Project **Financial Statement Presentation**

Topic **Sweep issues**

Purpose

1. The staff draft of the exposure draft carries forward some proposals from the discussion paper, *Preliminary Views on Financial Statement Presentation*, that the boards have not re-deliberated because comment letter respondents had little or no concerns about these particular proposals. The purpose of this paper is to briefly describe those issues and how the staff handled each issue in the staff draft. At the February joint meeting, the staff will ask the boards if they agree with the staff treatment of the following:
   (a) Statement of changes in equity (SCE)
   (b) Classification policy
   (c) Long-term contractual maturity information
   (d) Net presentation in the financial statements
   (e) Disaggregation on the statement of cash flows (SCF)
   (f) Required subtotals.

Statement of changes in equity

1. The boards decided in Phase A of this project that a statement of changes in equity should be part of a complete set of financial statements. The IASB revisions to IAS 1, *Presentation of Financial Statements*, in 2007 incorporated that decision. The FASB has yet to formally expose that decision. In developing the discussion paper, the boards decided to retain the existing requirements in IAS 1 (revised 2007) on the statement of changes in equity and

not consider any further changes to the statement of changes in equity in Phase B of the project.

2. After the discussion paper was issued, the IASB proposed amending paragraphs 106 and 107 of IAS 1 as part of the August 2009 Exposure Draft, *Improvements to IFRSs*. The proposed amendment (see below) is the result of constituent feedback and allows for the presentation of the components of changes in equity either on the statement of changes in equity or in the notes to financial statements.

> **Proposed amendment to IAS 1 *Presentation of Financial Statements***
>
> **Structure and content**
>
> **Statement of changes in equity**
>
> 106 An entity shall present a statement of changes in equity showing in the statement <u>or in the notes</u>:
>
> (a) total comprehensive income for the period, showing separately the total amounts attributable to owners of the parent and to non-controlling interests;
>
> (b) for each component of equity, the effects of retrospective application
>
> (c) [deleted]
>
> (d) for each component of equity, a reconciliation between the carrying amount at the beginning and the end of the period, separately disclosing changes resulting from:
>
> (i) profit or loss;
>
> (ii) each item of other comprehensive income: and
>
> (iii) transactions with owners in their capacity as owners, showing separately contributions by and distributions to owners and changes in ownership interests in subsidiaries that do not result in a loss of control.
>
> **107** An entity shall present, either in the statement of equity or in the notes, ~~the amounts of dividends recognized as distributions to owners during the period and~~ the ~~related~~ amount per share <u>of dividends recognized as distributions to owners.</u>

3. The staff is concerned that the proposed wording suggests that an entity can present all items in paragraph 106 in the notes to financial statements. Respondents to the annual improvements exposure draft expressed similar concerns. The IFRIC staff might raise this issue at the March IFRIC meeting.

4. The staff draft includes paragraphs 106–109 from IAS 1 (revised 2007) on the statement of changes in equity. Paragraphs 106 and 108 in IAS 1 are the same as (or similar to) what was in the discussion paper.

Classification policy

5. The discussion paper proposed that the classification of assets and liabilities in the operating, investing, financing assets, and financing liabilities categories would be an accounting policy. Thus, management would be required to explain its classification policy in its accounting policy note disclosure.

6. Because of the changes made to narrow the definitions of most sections and categories, an entity's management will have less flexibility in classifying items than it did in the discussion paper. However, because management will still classify items (other than cash) at the reportable segment level, it may classify items differently between reportable segments.

7. As noted in the discussion paper, requiring classification to be an accounting policy should result in consistency in period-to-period presentation for a given entity. Therefore, the staff think classification should remain an accounting policy and that management should be required to disclose information about the bases for its classifications.

8. Thus, the staff draft retains the requirement that an entity's policy for classifying its assets and liabilities be an accounting policy that is described in its accounting policy note. As in the discussion paper, the disclosure about an entity's classification policy should include a description of the type(s) of businesses in which an entity engages and provide a user with the necessary information to understand management's approach to the business. An entity's explanation of its classification policy also should address classification that varies by reportable segment.

Long-term contractual maturity information

9. In December 2009, the boards agreed with the staff recommendation to not retain the discussion paper requirement that an entity disclose information about

the maturities of its contractual *short-term* assets and liabilities. The discussion paper also proposed that an entity disclose information about the maturities of its contractual *long-term* assets and liabilities.

10. At the December joint meeting, the staff recommended that the exposure draft not retain the requirement to disclose information about the maturities of its contractual *long-term* assets and liabilities because IFRS and US GAAP currently require disclosure of similar information about long-term contractual assets and liabilities. The staff think that the boards agreed with that recommendation, but that tentative decision was never captured in the summary of decisions made at the December joint meeting. At the February joint meeting, the staff would like the boards to affirm that the exposure draft should not include a requirement to disclose information about the maturities of its contractual *long-term* assets and liabilities.

