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Cc Ms Kim Petrone, Senior Project Manager, Financial Accounting Standards Board

Financial Statement Presentation

Dear Ms Gomez

As you know we are keen supporters of your project to improve financial statement presentation. Lack of disclosure, inappropriate aggregation of items under meaningless titles such as “other”, and a lack of comparability between similar entities are all problems that limit users’ ability to extract full value from the financial information provided by companies, and we are keen to do all we can to assist you in producing GAAP that reduces these problems.

In that context, and in the context of all the work that has already been done in this area, this Discussion Paper fell short of our expectations.

Problems with the Discussion Paper
There are a number of significant gaps in the Discussion Paper (DP).

1. It does not clearly identify many of the specific issues that users have with performance reporting. It does not assess the advantages and disadvantages of addressing these issues within either the existing, or proposed, reporting framework.

2. It does not refer to, or appear to build on, any of the work done previously (for example: Steve Cooper’s UBS research note “Financial Reporting for Investors” (UBS Investment Research, April 2007), the July 2007 CFA CBRM paper, the November 2006 PAAINE discussion document, or even the IASB’s own earlier “matrix” proposals.

3. It does not refer to any of the work/discussions of the Joint International Group set up in 2004 to support the project.

4. It does not refer to the proposals for a principles-based disclosure standard developed by the Investors Technical Advisory Committee, outlined in their letter to the FASB in December 2007.

5. The proposals it puts forward appear to ignore our frequent requests for a Net Debt reconciliation, including the detailed presentation that CRUF members gave to the Joint Boards in June 2008.

6. The DP appears to suggest that anything which does not fall into one of the proposed categories should be classified as "Operating". This approach is the exact opposite of what many users would want to see done in such circumstances.

7. The DP discusses a balance sheet to balance sheet reconciliation but does not include it as a core recommendation. A number of CRUF participants view this as a serious omission.

Comprehensive Income is not decision-useful
Whilst the components that make up comprehensive income are useful (and in many cases we would like to see more information on items that currently get "lost" in Other Comprehensive Income), it is disappointing to see that the DP persists in promoting the merits of Comprehensive Income per se in the face of investor indifference.

Comprehensive income has been reported under US GAAP for a number of years. If users found Comprehensive Income useful as a concept they would incorporate it in their valuation multiples or other analysis of companies. The fact that they do not do so anywhere in the world, and that companies do not mention it in their discussions with analysts, should be taken as reliable evidence that it is not a decision-useful piece of information in itself – it is merely a final total.

The problems users face are clear
The main problems that users face when attempting to analyse businesses are clear and often relate to the "flow" statements in terms of their ability to convey information about the performance of the business.

In particular, users struggle with the following issues in many current financial statements:

1. The P&L does not differentiate between items that are simply the result of changes in balance sheet fair values, and those that relate to the operational performance of the business (what we have described on a number of occasions as "items with a multiple of one" compared to items where investors would value them using a multiple greater than one).

2. The cashflow statement is frequently difficult to reconcile to the other two statements, and often aggregates items in a way which is unhelpful to users.

3. Many users want to be able to identify the core operating activities of the business and the performance relating to that. The current financial statements do little to facilitate this analysis.

4. Items with very different economic characteristics are aggregated more often than we would like, either under the heading of "other" or by netting off items which would more helpfully be shown gross, impeding our analysis.

5. Mergers and acquisitions have a significant impact on the financial statements of companies and make analysing the subsequent operating performance of the business very difficult (particularly when such events occur frequently).

6. The way in which businesses hedge their exposure to economic risks such as interest rates and forex is very difficult to assess using published accounts.

7. Understanding the link between tax payments and the tax charge in the P&L is often impossible.

8. Pension accounting continues to cause significant difficulties.

9. Understanding how events have been reflected in the three statements and how those statements link up is often difficult, sometime impossible.

The DP misses a number of opportunities
The DP appears to help with some aspects of several of these problems (particularly by the proposed use of reconciliations), and does acknowledge user demand for more information about items with very different economic characteristics to facilitate better forecasting, but it does nothing to tackle M&A impacts, how businesses show the effects of hedging, or tax. We acknowledge that all these issues are very difficult but unless we have a go at grappling with them we fear that they will never be resolved (or at least clearly understood as beyond the capacity of the current framework and therefore off the agenda). The DP provided an ideal opportunity to do just that.

The balance sheet focus in standard-setting
We are concerned that the structure and approach of the DP demonstrates yet again that the balance sheet is the primary focus for staff when developing standards. We would like to take this opportunity to reiterate that, while the balance sheet is a very important statement for users, the primary focus of communication with management is about business activity, and therefore the income statement and cash flow statement that describe aspects of this are equally important to our understanding of these activities. Standards should be developed with this in mind.

Evidence-based standard setting
Change is not cost-free for users, nor is the process of participating in a consultation exercise such as this one. There is little in the DP to suggest that the Boards have considered this issue in sufficient depth, and combined with the other issues that we are being asked to comment on at the same time, debating Board proposals represents a significant potential drain on our collective resources when these resources are already being stretched by unusually turbulent markets.

Many investment techniques rely upon being able to compare companies with peers in the sector and/or the wider market, either in a particular period or across time (potentially decades). Given this fact, any change in the information that is presented – particularly if it results in the disappearance of line items, subtotals, or totals – is potentially costly to users and needs to have clear benefits for users to outweigh the negative impacts of change.

We would prefer to see greater evidence that proposed changes (in this DP and elsewhere) are being put forward in response to user demand, with clear analysis of the potential (practical) benefits to be gained.

Overall conclusion
Although this Discussion Paper might be judged a success in that is has already generated a lot of discussion, it does not move the debate forward to the extent that we had hoped.

We address the specific questions in the attached appendix and also include a number of suggestions of our own with regards to an improved cashflow, better segmental disclosures, the treatment of discontinued operations, associates and JVs, and disclosures regarding tax and balance sheet changes.

We believe there is much that can be done to improve performance reporting and to enhance communications between companies and the users of their accounts without needing to adopt some of the more radical proposals in this Discussion Paper. We would like to see rapid progress with the improvements where there is already strong agreement among users and preparers about current flaws in financial statement presentation.

As always we will support both Boards in their efforts to bring about improvements in this area but we would urge a pragmatic and targeted approach which delivers tangible results within a reasonably short timeframe.

About the Corporate Reporting Users' Forum (CRUF)

The CRUF came together in 2005 as a discussion forum to help its participants in their approach to the debate on current and future corporate reporting requirements. In particular, participants are keen to have a fuller input into the deliberations of accounting standard setters such as the IASB. CRUF participants come from all around the world, including individuals from both buy- and sell-side institutions, and from both equity and fixed income markets.

