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International Accounting Standards Board

INFORMATION FOR OBSERVERS

Board Meeting: **19 June 2008, London**

Project: **Financial Statement Presentation**

Subject: **Sweep Issues (Agenda Paper 9B)**

INTRODUCTION

1. An **objective of the June 2008** Board meeting on financial statement presentation is to address and resolve the sweep issues identified by the staff and Board advisors during their review of drafts that preceded the May 30 preballot draft. Those issues are as follows:

Issue 1: Sections and categories

a) Defining the operating and investing categories
b) Labels for the financing and equity sections

Issue 2: The reconciliation schedule

a) Disaggregation of changes in assets and liabilities not attributable to remeasurements
b) The indirect schedule

Issue 3: Disaggregation by **function and nature**

Issue 4: The **statement of changes in equity**

Issue 5: Disaggregation in the **discontinued operations section**

Issue 6: Disclosure of **total assets and total liabilities.**

ISSUE 1: SECTIONS AND CATEGORIES

Issue 1a: Defining the Operating and Investing Categories

2. Paragraphs 2.35–2.50 of the preballot draft describe how the Boards arrived at the classification scheme for the financial statements. In summary, the Boards started with a decision to separate an entity's value-creating activities (later referred to as "business") and its financing activities. The Boards spent a lot of time defining the financing section and concluded that (a) the financing section should include financing assets as well as financing liabilities and (b) equity financing should be presented in a section separate from other financing activities. The Boards affirmed that discontinued operations should continue to be shown in a separate section. The Boards then discussed the business section and agreed that investing activities should be presented separately from operating activities within that section. The investing category was defined as "assets and liabilities not classified in the financing section that management views as not integral to the entity's main business activities." The Boards never explicitly defined the operating category. The staff's working definition has been:

> The **operating category** would include assets and liabilities that management views as integral to the business activities it is currently engaged in and unrelated to financing those activities. Assets and liabilities that are integral to an entity's business would be those that management views as related to producing and delivering goods or providing services (for example, accounts receivable, inventory, equipment, accounts payable, pension obligations, and, for a financial services business, deposits and loans).

3. In the preballot draft the business section and related categories are defined and explained as follows:

> 2.20. The **business section** should include amounts related to assets and liabilities that management views as part of its continuing business activities. Business activities are those activities conducted with the intent of creating value, such as producing goods or providing services. The business section would

normally include assets and liabilities that are related to transactions with customers, suppliers, and employees (in their capacities as such) because such transactions usually relate directly to an entity's value-creating activities.

2.21. The **operating category** should include assets and liabilities that management views as related to the central purpose(s) for which the entity is in business (and changes in those assets and liabilities). An entity uses its operating assets and liabilities in its primary revenue and expense generating activities. If an entity cannot clearly identify an asset or liability as relating to operating, investing, or financing activities, the entity should presume the asset or liability relates to its operating activities.

2.22 The **investing category** should include assets and liabilities that management views as unrelated to the central purpose for which the entity is in business (and any changes in those assets and liabilities). An entity would use its investing assets and liabilities to generate a return, but would not use them in its primary revenue and expense generating activities.

Defining the business section

2.47. The Boards decided that an asset or liability that is not related to an entity's financing activities and is not related to a discontinued operation should be classified in the business section. However, the Boards agreed that to provide more transparency about an entity's business activities, the business section should be further separated into two categories—operating and investing.

2.49. Because management knows how assets and liabilities are deployed in its business activities, it is in the best position to determine whether an asset or liability should be classified in the operating or investing category. For example, consider a clothing manufacturer that creates value by converting raw materials into goods for sale. The assets and liabilities that this manufacturing entity might classify in the operating category include accounts receivable, inventory, equipment, accounts payable, intangible assets, and pension obligations. However, an entity that creates value by providing financial services to others might include cash, commercial paper, available-for-sale securities, trading portfolio assets and liabilities, deposits, loans, and insurance liabilities in its operating category.

2.50. The clothing manufacturer also might have a portfolio of bonds held for trading purposes that is not related to its central business purpose. It might classify that asset in the investing category. Likewise, the financial services entity might own a valuable art collection unrelated to its central business purpose. It would classify that collection in the investing category.

4. Staff and Board advisors that reviewed drafts of the preballot draft raised some concerns with the terms *operating* and *investing* and their accompanying

definitions. One concern is that we should not use words that are defined to mean something other than what an English language dictionary would tell us the word means. Another way to say that is that the standard should use a term that **clearly conveys** what the Boards intended that term to mean. For example, we should not use functional terms (operating and investing) to convey a significance-based distinction (primary, central). The following paragraphs describe some of the reviewers' concerns and possible alternatives to the definitions in the May 30 preballot draft.

Define the Categories in Terms of *Significance*

5. The use of "central purpose" and "primary revenue and expense generating" in the definitions (paragraphs 2.21 and 2.22) caused some reviewers to comment that the classification of items in the operating and investing categories seems to be based on **significance** and it seems like we are trying to make a "core" and "noncore" distinction.

6. Reviewers expressed concern that a core and noncore distinction may not be useful because the concept of *core earnings* has many interpretations and could lead to inconsistent classifications of operating or investing items. For example, management might consider some activities that produce goods or services as non-core because they are peripheral to the main business or could be disposed of without affecting the rest of the business.

7. Similarly, some reviewers expressed concern that management may classify less profitable activities as *investing* to protect their "operating" returns or ratios.

8. One reviewer was concerned that the definitions could result in an entity classifying activities that involve the supply of goods or services as investing because those activities are not related to an entity's central purpose or its primary revenue or expense streams. The reviewer did not like the possibility of the investing category including revenues, cost of sales, and so forth.

9. Many of the Boards' discussions regarding the operating and investing categories have included references to "core" and "non-core" as well as the desire to understand which activities are generating an entity's primary revenue streams. However, many of the Boards' discussions also focus on understanding how an asset or liability functions within an entity's business model.

