Department of Accounting and Finance

17 May 2006

The Chairman
Australian Accounting Standard Board
PO Box 204
Collins Street West
Victoria 8007

Submission on ED 148: Proposed amendments to AASB 101 *Presentation of Financial Statements:* A Revised Presentation

My submission on the proposals of the AASB in relation to the implementation of the IASB Exposure Draft in Australia is attached, as is a copy of my submission to the IASB on that exposure draft.

Preparing the submission would have been facilitated by the Board providing a mark-up of the proposed changes as the Financial Reporting Standards Board did in New Zealand; a mere description of them does not facilitate a proper appreciation of what is intended. It would also have helped if the Board had provided in MS Word or RTF format a copy of the AASB specific aspects of the exposure draft as this would facilitate the preparation of submissions by constituents. If the IASB is able to do so, I cannot see why the AASB cannot show the same level of consideration to those who wish to participate in its due process. I am also greatly concerned that the Board was either unwilling or unable to present reasoned arguments in support of changes to the Australian-specific requirements of AASB 101. A mere statement that the AASB no longer considers something to be appropriate without more is not what one expects from competent, professional standard setters; indeed it is completely unacceptable behaviour and brings the standard setting process into disrepute.

If technical staff of the Board wish to discussion any matter raised in the submission I can he contacted either by email:

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Yours truly,

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Submission by

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to

Australian Accounting Standards Board

ED 148: Amendments to AASB 101 *Presentation of Financial Statements*: A Revised Format

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Attachments: Submission on ED 148
Copy of Submission to IASB

Submission by
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ED 148: Amendments to AASB 101 *Presentation of Financial Statements*: A Revised Format

(a) Material to be added and deleted

A. Australian Text Proposed to Be Retained in the [Revised] AASB 101

A.1 Application and Materiality

It is proposed to retain paragraphs Aus1.1 to Aus1.10 of the existing AASB 101 that relate to the application of the existing AASB 101 in the [revised] AASB 101. The AASB notes, however, that the existing AASB 101 applies more broadly than most other AASB Standards. Most AASB Standards are mandatory only for reporting entities, whereas AASB 101, AASB 107 *Cash Flow Statements* and AASB 108 *Accounting Policies, Changes in Accounting Estimates and Errors* apply to entities that are required to prepare financial reports in accordance with Part 2M.3 of the Corporations Act even when they are not reporting entities. In view of the additional requirements proposed in the [revised] AASB 101 (for example, the proposal to require a third statement of financial position), some may consider it appropriate to limit the application of the [revised] AASB 101, or at least aspects of it, to reporting entities.

The rationale for excluding some entities from full application of the [revised] AASB 101 is not convincing. The mere assertion that non-reporting entities would have difficulty in providing the third statement of financial position is, without compelling empirical evidence in support of it, insufficient reason for providing an exemption from the requirements of the [revised] AASB 101. The minor changes made in the [revised] AASB 101 are not sufficient reason to change the policy decision made when the original AASB 101 was made.

It is my recollection that the Board's predecessor gave undertakings as part of the process leading to the replacement of the former requirements in schedule to the regulations that the core standards would apply to all entities required to lodge a financial report. In those circumstances, it is in my view inappropriate of for the Board to consider dropping this requirement.

A.2 Definitions of Certain Terms

Paragraph Aus11.1 provides definitions for a number of terms that are not included in the IASB ED. The AASB proposes to retain each of the following terms:

- *Annual reporting period*: as the term is referred to in the application paragraphs.
- *Australian equivalents to IFRSs*: as the term is specific to Australian reporting requirements.
- *Entity*: as the term is referred to in the application paragraphs.
- *Related practice*: as the term is specific to additional Australian reporting requirements that the AASB proposes to retain.

It is agreed that these definitions must be retained.

A.3 True and Fair View and Compliance with Australian Accounting Standards

Paragraph Aus13.1 explains that the Corporations Act requires an entity's financial report to comply with Australian Accounting Standards and, if necessary to give a true and fair view. Paragraph Aus13.2 requires the entity to state whether its financial report has been prepared in accordance with Australian Accounting Standards.

This paragraph must be retained.

A.4 Explicit and Unreserved Statement of Compliance

Paragraphs Aus14.1, Aus14.2 and Aus14.3 relate to the circumstances under which an entity can make a statement of explicit and unreserved compliance that is specifically applicable to parent financial statements, consolidated financial statements, and entities such as for-profit public sector entities and not-for-profit entities in the context of Australian Accounting Standards.

It is agreed that these requirements must be retained.

A.5 English Language

Paragraph Aus45.1 requires the financial report to be presented in the English language, which the AASB considers to be an important requirement to retain, particularly since it was originally a key requirement of the corporations legislation.

This paragraph must be retained.

A.6 Auditor Remuneration

Paragraphs Aus126.1 and Aus126.2 require disclosure of the payments made to auditors and related practices. The AASB considers this information to be useful to users.

This information is useful to financial report users. The including of detailed disclosures on these matters was strongly supported by the CLERP 9 discussion paper and by other recent reports.

A.7 Dividend and Franking Details

Paragraphs Aus126.4, Aus126.5 and Aus126.6 relate to the disclosure of dividend and franking details. The AASB considers this information to be useful to users.

It is agreed that this information is useful to users and must be retained.

A.8 Certain Illustrative Example

Example 3 of the Australian Implementation Guidance illustrates the disclosures of dividends paid or provided for and of the franking account balance. The AASB proposes to retain the example, as it believes that the example is useful to users (also see Item B.15).

The retention of this guidance would be useful.

B. Australian Text Proposed Not to Be Included in the [Revised] AASB 101

B.1 Application Paragraphs

Paragraphs Aus1.5 and Aus1.6 list a number of Standards, which are no longer applicable. Paragraph Aus1.7 notes that the notice about the Standard is published in the *Commonwealth of Australia Gazette*. The publication of the notice is no longer required.