The CRUF is a discussion forum. Different individuals take leadership in discussions on different topics and in the initial drafting of representations. It does not seek to achieve consensus views, though at times some or all of its participants will agree to make joint representations to standard setters or to the media. It would not be correct to assume that those individuals who do not participate in a given initiative disagree with that initiative.

We sign this letter in our individual capacity as participants of the Corporate Reporting Users' Forum (www.CRUF.com) and not as representatives of our respective organizations. The views expressed are those of individual CRUF participants and do not necessarily reflect the views of the respective organizations where we are employed.

The participants in the Forum that have specifically endorsed this response are listed below. Of those who have endorsed this response, 57% are from Europe, 31% from North America, 8% from Australasia and 4% from the Indian subcontinent.

Peter Elwin	Head of Accounting & Valuation Research	Cazenove Equities
Nick Anderson	Head of Research	Insight Investment
Norbert Barth	Executive Director, Equity Research	WestLB AG
Winfried Becker	Senior Vice President Equity Research Engineering/ Industrials	Oppenheim Research GmbH
Terri Campbell, CFA		
Chris Cornett, CPA	Research Analyst	
Anthony Corr	Principal, Executive Director	Continuum Capital
Zhen Deng, PhD		

Ralf Frank	Managing Director	DVFA
Susannah Haan		
Roger Hirst	Head of London Research	Main First Bank AG
John Kattar, CFA	Chief Investment Officer	Eastern Bank Investment Advisors
Paul Lee	Director	Hermes Investment Management Ltd
Eric P. Linder, CFA	CEO	Savanet, LLC
Scott Nammacher	Managing Director	Empire Valuation Consultants, LLC
Jeremy Perler, CFA, CPA		
Petra Pflaum	Director, Senior Fund Manager Equities German & European Small & Mid Caps	DWS Investment GmbH
Christopher Pidcock	Managing Director, Equity Strategist	Goldman Sachs JBWere
Peter Reilly	Head of Capital Goods, European Equity Research	Deutsche Bank
Scott Russian, CFA		
Rajesh Sehgal, CFA	Sr. Executive Director/Sr. Vice President, Emerging Markets Group	Templeton
Richard Singleton		
Crispin Southgate		Institutional Investment Advisors Limited
Deborah Taylor	Research Analyst, Accounting & Valuation	Citigroup Investment Research
Marion Scherzinger ACCA	Financial Analyst	
Jed Wrigley	Portfolio Manager Director – Accounting and Valuations	Fidelity Investments

Appendix 1 - CRUF response to FSP Discussion Paper questions

1.0 Objectives of financial statement presentation

1.1. Cohesiveness

The discussion paper rightly acknowledges user concerns that the many alternative formats available to present financial information make it difficult to compare financial data between entities. However, the cohesiveness concept goes no further than providing a consistent framework for presenting financial information and does not necessarily result in consistency in the way that similar financial items are presented by different entities.

Cohesiveness should not be confused with consistency of outcome, and the latter is more important to users than the former. The proposals placed too much emphasis on the alignment of line items across the financial statements. While cohesiveness may result in a degree of presentational elegance, it does not result in a format that is more helpful to users when making investment decisions.

We have significant concerns that the required alignment across the financial statements will fail to best reflect the economic reality of the reporting entity.

The treatment of defined benefit (DB) pension assets / liabilities illustrates some of the potential difficulties with this approach. If an entity chooses to present net plan assets / liabilities in the operating category of the statement of financial position, all related profit & loss items would also be presented as operating. Many users feel that this treatment distorts the calculation of operating profit as well as key user metrics such as operating margin and return on assets. A few CRUF participants agree with the view expressed by the CFA Institute that pension liabilities are operating and so would not choose pensions as an example of the flaws in the cohesiveness concept.

Users who believe that the economic reality of a DB pension scheme would be best portrayed by presenting the net liability in financing and the current service cost as operating fear that a rigid application of the cohesiveness approach would not adequately reflect the economic reality of a pension liability. (As an aside, we understand that the IASB's pensions working group has already discussed this particular issue at some length and we are encouraged by the direction these discussions appear to be taking).

We are also concerned by the treatment of lease obligations as operating liabilities suggested by the ToolCo example. Economically, the underlying impact of financing an asset from debt finance and lease finance is identical and users want this reflected in the financial statements (as it is at present).

It would also be helpful to understand in more detail the Boards' current thinking on how hedging positions should be shown on the balance sheet and in the other statements.

Overall, many of us are not convinced that the cohesiveness principle will be helpful in practice.

1.2. Disaggregation

The discussion paper's objective for disaggregation is to ensure that data is disaggregated 'in a manner that makes it useful in assessing the amount, timing and uncertainty of cashflows'. We

welcome such an objective but question whether using balance sheet classification as a driver for cashflow statement and income statement disaggregation satisfies this objective, since flow statement data requirements are not always aligned with balance sheet items. In particular we note that:

- Certain balance sheet items (such as pensions and leasing) consist of one or two balance sheet items but may have many more elements to them from a 'flow perspective' and therefore require further disaggregation in the flow statements to distinguish between operational and financing flows.

- Users analyse the income statement and cashflow statement to understand the drivers for revenues and costs, and how cash resources are utilized by the business. If, as the discussion paper proposes, information is disaggregated based on asset and liability classification and measurement type, the flow statement data may not be disaggregated in a manner which helps assess the amount, timing and uncertainty of cashflows.

The proposed method for disaggregation results in a large amount of additional data on the face of the income statement and cashflow statement. Some CRUF participants are concerned about the risk of information overload in the primary statements given such an approach but others are more relaxed (and a minority have indicated that they would find such an approach helpful).

The key area where additional disaggregation of data is required by users is at a business segment level. Whilst segmental disclosures are outside the scope of the discussion paper, we feel that the discussion paper misses this key point since it proposes increasing the level of disaggregation on a consolidated rather than segment basis.

We refer you to our letter dated 16th May 2006 for more details regarding our requirements from Segmental Reporting (http://www.cruf.co.uk/ED8_comment_letter.pdf), as well as additional comments in sections 7.0 and 8.0 of this Appendix.

1.3. Liquidity and financial flexibility

We agree with the Discussion Paper's assertion that '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' (refer to our answer to Question 22 in Section 22 of this Appendix as well).

1.4. Linkage – a better concept than cohesiveness

To reiterate the point made earlier, comparability between similar companies and between transactions with similar underlying economics is an essential characteristic that users require from financial statements, but we are concerned that the balance sheet approach underlying the application of both the cohesiveness and the disaggregation concepts will not result in useful information for users if it is rigidly followed through the other two statements.

What we need is to be able to trace the impact of a particular transaction (or class of transactions) across the three statements, and to see how they link together in that respect.

This is best done in separate note disclosures covering each of the key balance sheet lines, reconciling the opening and closing positions by identifying how the changes have been reflected in

individual lines on the other two statements. It would also be helpful to see this information summarised in a statement reconciling the opening and closing balance sheets.