Define the Categories in Terms of *Function*

10. Some reviewers suggested that the definitions should emphasize the **function** of an asset and liability in an entity's business model, noting that the terms *operating* and *investing* imply a functional distinction. A functional distinction would not be based on "how management views its operations" but rather on the objectives of the activities themselves. For example, the categories could be defined as follows:

    a. **Operating** relates to whether the activities attempt to produce future net cash inflows by actively combining resources (including fixed assets, working capital, intangible and human resources) to produce an output (good or service) that is sold to customers with a view to making a profit.

    b. **Investing** is a more passive (though not necessarily entirely passive) activity that involves putting money at risk to earn a return in the form of interest, dividends, or increased market prices for the asset.

11. The definition of investing is similar to the definition in paragraph 3 of AICPA SOP 07-1, *Clarification of the Scope of the Audit and Accounting Guide* Investment Companies *and Accounting by Parent Companies and Equity Method Investors for Investments in Investment Companies*, in which an *investment company* is defined as "a separate legal entity whose business purpose and activity are investing...for current income, capital appreciation, or both." In addition, an investing company(ies) should have no synergy with the express purpose of the business—making a distinction between strategic investments and non-strategic investments. The Boards considered and rejected the SOP 07-1 definition in early discussions about including a strategic investment category in the business section. At that time, the Boards viewed a strategic investment category as too narrow because it

might preclude an asset that earned any amount of capital appreciation from being considered a strategic investment.

12. If the Boards were to use a narrower definition of investing similar to that in SOP 07-1, the distinction between *investing assets* and *financing assets* would be less clear because all financing assets would also meet the definition of investing assets. For example, in the functional operating/investing distinction described above, much of a financial institution's operations might fall into the investing category.

Do Not Define the Categories

13. Another suggestion from reviewers was that the Boards not define *operating* or *investing*; rather, an entity would decide what is operating and investing for its business(es). In other words, the document would define the business section but would include no guidance other than that management should classify business assets and liabilities into operating and investing categories and explain its classification policy in the accounting policy note.

14. The staff observes that allowing management to define what operating and investing means in terms of their business(es) has the potential to provide the best opportunity for users of financial statements to see the business as management sees it. However, as each entity is unique, this approach also allows for the least amount of consistency and comparability between entities—even those in similar industries. In addition, reviewers' comments and discussions by the Boards indicate a preference for some guidance regarding the operating and investing categories.

Eliminate the Investing Category

15. In considering this further, the staff suggests that another alternative would be to not have an investing category in the business section. This would not preclude an entity from making such a distinction on its own and it might be a natural consequence of the "disaggregation by function and nature" principle for the statement of comprehensive income. The business section is defined as "amounts

related to assets and liabilities that management views as part of its continuing activities conducted with the intent of creating value, such as producing goods or providing services". If the Boards prefer to not specify or define an investing category, the resulting section could be labelled "operating" so as to not confuse people with the broader definition of *business* in FASB Statement No. 141(R), *Business Combinations*, and IFRS 3 (revised 2008) *Business Combinations*.

16. The main reason there are two categories in the business section is that the Boards wanted to distinguish between assets that are used to produce goods and services (the revenue line) from other types of assets. After the Boards defined what would be in the financing assets category, they considered where an entity should present financial assets that do not meet the financing asset definition, specifically equity method investments. The Boards decided that those types of assets should be in presented in a separate category. However, the Boards have noted many times that developing an adequate definition that distinguishes between those categories may prove difficult. Members of the Joint International Group (JIG) have also struggled with the definition of the investing category.

Staff Views

17. The staff believes that the definitions of the operating and investing categories in the preballot draft adequately convey the Boards' intent (as expressed in public meetings) and that the definitions should include both function and significance (as they currently do). The staff raised this issue because Board members should be aware of the potential for constituents to be confused about the definitions because of the labels being used. If the Boards agree that the definitions convey their intent, they should consider whether the labels should be changed. The staff notes that there will be time during redeliberations to further refine the definitions and reconsider labels with the benefit of constituent input. The staff welcomes suggested changes to the application and basis paragraphs in the preballot draft to further explain the Boards' intent.

18. The staff expects that the discipline of having an entity provide a robust description of its classification policy will address many of the concerns about what gets classified in which category. However, some may view the need to read this note disclosure in order to understand why an entity classified something in the operating category rather than the investing category (or vice versa) as adding complexity to rather than simplifying the presentation of financial information.

19. The staff would also support eliminating the investing category and having one section entitled "operating". The preliminary views documents could ask respondents to comment on whether further disaggregation within the operating section would be useful and on what basis any further separation should be made.

Questions for the Boards

Q1. Do the definitions of *operating* and *investing* in the preballot draft (included in paragraph 3 of this memo) adequately describe your intent? (Answering "yes" means that you agree to the definitions which emphasize significance over function.)

Q2. If the definitions are adequate, should we use labels other than *operating* and *investing* for the categories? If so, what are those labels?

Q3. If the definitions are not adequate, should we (choose one):

a. Define *operating* and *investing* in a functional manner similar to paragraph 10 above (that is, emphasize function over significance)

b. Not define those terms and let management decide (as described in paragraphs 13 and 14 above)

c. Remove the investing distinction and have a single operating section with no predefined categories? This would mean that an entity could further disaggregate this section as long as its defined categories were included in the statements of financial position, comprehensive income, and cash flows.

Issue 1b: Label for the Financing and Equity Sections

20. In January 2007, the Boards agreed that equity items should be presented in a section separate from the section for financing assets and liabilities. Those sections

have been referred to as the *equity section* and the *financing section*, respectively. One of the main tenets of the classification scheme is that financing activities should be presented separate from business (or value-creating) activities. Most users understand financing activities to include debt financing and equity financing. The separation of these two types of financing has created a labeling issue for the two resulting sections. The preballot draft explains that equity financing is part of an entity's overall financing activities. To make that clear, the staff considered labeling the equity section as *owner financing* or *equity financing*; however, that raised the question of what to label the financing section. *Nonowner financing* was an alterative the staff considered. Another possibility would be *debt financing* or *liability financing*, but currently that section also includes assets.

