



April 6, 2009

By Email: commentletters@iasb.org

Re: Discussion Paper: Preliminary Views on Financial Statement Presentation

Dear Sir/Madam:

The Certified General Accountants Association of Canada (CGA-Canada) welcomes the opportunity to comment on the Discussion Paper: **Preliminary Views on Financial Statement Presentation**. Our comments are restricted to the fundamental and critical questions relating to Chapter 2 of the DP: Objectives and principles of financial statement presentation (Q1 to Q10). While we are of the view that the other issues flow and evolve from these objectives and principles, additional comments follow these responses.

Precursor to our comments, we would affirm that CGA-Canada continues to support high quality accounting standards which preserve or otherwise restore the confidence of stakeholders of the current financial reporting regime and which enhance the credibility of the profession during this time of global economic crisis.

*1. Would the **objectives of financial statement presentation** proposed in paragraphs 2.5–2.13 improve the usefulness of the information provided in an entity’s financial statements and help users make better decisions in their capacity as capital providers? Why or why not? Should the boards consider any other objectives of financial statement presentation in addition to or instead of the objectives proposed in this discussion paper? If so, please describe and explain.*

Comments

We believe that the objectives proposed in paragraphs 2.5-2.13 do serve to improve the usefulness of information in an entity’s financial statements and do help users make better decisions in their capacities as capital providers. The proposed model is more logical, informative and integrated than the extant model. We particularly welcome the proposal for a single statement of comprehensive income and the equal prominence accorded to the other comprehensive income section within that statement. In addition to the objectives proposed in the discussion paper, we believe that the boards should consider the objective of understandability in accordance with paragraph QC23 of the joint IASB/FASB exposure draft on “Conceptual Framework for Financial Reporting: The Objective of Financial Reporting and Qualitative Characteristics and Constraints of Decision-Useful Financial Reporting Information.” For example, many users of the financial statements who are not professional accountants may be confounded by interchangeable terms like profit or loss and Net Income. If the financial statements use well defined and the terms standardized, their comprehensibility will be enhanced. The importance of cognitive style is documented in the research paper: *Patel, Chris and Day, Ron, The Influence of Cognitive Style on the Understandability of a Professional Accounting Pronouncement by Accounting Students. BRITISH ACCOUNTING REVIEW, Vol 28, No 1, March 1996.*

2. Would the *separation of business activities from financing activities* provide information that is more decision-useful than that provided in the financial statement formats used today (see paragraph 2.19)? Why or why not?

Comments

We do not subscribe to the view that the users analyze or should analyze the financial statements of a firm independent of its capital structure. We believe that the linkages between operating results and the financial leverage employed by the firm are important for equity analysts as well as credit analysts. These linkages have become more focal because of the ongoing global economic crisis which is rooted in the indiscriminate leveraging and questionable financing of their portfolios by financial institutions and other institutional investors. We suspect that the proposal to segregate business performance and financing is derived from the Modigliani-Miller (MM) proposition that the value of the firm depends on its profitability and not on its capital structure (Modigliani and Miller 1958). This proposition has come under increased scrutiny recently. For example, please refer to the research paper: *Glickman, Murray, Modigliani-Miller On Capital Structure: A Post-Keynesian Critique (December 1996). UEL Department of Economics Working Paper No. 8.*

We believe that it is equally important to achieve vertical cohesiveness between business results and finance, as is the importance of achieving horizontal cohesiveness among the statement of financial position, statement of comprehensive income and statement of cash flows. The users of the financial statements should not be encouraged to view the results of business operations independent of capital structure. The true value added by the business can be gauged with reference to its risk return framework and not by ignoring the financial risk emanating from, and related to, the capital structure of the business. We believe that integration of results of business operations and the related capital structure in the financial statements enhances usefulness in assessing the amount, timing and uncertainty of future cash flows. Please refer to the additional comments below for the modified financial statement format advocated for.