We agree with the approach suggested by the Investors Technical Advisory Committee in their letter to the FASB dated 11th December 2007 regarding a principles-based disclosure standard (http://www.fasb.org/investors_technical_advisory_committee/ITACDisclosureProposal.pdf), and believe that their proposals would provide a suitable framework for the disclosures we require. We urge the Boards to include these ideas within the overall scope of this project, even if a separate standard is required.

2.0 Separation of business activities from finance activities

We support the proposal to separate business activities from financial activities, but we have a number of concerns with the specific application of this approach and some suggestions for improvements that were not considered in the Discussion Paper (see answers to later questions and the additional material in Appendix 2)

In particular, we are concerned by the introduction of an "Investing" category. The term "investing" is already widely used in financial accounting. We believe that, by introducing a new definition for the term, the Board may inadvertently create confusion and some CRUF participants would prefer not to have this category at all. Instead, CRUF participants would prefer to see a category of 'Unconsolidated Business Activities' presented within the business section of the financial statements (see Section 9.2 for more detail). This might also provide a useful place to put pension liabilities given the difficulties in clearly differentiating between their operating and financing characteristics, and could provide information in a way which satisfied those who regard the pension liability as operating whilst providing clear disclosures for those who don't.

We also think that restricting the assets and liabilities that can be classified as "Financing" to those that qualify as financial assets or liabilities is too limited. We would prefer this section of the balance sheet to contain all the elements that we would consider to be "Net Debt" (see Appendix 2, section 5 for more details).

3.0 Separation of equity

We are used to seeing equity identified separately from other sources of capital and we support the DP's proposal to continue this approach.

4.0 Discontinued Operations

The CRUF participants have discussed various options for the presentation of discontinued operations at the consolidated level.

Whilst some would present discontinued operations as a separate item in group accounts, others believe that current accounting for, and presentation of, discontinued operations does not adequately reflect the operational performance of the business for the period.

For that reason, these CRUF participants believe that discontinued operations should remain fully consolidated until they are actually disposed of, as management still has control of the operations and an obligation to deliver profits and cash flow.

There is less debate amongst CRUF participants about the treatment of discontinued operations at a segmental level. Discontinued operations should be included in the segmental analysis, which we believe could best be presented as shown in Appendix 2, section 2.

This additional disclosure would be necessary to allow investors to understand the impact of sale on each of the categories within the main financial statements. We assume that if management are intending to discontinue an operation, such disclosure should not require extra costs for preparers as it will be readily available.

Should the IASB decide not to adopt this proposal and to continue with the current approach (consolidation at the level of a single line), we would still recommend that the above disclosure is given in the notes so that users can reconstruct the operations, allowing them to make better year on year comparisons.

5.0 Through the eyes of management - comply or explain

Although we acknowledge the benefits of encouraging managements to present the financial information in the way which they believe best explains their business and its activities in the period, we are concerned that applying this principle unchecked will result in a serious deterioration in the comparability of information between similar companies.

Many investment techniques rely upon being able to compare companies with peers in the sector and/or the wider market, either in a particular period or across time. Some time-series comparisons cover many years and so any fundamental change in the way that financial data is presented will potentially have a negative impact on such efforts. Given this fact, any changes in the information that is presented – particularly if it results in the disappearance of line items, subtotals, or totals – needs to have clear benefits for users to outweigh the negative impacts of change.

We already face a proliferation of pro-forma data provided by companies, based upon an unhelpfully wide range of methodologies. At present it is usually possible to re-engineer this data to be comparable by relating it back to the underlying GAAP data, but if the GAAP data itself was even more divergent than it currently is (because each company had shifted towards its current pro-forma stance) this re-engineering would be much more difficult, if not impossible.

We welcome the suggestion that management's classification of items should be regarded as an accounting policy, subject to all the usual restrictions if a change is made, but we think that further constraints are required.

We believe there are a number of possible constraints that the Boards could explore, but we suggest the following as alternatives worth considering:

- Requiring particular presentational approaches in some standards (for example, the various line items that arise from pensions accounting could be specified to be consistently categorized in the same manner by all companies).

- Standard line items could be classified and required by the final FSP Standard itself in detailed ToolCo examples.

- More detailed principles for classifying items could be developed and set out within the eventual FSP Standard.

- Requiring management to explain the business model and how the treatment of items in particular businesses is in line with that model.

With either of the first two approaches it would be possible to include a management "comply or explain" override, with clear auditor responsibility for vetting this particular accounting policy and the reasons for overriding the GAAP requirements, and a requirement that the approach should be followed consistently in all company announcements.

Whilst we believe further constraints are necessary, it should also be possible to create a hierarchy whereby key constraints are mandatory but are specified at a high level, leaving management greater flexibility within each area to classify things in accordance with the business model.

6.0 Balance sheet format

The performance of the operating assets is a key area of focus for users. Given this, we welcome the intention within the discussion paper to make it easier for users to calculate key financial ratios, by changing the balance sheet format to clearly identify operating assets and liabilities. That said many of us do not regard this change as a high priority.

7.0 Segmental classification of assets and liabilities

The concept of classifying assets and liabilities at a segmental level, and thus allowing different approaches in different segments, makes sense given that (in a minority of businesses) business segments are sometimes very different from each other. Car manufacturers are a case in point, with a manufacturing segment and a segment devoted to providing financial assistance to customers.

However, we are very concerned about how this might be applied in practice. For the vast majority of businesses their operating segments may be doing different things but the assets and liabilities employed within those segments are fundamentally similar, and we would expect this to be reflected in the accounting.

Providing additional information in the MD&A or pro-forma disclosures may prove to be a better solution than applying different accounting treatments in different segments, providing the link between the MD&A analysis and the figures in the financial statements is made clearer than is often the case at present.

As noted in Section 5 above, we would prefer to see strong constraints applied if a "business model" ("through the eyes of management") approach was to be adopted.

8.0 Segmental disclosure requirements

The purpose of segmental reporting should be to enable users to identify the performance of the components of a business. It should help users build forecasts of entity cash flows and facilitate sum-of-parts type valuations of businesses.

As you know, a number of us were disappointed with the disclosure regime introduced in IFRS 8 and our letter dated 16 May 2006 provides more detail regarding our requirements (http://www.cruf.co.uk/ED8_comment_letter.pdf).

The key points that we asked for in our 2006 letter were for entities to disclose sufficient information to enable users to identify segment performance, cash flow and return on capital. We would like to see more detailed segments disclosed in addition to those reported on to the chief operating decision maker if a failure to do so would materially hinder users' ability to understand and to identify the performance of the components of a business.

