Topic: **Proposal for limited scope amendment to IAS 1 *Presentation of Financial Statements***

Introduction

1. IAS 1 *Presentation of Financial Statements* gives preparers several options as to how and where some components of income can be displayed. These options reduce the comparability of financial statements.

2. At the July Board meeting, the IASB and FASB discussed the tentative decision made by the FASB the previous week to require a single Statement of Comprehensive Income (SCI) as part of its project on Financial Instruments: Recognition and Measurement. During the discussion, the staff noted that the IASB had made tentative decisions in its financial instruments and pensions project that would benefit from a requirement for a single SCI.

3. The boards decided, at the joint meeting in July, not to amend the scope of the *Financial Statement Presentation Project* (FSP Project) to review the components of other comprehensive income (OCI). Any systematic review of OCI would be undertaken after the current phase of the FSP Project has been completed.

4. In the interim, however, the IASB staff stated that they intended bringing a proposal to the IASB to consider removing the option in IAS 1 *Presentation of Financial Statements* that permits all items of income and expense recognised in a period to be displayed in two statements: a statement displaying components of profit and loss (separate income statement) and a second statement beginning

with profit or loss and displaying components of other comprehensive income (statement of comprehensive income). As noted above, the FASB has already made a decision to require that all components of income be displayed in a single statement. If the IASB decides to propose amending IAS 1, it seems to me that it would be preferable for the IASB and FASB to develop together exposure drafts to amend their respective requirements. This would allow the boards to expose the proposals at the same time and would provide potential respondents with the opportunity to see how such a proposal could help make it easier to compare IFRS and US GAAP compliant financial statements.

5. With this in mind, this paper has been written primarily for the benefit of the IASB because the IASB has yet to formally consider this proposal. It also serves as a background paper for a discussion at the joint meeting, at which the staff will ask the boards if (assuming that the IASB supports this proposal) they want to work together to develop exposure drafts to amend IAS 1 and the FASB Accounting Standards Codification (ASC).

Discussion

6. In the Discussion Paper, *Preliminary Views on Financial Statement Presentation* (FSP), the IASB proposed that "an entity should present comprehensive income and its components in a single statement of comprehensive income. Items of other comprehensive income should be presented in a separate section that is displayed with prominence equal to that of all the other sections." (Paragraph 3.24) The scope of the project made it clear that, in the FSP project, the board was not considering changes to existing requirements (a) for items which must be presented in other comprehensive income (OCI) and (b) whether, when and how items of OCI must be reclassified to profit or loss.

7. The comments received on the FSP project's tentative conclusion that there should be a single statement of comprehensive income were split (Staff Paper 17C, July 2009 Board Meeting).

8. Those that disagree think that:

    (a) the primary focus of entities and their investors is operating income and net income;

    (b) including OCI items, which do not relate to core business results of an entity, within a single statement along with operating income and net come may confuse users of financial statements and lead to significant misinterpretations of an entity's performance; and

    (c) there should be a separate statement of OCI or the option of either a single SCI or a two statement approach should be retained (Staff Paper 17C, July Board Meeting).

9. Those that support a single statement generally believe that greater transparency, consistency, and comparability would result. (Staff Paper 17C, July 2009 Board Meeting).

10. There is stronger support for a single statement from some users of financial statements. Our consultations suggest that they think that transparency, consistency and comparability would be improved. They are also not concerned that they would be confused or misled by a single statement that clearly sets out items of profit and loss and OCI. On the contrary, they believe that such a presentation makes it easier to comprehend the relationship between movements in the statement of financial position (SFP), items of OCI and profit and loss for the period.

Proposal

Removal of the two-statement option

11. The proposal I am asking the Board to consider is a limited scope amendment to IAS 1 to eliminate the option in paragraph 81(b) that permits an entity to present all items of income and expense recognised in a period in two statements: a statement displaying components of profit or loss (separate income statement)

and a second statement beginning with profit or loss and displaying components of other comprehensive income (statement of comprehensive income).

8. Nothing in this proposal would change which items can or must be presented in OCI or whether an item must be reclassified (ie recycled) upon derecognition. The proposal is simply to remove an option.

9. Requirements in IFRS and the FASB ASC in relation to OCI differ. The components of OCI are not the same and nor are the reclassification (recycling) requirements. Some components of OCI in IFRS are never reclassified.

