

Heads Up

In This Issue:

- What Would Change?
- What Should Entities Do?
- Appendix

In the staff draft, the FASB takes a fresh look at the manner in which financial information is presented in an entity's statement of financial position, statement of comprehensive income, and statement of cash flows.

About Face

FASB Proposes Sweeping Changes to Financial Statement Presentation

by Mark Crowley and Stephen McKinney, Deloitte & Touche LLP

On July 1, the FASB posted to its Web site a "staff draft" of an exposure draft on financial statement presentation.¹ The staff draft reflects the FASB's tentative decisions through April 2010; however, the work on the project is continuing and the proposal is subject to change before the Board issues an exposure draft for public comment. As part of the project, the Board is also conducting outreach activities focused primarily on "(1) the perceived benefits and costs of the proposals and (2) the implications of the proposals for financial reporting by financial services entities." Although the FASB has not formally requested comments on the staff draft, it welcomes input from interested parties. Before it publishes an exposure draft, the Board will consider whether to revise any of its decisions on the basis of the input it receives. It expects to issue the exposure draft for public comment in early 2011 and a final Accounting Standards Update during the fourth quarter of 2011.

In the staff draft, the FASB takes a fresh look at the manner in which financial information is presented in an entity's statement of financial position, statement of comprehensive income, and statement of cash flows. The intent of the proposal is to create a single model for presenting financial statements that will enhance the usefulness of the information provided in the financial statements and increase comparability and consistency within and across entities. The proposed guidance would apply to most entities.²

Currently, there is limited guidance on how entities should present information in their financial statements. As a result, alternative presentations have developed, creating inconsistencies among similar entities and difficulties in understanding relationships within an entity's financial statements. Accordingly, the [introduction](#) to the staff draft identifies the following "core principles" of financial statement presentation to "enhance the understandability" of an entity's financial information:

- Cohesiveness: "the relationship between items in the financial statements is clear and that an entity's financial statements complement each other as much as possible."
- Disaggregation: "separating resources by the activity in which they are used and by their economic characteristics."

¹ The IASB posted a [similar draft](#) to its Web site.

² The proposed guidance would not apply to the structure and content of general-purpose financial statements prepared by a not-for-profit entity or benefit plan within the scope of the following FASB Accounting Standards Codification (ASC) Topics: ASC 960, *Plan Accounting — Defined Benefit Pension Plans*; ASC 962, *Plan Accounting — Defined Contribution Pension Plans*; and ASC 965, *Plan Accounting — Health and Welfare Benefit Plans*. Further, certain provisions would not apply to nonpublic entities, certain investment companies, common trust funds, variable annuity accounts, or similar funds that meet specific requirements.

Editor’s Note: The Board’s discussion paper issued in November 2008³ proposed a third core principle: the liquidity and financial flexibility objective. That is, an “entity should present information in its financial statements in a manner that helps users to assess the entity’s ability to meet its financial commitments as they become due and to invest in business opportunities.” While the staff draft incorporated most of the concepts proposed in the discussion paper, the Board concluded that an entity should consider liquidity and financial flexibility in the context of the disaggregation principles. Accordingly, this principle was eliminated in the staff draft.

Under the staff draft’s proposed presentation format, there would be common sections and categories, along with similar subtotals, in each of the statements within the financial statements.

What Would Change?

Under the staff draft’s proposed presentation format, there would be common sections and categories, along with similar subtotals, in each of the statements within the financial statements. Financial information would be split between financing activities and business (operating and investing) activities. The “financing section” comprises the assets and liabilities related to an entity’s obtaining or repaying capital and is further separated into debt and equity categories. The “business section” comprises the entity’s assets and liabilities related to its “day-to-day business functioning” (operating category) and those that generate a return (investing category). Certain liabilities directly related to an entity’s operating activities would be presented within an operating finance subcategory of the business section. Income taxes and discontinued operations would be presented separately. The proposed format largely resembles the current presentation in the statement of cash flows under the indirect method.

Within each section or category, financial information would be further disaggregated by function, nature, and measurement basis depending on the level that provides the most relevant and useful information. Function would be based on the use in the entity’s primary activities (e.g., manufacturing or selling), and nature would be based on the “economic characteristics or attributes . . . that do not respond similarly to similar economic events.” The following is a brief summary of the changes:

- *Statement of financial position* — An entity would present assets and liabilities by major activity within operating, investing, and financing categories (the classification would be based on how the entity uses its assets and liabilities and how it views its activities). Because of this, assets and liabilities would be presented together within a section and category (unlike the current presentation, in which all assets are presented together and all liabilities are presented together).

The entity would distinguish short-term assets and liabilities from those that are long-term. The staff draft defines “short-term” as when the asset or liability has a “contractual maturity or . . . expected date of realization or settlement is within one year of the reporting date.” Further, under the staff draft the entity would present assets and liabilities in order of liquidity if that presentation was more relevant for the entity.

- *Statement of comprehensive income* — An entity would present comprehensive income in a single statement and, in keeping with the “cohesiveness” core principle, would be required to classify income and expense items on the statement of comprehensive income consistently with how the entity classifies the assets and liabilities that gave rise to those income and expenses.

Under the proposal, an entity would disaggregate income and expense by function in the statement of comprehensive income. However, if the entity believes that disaggregating income and expenses by nature is useful in assessing “the amount, timing, and uncertainty of future cash flows,” it must also present the by-nature and by-function information in its segment footnote if

³ FASB Discussion Paper, *Preliminary Views on Financial Statement Presentation*; IASB Discussion Paper, *Preliminary Views on Financial Statement Presentation*.

(1) it has more than one reportable segment and (2) provides segment disclosure as required by ASC 280.⁴ If the entity does not meet either of these conditions, the entity may disclose the by-nature information either in the statement of comprehensive income or in the financial statement footnotes.