Of particular concern to us is that, unlike IAS 14, IFRS 8 does not include a mandatory requirement to analyse liabilities by segment. Segment return on capital is frequently used in the analysis of businesses and to analyse only gross assets by segment fails to provide sufficient information to derive meaningful returns. Clearly analysing liabilities by segment is generally restricted to what might be termed 'operating liabilities', but this is exactly what is required to generate segment return on capital given that the performance metric analysed by segment is generally a pre-interest operating income measure. Given this, we are particularly keen to see more disclosures of operating assets and liabilities at a segment level.

9.0 Defining "Business", "Operating" and "Investing"

9.1. "Operating" should not be the default category

Many of us believe that using the operating category as the default section for items that do not meet the criteria for either investing or financing (as suggested in paragraph 2.35 of the DP) is completely at odds with how users analyse businesses and will not enhance the usefulness of the financial statements, but some of us take the opposite view.

9.2. "Investing" - rename as "Unconsolidated Business Activities"

We believe the term 'investing' is potentially confusing given its wide range of uses. We would prefer to see this section of the balance sheet referred to as "Unconsolidated Business Activities".

We would prefer strong guidelines regarding what could be classified under this heading to ensure comparability between companies.

Users would find it helpful to have Equity Method Accounted Entities included within this section of the balance sheet (i.e. those entities that are currently included via single line consolidation in the main statements).

We believe that any entity which is not consolidated (fully or proportionately) should not be presented within the Operating category, although inclusion within the investing category still keeps them within the wider definition of a "Business" asset. This seems reasonable to us as the exercise of influence implies that there is a business reason for the investment that goes beyond a purely financial interest.

Users make extensive use of ratios when comparing and contrasting the valuation of different operating entities. The most common multiples used at the enterprise (or operating) level are EV/Sales, EV/EBIT, EV/NOPAT and EV/EBITDA, although industry specific metrics are also widely used.

We believe that a basic objective of financial statement presentation should be to ensure users are provided with useful information with minimum adjustments required to enable them to make these comparisons.

In this context it is useful to think of the Operating category as the “enterprise” that the analyst is comparing using these multiples. Because equity accounted entities are consolidated at the net income level they do not contribute towards the denominators of the relevant multiples and should therefore be excluded from the enterprise value. Thus users will deduct the value of these equity accounted entities from the market capital of the company when calculating these ratios and so clearly segregating them as non-operating business assets will assist users in this process.

There may also be merit in changing the way that investment companies account for their controlled investments, so that portfolio companies are not consolidated by the investment company (as is currently the case under US GAAP).

Our suggestions for additional disclosures and the appropriate accounting treatment for these entities are discussed in more detail in Appendix 2, section 3.

For similar reasons this section could provide an appropriate place to put pensions liabilities. Some analysts exclude pension deficits and surpluses from their definition of "Net Debt" but do wish to include them as separate components of the Enterprise Value. Like equity accounted investments, pensions are consolidated as a single line under current GAAP, and so this treatment would maintain that consistency. Including pensions in this section would also avoid some of the more difficult issues that arise when one tries to differentiate between the operating and financial characteristics that many of us identify within pensions.

Appendix 2, sections 3.2 and 7 provide more details regarding our requirements for pensions accounting.

10.0 Financing

As noted in answer to Question 2, we think that restricting the assets and liabilities that can be classified as “Financing” to those that qualify as financial assets or liabilities is too limited, but we acknowledge that this view is not universally held. We would prefer this section of the balance sheet to contain all the elements that we would consider to be “Net Debt”.

Using this approach would have a number of benefits for users:

- It would provide companies and users with a simple way to communicate about Net Debt and would provide a clear benchmark for any pro-forma approaches that companies wished to follow (in contrast to the current free-for-all).

- It would link in to the cashflow statement (if that is formatted as we suggest – see answers to Question 19 and our proposed format in Appendix 3).

We have outlined a definition of Net Debt in Appendix 2, section 4.

This definition follows on from our presentation to the IASB on 10 June 2008, when we explained to the Board what is wrong with IAS 7 and current cashflow disclosure, why reconciliation of cashflow to movements in net debt is critical to understanding the business, and key information that we would like to see disclosed. Some of this information used to be disclosed under UK GAAP e.g. acquired debt, inception of finance leases, proceeds from equity issues and the forex translation impact on debt and cash.

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11.0 Classifying assets and liabilities into short-term and long-term

We agree with the Discussion Paper's suggestion that assets and liabilities should be classified according to their lives since (we assume) this is in line with the approach currently used by most companies.

Classification by liquidity as a second alternative also seems sensible.

12.0 Cash equivalents

Whilst users do not typically differentiate between cash and cash equivalents in their valuations, we do accept that a strict definition of cash is important, especially in the current economic climate.

However, we believe that this further emphasises the importance of a Net Debt analysis for corporations which needs a detailed reconciliation. It is unhelpful if net cash flow, a potentially valuable number for users, can be distorted by redemptions or issuance of debt or purchase of money market funds despite the fact that these transactions are all arguably value neutral to shareholders.

13.0 Grouping different measurement bases

Classification of balance sheet items by measurement category will be useful in enabling analysts to compare like with like for balance sheet items and will also assist us in identifying when a change in the value from one period to the next is more likely to relate to external market changes, changes in management assumptions, or internal company activity.

14.0 A single Statement of Comprehensive Income

Given that the Discussion Paper has acknowledged the clear user demand for a Net Income subtotal, and that the proposed format makes this important subtotal easy to identify, we are not concerned by the existence of a page break or not.

We would agree with the CFA Institute that the OCI statement currently has no coherent conceptual basis and that including items in it often has more to do with compromises during the standard setting process rather than any clear rationale but we wish to see items with a "multiple of one" kept separate from the operating aspects of a company's performance so it is likely that Other Comprehensive Income will remain a requirement.

That said, we reiterate our opening comments about the fact that Comprehensive Income is not a decision-useful figure in itself, it is merely the final total (similar to the applause at the end of a concert – informative, but not what people come to see).

15.0 Categorising Other Comprehensive Income

It is important for users to be able to understand the items that are currently included within OCI and how they link to other entries elsewhere in the financial accounts (see our earlier comments about the use of labels such as "other" and our comments regarding forex in Section 18 below). We see benefits from indicating the categories to which items shown in OCI relate but clear disclosure and explanation in the notes is likely to be more useful.

We would expect the balance sheet reconciliations in individual notes to the accounts to provide this information (see our comments in paragraph 1.4 above).

16.0 Disaggregating P&L items by nature or function

The key focus for analysts when forecasting operating expenditure is to understand the driver for the costs e.g. are they fixed or variable. Therefore any presentational requirements should be aligned with helping analysts understand this, rather than just providing more disaggregated data.

Presentation of costs by nature is more useful for determining fixed or variable costs and therefore it is essential that costs are either presented by nature or separately disclosed as such.