Obviously there is no point in retaining Aus1.5 and Aus1.6. It would have helped stakeholders in formulating their response to this proposal if the Board had explained why the publication of a notice in the *Commonwealth of Australia Gazette* is no longer required. Without such an explanation I am unable to make an informed response.

B.2 Concise Financial Reports

Paragraph Aus3.1 notes that concise financial reports prepared in accordance with AASB 1039 *Concise Financial Reports* are treated in the same manner as for condensed interim reports prepared in accordance with AASB 134 *Interim Financial Reporting*. The AASB believes it is no longer necessary to retain this reminder about concise financial reports.

I disagree. There is no harm and there is a significant potential benefit in retaining the cross-reference. I note that the New Zealand FRSB proposes retaining the corresponding cross-reference.

B.3 Directors' Report and Remuneration Report

Paragraph Aus9.1 states that the Corporations Act requires entities to present reports such as Directors' Report and Remuneration Report outside the financial report. The AASB believes it is no longer necessary to retain this reminder about the Corporations Act requirement.

I disagree. There is no harm and there is a significant potential benefit in retaining the cross-reference.

B.4 Definition of General Purpose Financial Report

Paragraph Aus11.1 includes a definition of 'general purpose financial report'. Paragraph 7 of the IASB ED includes a definition of 'general purpose financial statements', which has been moved from paragraph 3 of the existing AASB 101 with some amendments. The AASB proposes not to retain the definition for 'general purpose financial report' included in paragraph Aus11.1, and proposes to adopt the definition as stated in paragraph 7 of the IASB ED. The AASB acknowledges that there might be some implications associated with this adoption, and notes that it is intending to review SAC *1 Definition of the Reporting Entity* (also see Item B.6). The AASB has included a question in the Specific Matter for Comment to seek constituents' views on this particular matter. (Refer to Specific Matter for Comment, question (b)).

For the reasons given in my submission to the IASB (see Attachment), the use of the term "general purpose financial statements" and "financial statements" rather than "general purpose financial report" and "financial report" is not supported. The change in terminology will cause considerable

confusion since in the case of entities regulated by the Corporations Act the term used is financial report. The Board would be derelict in the discharge of its responsibilities if it proceeds with this change. The Board is not bound to mindlessly follow what the IASB does, indeed to do so would be a breach of its statutory responsibilities.

However, it would be appropriate to consider a definition of "general purpose financial report" based on the form of words proposed by the IASB if an appropriate modification is made to them.

B.5 Identification of Framework Used in Preparation of Financial Statements

Paragraph Aus13.3 explains that the framework under which the report is prepared is identified in the summary of accounting policies, and that it may also be appropriate to state the relevant statutory and other requirements adopted in the preparation of the report. The AASB believes it is no longer necessary to retain this explanation.

I have no firm views on this proposal.

B.6 Disclosure whether Financial Report is a General Purpose Financial Report or a Special Purpose Financial Report

Paragraph Aus13.4 requires an entity to disclose that the financial report is a general purpose financial report (GPFR), or if applicable, a special purpose financial report (SPFR). Paragraph Aus105.1(a) comments that this disclosure normally precedes all the other items that are disclosed in the 'summary of accounting policies' note to the financial statements. The AASB notes that the IASB does not require an entity to specify in its financial report whether it is a GPFR or a SPFR. The AASB is intending to review SAC 1 and SAC 2 *Objective of General Purpose Financial Reporting* and the GPFR/SPFR dichotomy. Accordingly, the AASB proposes not to retain paragraph Aus105.1(a) and the definition of Special Purpose Financial Report in paragraph Aus11.1, and proposes to amend paragraph Aus13.4 to require an entity to disclose whether the financial report is a general purpose financial report.

I do not support this change. If a change is necessary, it should be made after the foreshadowed review of SAC's 1 and 2, not before. To do otherwise prejudges the outcome of that review, and could be interpreted as indicating that the foreshadowed review is sham.

B.7 Australian Currency

When the presentation currency is not Australian currency, paragraph Aus46.1 requires the entity to disclose the reason and justification for using a different currency. The AASB considers that the reason for using a different presentation currency, which entities are entitled to do under AASB 121 *The Effects of Changes in Foreign Exchange Rates*, will be evident from the financial report.

This requirement replicates that in AASB 121 Aus53.1, accordingly it would seem to be an unnecessary duplication. However, a cross-reference should be added to that requirement if the paragraph is deleted.

B.8 Rounding Basis

Paragraph Aus48.1 requires an entity to assess its regulatory framework to determine a rounding basis that is permitted under that regulatory framework. The AASB believes that it is no longer necessary to retain this paragraph.

I have no firm views on this matter.

B.9 Operating Cycle

Paragraph Aus56.1 requires disclosure of the length of the operating cycle where it is longer than twelve months and where current assets and current liabilities are presented separately from non-current assets and non-current liabilities, respectively. The AASB believes that it is no longer necessary to retain this paragraph and that the information will be evident from the financial report.

It is not immediately apparent why this information will be evident from the financial report. Given the significance of this information in the assessment of an entity's solvency and for other purposes, the Board has a responsibility to explain why it will be evident. I have scanned the IASB ED and cannot see any change to the standard that would render Aus56.1 redundant. Absent such explanation, the requirement must be maintained.

B.10 Retained Earnings

Paragraph Aus68.1 requires the entity to disclose on the face of the statement of financial position retained earnings attributable to equity holders of the parent. The AASB believes that it is no longer necessary to retain this paragraph.

For reasons given in my submission to the IASB, the use of the term "retained earnings" rather than the more appropriate term "retained profits" should no be permitted.

The AASB has a responsibility to explain to constituents why it no longer holds the belief that this information must be presented in the statement of financial position, and why note disclosure alone is now sufficient.