Net presentation in the financial statements

11. In developing the discussion paper, the boards agreed that the chapter related to the SCF would mention the current guidance provided in Accounting Standards Codification (ASC) Topic 230, *Statement of Cash Flows*, and IAS 7, *Statement of Cash Flows*, on netting or offsetting cash flows in the SCF. That guidance is very similar and was combined for drafting purposes. In addition, the staff provided guidance on cash flows for value added tax (VAT) based on comment letter responses.

12. Chapter 7 of the staff draft:

    (a) Includes the combined guidance in IFRSs and US GAAP about presenting net cash flows in the SCF. (The draft reflects the staff recommendation in IASB agenda paper 4D/FASB memorandum 76D, that the cash flows from loan originations and repayments of loans be shown gross, unless those loans meet the other netting criteria.)

    (b) Clarifies that the cash inflows and outflows related to VAT may be netted in the SCF (because it meets the existing criteria for netting). Payment of VAT is a cash inflow from customers that is not related to revenues.

13. In developing the discussion paper, the boards envisioned that the exposure draft would include a more general offsetting principle similar to that in IAS 1. Therefore, the staff draft includes the overall offsetting principle from IAS 1 (modified as follows):

> **An entity should not offset assets and liabilities or income and expenses unless required or permitted by an IFRS/the ASC.** Paragraph xx of this standard provides guidance on the net presentation of cash flows.
>
> An entity reports separately both assets and liabilities, and income and expenses. Offsetting ~~in the statements of comprehensive income or financial position or in the separate income statement (if presented)~~ amounts in the financial statements detracts from the ability of users both to understand the transactions, other events and conditions that have occurred and to assess the entity's future cash flows, except when offsetting amounts reflects the substance of the transaction or other event.
>
> Measuring assets net of valuation allowances—for example, obsolescence allowances on inventories and doubtful debts allowances on receivables—is not offsetting.

Disaggregation on the SCF

14. During the October 2009 joint meeting, the boards tentatively decided to retain the direct method SCF as a requirement in the exposure draft. The boards also agreed to a less disaggregated approach to the cash flow than was presented in the discussion paper.

15. The staff explained that identifying cash flows by function was an extremely costly aspect of compiling cash flow information and suggested that identifying cash flows that are consistent with by-nature disaggregation of expense items would be a more operational approach to preparing a direct method SCF. Using that as our starting point, the staff developed disaggregation guidance for the purpose of preparing a direct method SCF. The staff draft includes the following principle and application guidance in Chapter 7:

    (a) An entity should present separately cash flows of a dissimilar nature unless those cash flows are immaterial. An entity also should present separately cash flows that are nonrecurring.

(b) An entity should disaggregate similar cash inflows and outflows when the nature of the cash flow and timing of the payment in relation to its recognition in profit and loss is relevant to an understanding of the entity's increase or decrease in cash.

(c) An entity makes the judgement about whether to present separately similar cash inflows and outflows related to income and expense on the basis of an assessment of:

  (i) the nature of the expense the cash flow is related to and

  (ii) the extent to which the timing of the payments or receipts for income and expense items differ from its recognition in profit and loss.

(d) An entity makes the judgement about whether to present separately similar cash inflows or outflows related to the purchase and sale of assets or the issuance, imposition, and servicing of liabilities or equity on the basis of the assessment of:

  (i) the nature of the asset being purchased or sold or

  (ii) the nature of liability that is being issued, incurred, or serviced.

(e) An entity may make the assessment in (c) by considering the disaggregation of by-nature information presented or disclosed for items of income and expense. Using that information, an entity can assess:

  (i) which cash inflows and outflows can be aggregated because the resulting presentation of cash flows would be substantially redundant to the by-nature income and expense items presented or disclosed and

  (ii) which cash flows should be disaggregated because they are one time cash flows or are cash flows that differ from the recognition of related income or expense items attributable to more than the ordinary lag between recognition and payment.

Required subtotals

16. Paragraph 2.23 of the discussion paper addressed presentation of meaningful subtotals. That paragraph, which requires an entity to present subtotals and related headings for each section and category in the SFP, SCI, and SCF, is

included in Chapter 4 of the staff draft virtually unchanged. The staff would like the boards to affirm that subtotals and headings should be required as proposed in the discussion paper.

Summary of sweep issue recommendations

17. In summary, the staff recommend that the boards affirm the provisions in the staff draft related to the following:

    (a) The statement of changes in equity

    (b) Classification as an accounting policy

    (c) Disclosure of information about the maturities of its contractual *long-term* assets and liabilities (that is, not requiring in this project)

    (d) Net presentation on the statement of cash flows

    (e) A general offsetting principle

    (f) Disaggregation on the statement of cash flows

    (g) Required subtotals.

Question for the boards on sweep issues
Do the boards agree with the treatment of items a-g as described in this paper and as drafted in the staff draft?