Staff Recommendation

21. The May 30 preballot draft uses a variety of labels for the equity and financing sections. As noted in paragraph 2.39 of the preballot draft, the staff recommends that the draft retain the initial labels of equity *section* and *financing section* as those terms are familiar. It should be clear to those reading the preliminary views document that the equity section is part of an entity's financing activities even though the word *financing* is not used to describe the equity section. The staff also supports an *equity financing* label.

Questions for the Boards:

Q4. Do the Boards want to keep the *equity section* label or change it to *equity financing*?

Q5. Do the Boards want to keep the *financing section* label or change it to *nonowner financing*?

ISSUE 2: THE RECONCILIATION SCHEDULE

Issue 2a: Disaggregating Changes in Assets and Liabilities not Attributable to Remeasurements

22. The Boards last discussed the reconciliation schedule at their November 2007 meetings and came to a converged view of the reconciling items. In those meetings the Boards decided that at a minimum, an entity would disaggregate the reconciling items into the following four components:

Column B. Cash flows not affecting income
Column C. Accruals and systematic allocations
Column D. Recurring valuation changes
Column E. Remeasurements other than recurring valuation changes

23. Columns B and C include the changes that **are not** attributable to remeasurements (non-remeasurement adjustments) and Columns D and E include changes that **are** attributable to remeasurements. In June 2007, the FASB favored splitting Column C into (a) contractual accruals and (b) other accruals, systematic allocations, and other non-remeasurements; however, in November, they agreed with the IASB to combine those amounts into a single Column C.

24. In preparing the illustrations to be included in the discussion document, the staff considered whether cash flows in the current period that affect income in other periods should be categorized in the "cash flows not affecting income" or the "accruals and systematic allocations" column. The staff eventually concluded that cash flows in the current period that affect income in a prior or future period are more appropriately classified as "accruals and systematic allocations." As discussed in the preballot draft (paragraphs 2.2, 2.3, and 4.21), accrual-basis accounting includes liabilities and assets other than cash in the statement of financial position to better represent the economic resources and obligations of an entity. Thus, if an entity spends cash of $100 on inventory this period but only sells $80 of product, accrual accounting leads to a $20 increase in the inventory balance. Similarly, if an entity spends cash of $100 on inventory but sells $115 of product, accrual accounting leads to a $15 decrease in its inventory balance. As illustrated

Caption in Statement of Cash Flows	Total Cash Inflows (Outflows)	Accruals and systematic allocations	Total Comprehensive Income	Caption in Statement of Comprehensive Income
Cash Paid for inventory (Ex. 1)	(100)	20	(80)	Cost of goods sold
Cash Paid for inventory (Ex. 2)	(100)	(15)	(115)	Cost of goods sold

25. In the first example where the inventory balance increases by $20, the staff believes that the $20 positive reconciling item also should appear in the "accruals or systematic allocations" column because it is also the result of applying the accrual-basis of accounting. Both the $15 and $20 reconciling items can be accurately described as "accruals." The staff notes that the $20 positive reconciling item cannot be described as a "cash flow *never* affecting income," because the amount will affect income in future periods when the inventory is sold or written off. The $20 could be described as a "cash flow not affecting income *this period*," but the staff believes that using two separate columns for the $20 and $15 reconciling items will not provide meaningful additional information to users. Further, the use of two columns obscures the fact that both items are the result of applying accrual accounting. Thus, if a current-period cash flow affects income in prior or subsequent periods, that amount should appear in the column labeled "accruals and systematic allocations".

26. Given the staff's conclusion that all current-period cash flows that affect income in other periods would be labeled as "accruals," the staff considered what type of current-period cash flow would never affect income. The staff concluded that only cash flows in the equity section could be unambiguously classified as "cash flows not affecting income in any period." The staff views the reconciliation schedule as primarily informing users about differences between cash-basis and accrual-basis income, and as such, information about the cash flows related to transactions with

owners is not as relevant to this schedule. In addition, information about owner transactions is available in the statements of cash flows and changes in equity.

27. The staff also considered several other ways to disaggregate the “accruals or systematic allocations” column. One possibility was to put originating differences between cash flows and accrual income in one column and reversing differences in a second column (for example sales on account or the prepayment of insurance would be in the originating column and collection of the accounts receivable or expiration of prepaid insurance in a subsequent period would be in the reversing column). Another possibility was to split this column based on whether assets or liabilities were being acquired or disposed of. In the end, the staff concluded that the amount in the non-remeasurement accrual column taken in conjunction with the caption in the statement of cash flows or the statement of comprehensive income will reveal useful information regarding how the accrual accounting process is being applied by an entity. Further disaggregation of the “nonremeasurement accruals” column will likely lead to very complex guidance or will fail to produce any meaningful additional information.

28. Thus, the staff concluded that two changes should be made to the reconciliation schedule the Boards agreed to in November:

a. the “cash flows not affecting income” column should be eliminated from the schedule and

b. the equity section should be omitted from the cash flow information that is used as the starting point for the reconciliation schedule.

The staff believes that the reduction in line items and columns should make the reconciliation schedule simpler to prepare and use without any loss of relevant information.