B.11 Encouragement for Using Formats Illustrated

Paragraphs Aus69.1, Aus83.1 and Aus97.1 encourage an entity to adopt one of the formats of the financial statements presented in the Appendix of AASB 101, unless an alternative format is more relevant in understanding the entity's financial position, financial performance and movements in equity. The AASB proposes not to retain these paragraphs, consistent with the proposal noted at B.15 not to retain the Appendix and the Australian Implementation Guidance. Consistent with this view, the AASB also proposes to remove paragraph Aus12.1 of AASB 107 *Cash Flow Statements* that encourages an entity to adopt the cash flow statement format presented in the Illustrative Examples included in AASB 107.

The paragraphs serve no useful purpose; either preparers must use the format or nothing should be said. Also, given the quality of the guidance, it is best that it be withdraw as it seemed to encourage practices that were contrary to the *Corporations Act*.

B.12 Position of Statement of Compliance with Australian Accounting Standards

Paragraph Aus105.1(b) notes where the statement of compliance with Australian Accounting Standards is normally placed in the notes to the financial statements. The AASB believes that it is no longer necessary to retain this paragraph.

I disagree. Given the inability of the Board to explain why it is no longer appropriate, it would be improper to accept the proposal.

B.13 Economic Dependency

Paragraph Aus126.3 requires an entity to make disclosures about an economic dependency where the entity is dependent on another entity for a significant volume of revenue or financial support, and that dependency is not clearly discernible from a separate line item in the income statement or statement of financial position. The IASB ED does not include this requirement and the AASB proposes not to retain it in the [revised] AASB 101.

The introduction of this requirement was the result of a long and comprehensive due process; one involving a comprehensively explained rationale. Accordingly, the Board is obliged to provide a coherent argument why the requirement is to be removed. The absence of one suggests that there is no rationale other than mindlessly following what the IASB does. Accordingly the provision must be retained.

B.14 Capital Commitments and Other Expenditure Commitments

Paragraph Aus126.7 requires disclosure of details of capital commitments and other expenditure commitments and also requires these details to be presented in time bands. The IASB ED does not have this requirement, although paragraph 114(d)(i) of the IASB ED (or paragraph 105(d)(i) of the existing AASB 101) notes the disclosure about 'unrecognised contractual commitments' normally follows a certain order of notes to the financial statements. The AASB proposes to adopt the same approach as the IASB with regard to the disclosure of these items.

The background to the introduction of this requirement is similar to that in B.13; and for the reasons I gave in response to B.13 the proposal cannot be supported.

B.15 Illustrative Examples and Australian Implementation Guidance

The Appendix of AASB 101, *Appendix – Illustrative Financial Report Structure* (pages 49 to 57 of the existing AASB 101), provided illustrative examples of a statement of financial position, income statement and statement of changes in equity that meet the requirements of AASB 101. AASB 101 also included Australian Implementation Guidance (pages 58 to 74 of AASB 101). The IASB ED's Implementation Guidance (pages 78 to 95 of the IASB ED) provides illustrative examples of statements of financial position, recognised income and expense and changes in equity that meet the requirements of the IASB ED. The AASB proposes to replace the Appendix and the Australian Implementation Guidance with the IASB ED's Implementation Guidance on the basis that the IASB ED's Implementation Guidance provides examples that illustrate the new requirements of the IASB ED. These new requirements supersede the corresponding requirements of the existing AASB 101. (Refer to A.8 for the AASB's proposal to retain an example of the existing AASB 101)

The AASB notes that the order of the statement of financial position items that is illustrated in the examples included in the IAS 1 and the IASB ED is different from the order that is used in the illustrations included in the Appendix of AASB 101. For example, under AASB 101, current assets and current liabilities precede non-

current assets and non-current liabilities, respectively, on the statement of financial position. Under the IAS 1 and the IASB ED, the reverse applies. The AASB also notes that the illustrated order is not mandatory.

Given the serious errors in this material it is appropriate that it be removed. Also, it is implied above that the Illustrative Examples are part of the [draft] IAS 1, they are not. This is clearly stated immediately before the examples! As such they provide guidance but are in no sense mandatory.

C. Deletion Made by the AASB in the Existing AASB 101 that Is Proposed to Be Reinstated

C.1 Fair Presentation

Paragraphs 17 to 20 of IAS 1 specify circumstances in which an entity could depart from a requirement in a Standard or an Interpretation. They were not included in the existing AASB 101 because they are inconsistent with the Corporations Act with regard to the approach to 'true and fair view' under sections 295 and 297 of that Act. In addition, the existing AASB 101 does not include the opening sentence of paragraph 15 of IAS 1 (paragraph 12 of the IASB ED), which is also inconsistent with the Corporations Act. The AASB proposes to reinstate the deleted text since these inconsistencies do not apply to the entities that are not subject to the Corporations Act.

The argument presented is not convincing. The Board's predecessor and the profession lobbied forcefully for the including of the prohibition in the corporate law. The rationale for that prohibition applied equally to entities not regulated by the corporate law. In the circumstances, the Board has a responsibility to explain why the policy basis that was used to support the prohibition is no longer acceptable. The only reasonable basis I can think of to change that policy is that the IFRS based standards are so defective that it really does not matter if they are applied or not. If this is so, then the Board was derelict in the discharge of is statutory obligations in making the standards.

Again the Board appears to be mindless following what the IASB does rather than basing its decision on a compelling, logical, argument; if such arguments exist, it is inexplicable why they have not been put forward by the Board.

D. Deletions Made by the AASB in the Existing AASB 101 that Are Proposed Not to Be Reinstated

D.1 IASB's Application Paragraph

Paragraph 2 of IAS 1 is not included in the existing AASB 101 because it referred to the applicability of IAS 1, which was not applicable to Australian reporting entities. This paragraph was replaced by the corresponding paragraphs Aus1.1 to Aus1.10 in the existing AASB 101. The AASB will continue to have its own application paragraphs in Australian equivalents to IFRSs and paragraph 2 is redundant in the context of AASB 101.