Presentation of costs by function does provide some information in understanding how resources are allocated. However, there is currently large variation on how companies decide what to include within such functional categories as 'cost of sales' and 'administrative costs', limiting the usefulness of this data unless it is supplemented by providing analysis of costs 'by nature'.

17.0 Taxation

Whilst we believe users would benefit from some allocation of tax as this would help in the valuation process, we accept that tax-optimization in companies works across business segments and is organized at the group level. This does mean that preparers are unlikely to be able to allocate taxes to sub-categories in a meaningful and reliable way.

It is far more important to give sufficient information with respect to the real cash tax paid in the reporting period and tax assets arising from items such as carried forward losses (including the assumptions in their valuation as tax-assets). We would find it easier to forecast tax if companies disclosed a split of taxes paid (or charged, or both) and tax assets according to tax-jurisdictions (countries).

Notwithstanding the above, we require tax information relating to any items that are “unusual”, including but not limited to: impairments, remeasurements and restructuring provisions. Users will often adjust reported earnings for these balances and therefore need to know the tax impact of these adjustments. It is worth noting that these often have tax treatments that are different to normal transactions in terms of deductibility or occur in jurisdictions where utilisation of tax losses generated might be unlikely in a realistic time frame.

18.0 FX gains and losses

Paragraph 3.63 proposes that an entity should present foreign currency transaction gains and losses, including the components of any net gain or loss arising on remeasurement into its functional currency, in the same section and category as the assets and liabilities that gave rise to the gains or losses. We are not convinced that doing so will solve our problems.

Decision-useful information about the impact of foreign currency transactions and exposures will often cut across asset and liability categories. Paragraphs 3.63 to 3.69 also touch on, but do not effectively deal with, the problem that these impacts are reflected partly in profit and loss or net income and partly in other comprehensive income (as noted in Section 15 above).

Effective analysis of what did happen (as a result of transaction, translation and economic exposures to changing exchange rates) - to inform estimates of what might happen in the future - is often not possible because information regarding FX gains and losses is too compressed.

The proposal in paragraph 3.63 seems to be informed by pursuit of the cohesiveness principle. Where a same section or category disclosure of FX gains and losses is appropriate, it would be decision useful – for example, gains and losses on foreign currency debt. However, disclosure would still be required to help “unpack” otherwise compressed information.

An example of such disclosure within a category would be distinguishing, in a disclosed analysis of net debt, between (1) FX derivative transactions that relate to swapping the effective currency of borrowing from (2) FX derivative transactions aimed at hedging the currency (transaction) exposure of receivables and payables.

But where FX gains and losses cut across categories – for example, where a foreign currency operating asset or investment is hedged with foreign currency borrowing or an FX derivative – it is the linkage between those elements of different categories that is important. In our view, this can only be addressed by effective disclosure requirements rather than adjustments to the presentation of the main financial statements.

19.0 Cashflow statement

19.1. Direct vs indirect-direct vs indirect

There is widespread user dissatisfaction with the current cashflow statement to the point where the disclosed subtotals are rarely used on the basis that they cannot be trusted without detailed investigation and adjustment. But it is far from clear that simply switching to a direct cashflow approach would solve these problems.

That said, where companies are already required to present a direct cashflow, there is strong user support for this to continue without any weakening of this requirement.

Investors require indirect cashflow information as well as direct. In many cases users base their forecasts of operating cashflow on their own indirect reconciliation of EBITDA to operating cashflow, and they require a high quality indirect reconciliation from the company to assist with this. In many cases the quality of what is currently available is poor but eliminating it entirely would make things worse.

The key benefit from a high quality indirect reconciliation of operating profit to operating cashflow is that the working capital flows are made clear in the way that the majority of managements and users like to discuss them i.e. in terms of changes in receivables, inventory etc.

Where companies already provide a direct format cashflow it is clear that users appreciate being able to see “Cash received from customers” and having a clearly derived Operating Cashflow figure, but also take account of the information provided in the indirect reconciliation if it is a) provided, and b) is of sufficient quality.

It is also apparent that the majority of companies actually calculate the direct operating cashflows indirectly and then simply present them as a direct cashflow. If this “indirect-direct” approach is what the DP is proposing it would be helpful to require companies to explain the methodology they apply when calculating the synthetic direct cashflows. Simply presenting cashflow information in a direct format if it has been produced indirectly without explaining this is actively misleading.

19.2. User opinion is divided

Obviously, if an indirect approach is used the information can either be presented in a direct format (as the DP does) accompanied by an indirect reconciliation of operating income to operating cashflow, or by presenting the indirect reconciliation as the starting point, with accompanying direct cashflow information.

Appendix 3 illustrates the latter methodology, on the basis that for many users (particularly in Europe) this matches their current approach most closely, but for many users (particularly in Australia and the US) the "indirect-direct" format would be preferable, provided a high-quality indirect reconciliation was also provided along the lines suggested in Appendix 3.

In particular, we require:

- Disclosure of Cash Received From Customers – on the face of the cashflow statement and within the receivables note. If the figure cannot be extracted direct from the accounting system then the company should disclose how it has been estimated with a reconciliation in a note.
- An indirect reconciliation to calculate Operating Cashflow (pre-tax) that starts with Profits from Operations not Net Income.
- Direct cashflows for all items outside Operating Cashflow including pension deficit reduction payments, capital lease payments, and any cashflows relating to exceptional items.
- A reconciliation of changes in Net Debt identifying the impact of cashflows, M&A, non-cash changes, and FX.
- Details of hedging so that the company's exposure to changes in interest rates, FX and other external risks can be clearly understood, in cashflow terms as well as P&L and OCI.
- Separate identification of cashflows relating to discontinued operations, including prior year numbers.

19.3. Net debt reconciliation

As noted in our comments in Section 12 above, it makes sense to differentiate between cash and cash equivalents on the balance sheet, but it is essential that companies are required to provide an analysis of their Net Debt position as well, and a detailed reconciliation to the Statement of Cashflows. This will ensure that users' assessment of net cash flow is not distorted by redemptions or issuance of debt or purchase of money market funds (since these transactions are all value neutral to shareholders).

20.0 Costs of a direct cashflow approach

It is disappointing that the DP does not discuss the potential costs of implementing such a radical change (outside Australia) in more detail, and show how these will be justified by the benefits (as identified by users). Better questions are required and one would have hoped to see evidence that they had been asked during the production of the DP as well (for example, Question 19(a) asks if a direct-method cashflow would produce decision-useful information, but almost any information provided by a company (perhaps with the exception of Comprehensive Income) has the potential to be decision-useful).