29. Based on the above, the revised reconciliation schedule described and illustrated in the preballot draft (paragraphs 4.15–4.30 and on pages A12 and A13 of Appendix A) presents the changes in an entity’s assets and liabilities that (a) have current period effects on cash flows, income, or both, and (b) are not transactions

with owners. The columns in the revised schedule are as follows (reconciling columns in **boldface**):

Column A: Captions from Statement of Cash Flow (excluding equity transactions)
Column B: Amount from Statement of Cash Flow (excluding equity transactions)
Column C: Accruals and systematic allocations that are not remeasurements
Column D: Recurring valuation changes
Column E: Remeasurements other than recurring valuation changes
Column F: Amount from Statement of Comprehensive Income
Column G: Caption from Statement of Comprehensive Income
Column H: Unusual and Infrequent Events [FASB view]

30. In the preballot draft, the basis for the Boards' preliminary views regarding the reconciliation schedule notes that the characteristics of persistence and subjectivity were utilized in determining how to disaggregate components of comprehensive income. The draft also explains the disaggregation process used to prepare the schedule in three steps. The first step disaggregates income into cash flows and accruals because the two components of income have different persistence[1] and subjectivity. The second step disaggregates accruals into remeasurement accruals and non-remeasurement accruals, which is justified mostly by different persistence. The third step disaggregates remeasurement accruals into recurring fair value remeasurements and all other remeasurements. The rationale provided in the draft for that third step (disaggregation of remeasurements) does not mention persistence because in the staff's view, the disaggregation relates to subjectivity only. For those who would like to understand that view better, Chapter 5 of the preballot draft includes an example that demonstrates how unexpected remeasurements gains and losses for long-term assets or liabilities are unlikely to be persistent.

[1] Paragraph 4.16a of the preballot draft addresses the definition of persistence. That paragraph says: "An item of comprehensive income (that is, a revenue, expense, gain or loss) is *persistent* if it is indicative of future amounts of income. The important distinction is whether the current period income item is a useful predictor of future income items, either by itself or when combined with other information (for example, current revenue could be used to predict future revenue or current revenue could be combined with an expected growth rate to predict future revenue)."

Staff Recommendation

31. The staff recommends that the Boards modify their November 2007 decision to (a) eliminate the "cash flows not affecting income" column from the schedule and (b) omit the equity section from the cash flow information that is used as the starting point for the reconciliation schedule. Based on that recommendation, the reconciliation schedule presented in the preliminary views document would be as described in paragraph 29 above and as in the preballot draft.

Questions for the Boards:

Q6. Do the Boards agree that changes in assets and liabilities not attributable to remeasurements should be presented in one column in the reconciliation schedule and not further disaggregated (as illustrated in the preballot draft and described in paragraph 29 of this memo)?

Q7. Do the Boards agree that cash flows related to equity transactions need not be included in the reconciliation schedule?

Issue 2b: The Indirect Schedule

32. Currently, Statement 95 requires a reconciliation of *net income* to *cash flows from operating activities* if the direct method is used (referred to as the indirect schedule). That reconciliation is not required by IAS 7. In December 2006, the Boards expressed support for requiring an entity to present an indirect schedule in the notes if it prepared its statement of cash flows using the direct method. The Boards expressed that view prior to finalizing its discussions on the statement of cash flows and the reconciliation schedule.

33. Given the proposed format of the reconciliation schedule, the staff believes that an indirect schedule is no longer needed because the indirect schedule would contain no information beyond that provided in the reconciliation schedule. The purpose of the indirect schedule is to reconcile from income to operating cash flows. Because the right-hand side of the reconciliation schedule shows the line items on the statement of comprehensive income and the left-hand side of the schedule shows the cash flow

amounts, information that would be in an indirect schedule can be obtained by reading from right to left in the reconciliation schedule. The reconciliation schedule will present more detailed information than is currently found in the indirect schedule (and in a statement of cash flows prepared using the indirect method).

Staff Recommendation

34. Because the information in the reconciliation schedule presents the same information that would be contained in an indirect schedule, the staff recommends that an indirect schedule not be a required note disclosure. The preliminary views document can ask users whether the indirect schedule contains meaningful information beyond that contained in the reconciliation schedule.

Questions for the Boards:

Q8. Do the Boards agree that disclosure of an indirect schedule reconciling income to cash flows from operating activities should not be required?

Q9. Should the preliminary views document address the indirect schedule (the preballot draft does not mention this possible note disclosure)?

Q10. If so, should the should the preliminary views document include a question regarding the usefulness of the indirect schedule?

ISSUE 3: DISAGGREGATION BY FUNCTION AND NATURE

35. Paragraphs 3.40–3.43 of the May 30 preballot draft (see below) provide the Boards' preliminary views on disaggregation by function and nature in the statement of comprehensive income.

> 3.40. **An entity should disaggregate income and expense amounts within each section and category in the statement of comprehensive income according to their function, their nature, or both, as follows:**
>
> a. **An entity should disaggregate the income and expense items in the operating, investing, and financing categories by function if doing so will enhance the usefulness of the information for assessing an entity's ability to generate net cash inflows and for assessing the effectiveness with which management has fulfilled its stewardship responsibilities**.

b. **An entity should further disaggregate each income and expense item by its nature to the extent that doing so will enhance the usefulness of the information for assessing an entity's ability to generate net cash inflows and for assessing the effectiveness with which management has fulfilled its stewardship responsibilities.**

3.41. **An entity should present separately any income or expense item that would not be presented under (a) or (b) if that item is significant to understanding its operating results (for example, impairment of goodwill).**

3.42. *Function* refers to the primary activities in which an entity is engaged, such as, manufacturing, advertising, marketing, business development, selling 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 could include disaggregating service revenues from revenue from sales of products, or disaggregating cost of sales to present materials, labor, transportation, and energy costs.

3.43. If presenting both by-function and by-nature information in the statement of comprehensive income results in financial statements that are too lengthy and detract from the overall understandability of the financial information, an entity should present some or all of its by-nature information in the notes to financial statements.

36. The principles for disaggregation (**bold paragraphs**) are consistent with the disaggregation objective. In preparing the illustrative statement of comprehensive income, several issues arose about the Boards' intent regarding disaggregation by function and nature. The first issue is whether an entity can present revenues, expenses, gains, and losses that clearly relate to a certain functional activity outside of that function. For example, an entity has defined a "cost of goods sold" function (a subcategory within the operating category) that includes expenses related to manufacturing. The entity incurs a loss on the disposal of manufacturing equipment. If management views that loss as unrelated to the entity's manufacturing function, can it present the loss outside the "cost of goods sold" subcategory even though the equipment was used in only the entity's manufacturing activities?

