

FINANCIAL STATEMENT PRESENTATION DISCUSSION PAPER SUMMARY

INTRODUCTION

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 an entity. The International Accounting Standards Board (IASB) and the U. S. Financial Accounting Standards Board (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 fully understand the relationship between the financial statements and the financial results of an entity.

S2. This Discussion Paper invites comment on the Boards’ preliminary views on a proposed model for presenting information in the financial statements. The model is designed to make an entity’s financial statements more useful by requiring entities to provide detailed information organized in a manner that clearly communicates an integrated (cohesive) financial picture of an entity.

OBJECTIVES UNDERLYING THE PROPOSED PRESENTATION MODEL

S3. The Boards developed three objectives for financial statement presentation based on the objectives of financial reporting and the input the Boards received from users of financial statements and from members of their advisory groups. Those proposed objectives state that information should be presented in the financial statements in a manner that:

- a. **Portrays a cohesive financial picture of an entity’s activities.** A cohesive financial picture means that the relationship between items across financial statements is clear and that an entity’s financial statements complement each other as much as possible.
- b. **Disaggregates information so that it is useful in predicting an entity’s future cash flows.** Financial statement analysis aimed at objectives such as assessing the amount, timing, and uncertainty of future cash flows requires financial information that is disaggregated into reasonably homogeneous groups of items. If items differ economically, users may wish to take that into account differently in predicting future cash flows.
- c. **Helps users assess an entity’s liquidity and financial flexibility.** Information about an entity’s liquidity helps users to assess an entity’s ability to meet its financial commitments as they become due. Information about financial flexibility helps users to assess an entity’s ability to invest in business opportunities and respond to unexpected needs.

PROPOSED FORMAT FOR FINANCIAL STATEMENTS

S4. The proposed presentation model requires an entity to present information about the way it creates value (its business activities) separately from information about the way it funds or finances those business activities (its financing activities).

- a. An entity should further separate information about its business activities by presenting information about its operating activities separately from information about its investing activities.
- b. An entity should present information about the financing of its business activities separately depending on the source of that financing. Specifically, information about nonowner sources of finance (and related changes) should be presented separately from owner sources of finance (and related changes).
- c. An entity should present information about its discontinued operations separately from its continuing business and financing activities.
- d. An entity should present information about its income taxes separately from all other information in the statements of financial position and cash flows. In its statement of comprehensive income, an entity should separately present information about its income tax expense (benefit) related to:
 - (1) Income from continuing operations (the total of its income or loss from business and financing activities)
 - (2) Discontinued operations
 - (3) Other comprehensive income items.

S5. The table below illustrates the proposed classification scheme for the financial statements. (The section names are in ***bold italic type***; required categories within sections are indicated by bullet points.) An entity may present the sections and categories within a section in a different order as long as the order is the same in each statement. Each section and category within a section would have a subtotal. The statement of comprehensive income also would include a subtotal for profit or loss or net income and a total for comprehensive income. The statement of changes in equity is not included in this table because it would not include the sections and categories used in the other financial statements.

| Statement of Financial Position | Statement of Comprehensive Income | Statement of Cash Flows |
|---|--|--|
| <i>Business</i> <ul style="list-style-type: none"> • Operating assets and liabilities • Investing assets and liabilities | <i>Business</i> <ul style="list-style-type: none"> • Operating income and expenses • Investment income and expenses | <i>Business</i> <ul style="list-style-type: none"> • Operating cash flows • Investing cash flows |
| <i>Financing</i> <ul style="list-style-type: none"> • Financing assets • Financing liabilities | <i>Financing</i> <ul style="list-style-type: none"> • Financing asset income • Financing liability expenses | <i>Financing</i> <ul style="list-style-type: none"> • Financing asset cash flows • Financing liability cash flows |
| <i>Income taxes</i> | <i>Income taxes</i> on continuing operations (business and financing) | <i>Income taxes</i> |
| <i>Discontinued operations</i> | <i>Discontinued operations</i> , net of tax | <i>Discontinued operations</i> |
| | <i>Other comprehensive income</i> , net of tax | |

| | | |
|---------------|--|---------------|
| <i>Equity</i> | | <i>Equity</i> |
|---------------|--|---------------|

CLASSIFICATION GUIDANCE

S6. To prepare financial statements using the classification scheme, an entity should first classify its assets and liabilities into the sections and categories in the statement of financial position; that classification will determine the classification in the statements of comprehensive income and cash flows. Classification should be consistent with how the asset or liability is used within an entity and the way an entity views its activities. An entity with more than one reportable segment should classify items according to how they are used in its reportable segments. This approach should allow management to communicate the unique aspects of its business(es) to users of its financial statements. The classification decision would reside with management and its classification rationale would be presented in the notes to financial statements as part of the accounting policy discussion. The Boards support a management approach to classification rather than a prescriptive approach because they believe it will result in financial statements that reflect how management views and manages the entity and its resources.