Agreed.

D.2 Commentary on Alternative Formats Used to Present Changes in Equity

Paragraph 101 of IAS 1 notes the alternative formats applicable for showing changes in equity. This paragraph is not included in AASB 101 and now the same paragraph has also been proposed for deletion by the IASB. Therefore the notation for the deletion in the [revised] AASB 101 will be amended from '[Deleted by the AASB]' to '[Deleted by the IASB]'.

Non-issue.

D.3 Previous Application Paragraphs of IAS 1

Paragraphs 127 and 128 set out the application details for IAS 1, which are not relevant to AASB Standards. Consequently, they were replaced by the Australian application paragraphs Aus1.1 to Aus1.3 in the existing AASB 101.

Another non-issue.

Question (b)

The AASB's preliminary views proposed for adopting the definition of 'general purpose financial report' as included in paragraph 7 of the IASB ED. The AASB notes that the second paragraph of the definition proposes that "General purpose financial statements include those that are presented separately or within other public documents such as a regulatory filing or report to shareholders." This statement could be interpreted as defining all financial reports filed with a regulator on a public register to be general purpose financial reports, which would include those that are filed with, for example, the Australian Securities and Investments Commission, whether or not the entities are reporting entities;

This nonsense: in the first sentence it is stated that it is proposed to adopted the definition of "general purpose financial report" in paragraph 7 of the [draft] IAS 1, however as pointed out in the following sentence the definition is in fact one of "general purpose financial statements". Given the terminology adopted in the *Corporations Act* and in some other regulatory schemes, it would be completely inappropriate to include in AASB 101 a definition of "general purpose financial statements". Also, as noted in my submission to the IASB (see attachment), the usage of that term is questionable. I suspect what the Board intended to say was that the definition would be based on that of "general purpose financial statements" in [draft]

IAS 1, but would use the term "financial report" rather than "financial statements". Provided the definition of "general purpose financial statements" is otherwise unobjectionable, it is appropriate for the AASB to align the definition of "general purpose financial report" with that of "general purpose financial statements".

I doubt that it is correct to claim that there is a second paragraph in the definition of "general purpose financial statements" in paragraph 7 of the [draft] IAS 1; in the context it is in fact a commentary or discussion of the application of the definition. If it formed part of the definition it would be in bold text, which it is not. Be that as it may, the Board has identified a problem that needs to be addressed, particularly in light of the Board's proposal (which is not supported) to remove the requirement for financial reports of non-reporting entities to be expressly identified as special purpose financial reports except when there is full compliance with accounting standards necessary for a general purpose financial report. Since the relevance of the commentary depends on the institutional context in a particular country, it would be both proper and appropriate for the Board to vary the paragraph in question to make it clear that of itself, a requirement to lodge a financial report with a regulator that is then on the public record does not make the entity a reporting entity and does not therefore require the preparation of a general purpose financial report.

Question (c)

Whether certain entities should be required to prepare an additional comparative statement of financial position as proposed. These entities may include, for example:

(i) public sector entities (for example, general government sector): The AASB notes that three statements of financial position may create practical presentation difficulties for these entities. The AASB is particularly mindful of its proposal in ED 142 *Financial Reporting of General Government Sectors by Governments* to require the presentation of an additional statement: the original budget for these entities; and

(ii) entities required to prepare financial reports under Part 2M.3 of the Corporations Act that are not reporting entities;

In the basis for conclusions, the IASB indicates that the requirement to include a start-of-period statement of financial position will not impose a burden, which seems to me to be a reasonable proposition. While the logistics of doing so may be a challenge, that of itself is not a sound basis for excusing any sub-set of entities from compliance. Accordingly, if the

proposal for the inclusion of this third statement of financial position is sustainable – which it is in my view and the Board does not indicate that it has any reservations about the philosophy underlying the proposal – then it must extend to all entities that are within the scope of the Board's standards.

Question (d)

Whether the proposals give rise to any public sector entity issues that you believe require additional requirements or guidance in AASB 101. If yes, please describe the issues and provide reasons supporting your response;

I do not have the experience or expertise to comment on public-sector specific problems that may arise if the proposals in ED 148 are adopted.

Question (e)

Any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, particularly any issues relating to:

(i) not-for-profit entities; and

(ii) public sector entities; and

It is inappropriate for entities to be given the choice of splitting the statement of recognised income and expense into two statements. Doing so does not improve disclosure practices and provides unscrupulous management with an opportunity to manipulate the impression created by the financial report. It also runs the risk of reducing comparability. Accordingly, the Board must prohibit the provision of two statements excepts when legislation or directive with force of legislation prohibits the use of one statement rather than two.

If a choice is to be permissible, then it becomes the responsibility of the standard-setter to provide clear and unambiguous criteria that is to be used in making that choice; it is insufficient to rely on the criteria in AASB 108 which in this context are of little use is making such a determination.

Question (f)

Whether the proposals are in the best interests of the Australian economy.

There are numerous serious defects in the [draft] IAS 1, which will be adopted in the proposed new AASB 101. While many of these defects are in the current AASB 101, this does not change the fact that they greatly reduce the utility of the information presented in general purpose financial reports,

result in divergent reporting practices and facilitate the presentation of misleading or false information by disreputable preparers. Accordingly, the [draft] standard will, if it is not properly amended to remedy those serious defects, create a substantial risk of undermining the integrity of, and the public's confidence in, the Australian financial reporting system.