We understand that currently in Australia the direct cash flow statements are actually produced using an indirect process. Given the extensive feedback that the Boards have had on cash flow formats, it is disappointing that the Discussion Paper does not clarify whether the Boards are proposing that companies extract cashflow information directly from their underlying records, or are in fact proposing a cashflow produced indirectly but formatted to appear as if the information was directly extracted from the underlying accounting systems.

As noted in section 19 above, users require information about working capital movements that is lost if only a direct cashflow is shown. Such a change would also require analysts currently using the indirect method to have to re-write their spreadsheets – a time-consuming and therefore costly exercise which could be avoided if the indirect reconciliation continued to be provided.

21.0 Basket transactions

Since the definition of a basket transaction is both broad and vague, and since the Discussion Paper fails to clarify precisely how such transactions are currently accounted for and how this might change, it is difficult to feel confident that we have understood all the implications of the points raised in the Discussion Paper.

That said, we have not encountered any significant problems with transactions such as the disposal of a subsidiary that cannot be resolved by better note disclosure, so we do not see a need for any fundamental change in the accounting per se.

We do not support the suggestion that the effects should be allocated to different parts of a particular statement, since the level of arbitrary judgement involved would render the allocation meaningless and make the resulting information less informative than before.

To take the example of disposal of a subsidiary, the information that users require to assist their analysis is broadly as follows:

- Sale proceeds and information on how any P&L gain or loss was calculated
- Information on the assets and liabilities disposed of
- Information on any ongoing agreements (earn-outs, retentions, guarantees, etc)

Most of this information is obviously best dealt with in the notes, but it might be helpful to have the proceeds and the P&L impact disclosed as a separate section (depending on the final format adopted for these two statements and further clarification regarding the transactions that would be so treated).

To return briefly to the topic of the cost of adopting Board proposals that Question 20 raised, it is concerning to see that paragraph 3.92 makes the odd assertion that costs of any allocation exercise will be 'mitigated' by 'the relative lack of frequency of basket transactions'. Lack of frequency does not change the way that costs and benefits should be compared.

22.0 Disclosing maturities

Users find information about the maturity profile of an entity's liabilities useful (also see our comments in paragraph 1.3 regarding liquidity).

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23.0 Reconciliation of cash flows to comprehensive income

We agree with the DP's assertion that comparing cash flow to earnings amounts is highly relevant in the analysis performed by investors and analysts, and that it is currently a challenging endeavour.

Users are looking for insights into the differences between cash and earnings and how/why these differences have arisen. Some of us believe that the reconciliation proposed in the discussion paper will provide useful information, others are more sceptical (and in particular are concerned that it could result in a very lengthy reconciliation that may not provide meaningful information).

Some of us believe reconciliations of the beginning of period to end of period asset and liability amounts should be provided in a summary table for each line on the statement of financial position (with the caveat that we expect the Statement of Financial Position to contain only material data thus limiting the number of reconciliations required). Others would prefer such reconciliations to be provided in individual notes.

Many of these are already required under IFRS, including reconciliations of property, plant and equipment, and net pension assets or liabilities. Presenting such reconciliation information in the notes allows for more meaningful descriptions of the applicable changes than an overall table would be able to accommodate, but some of us believe that a balance sheet to balance sheet reconciliation similar to the BankCo example would provide a very useful summary so it is likely that both approaches will be required.

Having line item reconciliations for each item reported on the balance sheet (including clear identification of how changes flowed through the various sections of the Statement of Comprehensive Income and the Statement of Cashflows) would significantly enhance our ability as users of this information to understand the reasons behind changes from one period to the next, and would also significantly restrict the opportunities for material items to be obscured.

As noted in Section 1, we agree with the approach suggested by the Investors Technical Advisory Committee in their letter to the FASB dated 11th December 2007 regarding a principles-based disclosure standard (http://www.fasb.org/investors_technical_advisory_committee/ITACDisclosureProposal.pdf), and believe that their proposals would provide a suitable framework for the disclosures we require.

24.0 Changes in fair value

We have said on numerous occasions that we need to be able to identify better the changes to comprehensive income that result from external market movements outside the immediate control of management ("fair value" changes) and those that result from the collective efforts of the management and staff of the business to arbitrage between the suppliers and customers of the business.

In that context, the discussions in Chapter 4 are encouraging, and the concepts of persistence and subjectivity as tools for helping to disaggregate components of Comprehensive Income appear to be helpful.

What users need is a clear disclosure of those items of Comprehensive Income that arise as a result of balance sheet items being fair-valued, but not disposed of.

Column D in the ToolCo reconciliation on pages 116 & 117 appears to provide the information on fair value changes that users need, and might well be sufficient on its own as a memo column to the Statement of Comprehensive Income.

25.0 Alternative reconciliation formats

As discussed in our answer to Questions 23, we would like to see the period-on-period changes in each line item in the Balance Sheet either presented as a table or explained in the notes, or preferably, both.

26.0 Unusual or infrequent events

Users find it helpful when management disclose information about accounting entries that they believe arise from unusual or infrequent events, and the definitions supplied by APB 30 provide a sensible basis for identifying such events.

Some of us would prefer these items to be dealt with by pro-forma earnings and cashflow disclosures but others like the suggestion of a memo column in a reconciliation. We would also like to see more detailed discussions in a separate note explaining the P&L and cashflow impacts (including the effects on such things as tax as noted in our answer to Question 17).

Appendix 2 – important issues not discussed in the FSP Discussion Paper

The following topics are not raised in the Discussion Paper (or not addressed in the questions) but CRUF members consider them to be very important in the context of Financial Statement Presentation, and would like to see them addressed in any Exposure Drafts that result.

1.0 Mergers and acquisitions

1.1. Importance

The FSP DP makes no mention of M&A which we think is a major omission. While we recognise that a review of the standards for business combinations is outside the scope of the FSP, there is much that could be done in the form of increased disclosure that would address many of the current weaknesses.

Acquisitions and divestments are often the largest financial decisions made by management and as such can have very material impact both on the future cash generating capability of the company and on investors' assessment of whether management is investing wisely or not.

Many recent examples of accounting abuse have centred around buying and selling companies in ways that disguise the true transfer of value and/or distort subsequent operating performance. We recognise that the vast majority of managements are honest and scrupulous but allowing major loopholes to remain is inherently undesirable.

We believe that the operating profitability of a business should not be materially changed simply because there has been a change of ownership. New owners will usually try to improve profitability but these improvements should result from financial and operating decisions, not because of accounting standards. If standards do require profitability to be changed (e.g. by amortising intangible fixed assets that were identified as part of the accounting required following an acquisition), then it should be possible for investors to reverse these effects if they wish to do so when performing their own analysis.

At its simplest, investors want to know 1) what has been paid for acquisitions and 2) what return has the company made on its investment. It is often impossible to derive either.