PRESENTING A COHESIVE SET OF FINANCIAL STATEMENTS

S7. To present a cohesive set of financial statements, an entity should align the line items, their descriptions, and the order of presentation of information in the statements of financial position, comprehensive income, and cash flows. To the extent that it is practical, an entity should disaggregate, label, and total individual items similarly in each statement. Doing so should present a cohesive relationship at the line item level among individual assets, liabilities, income, expense, and cash flow items.

HOW THE FINANCIAL STATEMENTS MIGHT CHANGE

Statement of Financial Position

S8. As illustrated in the table above, the statement of financial position would be grouped by major activities (operating, investing, and financing), not by assets, liabilities, and equity as it is today. The presentation of assets and liabilities in the business and financing sections will clearly communicate the net assets that management uses in its business and financing activities. That change in presentation coupled with the separation of business and financing activities in the statements of comprehensive income and cash flows should make it easier for users to calculate some key financial ratios for an entity's business activities or its financing activities.

S9. Assets and liabilities would be disaggregated into short-term and long-term subcategories within each category unless an entity believes presenting assets and liabilities in order of liquidity provides more relevant information. Totals for assets and liabilities and subtotals for short-term and long-term assets and liabilities would be presented in the statement of financial position or in the notes to financial statements.

Statement of Comprehensive Income

S10. The proposed presentation model eliminates the choice an entity currently has of presenting components of income and expense in an income statement and a statement of comprehensive income (two-statement approach) or, alternatively, of presenting information about other comprehensive income in its statement of changes in equity (U.S. generally accepted accounting principles only). All entities would present a single statement of comprehensive income, with items of other comprehensive income presented in a separate section. This statement would include a subtotal of *profit or loss* or *net income* and a total for *comprehensive income* for the period. Because the statement of comprehensive income would include the same sections and categories used in the other financial statements, it would include more subtotals than are currently presented in an income statement or a statement of comprehensive income. Those additional subtotals will allow for the comparison of effects across the financial statements. For example, users will be able to assess how changes in operating assets and liabilities generate operating income and cash flows.

S11. Another important aspect of the Boards' proposed presentation model is that an entity should disaggregate line items when such presentation will enhance the usefulness of the information in predicting future cash flows. In addition to classifying its income and expense items into the operating, investing, and financing categories, an entity should disaggregate those items on the basis of their function within those categories. An entity should further disaggregate its income and expense items by their nature within those functions to the extent that this disaggregation will help users in predicting the entity's future cash flows.

- **Function** refers to the primary activities in which an entity is engaged, such as selling goods, providing services, manufacturing, advertising, marketing, business development, or administration.
- **Nature** refers to the economic characteristics or attributes that distinguish assets, liabilities, and income and expense items that do not respond equally to similar economic events. Examples of disaggregation by nature include disaggregating total revenues into wholesale revenues and retail revenues or disaggregating total cost of sales into materials, labor, transport, and energy costs.

Statement of Cash Flows

S12. In the statement of cash flows, an entity should present separately the main categories of its cash receipts and payments for operating activities, such as cash collected from customers and cash paid to suppliers to acquire inventory (a direct method), rather than reconciling profit or loss or net income to net operating cash flows (an indirect method) as most entities do today. The Boards observed that a direct method is more consistent than an indirect method with the proposed objectives of financial statement presentation. Presenting cash receipt and cash payment line items in the operating category provides a more useful disaggregation of cash flow information. In addition, a direct method presentation helps users relate information about operating assets and liabilities and operating income and expenses to operating cash receipts and payments.

New Reconciliation Schedule

S13. The proposed presentation model includes a new schedule (to be included in the notes to financial statements) that reconciles cash flows to comprehensive income. This reconciliation schedule disaggregates income into its cash, accrual other than remeasurements, and remeasurement components (for example, fair value changes). Users analyze those components separately because the components often differ in their ability to help users predict future cash flows and assess earnings quality.

COSTS AND BENEFITS

S14. The Boards hope to learn about the costs and benefits of their proposed presentation model through the comment letters they receive on this Discussion Paper and through discussions with interested parties during the comment period. In addition, a number of entities will be field testing the proposed presentation model during the comment period. The Boards will consider that input when they redeliberate the issues addressed in this Discussion Paper during the next stage of this project, the development of an Exposure Draft of a proposed standard.