Project	**Financial Statement Presentation**
Topic	**Cohesiveness principle and the section and category definitions**

Introduction

1. This paper for discussion at the financial statement presentation (FSP) working group[1] (WG) meeting addresses the IASB and the FASB's (collectively, boards) deliberations of the following topics:
   (a) the cohesiveness principle;
   (b) the definitions of sections and categories in the financial statements; and
   (c) the classification of assets and liabilities (and related items of income and expense, gain and loss, and cash flows) into those sections and categories.

Core presentation principle—cohesiveness

Discussion paper proposal

2. The discussion paper proposes that an entity should present information in its financial statements in a manner that portrays a cohesive financial picture of its activities (the cohesiveness objective). A *cohesive financial picture* means that the relationship between items across financial statements is clear and that an entity's financial statements complement each other as much as possible. Financial statements that are consistent with the cohesiveness objective display data in a way that clearly associates related information across the statements so that the information is understandable.

3. The discussion paper proposes application of the cohesiveness principle at the line item level. Aligning line items across the financial statements should

[1] The FSP "working group" encompasses both the Joint International Group and Financial Institution Advisory Group.

provide more information and increase the transparency of the information provided—something that financial statement users have requested repeatedly.

Deliberations for the exposure draft

4. In July 2009, the boards decided to re-position the cohesiveness objective as a core presentation principle. The boards also decided that the core presentation principles of cohesiveness and disaggregation will be designed to fulfill the objective of financial reporting: to provide financial information about the reporting entity that is useful to present and potential equity investors, lenders and other creditors in making decisions in their capacity as capital providers.[2]

5. In making the decision to retain cohesiveness as a core presentation principle, the boards also proposed that the exposure draft should require cohesiveness at something other than the line item level. The boards' revised proposal acknowledges that line item cohesiveness may be difficult to achieve in practice.

6. In December 2009, the boards tentatively decided to retain the discussion paper proposal that cohesiveness should apply to the statements of financial position, comprehensive income and cash flows. Further, the boards proposed that the cohesiveness principle should be applied at the category level.

7. To address classification issues that arise from a particular subset of long-term liabilities (pension obligations, asset retirement obligations, etc.), the boards proposed the addition of a new sub-category to the operating category of the financial statements. (See paragraphs 20—22 for discussion of the sub-category labelled *financing arising from operating activities*.)

Cohesiveness principle—excerpt from the staff draft of the exposure draft

8. The proposed drafting for the cohesiveness principle is included below (from Chapter 4 of the staff draft):

> **Cohesiveness principle**
>
> A reporting entity shall present information in its financial statements so that the relationship between items across financial statements is clear.

---

[2] From Chapter 1 of the exposure draft *An Improved Conceptual Framework for Financial Reporting* (September 2008).

> To present a cohesive set of financials statements, a reporting entity shall align the sections and categories in the statements of financial position, comprehensive income and cash flows.
>
> Financial statements that are consistent with the cohesiveness principle complement each other as much as possible. To that end, data is displayed in a way that clearly associates related information across the statements so that the information is understandable. For example, a reporting entity shall align the line item descriptions of information presented in the statements of financial position, comprehensive income and cash flows so that a user can find an asset or liability and the effects of a change in that asset or liability in the financial statements.

Defining the financial statement sections and categories

Discussion paper proposal

9. The discussion paper proposes that information should be presented in the financial statements in two broad sections—*business* and *financing*—and that the business section should be further disaggregated into *operating* and *investing categories*. The discussion paper defines the business section to include assets and liabilities (and changes in those assets and liabilities) that management views as part of its continuing business activities. The operating category is defined to include assets and liabilities that management views as related to the central purpose(s) for which the entity is in business. The investing category is defined to include business assets and liabilities that management views as unrelated to the central purpose for which the entity is in business.

10. The discussion paper proposes to define the financing section to include financing assets and financing liabilities. Financing assets and financing liabilities are financial assets and financial liabilities (as those terms are defined in IFRSs and US GAAP) that management views as part of the financing of the entity's business and other activities. In determining whether a financial asset or financial liability is part of an entity's financial activities, management should consider whether the item is interchangeable with other sources used to fund its business activities.

Deliberations for the exposure draft

11. The boards considered the definitions for the sections and categories at their September, October and December 2009 meetings, as well as at their January

2010 meeting. The boards expect to finalise their remaining tentative decisions on aspects of the category definitions at their February 2010 meeting.