17 May 2006

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Submission on Exposure Draft: Amendments to IAS 1 Presentation of Financial Statements: A Revised Presentation

My detailed comments on the Exposure Draft are attached. One pleasing aspect of the exposure draft is the proposal to use more appropriate terminology. Effective communication is enhanced if the terminology used is both descriptive and easily comprehended; it is also enhanced if the terminology adopted is used consistently and that a multitude of terms is not used to refer to the same concept. The continued presence of a multitude of terms for the same concept runs the risk of undermining both the integrity of, and confidence in, the financial reporting standard setting process.

The incremental improvements proposed in the Exposure Draft are, on balance, likely to improve the quality of financial reporting under International Financial Reporting Standards. Unfortunately, the rationale presented to support many of the requirements of the proposed standard is not convincing. It is difficult to see how they are consistent with the objectives of financial reporting.

While stakeholders benefit from being provided with a mark-up showing the proposed changes, the value of providing the mark-up is greatly reduced if, as in the present case, there are obvious errors in the mark-up. Also, the presentation of the material dealing with amendments to other standards is so poor that it is extremely difficult to work out which standard they relate to. Such presentation is completely unacceptable. It can only discourage stakeholder from reviewing the consequential amendments.

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Yours truly,

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CC Australian Accounting Standards Board

Submission by
Ian Langfield-Smith, Department of Accounting and Finance, Monash University
to
International Accounting Standards Board
on Exposure Draft
Amendments to IAS 1 Presentation of Financial Statements: A revised Format

Responses to questions asked

Questions 1 and 2 – A complete set of financial statements

The Exposure Draft proposes that the titles of the financial statements should be as follows:
(a) statement of financial position (previously 'balance sheet');
(b) statement of recognised income and expense;
(c) statement of changes in equity; and
(d) statement of cash flows (previously 'cash flow statement').
The Board does not propose to make the changes of nomenclature mandatory (see paragraph 31 of the draft Standard and paragraphs BC4 and BC5 of the Basis for Conclusions).

Question 1 – Do you agree with the proposed titles of the financial statements (bearing in mind that an entity is not required to use those titles in its financial statements)? If not, why?

I agree that the titles "balance sheet" and "income statement" are no longer appropriate. In the case of the income statement, the title is misleading, since the statement includes both items of income and items of expense, with the "outcome" being (under present IAS 1) period profit or loss. The title "balance sheet" gives no indication of the purpose of the statement.

I am unconvinced of the need to replace "cash flow statement' with "statement of cash flows"; the former is more forceful and in no way miss-describes the nature of the information contained in the statement. The alternative form of words is more verbose, and is viewed by some as pretentious and difficult to use. For authors of commentaries and textbooks, such as me, it is much easier to write for example, "cash flow statement" than "statement of cash flows". It is also easier for those with reading disabilities to read and understand.

I agree that it is appropriate to change from the title "balance sheet" to "financial position statement". I would prefer that the replacement title for the "income statement" were "financial performance statement", although the title "recognised income and expense statement" is suitably descriptive.

I doubt that the change in terminology is likely to confuse either users or preparers. In Australia, we changed from "profit and loss statement" to "statement of financial

performance" and from "balance sheet" to "statement of financial position" some years ago. This caused little if any confusion on the part of financial report users. There was some initial confusion on the part of some less well informed preparers and auditors. The main burden was on authors of text books and commentaries who had to rewrite their material using the revised terminology.

Further comments

It is inexplicable that standards that purport to deal with something called "financial statements" are called International Financial Reporting Standards. If their title is correct, then their subject matter must surely be a financial report rather than financial statements; surely if it is appropriate to include in the title of the standards the words "financial reporting", then the thing with which it deals logically must be described as a "financial report", rather than the nebulous and (in the context) misleading term "financial statements". The so-called financial statements include not only the financial statements; they also contain notes (to the financial statements), thus the title is both misleading and inappropriate. Further, the title Financial Report is more descriptive of the nature and objective of the report. It would also avoid the need – although I doubt if there a need presently – to use the verbose, awkward and potentially confusing term "recognised on the face of the [name of the financial statement]".

I agree that the new terminology should not be mandatory; however, the use of alternative terminology must only be permitted where that terminology properly reflects the nature of the information included in the financial statement and the terminology used in that statement. For example it would be inappropriate to use the term "income statement" since income is a gross item, and (if that approach to terminology is adopted) the result is net income and the appropriate title would be "net income statement".

It is important that terminology used is consistent throughout the financial report.

The Exposure Draft introduces a requirement to present a statement of financial position as at the beginning of the earliest period presented in the financial statements. Therefore, in addition to notes, an entity would be required to present three statements of financial position, and two of each of the other statements that form part of a complete set of financial statements (see paragraphs 31 and 39 of the draft Standard and paragraphs BC6–BC9 of the Basis for Conclusions).

Question 2 – Do you agree that a statement of financial position as at the beginning of the period should be part of a complete set of financial statements, and that an entity presenting

comparative information should therefore be required to present three statements of financial position in its financial statements? If not, why?

I agree that it is appropriate to provide a financial position statement reflecting the financial position at the commencement of the earliest period for which comparative amounts are provided. This will facilitate the calculation of financial ratios and would not impose an unreasonable burden on preparers.

Questions 3–5 – Reporting owner changes in equity and recognised income and expenses

The Exposure Draft proposes to require entities to present all changes in equity arising from transactions with owners in their capacity as owners (ie 'owner changes in equity') separately from other changes in equity (ie 'non-owner changes in equity' or 'recognised income and expense'). Non-owner changes in equity would be presented in either (a) a single statement of recognised income and expense, or (b) two statements: a statement displaying components of profit or loss and a second statement beginning with profit or loss and displaying components of other recognised income and expense (see paragraphs 81 and 82 of the draft Standard and paragraphs BC11–BC20 of the Basis for Conclusions).

Question 3 – Do you agree that non-owner changes in equity should be referred to as 'recognised income and expense' (bearing in mind that an entity is not required to use the term in its financial statements)? If not, why?

As an interim measure, I would support the change.