37. The staff believes that the Boards' preliminary views could be interpreted to allow excluding a manufacturing item from cost of goods sold if including it would not enhance the usefulness of the information (that is, the subtotal "cost of goods sold" is more meaningful without the loss than with it). Thus, the illustrative example on page A-9 of the preballot draft includes the line item *gain on disposal of PPE* in an "other operating" subcategory (that illustration is included after the Questions that follow the next paragraph).

38. A related issue is whether the Boards want to provide more latitude for presenting by-nature information in the notes. The staff recalls that one company in the recasting exercise presented a statement of comprehensive income that many viewed as overly detailed and too long to be useful. As drafted, the principle in paragraph 3.43 of the preballot draft would direct an entity to present by-nature information in the notes to financial statements *only* if presenting the by-nature information on the face resulted in financial statements that are too lengthy and detract from the overall understandability of the financial information. The staff's interpretation is that an entity can choose which by-nature information to present on the statement of comprehensive income by evaluating whether it "will enhance the usefulness" of that statement, as stated in paragraph 3.40b. The staff has illustrated this interpretation in Appendix A of the preballot draft (see the illustration that precedes paragraph 39).

Questions for the Boards

Q11. Are the principles stated in paragraphs 3.40 – 3.42 of the preballot draft (repeated in paragraph 35 of this paper) consistent with the Boards' intent?

Q12. Do the Boards agree with the following staff interpretation of the "by-nature" disaggregation principle (paragraph 3.40(b)): a revenue, expense, gain, or loss that relates directly to a function should not be presented "by nature" within that function if doing so would <u>not</u> enhance the usefulness of the resulting information?

Q13. Does the principle stated in paragraph 3.43 (see paragraph 35) reflect the Boards' intention for presentation of by-nature information?

Q14. Do the illustrations from the preballot draft (see the next two pages) reflect the Boards' intention for presentation of by-nature information?

These illustrations are presented for discussion purposes only and should be read only in the context of the meeting papers. Not all aspects of the sample financial statements have been discussed by or represent the current position of the Boards (and those that have are subject to change).

Statement of Comprehensive Income		
	2010	**2009**
BUSINESS		
Operating		
Sales - retail	697,520	647,850
Sales - wholesale	2,790,080	2,591,400
Total revenue	3,487,600	3,239,250
Cost of goods sold		
Change in inventory	(60,250)	(46,853)
Labor	(405,000)	(450,000)
Materials	(1,043,100)	(925,000)
Overhead - depreciation	(219,300)	(215,000)
Overhead - transportation and other	(160,800)	(135,000)
Loss on obsolete and damaged inventory	(29,000)	(9,500)
Total cost of goods sold	(1,917,450)	(1,781,353)
Gross profit	1,570,150	1,457,897
Selling Expenses		
Compensation expense	(56,700)	(52,500)
Advertising expense	(60,000)	(50,000)
Other selling expenses	(13,500)	(12,500)
Bad debt expense	(23,068)	(15,034)
Total selling expenses	(153,268)	(130,034)
General and administrative expenses		
Pension expense	(103,950)	(94,500)
Stock compensation expense	(22,023)	(17,000)
Wages	(321,300)	(297,500)
Other	(12,960)	(12,000)
Depreciation expense-Building	(1,500)	(1,500)
Depreciation expense-PPE	(58,320)	(57,000)
Accretion expense on ARO	(810)	(750)
Interest expense on lease liability	(14,825)	(16,500)
Research and development	(8,478)	(7,850)
Litigation expense	(1,998)	(1,850)
Total general and administrative expenses	(546,164)	(506,450)
Income before other operating items	*870,718*	*821,413*
Other operating		
Loss on sale of receivables	(4,987)	(2,025)
Gain on disposal of PPE	35,650	-
Realized gain on future contracts	3,996	3,700
Impairment loss on goodwill	-	(35,033)
Equity in earnings of affiliate	23,760	22,000
Total other operating income	58,419	(11,358)
Total continuing operating income	**929,137**	**810,055**
Investing		
FV change in investment in affiliate	7,500	3,250
Realized gain on AFS securities	15,750	7,500
Dividend income	54,000	50,000
Total continuing investing income	**77,250**	**60,750**
Total continuing business income	**1,006,387**	**870,805**
FINANCING		
Gain on extinguishment of ST debt	4,000	-
Interest expense	(111,353)	(110,250)
Total continuing financing expense	**(107,353)**	**(110,250)**
Income from continuing operations before taxes	**899,035**	**760,555**
Income tax expense	(335,860)	(293,176)
Net income from continuing operations	**563,175**	**467,380**
DISCONTINUED OPERATIONS (after tax)		
Loss on discontinued operations	(21,060)	(22,750)
Net income	**542,115**	**444,630**
OTHER COMPREHENSIVE INCOME (after tax)		
FCTA - Consolidated Sub	2,094	(1,492)
FCTA on equity method investee (operating)	(1,404)	(1,300)
Revaluation Surplus (operating)	3,653	-
Unrealized gain on futures contract (operating)	1,825	1,690
Unrealized gain on AFS securities (investing)	17,193	15,275
Total other comprehensive income	**23,361**	**14,173**
Total comprehensive income	**565,476**	**458,802**
Earnings per common share	7.43	6.28
Earnings per common share - assuming dilution	7.19	6.10