1.2. Current weaknesses – identifying the purchase price

It can often be difficult to work out the total enterprise value of an acquisition or disposal. Investors want to know the total consideration for an acquisition, i.e. all payments (cash, shares, market value of other assets) less the value of acquired financial assets (acquired cash, acquired debt, pension liabilities, any other quasi-debt liabilities). This will probably be how the management will have looked at the proposed acquisition so the information will almost always be readily available.

The current cash flow line item for acquisitions is cash paid less cash acquired with the business. This is both incomplete (because it omits debt at the acquired business) and easy to manipulate.

Some transfers of value (e.g. paying in shares) can be worked out by investors but others such as acquired debt are usually completely invisible. Total transferred pension assets and liabilities can sometimes be worked out from the pension note but individual transfers will be opaque if there has been more than one transaction.

Cash spent on acquisitions is sometimes lumped together with purchase of fixed assets and investments, reducing visibility even further.

1.3. Current weaknesses – acquisition intangibles

We have set out our views regarding acquisition intangibles in two letters to the Boards. On 1st August 2007 we wrote urging the Boards not to commence a project on this topic (http://www.cruf.co.uk/intangibles_letter_%20july07.pdf). We also noted our concerns regarding the accounting associated with acquisition intangibles in our letter to the joint Boards dated 5th June 2008 (http://www.cruf.co.uk/joint_boards_letter_PE_june5th.pdf).

To repeat the comments some of us made in June 2008, we do attribute value to intangibles that have a value as separable assets in the market and/or are valued as such in market transactions (patents, licences, and brands might be obvious examples) and find it useful to have these assets separately identified, but, in general, we do not regard the process of re-analysing what would previously have been classified as goodwill as helpful if it involves theoretical calculations that would not have been performed in the normal course of assessing the acquisition or merger, particularly in the light of the costs involved.

In the vast majority of cases the amortisation charges that result from the identification of these "acquisition intangibles" are not regarded as economically meaningful by users (in many cases they might even be regarded as double-counting the costs associated with maintaining the intangibles concerned). Many companies do not provide a clear breakdown of their intangible amortisation charges making it difficult to separate this amortisation from that which might be regarded as more meaningful (for example, the amortisation of a patent or licence).

As we noted in our July 2007 letter, it is clear from price-to-book ratios in the market, academic research, and analyst comments, that the current accounting framework fails to capture the value of many intangibles, but market practice is not to seek to determine the values of individual intangibles when valuing a business. Instead the value of intangibles is implied from the valuation process for the whole business (and in practice, the value of many individual intangibles is rarely considered at all except for IFRS 3 purposes). It is the impact that intangibles have on operating performance that matters to us.

Reporting on intangibles is much more suited to the management commentary than the balance sheet.

1.4. Current weaknesses – restructuring costs and provisions

Investors should be able to see what provisions have been created during the initial consolidation so they can judge whether subsequent operating performance is real or synthetic.

1.5. Current weaknesses – information about acquired businesses and their contribution to results

Disclosure on the date of consolidation and the post acquisition contribution is generally poor. We do not favour pro forma accounts but investors want enough information so that they can model the full-year effect of acquisitions (or divestments) made part-way through the year. For example, under IFRS when a company makes a large acquisition late in its financial year of an entity for which no separate accounts are publicly available, then it can be impossible to model the future with any accuracy (US GAAP has already solved this problem).

1.6. Suggestions

- Ensure that users can establish the market value of all financial assets that are transferred during an acquisition or divestment.

- In particular, the cash cost in the cash flow statement should be net of debt as well as being net of cash.

- The value of other transferred assets should be visible in the notes if not in the primary statements.

- Acquisitions should never be lumped in with capital expenditure, purchase of investments or other unrelated activities in the cash flow statements. Divestments should never be lumped in with sale of fixed assets.

- It should be possible to derive operating profitability of acquired businesses in a way that is consistent with organically developed businesses.

- Where material, companies should give enough information about the timing and impact of major acquisitions so that users can produce pro forma estimates.

- Full disclosure should be required on the adjustments made to the acquired assets and liabilities when they are consolidated, with particular focus on headings that can distort subsequent operating profitability (provision creation, inventory writedown etc.).

2.0 Discontinued Operations

As noted in our answer to Question 4, some of us believe that current accounting for, and presentation of, discontinued operations does not meet users' needs. In particular it does not reflect the operational performance of the business for the period.

- Investors lose visibility of the operating performance of what can be a key value driver for what can be an extended period.

- The decision about what financial assets to treat as discontinued (such as cash balances and customer advances) is subjective and opaque.

- Discontinued activities are not treated consistently across the income statement, balance sheet and cash flow.

- It gives management the option to flatter reported profitability by burying loss-making assets inside Discontinued Operations.

We believe that these operations should remain fully consolidated until they are actually disposed of, as management still has to control the operations and deliver profits and cash flow.

Discontinued operations should be included in the segmental analysis, which we believe could best be presented as follows:

	Segment 1		Segment 2		Segment 3		Continuing Segments		Discontinued Operations		Consolidated Operations	
	20XX	20XY	20XX	20XY	20XX	20XY	20XX	20XY	20XX	20XY	20XX	20XY
Income												
Sales												
Operating Profit before Remeasurement												
Remeasurements												
Operating Profit												
Statement of Cash Flows												
Depreciation												
Capital Expenditures												
Changes in Working Capital												
Operating Cash Flow												
Statement of Financial Position												
Intangible Fixed Assets												
Tangible Fixed Assets												
Other operating Assets												
Net Operating Assets												

Additional disclosure for discontinued operations would be required in an additional note:

	Discontinued 1		Discontinued 2		Other Discontinued		Total Discontinued	
	20XX	20XY	20XX	20XY	20XX	20XY	20XX	20XY
Comprehensive Income								
Sales								
Operating Profit before Remeasurement								
Remeasurements								
Operating Profit								
Investing Result								
Financial Result								
Taxation								
Net Income								
Statement of Cash Flows								
Operating Cash Flow								
Investing Cash Flow								
Financing Cash Flow								
Tax Cash Flow								
Change in Cash & Cash Equivalents								
Statement of Financial Position								
Intangible Fixed Assets								
Tangible Fixed Assets								
Other operating Assets								
Net Operating Assets								
Net Investing Assets								
Net Financing Assets								
Net Tax Assets								
Shareholders Equity								
Percentage Ownership								

This additional disclosure would be necessary to allow investors to understand the impact of sale on each of the categories within the main financial statements. We assume that if management are intending to discontinue an operation, such disclosure should not require extra costs for preparers as it will be readily available.

3.0 "Unconsolidated business activities" – additional disclosures

As noted in our answer to Question 9, many CRUF members believe that the proposed "Investing" category is unhelpful. Instead we suggest an alternative section within Operating, entitled "Unconsolidated Business Activities" which could contain:

- Equity Accounted Entities – single line consolidation in the main statements.
- Pension deficits or surpluses.
- Controlled Investments – businesses which, although controlled, are held from inception with the intention of resale, with such investment activity being the main activity undertaken by the holding company.