Is the terminology used in the Standard important if entities are permitted to use other terms in their financial statements? If so, what term would you propose instead of 'recognised income and expense'?

A possible alternative term could be comprehensive profit.

Question 4 – Do you agree that all non-owner changes in equity (ie components of recognised income and expense) should be presented separately from owner changes in equity? If not, why?

I agree that they should be reported separately, provided the distinction is applied properly and consistently.

Question 5 – Do you agree that entities should be permitted to present components of recognised income and expense either in a single statement or in two statements?

Only one statement should be required.

If so, why is it important to present two statements rather than a single statement?

Inapplicable.

If you do not agree, why? What presentation would you propose for components of recognised income and expense that are not included in profit or loss?

I do not believe that it is appropriate to give entities the choice. Since period profit or loss is only a partial measure of the aggregate of all items of income and expense recognised in a reporting period, to allow some items of income and expense to be reported in a separate statement is potentially misleading. However, the presenting of a single statement may be inconsistent with domestic legislation, in which case two statements should be permitted. In all other cases, only one statement should be allowed.

Questions 6 and 7 – Other recognised income and expense—reclassification adjustments and related tax effects

The Exposure Draft requires the disclosure of reclassification adjustments relating to each component of other recognised income and expense (see paragraphs 92–96 of the draft Standard and paragraphs BC21–BC23 of the Basis for Conclusions).

Question 6 – Do you agree with this proposal? If not, why?

Such 'recycling' of previously recognised income and expense is inappropriate. It has the potential to confuse users of the financial report and fails to properly attribute them to the period in which they were initially recognised. This process is completely unacceptable; it undermines the credibility of the financial reporting process.

The Exposure Draft requires the disclosure of income tax relating to each component of other recognised income and expense (see paragraph 90 of the draft Standard and paragraphs BC24 and BC25 of the Basis for Conclusions).

Question 7 – Do you agree with this proposal? If not, why?

I agree that this disclosure should be made. However, I do not support including of after tax amounts for each component, with the gross amount only disclosed in the notes. Both the gross amount and the associated income tax expense must be included in the financial statement.

Question 8 – Presentation of per-share measures

The Exposure Draft does not propose changes to IAS 33 Earnings per Share. Therefore, earnings per share will be the only per-share measure presented on the face of the statement of recognised income and expense. If an entity presents any other per-share measure, that information is required to be calculated in accordance with IAS 33 and presented in the notes (see paragraph BC26 of the Basis for Conclusions).

Question 8 – Do you agree that earnings per share should be the only per-share measure that is required or permitted to be presented on the face of the statement of recognised income and expense? If not, which other per-share measures should be required or permitted to be presented on the face of a statement and why?

I support the proposal. However, the terminology is inappropriate; the proper term is 'profit or loss per share'. For the credibility of the financial reporting process to be maintained, it is essential that the terminology adopted is consistent. The use of multiplicity of terms to for the same concept creates potential for confusion on the part of both preparers and users of a financial report. It shows an unacceptable lack of rigour, and is inconsistent with a professional approach to the standard setting process.

Comments on mark-up

Note: All references are to the new paragraph numbers in the [draft] unless stated otherwise.

Paragraph 1

For the reasons explained on page 1, the term "general purpose financial report" is preferable to the term "general purpose financial statements". The use of the term "an entity shall" is problematic; of itself it fails to clearly communicate what is intended by its use. It is essential that this usage be explained, preferably by including an appropriately worded definition. This term is not explained elsewhere: it is not explained in either in the *Preface to International Financial Reporting Standards*, IFRS 1, or *The Framework for the Preparation and Presentation of Financial Statements*.

Paragraph 4

The expression "prepared in accordance with" is verbose, suggest the shorter and more emphatic phrased "prepared under".

Paragraph 7

The drafting style used for the definitions must be consistent. Unfortunately, there are some variations in the style adopted; however, they are only minor and can, with this interim revision, be ignored.

"General purpose financial statements": For the reasons given on page 2, the more appropriate term would be "general purpose financial report". In the discussion in the paragraph following the definition, I suggest "equity holders" rather than "shareholders".

"Other recognised income and expense": the drafting of the definition is cumbersome, making it extremely difficult to comprehend its meaning without repeated reading. On an initial reading, it suggests the opposite of what is in fact intended. I remind the Board of its ethical and legal obligations to ensure that the drafting of its standards does not, either directly or indirectly, discriminate against those with reading disabilities. While this should not be necessary, the propensity of the Board to develop standards with drafting that is inappropriate for those with reading disabilities makes it necessary to do so. I suggest the following is easier to understand:

> *Other recognised income and expense* is the total of (a) aggregate income *less* (b) aggregate expenses (including reclassification adjustments), recognised directly in equity. They are not recognised in profit or loss because other Standards or Interpretations permit or require their recognition directly in equity.

The definition uses the term "recognised directly in equity"; this term is used in many other standards and basis for conclusions[1]. There seems to be a difference between the meaning of "recognised directly in equity" and the term "accounted for as a deduction from equity" used in IAS 32 paragraph 35 (consistency of usage suggests that the appropriate term is "recognised as a deduction from equity"). Paragraph 109 indicates that transaction costs directly related to transactions with equity holders in their capacity as equity holders are expenses that are excluded from "other recognised income and expense". The possibility of confusion would be reduced if there were definitions of both these terms; if no definition is provided there must at a minimum be a clear discussion of the differences between them.

In the definition of **"reclassification adjustments"**, clarity would be improved if the following minor changes were made:

> *Reclassification adjustments* are amounts reclassified to profit or loss in the ~~current~~ reporting period that were recognised in other recognised income and expense in previous reporting periods.

Paragraph 11

In the second line the word "such" is redundant.

[1] It is intended that this usage be discontinued, see Appendix of the Exposure Draft. However, some elaboration is still required in IAS 1.