10. If the FASB and IASB projects on financial instruments add more items to OCI it will be increasingly difficult to compare an income statement prepared in accordance with the FASB ASC with one prepared in accordance with IFRS. The main difficulty is the choice entities have in how and where they present components of OCI. Eliminating that choice will make it easier to compare income statements prepared in accordance with IFRS and will help identify points of difference between IFRS and FASB ASC.

Question 1: Single Statement
The staff recommend that the Board tentatively decide to eliminate the option in paragraph 81of IAS 1 *Presentation of Financial Statements* that permits an entity to present all items of income and expense recognised in a period in two statements: a statement displaying components of profit or loss (separate income statement) and a second statement beginning with profit or loss and displaying components of other comprehensive income (statement of comprehensive income).

Two sections

11. It is clear from comment letters and other consultation that users (and preparers) think that the components of OCI are different from other components of income. In recommending that the two-statement option be removed, I think it is also appropriate to preserve the distinction between OCI and other components of income by requiring that the single statement of comprehensive income be presented in two sections:

    (a) Profit or loss, and

(b) Other comprehensive income.

12. In making the second recommendation, I note that Para 8 of IAS 1 states that an entity is not required to use the terms *comprehensive income*, *profit or loss* or *other comprehensive income*. An entity is permitted to use other terms to describe totals as long as the meaning is clear. For example, *net income* is suggested as an appropriate term to use instead of *profit or loss*.

13. An illustration of how such a statement might be displayed (based on an example in IAS 1) is shown in **Appendix A**.

Question 2: Two sections
The staff recommend that the Board tentatively decide to require that the single statement of comprehensive income be displayed with two sections: *profit or loss* and *other comprehensive income*. An entity would be able to change the title of these sections (as long as the meaning is clear) but the components of income displayed in each section may not be changed.

Presentation within OCI

14. Some components of OCI are reclassified into profit or loss when the related item is derecognised (AFS revaluations, cumulative differences on foreign operations and cash flow hedges). Other components are not reclassified.

15. Presumably the board distinguished between reclassified items and non-reclassified items when it made the display decisions in the relevant standard. It seems appropriate to display items with similar reclassification requirements together.

Question 3: OCI Reclassification
The staff recommend that the Board tentatively decide to require that components of OCI that will not be reclassified into profit or loss in future periods be displayed together and that components of OCI that will be reclassified into profit or loss in future periods be displayed together.

IASB Staff paper

Other issues to consider

16. There are two other items that the Board may wish to consider including in this project that are also of a limited nature and involve only display. They are:

    (a) whether each component of OCI should be displayed before its income tax effects with the total tax effect of OCI items displayed on one line (as is the current practice) or with the income tax effect, which is currently provided in a note, displayed with the related item of OCI on the face of the statement; and

    (b) whether items of OCI that will be reclassified should be shown gross with amounts reclassified in the current year shown separately on the face of the statement.

Income tax

17. Currently, components of other comprehensive income are able to be presented either net of tax or gross with one amount shown for the aggregate amount of income tax relating to those components.

18. Under the FASB proposal currently being developed in the Financial Instruments project, changes in the fair value of investments in most equity instruments would be recognised in net income (profit or loss).[1] Under the IASB exposure draft, *Financial Instruments: Classification and Measurement*, the change in the fair value of investments in equity instruments generally will be recognised in profit or loss. However, for investments in equity instruments not held for trading, an election may be made on initial recognition to include the change in the fair value in OCI. If this option is elected, dividends received on these investments will also be included in OCI, there will be no reclassification of gain or loss on sale of the investment, and thus, there will be no need for an impairment charge. The Basis for Conclusions, *Financial*

[1] The scope of the project excludes equity investments in consolidated subsidiaries and an interest in a variable interest entity that the entity is required to consolidate.

Instruments: Classification and Measurement, (paragraph BC68) indicates that his election may be appropriate for what an entity views as a 'strategic' investment made with the intention of establishing or maintaining a long-term operating relationship.

19. The Basis for Conclusions (paragraph BC75) also notes that "all options result in decreased comparability. However, the Board believes that the proposals that accompany this option – that the election is irrevocable and additional disclosures are required - address some of those concerns."

20. To enable a financial statement user to easily adjust a statement of comprehensive income prepared under IFRS to one prepared under US GAAP requires that the components be presented on the same tax basis. Allowing a choice of gross or net of taxation effects reduces the ability to make such adjustments.

