measures. Since those additional costs are expected to outweigh any benefits for users, the introduction of disclosing analyses of changes should be subject to due consideration in light of costs and benefits.