Paragraph 24

The use of the term "present" in paragraph 24 and elsewhere is problematic. It is unclear how "present" is differentiated from "disclosed". Suitably worded definitions of both "presented" and "disclosed" must be added to paragraph 7 as they are central to the proper application of the proposed standard. The discussion in paragraph 48 of the nature of disclosure can be used as the basis for the definition of "disclosed" and accompanying discussion.

Paragraph 25

In the last sentence of paragraph 25 the term "not sufficiently material to warrant separate presentation" is used; this seems to be another way of saying that the information is not "relevant to an understanding" of either the entity's financial position (see paragraph 55) or financial performance (see paragraph 85). Efficient and effective communication is predicated on consistency in usage, accordingly paragraph 25 must be redrafted so that the terminology is consistent with that in paragraphs 55 and 85. A failure to do so can only undermine the credibility of the standard setting process.

Paragraph 25

In the last line, the context suggests that it should be "if the disclosure of the information is not material" rather than "the information is not material".

Paragraph 27

Paragraph 27 requires must be rewritten as it is both awkward and difficult to follow; I suggest the following wording;

> An entity shall not offset assets and liabilities or income and expenses, unless it is either required to do so, or permitted to do so, by a Standard or an Interpretation.

Paragraph 29

The discussion in paragraph 29 appears to contradict the principle established in paragraph 28; that is offsetting is only possible if it is expressly allowed (required or permitted) by a Standard or Interpretation. However in paragraph 29 it is stated that:

> An entity undertakes, in the course of its ordinary activities, other transactions that do not generate revenue but are incidental to the main revenue-generating activities. An entity presents the results of such transactions ~~are presented~~, when this presentation reflects the substance of the transaction or other event, by netting any income with related expenses arising on the same transaction.

The logic of this analysis is questionable. Here we are apparently applying the definition of revenue in AASB 118, which is much wider than the definition in the *Framework*, and as a matter of logic, this discussion is on the basis that the scope limitations imposed by AASB 118.1-6 do not apply. This interpretation is supported by the two examples of permissible offset, both of which would be excluded from the scope of AASB 118. In the case of both the disposal of non-current assets and a reimbursement under a contract (such as an insurance contract), a revenue as defined in AASB 118 is produced. The examples seem to be limited to exceptions created in other standards. The first example is the disposal of non-current assets; in the case of property, plant and equipment, the requirement to offset is imposed by AASB 116.68 and 71, and the disposal of investments is regulated by AASB 139 which envisages offset in many of its provisions. In the second example reference is made to AASB 137, which expressly permits such offsets. So, despite what is said in the extract, it appears that it is not intended to create an exception in paragraph 28. Accordingly, in the context, it appears that the exceptions referred to flow from the requirements of various other standards; if this so, the discussion is both inaccurate and potentially misleading. If, contrary to the impression created, it is intended that paragraph 29 creates an exception to paragraph 28, then it should be done unambiguously. However, I consider such an exception to be completely unacceptable. No criteria are given allowing a proper determination of what is the substance of the event or transaction and it provides unfettered discretion to management which is open to a completely unacceptable risk of abuse.

In all cases, appropriate details of any offset must be disclosed in the notes; given the fundamental nature of the principle established in paragraph 28, any offset is clearly material by nature; its amount can add to its materiality but cannot detract from it. This disclosure requirement would not impose a burden on preparers.

Paragraph 30

The offsetting of gains and losses is by its nature is material, and the aggregate of all gains and the aggregate of all losses must be disclosed in the notes. Such information is central to a full understanding of the operations of an entity. It is unclear what significance is to be placed on the words "an entity reports such gains and losses separately". Does this mean that separate line items are included for both the aggregate of gains and the aggregate of losses, or does it mean something different? As currently expressed, it fails to give an unambiguous meaning. Since an exception is being created to a general principle, one would expect it to be clearly and concisely expressed, without the risk of confusion. A failure to remedy this

problem will undermine the credibility of, and confidence in, the financial reporting standard setting process.

Paragraph 31

For the reason presented on page 2, the collective term should be "financial report" not "financial statements". The introductory line would then become "The financial report comprises:"; also, there should be requirement to include in the report any statement or declaration, made by any of the board of directors (or its equivalent), chief executive officer, or chief financial officer, about compliance with legal obligations in relation to the preparation and presentation of the report. It would, of course, not include the report of the independent auditor or the report of the board of directors.

For the reasons given on page 2, the choice of title cannot be unrestricted. It must properly reflect the information presented in the statement, and it must be consistent with the terminology used in the statement. Thus, it would be proper to call it a "net income statement" if the term "period net income" were used rather than "period profit of loss", but it would be inappropriate to use the title "income statement", since the statement includes both income and expense items.

Paragraph 32

This requirement is essential if the integrity of the financial reporting process is to be protected.

Paragraph 38

Suggest using the less verbose "for" rather than "in respect of". Also, clarity may be improved if the term "reporting period" rather than "period" were used.

Paragraph 48

This discussion should be transferred to paragraph 7, where a definition of disclosure should be provided. It is extremely poor practice to define terms anywhere other than the definition section if the definition applies generally, as is the case here. It shows a lack of respect for those who have to apply the standard. It is not the sort of behaviour one should reasonably be able to expect of competent professional standard setters.

Paragraph 51

In paragraph 51 it is recognised that a financial report can either be for an individual entity or a group of entities. However, the obligation to present the report, to use the terminology in the [draft] standards is on the entity, which as noted earlier is indeterminate. Since in many jurisdictions a group of entities is not recognised as a legal entity with financial reporting obligations, a different form of words needs to be used. Presumably, for consolidated financial statements, the entity required to prepare the consolidated financial statements is the parent entity – that is, the entity controlling the group. It would also assist readers in understanding the standard, if the fact that the report may relate to either individual entity, a group of entities or both, was made in the introduction and at that stage the usage of the term "entity should" and the like is then appropriately explained.