Additional Expenses by Nature		
	2010	**2009**
Service cost	(86,350)	(78,500)
Interest cost	(35,600)	(28,000)
Return on plan assets	18,000	12,000
Pension expense	(103,950)	(94,500)
	-	-
Television Advertising	(35,000)	(25,000)
Print Advertising	(7,500)	(10,000)
Sponsorships	(17,500)	(15,000)
Advertising expense	(60,000)	(50,000)
Transportation Wages	(83,160)	(77,000)
Maintainance - Wages	(28,890)	(26,750)
Feul Costs	(22,500)	(16,500)
Mainainance - Materials	(2,808)	(2,600)
Plant Utilities	(23,442)	(12,150)
COGS - Overhead - transportation and other	(160,800)	(135,000)
Wages	(6,700)	(5,550)
Materials	(170)	(175)
Overhead	(1,017)	(950)
Licensing fees	(170)	(355)
Equipment rental	(422)	(820)
Research and development	(8,478)	(7,850)

ISSUE 4: STATEMENT OF CHANGES IN EQUITY

39. The preballot draft includes the following preliminary view:

> 3.92 **An entity should present a statement of changes in equity that provides information about the beginning and ending balance of each component of equity and how each balance changed during the period. In preparing that statement, an entity should present**
>
> a. **Total comprehensive income for the period, showing separately the total amounts attributable to owners of the parent and to the noncontrolling interest;**
>
> **b. For each component of equity, the effects of retrospective application or retrospective restatement recognized in accordance with FASB Statement No. 154,** ***Accounting Changes and Error Corrections*****, or IAS 8,** ***Accounting Policies, Changes in Accounting Estimates and Errors*****;**
>
> **c. The amounts of transactions with owners in their capacity as owners, showing separately contributions by and distributions to owners; and**
>
> **d. For each component of equity, a reconciliation between the carrying amount at the beginning and the end of the period, separately disclosing each change.**
>
> 3.93 **An entity should present, either in the statement of changes in equity or in the notes, the amount of dividends recognized as distributions to owners during the period, and the related amount per share.**

40. While that view is consistent with the decisions the Boards made in Phase A of this project, it does not include the views expressed in Phase B about the details of the statement of changes in equity. That is, the statement should present

a. Information about transfers between owners in their capacity as owners (for example, by including a line for conversions of one type of equity into another)

b. The amount of value received in exchange for equity instruments, without disaggregating the value into par and amounts in excess of par (for example, additional paid in capital should be combined with par value)

c. Accumulated OCI in the aggregate and the details for each OCI item should be presented in the notes.

Staff Recommendation

41. The Boards focus in Phase B has been on the statements of financial position, comprehensive income, and cash flows. The changes suggested above are minor in comparison to other changes envisioned by the Boards' preliminary views. In the interest of identifying issues that could be excluded from the scope of Phase B to keep the project on track, the staff recommends that the Phase B discussion of the statement of changes in equity be limited to the issues addressed in Phase A. See below for the remaining paragraphs from the preballot draft describing the staff's recommendation for the Boards' views on this issue:

> 3.95 The Boards agreed in Phase A of this project that a statement of changes in equity should be part of a complete set of financial statements. The Boards also agreed that the form and content of that statement should be similar to what entities currently provide in their financial statements. The changes the IASB made in 2007 to the IAS 1 requirements for the statement of changes in equity were the result of the decisions the Boards reached in Phase A of this project. The Boards concluded that Phase B of this project should focus on making improvements to the other statements that constitute a complete set of financial statements except for the statement of changes in equity. Thus, the Boards' preliminary view is the same as what is required in the 2007 revision to IAS 1.
>
> 3.96 Current guidance in U.S. GAAP on presenting information about changes in shareholders equity is found in Rule 3-04 of SEC Regulation S-X. U.S. GAAP permits information about changes in shareholders' equity to be presented in the notes to financial statements; that presentation was permitted by IAS 1 prior to its 2007 revision. Following the Boards' preliminary view, an entity applying U.S. GAAP will no longer have the option of presenting information about shareholders' equity in the notes to financial statements. That is the main change to current practice for reporting information on shareholders' equity.

42. If the Boards agree with the staff recommendation, an entity will be permitted to present information about changes in the accumulated balance of **individual** OCI items in the statement of changes in equity. The Boards previously said that they wanted that detailed information in the notes in an effort to focus the statement of changes in equity on the other components of equity. Given the Boards' decision not to change the presentation of OCI items in the statement of comprehensive income, the staff believes it is appropriate to provide entities a choice of where to present that detailed information.

Questions for the Boards

Q15. Do the Boards agree to limit their preliminary views on the statement of changes in equity to the decisions reached in Phase A and included in the revision to IAS 1?

Q16. Do the Boards agree to limit the scope of Phase B to not consider any further changes to the statement of changes in equity?

ISSUE 5: DISAGGREGATION IN THE DISCONTINUED OPERATIONS SECTION

43. The Boards' preliminary views on the discontinued operations section are as follows.

> The **discontinued operations section** should include all amounts related to a discontinued operation, as that term is defined in Statement 144 and IFRS 5, as follows:
>
> a. The assets and liabilities of a disposal group classified as held-for-sale would be presented in the statement of financial position
>   - [FASB view] as single amount (net assets or net liabilities)
>   - [IASB view] on a gross basis (assets separate from liabilities).
>
> b. An entity should combine the revenue, expense, gain and loss of a discontinued operation, and any gain or loss from disposal or from measurement to fair value and present that amount as a single line in the statement of comprehensive income.
>
> c. An entity should combine the cash flows from its discontinued operations and present that amount as a single line in the statement of cash flows.

44. The May 30 preballot draft does not include those views because the staff is of the opinion that they conflict with the Boards' other preliminary views on disaggregation. The staff believes disaggregation within the discontinued operations section should follow the same objective as the other sections in the financial statements. That is, it should allow an entity the discretion to determine what disaggregated information would make its financial statements useful in assessing future cash flows and in assessing how well management has discharged

its stewardship responsibilities. The staff notes that the preliminary views described in paragraph 43 above are prescriptive and, therefore, would not allow an entity to determine the appropriate level of disaggregation within the discontinued operations section in the financial statements.