3. Should *equity* be presented as a section separate from the financing section or should it be included as a category in the financing section (see paragraphs 2.19(b), 2.36 and 2.52–2.55)? Why or why not?

Comments

The funds contributed by the owners is usually a major component of the capital structure of a firm and for the reasons stated above, we believe that equity should be presented as a category separate from the financing category in the business section rather than as a separate section. Although, the statement of comprehensive income presents transactions with non-owners, the providers of equity do have an exclusive claim on the residual comprehensive income. Hence there is no real conflict with the cohesiveness objective of the proposed presentation model if equity is presented as a separate category in the business section. Please refer to the additional comments below for the modified financial statement format advocated for.

4. In the proposed presentation model, an entity would present its *discontinued operations* in a separate section (see paragraphs 2.20, 2.37 and 2.71–2.73). Does this presentation provide decision-useful information? Instead of presenting this information in a separate section, should an entity present information about its discontinued operations in the relevant categories (operating, investing, financing assets and financing liabilities)? Why or why not?

Comments

We endorse the presentation of discontinued operation in separate presentation as such presentation provides decision-useful information and facilitates assessment of the amount, timing and uncertainty of future cash flows.

5. *The proposed presentation model relies on a **management approach** to classification of assets and liabilities and the related changes in those items in the sections and categories in order to reflect the way an item is used within the entity or its reportable segment (see paragraphs 2.27, 2.34 and 2.39–2.41).*

(a) Would a management approach provide the most useful view of an entity to users of its financial statements?

(b) Would the potential for reduced comparability of financial statements resulting from a management approach to classification outweigh the benefits of that approach? Why or why not?

Comments

The management approach to classification of assets and liabilities and the related changes in those items in the sections and categories in order to reflect the way an item is used within the entity or its reportable segment is not supported by the joint IASB/FASB exposure draft on “Conceptual Framework for Financial Reporting: The Objective of Financial Reporting and Qualitative Characteristics and Constraints of Decision-Useful Financial Reporting Information.” We quote the following paragraph in this exposure draft.

“OB8. Managers and the governing board of an entity (herein collectively referred to as management) also are interested in financial information about the entity. However, management’s primary relationship with the entity is not that of a capital provider. Management is responsible for preparing financial reports; management is not their intended recipient. Other users who have specialized needs, such as suppliers, customers, and employees (when not acting as capital providers), as well as governments and their agencies and members of the public, also may find useful the information that meets the needs of capital providers; however, financial reporting is not primarily directed to these other groups because capital providers have more direct and immediate needs.”

In accordance with the assertions made in this paragraph, we believe that the reliance on management approach to classification is not appropriate because of potential abuse of this privilege, agency theory and expected reduction in the comparability of the financial statements.

6. *Paragraph 2.27 proposes that both assets and liabilities should be presented in the business section and in the financing section of the **statement of financial position**. Would this change in presentation coupled with the separation of business and financing activities in the statements of comprehensive income and cash flows make it easier for users to calculate some key financial ratios for an entity’s business activities or its financing activities? Why or why not?*

Comments

It is contended that because of cohesiveness among the financial statements, disaggregation of information and presentation of information about liquidity and financial flexibility, the linkages between the financial reporting terms will become relatively clear and the financial statements will become complementary. Hence it would be easier for users to calculate some key financial ratios for an entity’s business activities or for its financing activities. As the migration towards XBRL reporting of financial information gains momentum, the real issue will be providing timely access to this information rather than the mechanics of financial statement analysis.

7. Paragraphs 2.27, 2.76 and 2.77 discuss classification of assets and liabilities by entities that have **more than one reportable segment** for segment reporting purposes. Should those entities classify assets and liabilities (and related changes) at the reportable segment level as proposed instead of at the entity level? Please explain.

Comments

We support the view that entities should classify assets and liabilities (and related changes) at the reportable segment level as proposed rather than at the entity level because segment-level classification is consistent with the disaggregation objective of the proposed presentation model. We reproduce below quotes by Warren E. Buffett, Chairman of Berkshire Hathaway Inc, in his 2008 annual letter to the shareholders.