Gross of taxation effects

21. As a first step, I am recommending that the option to present components of income net of income tax effects be removed.

Question 5: Income tax related to components of OCI
The staff recommend that the Board tentatively decide to remove the option that allows an entity to display components of OCI net of income tax effects.

Displaying related tax

22. Our consultation with users suggests that some users think that displaying the income tax effect of each component of comprehensive income on the face of the comprehensive income statement would enhance transparency and ensure that financial statement users do not misinterpret an entity's performance.

23. **Appendix B** provides an illustration of a statement of comprehensive income with tax effects displayed on the face along with their related OCI items.

24. I am reluctant to recommend proposing that the tax effect of each component be presented along with the related OCI component. Although such an approach

might make it easier for an analyst to adjust the income statement, if this information is relevant for OCI components it seems equally relevant for other components of income. Although I do not support this proposal I think it is appropriate to ask the question of the Board.

Question 6: Income tax related to components of OCI
Does the Board want to tentatively decide to require that the income tax effect of an OCI item be displayed with the related OCI item in the statement of comprehensive income?

Reclassified amounts

25. Currently, IAS 1 permits items of comprehensive income to be displayed in the aggregate, with disclosure of the current year gain or loss and reclassification adjustment presented in the notes. Alternatively, a disaggregated presentation can be used. Disaggregated presentation improves transparency and comparability by separating current period changes from accumulated changes from previous periods. This should help ensure that financial statement users do not misinterpret an entity's performance.

26. The FASRI Experimental Study on Financial Statement Presentation presented at the September Board meeting (Agenda paper 8A) support this view. The results of that study indicate that "Financial statements that are classified and disaggregated on their face appear to help analyst forecasts and judgements the most."

27. **Appendix C** provides an illustration of a statement of comprehensive income with the items of other comprehensive income disaggregated to show the current period gain or loss and reclassification adjustments on the face of the statement of comprehensive income.

Question 7: Current period and reclassified components of OCI
The staff recommend that the Board tentatively decide to eliminate the presentation alternative which permits items of other comprehensive income to be displayed in the aggregate, with disclosure of the current year gain or loss and reclassification adjustment presented in the notes.

Appendix A: Illustration[2]

Revenue	390,000
Cost of sales	(245,000)
Gross profit	145,000
Other income	20,667
Distribution costs	(9,000)
Administrative expenses	(20,000)
Other expense	(2,100)
Finance costs	(8,000)
Share of profit of associates	35,100
Profit before tax	161,667
Income tax expense	(40,417)
Profit for the year from continuing operations	121,250
Loss for the year from discontinued operations	-
PROFIT FOR THE YEAR	121,250
Other comprehensive income:	
Items that will not be reclassified:	
Gain (loss) on strategic equity securities including dividends received[3]	520
Gain (loss) on property revaluation	933
Actuarial gains (losses) on defined benefit pension plans[4]	(667)
Share of other comprehensive income of associates[5]	-
Items that will be reclassified:	
Available-for-sale financial assets[6]	(24,000)*
Exchange differences on translating foreign operations	5,334 *
Cash flow hedges[7]	(667)*
Share of other comprehensive income of associates[8]	400
Income tax relating to all components of OCI	4,547 **
Other comprehensive income, net of tax	(13,600)
TOTAL COMPREHENSIVE INCOME	107,650

* This illustrates the aggregated presentation, with disclosure of the current year gain or loss and reclassification adjustment presented in the notes. Alternatively, a gross presentation can be used.

** The income tax relating to each component of OCI is disclosed in the notes.

[2] Based on Illustrative presentation of financial statements in IAS 1 (September 2007).
[3] Proposed in ED *Financial Instruments: Classification and Measurement.*
[4] Classification based on proposal in Discussion *Paper Preliminary Views on Amendments to IAS 19*.
[5] This means the share of associates' OCI items attributable to owners of the associates that will not be reclassified. It is after tax and non-controlling interests in associates.
[6] Proposed to be eliminated in ED *Financial Instruments: Classification and Measurement.*
[7] Hedge accounting is being currently reconsidered by the IASB.
[8] This means the share of associates' OCI items attributable to owners of the associates that will be reclassified. It is after tax and non-controlling interests in associates.