Statement of Financial Position

45. Both Statement 144 and IFRS 5 require an entity to present the assets and liabilities of a discontinued operation separately and specify that those assets and liabilities should not be offset and presented as a single amount (this is similar to the IASB's preliminary view). The staff believes separately presenting assets and liabilities in the discontinued operations section is consistent with Boards' preference for assets and liabilities to be presented on a gross rather than a net basis (what has been referred to as the "netting principle"). As that is current practice the staff does not think the document needs to be explicit on this point. However, if the Boards believe the document should be explicit on this point, the staff recommends retaining current guidance (that is, the FASB should agree to the IASB view of presenting assets and liabilities separately in the discontinued operations section).

Statement of Comprehensive Income

46. The Boards' preliminary view is similar to current guidance in Statement 144 and IFRS 5 that requires (a) the post-tax profit or loss of discontinued operations and (b) the gain or loss on the disposal or from measurement to fair value to be reported as a [separate component of income/single amount] in the statement of comprehensive income.

47. However, the staff believes that **requiring** an entity to combine the revenue, expense, gain, or loss of a discontinued operation and any gain or loss from disposal or from measurement to fair value as a single line in the statement of comprehensive income is inconsistent with disaggregation objective. Requiring an entity to aggregate these activities into one line item would not allow an entity to determine what disaggregated information would be most useful to users of its financial statements in assessing the entity's future cash flows. Therefore, the staff

believes that there should not be specific disaggregation guidance for the discontinued operation section in the statement of comprehensive income, but for an entity to apply the disaggregation objective in the same manner it would in presenting line items in the other sections.

Statement of Cash Flows

48. Current guidance in IFRS 5 requires the disclosure of the net cash flows attributable to the operating, investing, and financing activities of discontinued operations. U.S GAAP currently does not have cash flow requirements for discontinued operations; however, the FASB has agreed to include that IFRS 5 disclosure requirement in the forthcoming proposal on the joint discontinued operations project. The Boards' preliminary view is to require an entity to combine the cash flows from its discontinued operations and present that amount as a single line in the statements of cash flows. To be consistent with the prior discussion related to the statement of comprehensive income, current IFRS 5 guidance, and the proposed guidance in the joint discontinued operations project, the staff recommends that the preliminary views document not require an entity to present the cash flows related to its discontinued operations as a single line in the statements of cash flows.

Staff Recommendation

49. The staff recommends not including any specific requirements for disaggregating (or aggregating) within the discontinued operations section Being silent on presentation (as in paragraph 2.25 of the preballot draft) will allow an entity to apply the overall disaggregation objective and include additional line items in its discontinued operations section as appropriate in order to explain the components of its financial results.

Question for the Boards:

Q17. Do the Boards agree that there should not be specific disaggregation requirements for presenting information in the discontinued operations section? That is, the preliminary view in paragraph 2.25 of the preballot draft

is adequate (see below)?

2.25 The **discontinued operations section** should include all amounts related to a discontinued operation, as that term is defined in FASB Statement No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, and IFRS 5, *Non-Current Assets Held for Sale and Discontinued Operations*.

ISSUE 6: DISCLOSURE OF TOTAL ASSETS AND TOTAL LIABILITIES

50. The Boards' preliminary view is that an entity should disclose total assets and total liabilities in the notes to financial statements. In addition, if an entity presents a classified statement of financial position it should disclose a total for short-term assets, short-term liabilities, long-term assets, and long-term liabilities.

51. The Boards concluded that note disclosure of this information is appropriate because providing those totals in the statement of financial position along with the other required totals would result in a cluttered statement. While that may be true, the staff is of the view that the note disclosure seems odd because it is presented apart from the related information in the statement of position. As illustrated in the preballot draft, the note disclosure could look like this:

	December 31, 2010		December 31, 2009	
	Assets	**Liabilities**	**Assets**	**Liabilities**
Short-term	2,948,417	(2,137,310)	2,230,945	(2,326,436)
Long-term	4,624,074	(2,744,813)	4,985,143	(2,762,600)
Total	7,572,491	(4,882,123)	7,216,088	(5,089,036)

Staff Recommendation

52. The staff recommends that the Boards change their preliminary view to permit an entity to present those totals in the statement of financial position. The totals could be presented at the bottom of that statement, much the same way per share amounts are presented at the bottom of the statement of comprehensive income. As the document does not require a specific format for the statement of financial position, it is possible for those totals to be presented in other manners as illustrated on the last two pages of this paper.

Questions for the Boards

Q18. Do the Boards agree with the staff recommendation in paragraph 52? That recommendation is included in paragraph 3.24 of the preballot draft, as follows:

3.24. An entity should disclose total assets and total liabilities [either on the statement of financial position or] in the notes to financial statements. An entity that presents its assets and liabilities in short-term and long-term subcategories (see paragraph 3.3) also should disclose a total for short-term assets, short-term liabilities, long-term assets, and long-term liabilities.

These illustrations are presented for discussion purposes only and should be read only in the context of the meeting papers. Not all aspects of the sample financial statements have been discussed by or represent the current position of the Boards (and those that have are subject to change).