“Each of these has vastly different balance sheet and income account characteristics. Therefore, lumping them together, as is done in standard financial statements, impedes analysis. So we’ll present them as four separate businesses, which is how Charlie and I view them.”

8. The proposed presentation model introduces sections and categories in the statements of financial position, comprehensive income and cash flows. As discussed in paragraph 1.21(c), the boards will need to consider making **consequential amendments to existing segment disclosure requirements** as a result of the proposed classification scheme. For example, the boards may need to clarify which assets should be disclosed by segment: only total assets as required today or assets for each section or category within a section. What, if any, changes in segment disclosures should the boards consider to make segment information more useful in light of the proposed presentation model? Please explain.

Comments

We believe that, upon adoption of the proposed model, IFRS 8 *Operating Segment* and SFAS 131 *Disclosures about Segments of an Enterprise and Related Information* would be redundant so far as they relate to financial information disclosures. This is because the disaggregation objective articulated in paragraph 2.7 of the proposed presentation model states that an entity should disaggregate information in its financial statements in a manner that makes it useful in assessing the amount, timing and uncertainty of its future cash flows and as per paragraphs 2.27 and 2.40 of the proposed presentation model, an entity should classify assets and liabilities at the reportable segment level following the *management approach*. These provisions in the proposed presentation model, when considered together, should be sufficient to provide all the financial information currently required by the segment reporting standards mentioned above. For achieving completeness, the descriptive information disclosures required by IFRS 8 and SFAS 131 should be incorporated in the proposed presentation model rather than through separate standards.

9. Are the business section and the operating and investing categories within that section defined appropriately (see paragraphs 2.31–2.33 and 2.63–2.67)? Why or why not?

Comments

We believe that the business section and the operating and investing categories within that section are appropriately defined but for the reasons stated in the comments to question 5, we do not endorse *management approach* for such classification. The proposed presentation model should provide high level principles based guidance for such classification, though not detailed prescriptive rules.

10. Are the financing section and the financing assets and financing liabilities categories within that section defined appropriately (see paragraphs 2.34 and 2.56–2.62)? Should the financing section be restricted to financial assets and financial liabilities as defined in IFRSs and US GAAP as proposed? Why or why not?

Comments

We believe that the financing section and the financing assets and financing liabilities categories within that section are defined appropriately and that the financing section be restricted to financial assets and financial liabilities as defined in IFRSs and US GAAP as proposed because the alternative definitions considered by the boards would not be compatible with the existing definitions of these terms in the other standards; and if adopted, would create avoidable confusion and complexity

Additional Comments

For the reasons stated in our comments on Q2 & Q3, we suggest the following modified format for the financial statement presentation.

| Statement of financial position | Statement of comprehensive income | Statement of cash flows |
|---|--|--|
| Business <ul style="list-style-type: none"> • Operating assets and liabilities • Investing assets and liabilities • Financing (non-owner) assets • Financing (non-owner) liabilities • Equity | Business <ul style="list-style-type: none"> • Operating income and expenses • Investment income and expenses • Financing (non-owner) assets Income • Financing (non-owner) liability expenses | Business <ul style="list-style-type: none"> • Operating cash flows • Investing cash flows • Financing (non-owner) assets cash flows • Financing (non-owner) liability cash flows • Equity cash flows |
| Income taxes | Income taxes on continuing operations (business and financing) | Income taxes |
| Discontinued operations | Discontinued operations, net of tax | Discontinued operations |
| | Other comprehensive income, net of tax | |

Should you wish to discuss the contents of this comment paper or require further elaboration on any of the items presented herein, please do not hesitate to contact Kamalesh Gosalia (kgosalia@cga-canada.org) or the undersigned at rlefevre@cga-canada.org.

Sincerely,
[Original Signed by:]

Rock Lefebvre, MBA, CFE, FCIS, FCGA
Vice-President, Research & Standards