Paragraphs 66 and 69

Respectively, these paragraphs define the terms current assets and current liabilities. As they are definitions they should either be defined in paragraph 7 with the other definitions, or a cross-reference definition should be included in that paragraph; for example "*current asset*" has the meaning in paragraph 66".

The practice of defining important terms other than in the definitions section is completely unacceptable: it cannot in any way be described as being best practice. Such lack of rigour is not what one expects from competent, professional standard-setters. It also shows a lack of respect for those who are reading the standard.

Paragraph 67

I find this paragraph rather peculiar. While alternative terminology to "non-current assets" may be appropriate, that terminology must be appropriate – it must indicate their nature. For example, the use of "fixed assets" is not appropriate since it is both inaccurate and misleading. My response to that usage is: "My God, I'm glad they have been fixed. I did not even know they were broken. Why were we not told?" It may also be taken as meaning assets to which the legal doctrine of fixtures applies, which would also be inappropriate.

Paragraph 66-68

There should be a cross-reference somewhere in the discussion to the requirements of IFRS 5 limiting when non-current assets can be reclassified as current. The absence of a cross-reference to this important requirement is inexplicable.

Paragraph 78(b)

It is a misuse of the English language and incorrect to suggest that a prepayment is a receivable. At a stretch, if there is an unconditional right of repayment, it could be considered a receivable. In all other cases it is clearly improper to classify prepayments and receivables together since they have significantly different financial properties. Doing so fails to present fairly and would be contrary to the legal requirement in Australia of giving a true and fair view.

Paragraph 79(a)

There seems to be a typographical error: the words in the first line "the number of shares authorised" should be on the next line and be preceded by (i); the subsequent items will need renumbering. This would then be consistent with what is in the current version of IAS 1. Such an obvious error reflects poorly on the Board's quality control procedures and undermines the credibility of the mark-up provide in the exposure draft. One can only wonder how many other incorrect mark-ups have been made.

Paragraph 81

As indicated, two separate statements should only be allowed when presenting a combined statement is contrary to domestic law.

Paragraph 82(b)

It is unclear in this context what is meant by the term "finance costs"; presumably it is wider than "borrowing costs". Also, the correct description is "finance expense" not finance costs. I assume that it is intended that interest on borrowings (other than that capitalised under IAS 23) is a component. Including other "interest" type expenses is problematic; clearly interest recognised under IAS 17 is properly included, however, interest recognised under IAS 37 and 19 cannot properly be characterised as relating to financing the entities activities. To so describe them would be misleading and result in financial statements that fail to present fairly the financial performance of the entity, and also breach legislative requirements such as ones requiring a true and fair view.

Paragraph 90

The heading preceding paragraph 90 seems not to relate to the content of paragraph 90. The heading should be changed or the paragraph moved to immediately before the heading.

Paragraph 92

The paragraph should be deleted; reclassification adjustments should not be permitted (for the reasons given earlier).

Paragraph 97

Since the application of accounting standards is assumed to be subject to materiality, the including of a materiality requirement in paragraph 97 is problematic. I suspect what is meant is something like "material in explaining the entities financial performance". From the examples in paragraph 98 it seems that it is the nature and occurrence of the items rather than their amount that makes them material.

Paragraph 106

If transaction costs relating to transactions with equity holders in their capacity of equity holders are excluded from the calculation of total recognised income and expense, then logically they must be disclosed in the statement of changes in equity. However, none of the line items mentioned in paragraph 106 would include such amount. It cannot be included in 106(c), since that paragraph only relates to disclosure of contributions by and distributions to equity holders in the capacity as equity holders; in IAS 32 and associated basis for conclusions, it is clear that the transaction costs are not themselves transactions with equity holders. This is also clear from paragraph 109 of [draft] IAS 1.

The disclosure of these transaction costs is problematic. For example, in Australia it would be improper to deduct transaction costs incurred in issue or redemption of contribution in presenting the amount of paid up capital, as it would imply there has been an unlawful capital reduction. I suspect similar problems would arise in other jurisdictions. Of course, the most sensible solution would be to include the transaction costs in determining period profit or loss. It is incomprehensible why the transaction costs incurred in paying dividends should be excluded from period profit or loss. Such exclusion fails to hold management accountable for an important aspect of its conduct. Absent an appropriate line item, there is no way to include the so-called "transaction costs". Nothing in paragraphs 106 or 107 allows the introduction of new line items (as distinct from sub-line items); if an express requirement is needed for addition of line items to the statement of financial position and the statement of recognised income and expense, then the rules of interpretation give rise to an inevitable conclusion that additional line items cannot be included.

The examples that accompany the [draft] standard do not include ones showing how transaction costs for the issue or redemption of equity instruments is treated, or how those relating to dividend distributions are treated. Given the obscurity of the requitement and the poor discussion of it, the absence of any example is inexplicable. One is forced to conclude that the Board has no idea of how this absurd requirement is to be implemented.

Paragraph 134

This heading preceding this paragraph is misleading; it should be "Capital management" or "Management of capital".

Paragraph 137(b)

Further discussion on what this paragraph is intended to deal with is needed. The discussion would need to address both those "cumulative" preference shares classified as equity and those classified as liabilities. Presumably the non-recognition is due to an absence of available profits or because payment of the dividend would breach insolvent trading laws. In all other cases, the common terms and conditions of issue of cumulative preference shares would mean that both the definition and recognition criteria for liabilities would have been satisfied.

Amendments to other standards

This section is very difficult to follow. There should be a bold heading for each standard. Readers should not have to engage in an extensive search to work out which standard the proposed amendment relates to. This is not the sort of presentation we are entitled to expect of competent professional standard setters. It can only discourage stakeholders from reviewing the consequential amendments to other standards.