Appendix B: Illustration—OCI displayed with their related tax effect[9]

Revenue	390,000
Cost of sales	(245,000)
Gross profit	145,000
Other income	20,667
Distribution costs	(9,000)
Administrative expenses	(20,000)
Other expense	(2,100)
Finance costs	(8,000)
Share of profit of associates	35,100
Profit before tax	161,667
Income tax expense	(40,417)
Profit for the year from continuing operations	121,250
Loss for the year from discontinued operations	-
PROFIT FOR THE YEAR	121,250
Other comprehensive income:	
Items that will not be reclassified:	
Gain (loss) on strategic equity securities including dividends received[10] (net of 120 tax)	400
Gain (loss) on property revaluation (net of 333 tax)	600
Actuarial gains (losses) on defined benefit pension plans (net of 167 tax benefit)[11]	(500)
Share of other comprehensive income of associates[12]	-
Items that will be reclassified:	
Available-for-sale financial assets [13] (net of 6,000 tax benefit)	(18,000)*
Exchange differences on translating foreign operations (net of 1,334 tax)	4,000 *
Cash flow hedges[14] (net of 167 tax benefit)	(500)*
Share of other comprehensive income of associates[15]	400
Other comprehensive income, net of tax	(13,600)
TOTAL COMPREHENSIVE INCOME	**107,650**

* This illustrates the aggregated presentation, with disclosure of the current year gain or loss and reclassification adjustment presented in the notes. Alternatively, a gross presentation can be used.

---

[9] Based on Illustrative presentation of financial statements in IAS 1 (September 2007).
[10] Proposed in ED *Financial Instruments: Classification and Measurement.*
[11] Classification based on proposal in Discussion *Paper Preliminary Views on Amendments to IAS 19.*
[12] This means the share of associates' OCI items attributable to owners of the associates that will not be reclassified. It is after tax and non-controlling interests in associates.
[13] Proposed to be eliminated in ED *Financial Instruments: Classification and Measurement.*
[14] Hedge accounting is being currently reconsidered by the IASB.
[15] This means the share of associates' OCI items attributable to owners of the associates that will be reclassified. It is after tax and non-controlling interests in associates.

Appendix C: Illustration–OCI Disaggregated[16]

Revenue	390,000
Cost of sales	(245,000)
Gross profit	145,000
Other income	20,667
Distribution costs	(9,000)
Administrative expenses	(20,000)
Other expense	(2,100)
Finance costs	(8,000)
Share of profit of associates	35,100
Profit before tax	161,667
Income tax expense	(40,417)
Profit for the year from continuing operations	121,250
Loss for the year from discontinued operations	0
PROFIT FOR THE YEAR	121,250
Other comprehensive income:	
Items that will not be reclassified:	
Gain (loss) on strategic equity securities including dividends received[17] (net of 120 tax)	400
Gain (loss) on property revaluation (net of 333 tax)	600
Actuarial gains (losses) on defined benefit pension plans (net of 167 tax benefit)[18]	(500)
Share of other comprehensive income of associates[19]	-
Items that will be reclassified:	
Available-for-sale financial assets [20]	
Gains arising during the period (net of 333 tax)	1,000
Reclassification of gains included in profit or loss (net of 6,333 tax benefit)	(19,000)
Exchange differences arising on translating foreign operations (net of 1,667 tax) [21]	4000
Cash flow hedges[22] (net of 167 tax benefit)	
Gains (losses) arising during the period (net of 1,168 tax benefit)	(3,500)
Reclassification of gains included in profit or loss (net of 833 tax)	2500
Amounts transferred to initial carrying amount of hedged item (net of 167 tax)	500
Share of other comprehensive income of associates[23]	400
Other comprehensive income, net of tax	(13,600)
TOTAL COMPREHENSIVE INCOME	**107,650**

[16] Based on Illustrative presentation of financial statements in IAS 1 (September 2007).
[17] Proposed in ED *Financial Instruments: Classification and Measurement.*
[18] Classification based on proposal in Discussion *Paper Preliminary Views on Amendments to IAS 19*.
[19] This means the share of associates' OCI items attributable to owners of the associates that will not be reclassified. It is after tax and non-controlling interests in associates.
[20] Proposed to be eliminated in ED *Financial Instruments: Classification and Measurement.*
[21] There was no disposal of a foreign operation. Therefore, there is no reclassification adjustment for the period presented.
[22] Hedge accounting is being currently reconsidered by the IASB.
[23] This means the share of associates' OCI items attributable to owners of the associates that will be reclassified. It is after tax and non-controlling interests in associates.