STATEMENT OF FINANCIAL POSITION

	For years ending December 31, 2010	2009
BUSINESS		
Operating		
Accounts receivable, trade (net of allowance of 23,642, 13,534,and 10,500)	922,036	527,841
Inventory	679,474	767,102
Futures contract - Cash flow hedge	6,552	3,150
Prepaid advertising	80,000	75,000
Total short-term operating assets	1,688,062	1,373,092
Property, Plant and Equipment (less accumulated depreciation of 2,264,620, 2,022,000, and 1,750,000)	2,743,460	3,041,500
Building (net of accumulated depreciation of 1,500, 3,000, and 4,500)	27,620	23,500
Investment in equity method investee	261,600	240,000
Goodwill	189,967	189,967
Total long-term operating assets	3,222,647	3,494,967
Advances from customers	(182,000)	(425,000)
Accounts payable, trade	(612,556)	(505,000)
Current portion of lease liability	(35,175)	(33,500)
Interest payable on lease liability	(14,825)	(16,500)
Wages payable	(173,000)	(200,000)
Accrued pension liability	(293,250)	(529,500)
Share-based compensation liability	(39,586)	(21,165)
Total short-term operating liabilities	(1,350,392)	(1,730,665)
Lease liability (excluding current portion)	(261,325)	(296,500)
Litigation reserve	(3,848)	(1,850)
Asset retirement obligation	(29,640)	(14,250)
Total long-term operating liabilities	(294,813)	(312,600)
Net Operating Assets	3,265,504	2,824,795
Investing		
AFS securities	453,600	485,000
Investment in affiliate at FV	46,750	39,250
Total investing assets	500,350	524,250
Net Business Assets	3,765,854	3,349,045
NON-OWNER FINANCING		
Financing assets		
Cash	1,260,355	857,852
Total financing assets	1,260,355	857,852
Financing liabilities		
Short-term debt	(553,500)	(400,000)
Interest payable	(140,401)	(112,563)
Dividends payable	(20,000)	(20,000)
Total short-term financing liabilities	(713,901)	(532,563)
Long-term debt	(2,050,000)	(2,050,000)
Total long-term financing liabilities	(2,050,000)	(2,050,000)
Net Financing Assets	(1,503,546)	(1,724,710)
DISCONTINUED OPERATIONS		
Assets held for sale	856,832	876,650
Liabilities held for sale	(400,000)	(400,000)
Net assets held for sale	456,832	476,650
INCOME TAXES		
Short-term		
Income taxes payable	(73,017)	(63,208)
Long-term		
Deferred tax asset	44,245	89,276
Net income tax asset (liability)	(28,772)	26,068
Net assets	2,690,368	2,127,052
OWNER FINANCING		
Common Stock and APIC	(1,515,600)	(1,507,500)
Treasury stock	88,360	164,500
Retained Earnings	(1,100,594)	(644,880)
Accumulated OCI	(162,534)	(139,173)
Total equity	(2,690,368)	(2,127,052)

Total short-term assets	2,948,417	2,948,417
Total long-term assets	4,624,074	4,624,074
Total assets	7,572,491	7,572,491
Total short-term liabilities	(2,137,310)	(2,326,436)
Total long-term liabilities	(2,744,813)	(2,762,600)
Total liabilities	(4,882,123)	(5,089,036)

These illustrations are presented for discussion purposes only and should be read only in the context of the meeting papers. Not all aspects of the sample financial statements have been discussed by or represent the current position of the Boards (and those that have are subject to change).

STATEMENT OF FINANCIAL POSITION

	For years ending December 31,			For years ending December 31,	
	2010	**2009**		**2010**	**2009**
BUSINESS ASSETS			**BUSINESS**		
Operating assets			**Operating liabilities**		
Accounts receivable, trade (net of allowance of 23,642, 13,534,and 10,500)	922,036	527,841	Advances from customers	(182,000)	(425,000)
Inventory	679,474	767,102	Accounts payable, trade	(612,556)	(505,000)
Futures contract - Cash flow hedge	6,552	3,150	Current portion of lease liability	(35,175)	(33,500)
Prepaid advertising	80,000	75,000	Interest payable on lease liability	(14,825)	(16,500)
			Wages payable	(173,000)	(200,000)
			Accrued pension liability	(293,250)	(529,500)
			Share-based compensation liability	(39,586)	(21,165)
Total short-term operating assets	1,688,062	1,373,092	Total short-term operating liabilities	(1,350,392)	(1,730,665)
Property, Plant and Equipment (less accumulated depreciation of 2,264,620, 2,022,000, and 1,750,000)	2,743,460	3,041,500	Lease liability (excluding current portion)	(261,325)	(296,500)
Building (net of accumulated depreciation of 1,500, 3,000, and 4,500)	27,620	23,500	Litigation reserve	(3,848)	(1,850)
Investment in equity method investee	261,600	240,000	Asset retirement obligation	(29,640)	(14,250)
Goodwill	189,967	189,967			
Leased asset					
Total long-term operating assets	3,222,647	3,494,967	Total long-term operating liabilities	(294,813)	(312,600)
Investing assets					
AFS securities	453,600	485,000			
Investment in affiliate at FV	46,750	39,250			
Total investing assets	500,350	524,250			
NON-OWNER FINANCING ASSETS			**NON-OWNER FINANCING**		
Financing assets			Financing liabilities		
Cash	1,260,355	857,852	Short-term debt	(553,500)	(400,000)
Total financing assets	1,260,355	857,852	Interest payable	(140,401)	(112,563)
			Dividends payable	(20,000)	(20,000)
			Total short-term financing liabilities	(713,901)	(532,563)
			Long-term debt	(2,050,000)	(2,050,000)
			Total long-term financing liabilities	(2,050,000)	(2,050,000)
DISCONTINUED OPERATIONS			**DISCONTINUED OPERATIONS**		
Assets held for sale	856,832	876,650	Liabilities held for sale	(400,000)	(400,000)
Net assets held for sale	856,832	876,650			
INCOME TAXES			**INCOME TAXES**		
Long-term			Short-term		
Deferred tax asset	44,245	89,276	Income taxes payable	(73,017)	(63,208)
Total assets	**7,572,491**	**7,216,088**	**Total liabilitites**	**(4,882,123)**	**(5,089,036)**
			OWNER FINANCING		
			Common Stock and APIC	(1,515,600)	(1,507,500)
			Treasury stock	88,360	164,500
			Retained Earnings	(1,100,594)	(644,880)
			Accumulated OCI	(162,534)	(139,173)
			Total equity	**(2,690,368)**	**(2,127,052)**
Total short-term assets	2,948,417	2,230,945	Total short-term liabilities	(2,137,310)	(2,326,436)
Total long-term assets	4,624,074	4,985,143	Total long-term liabilities	(2,744,813)	(2,762,600)
Total assets	7,572,491	7,216,088	Total liabilities	(4,882,123)	(5,089,036)