Editor’s Note: The IASB requires by-nature income and expense information to be presented in note disclosure separately from the entity’s segment disclosure. The IASB’s proposal does not require additional information to be shown in segment disclosures. After completion of this project, the IASB will determine whether segment guidance under IFRSs should more closely align with the FASB’s guidance.

- *Statement of cash flows* — An entity would present main categories of cash receipts and cash payments separately for operating activities (i.e., direct method). The entity would no longer reconcile net income to net operating cash flows by using the indirect method of presentation. In addition, a reconciliation of operating income to net operating cash flows would be required as part of the statement of cash flows.
- *Notes to the financial statements* — Entities would disclose the rationale they used to classify assets and liabilities into categories and sections in the statement of financial position. In addition, they would be required to provide a reconciliation of beginning to ending balances of select assets and liabilities that management deems important to understanding the entity’s financial position. The analysis of changes in assets and liabilities must disclose changes resulting from cash and noncash transactions, accounting allocations (e.g., depreciation), accounting allowances or reserves, and remeasurements (e.g., fair value changes). Other disclosures would include information about remeasurements, operating cycles, cash and investments, and borrowing facilities.

Editor’s Note: For illustrations of how the financial statements of a manufacturing entity and a financial services entity would look under the new guidance, see paragraphs IG28 and IG32 of the staff draft.

The staff draft does not prescribe the order in which an entity would present sections and categories. An entity would be permitted to reorder the sections and categories as long as the order was consistent in each financial statement.

The [Appendix](#) of this *Heads Up* illustrates the presentation format proposed in the staff draft.

What Should Entities Do?

Entities may want to reassess their financial reporting processes to evaluate how they would adhere to these proposed new requirements, particularly to the shift to the direct method of presenting cash flows. This assessment could include an evaluation of the following:

- Information technology systems or other processes used to gather information in preparing the financial statements.
- Internal controls over the financial reporting process.
- Resources within the financial reporting function for implementing necessary changes.

Further, if finalized, the guidance would most likely require entities to disaggregate their financial information and provide disclosures beyond what entities currently present in their financial statements. Thus, entities may need to evaluate (1) the effect of having to provide this additional financial information (e.g., the time it takes to identify, gather, and prepare the financial statements) and (2) how financial statement users analyze the information.

An entity would be permitted to reorder the sections and categories as long as the order was consistent in each financial statement.

⁴ FASB Accounting Standards Codification Topic 280, *Segment Reporting*.

Appendix — Illustration of Proposed Format of Financial Statements

The table below, reprinted from the [introduction](#) to the staff draft, outlines the presentation format under the proposed guidance.

Statement of Financial Position	Statement of Comprehensive Income	Statement of Cash Flows
Business section	Business section	Business section
Operating category	Operating category	Operating category
Operating finance subcategory	Operating finance subcategory	
Investing category	Investing category	Investing category
Financing section	Financing section	Financing section
Debt category	Debt category	
Equity category		
	Multi-category transaction section	Multi-category transaction section
Income tax section	Income tax section	Income tax section
Discontinued operation section	Discontinued operation section , net of tax	Discontinued operation section
	Other comprehensive income , net of tax	

Subscriptions

If you wish to receive *Heads Up* and other accounting publications issued by Deloitte's Accounting Standards and Communications Group, please [register](http://www.deloitte.com/us/subscriptions) at www.deloitte.com/us/subscriptions.

Dbriefs for Financial Executives

We invite you to participate in *Dbriefs*, Deloitte's webcast series that delivers practical strategies you need to stay on top of important issues. Gain access to valuable ideas and critical information from webcasts in the "Financial Executives" series on the following topics:

- Corporate governance.
- Financial reporting.
- Risk intelligence.
- Driving enterprise value.
- Financial reporting for taxes.
- Transactions and business events.

Dbriefs also provides a convenient and flexible way to earn CPE credit — right at your desk. Join *Dbriefs* to receive notifications about future webcasts at www.deloitte.com/us/dbriefs.

Registration is available for this upcoming *Dbriefs* webcast. Use the link below to register:

- [Tax Accounting: Mid-Year Update](#) (July 12, 2 p.m. (EDT)).

Technical Library: The Deloitte Accounting Research Tool

Deloitte makes available, on a subscription basis, access to its online library of accounting and financial disclosure literature. Called Technical Library: The Deloitte Accounting Research Tool, the library includes material from the FASB, the EITF, the AICPA, the PCAOB, the IASB, and the SEC, in addition to Deloitte's own accounting and SEC manuals and other interpretive accounting and SEC guidance.

Updated every business day, Technical Library has an intuitive design and navigation system that, together with its powerful search features, enable users to quickly locate information anytime, from any computer. In addition, Technical Library subscribers receive *Technically Speaking*, the weekly publication that highlights recent additions to the library.

For more information, including subscription details and an online demonstration, visit www.deloitte.com/us/techlibrary.

Heads Up is prepared by the National Office Accounting Standards and Communications Group of Deloitte as developments warrant. This publication contains general information only and Deloitte is not, by means of this publication, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. This publication is not a substitute for such professional advice or services, nor should it be used as a basis for any decision or action that may affect your business. Before making any decision or taking any action that may affect your business, you should consult a qualified professional advisor.

Deloitte shall not be responsible for any loss sustained by any person who relies on this publication.

As used in this document, "Deloitte" means Deloitte & Touche LLP, a subsidiary of Deloitte LLP. Please see deloitte.com/us/about for a detailed description of the legal structure of Deloitte LLP and its subsidiaries.

Copyright © 2010 Deloitte Development LLC. All rights reserved.