12. In their deliberations for the exposure draft, the boards have modified substantially the proposed definitions of the sections and categories. The revisions were in response to feedback indicating that the discussion paper definitions would not result in financial statement that were prepared consistently from reporting entity to reporting entity—that is, the degree of flexibility given to management to determine classification might reduce the comparability of the financial statements.

Major changes

13. A reporting entity classifies its assets and liabilities in accordance with the section and category definitions proposed in the exposure draft. Management determines whether an asset or liability meets the definitional criteria based primarily on how the reporting entity uses the asset or liability in its reportable segments. However, cash is classified at the reporting entity level and is <u>always</u> presented as part of the operating category. The classification of items of income and expense, gain or loss, and cash flows is based on the classification of the related asset or liability.

14. The discussion paper proposes a distinction between the operating and investing categories based on a core/non-core concept. For the exposure draft, the boards tentatively decided to define the operating category to include assets that are a) part of the day-to-day operations of the reporting entity and b) generate revenue through a process that requires the interrelated use of the net resources of the reporting entity. That process also includes the application of employee and management expertise. Liabilities that arise from day-to-day business activities and are likely to be replaced by similar obligations within the reporting entity's operating cycle are also classified in the operating category.

15. For the exposure draft, the boards propose to define the investing category to include single assets that generate a return and that return is non-revenue income for the reporting entity. No significant synergies are created from combining investing assets.

16. To enhance the understandability of the financing section, the boards propose to equate that section to the capital structure of the reporting entity. Specifically, the boards tentative decided to define the financing section to include items that are part of a reporting entity's activities to obtain (or repay) capital. The financing section includes two categories: debt and equity.

17. The boards propose to define the debt category to include borrowing arrangements that are transacted on an arm's length basis at market terms. Additionally, assets and liabilities that arise from transactions involving an entity's own equity such as a dividend payable, a written put option on a reporting entity's own shares or a prepaid forward purchase contract for a reporting entity's own shares should be included in the debt category. Assets and liabilities that arise from transactions involving an entity's own equity are presented separately from borrowing arrangements within the debt category.

18. The boards expect to finalise the presentation of non-equity sources of financing at their February 2010 meeting.

A new section and a new sub-category

19. At their December 2009 meeting, the boards tentatively decided to create a new section on the statements of comprehensive income and cash flows to present the effects of a single acquisition or disposal transaction that recognises or derecognises assets and liabilities that are classified in more than one section or category on the statement of financial position. That section is labelled **multi-category transactions**.

20. At that same meeting, the boards also tentatively decided to create a sub-category in the operating category labelled **financing arising from operating activities** for liabilities that:

    (a) are not entered into for the purpose of obtaining (or repaying) capital;

    (b) are classified as long-term; and

    (c) have a time value of money component that is evidenced by either interest or an accretion of the liability due to the passage of time.

21. The boards recognise that some liabilities straddle the line between operating and financing—that is, the liability is closely related to an operating activity (eg remunerating employees) but the funding of that long-term liability often

becomes a financing decision because of its size. Further, the option to postpone settlement of the liability (ie a cash outflow) for a significant period of time is a source of financing to the entity. Use of this sub-category is particularly important on the statement of comprehensive in that it separates effects that are included in a 'core' operating income total from effects that are not.

22. The boards expect to finalise their proposals on the presentation of financing arising from operating activities at their February 2010 meeting.

Definitions—summary of the proposed format of the financial statements

23. The proposed drafting for the definitions is in Chapter 4 of the staff draft. The table below is included to help WG members better understand the proposed format of the financial statements to be included in the exposure draft.

SFP	SCI	SCF
Business	**Business**	**Business**
Operating	Operating	Operating
Financing arising from operating	Financing arising from operating	
Investing	Investing	Investing
Financing	**Financing**	**Financing**
Debt + other	Debt +other	Debt + other
Equity		Equity
	Effect of multicategory trans	**Effect of multicategory trans**
Income taxes	**Income taxes**	**Income taxes**
Discontinued ops	**Discontinued ops, net of tax**	**Discontinued ops**
	OCI, net of tax	

Discussion questions—section and category definitions

1. Do you think that the changes to the operating and investing definitions are an improvement?
2. Do you think that the changes to the financing section are an improvement?
3. Do you think the segregation of items that have both operating and financing characteristics in the operating category is an improvement?
4. Are the definitions in Chapter 4 clear and operational?