3.1. Equity Accounted Entities

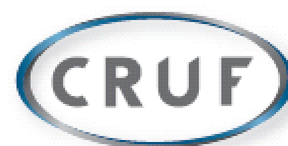
We believe that any entity which is not consolidated (fully or proportionately) should not be presented within the Operating category, although inclusion within the investing category still keeps them within the wider definition of a "Business" asset. This seems reasonable to us as the exercise of influence implies that there is a business reason for the investment that goes beyond a purely financial interest.

Users make extensive use of ratios when comparing and contrasting the valuation of different operating entities. The most common multiples used at the enterprise (or operating) level are EV/Sales, EV/EBIT, EV/NOPAT and EV/EBITDA, although industry specific metrics are also widely used (e.g. EV/Tonne of Capacity for cement companies).

We believe that a basic objective of financial statement presentation should be to ensure users are provided with useful information with minimum restatements required to enable them to make these comparisons.

In this context it is useful to think of the Operating category as the "enterprise" that the analyst is comparing using these multiples. Because equity accounted entities are consolidated at the net income level they do not contribute towards the denominators of the relevant multiples and should therefore be excluded from the enterprise value. Thus users will deduct the value of these equity accounted entities from the market capital of the company when calculating these ratios and so clearly segregating them as non-operating business assets will assist users in this process.

Although consolidations is outside the scope of this Discussion Paper it is worth making the point that, although we do not believe that such equity accounted investments should be consolidated at fair value, we do believe that users would benefit from a management indication of fair value where this is materially different from book value. In our view current disclosure is inadequate for users to perform their own, even rudimentary, valuation. We consider the following information should be presented in the notes (as it is broadly already under US GAAP):



	Associate 1		Associate 2		Associate 3		Other Associates		Total Associates	
	20XX	20XY	20XX	20XY	20XX	20XY	20XX	20XY	20XX	20XY
Comprehensive Income										
Sales										
Operating Profit before Remeasurement										
Remeasurements										
Operating Profit										
Investing Result										
Financial Result										
Taxation										
Net Income										
Statement of Cash Flows										
Operating Cash Flow										
Investing Cash Flow										
Financing Cash Flow										
Tax Cash Flow										
Change in Cash & Cash Equivalents										
Statement of Financial Position										
Intangible Fixed Assets										
Tangible Fixed Assets										
Other operating Assets										
Net Operating Assets										
Net Investing Assets										
Net Financing Assets										
Net Tax Assets										
Shareholders Equity										
Acquisition related adjustments										
Adjusted Equity										
Percentage Ownership										
Net Income Consolidated										
Cash Dividends Received										
Net Assets Consolidated										

3.2. Pension deficits and surpluses

The Discussion Paper proposes that pension deficits and surpluses should be classified as Operating – an approach that many (but not all) users find unhelpful. Space does not permit a detailed discussion of all the issues that arise when trying to determine the best way to account for pensions but Section 7 in this Appendix provides a summary.

A compromise between treating pensions as operating or as financing would be to include them under the heading of Unconsolidated Business Activities on the balance sheet. This would facilitate analysis of the underlying operations of the business separate from the pension scheme while still emphasising the fact that the pension liability arises as a result of the operations of the business.

As discussed in Section 7, adopting this approach could be adopted irrespective of whether one views the pension liability as operating or not. Most CRUF participants require the financial elements to be included within Financing.

3.3. Controlled Investments

Some of us believe that in a limited number of cases, investment companies should be permitted to not consolidate the businesses that they control. These cases are limited to investments that are made with the intention to resell them and where that is the core objective of the acquirer.

Disclosure regarding these businesses would be the same as for the equity accounted entities discussed above except that we would also anticipate that a Fair Value would be given in every

case and this would be the carrying value in the balance sheet. The logic for this treatment is that a sale is the ultimate intent and management should therefore explicitly use their influence over the business to maximise the exit price and this is the most appropriate measure of performance. The additional information would, however, allow users to formulate their own impressions of the carrying value to satisfy themselves that management have applied reasonable judgement.

We would anticipate that only significant investments would be analysed individually, alternatively other categories could be used to consolidate similar businesses and we would rely on a "through the eyes of management" approach for this. Such groupings might occur for larger VC companies who would typically group their investments by the maturity of the investee businesses or by economic sector classification.

	Investment 1		Investment 2		Investment 3		Other Investments		Total Investments	
	20XX	20XY	20XX	20XY	20XX	20XY	20XX	20XY	20XX	20XY
Comprehensive Income										
Sales										
Operating Profit before Remeasurement										
Remeasurements										
Operating Profit										
Investing Result										
Financial Result										
Taxation										
Net Income										
Statement of Cash Flows										
Operating Cash Flow										
Investing Cash Flow										
Financing Cash Flow										
Tax Cash Flow										
Change in Cash & Cash Equivalents										
Statement of Financial Position										
Intangible Fixed Assets										
Tangible Fixed Assets										
Other operating Assets										
Net Operating Assets										
Net Investing Assets										
Net Financing Assets										
Net Tax Assets										
Shareholders Equity										
Acquisition related adjustments										
Adjusted Equity										
Percentage Ownership										
Net Income Consolidated										
Fair Value Adjustment										
Consolidated Income										
Cash Dividends Received										
Net Assets Consolidated										
Fair Value Adjustment										
Investment at Fair Value										

4.0 Working Capital

We are unsure of the implications of adopting a strict one-year definition of current assets but we are concerned that this approach might have unintended consequences in the context of working

capital (which by its very nature in some businesses will consist of assets and liabilities with lives in excess of one year).

We would appreciate clarification on this point.

5.0 Net Debt – possible definition

Our proposed cashflow format (Appendix 3) includes a Net Debt reconciliation, and our answer to Question 10 notes our preference for using this concept to determine what should be included within the Financing section of the balance sheet.

We regard Net Debt as the sum of externally provided non-equity financing (including derivatives) less cash, cash equivalents and marketable securities.

We would expect the following to be included:

- Bank and other borrowings
- Lease liabilities (there is obviously a separate debate to be had about the extent to which leases should be capitalised)
- Preferred stock classified as a liability
- Net derivative financial positions

Less:

- Cash
- Cash equivalents
- Marketable securities

6.0 Disclosure of debt covenant information

Current financial statements do not provide sufficient information regarding the terms agreed between the company and its lenders (debt covenants). The following example shows the sort of extra disclosure that users would find useful.

Capital structure

The following table shows each of the covenants, and the current position.

Summary covenants and current position

	Covenant	**2008 actual**	**2007 actual**
Net assets[1]	>£350m	£402m	£468m
Gearing[2]	<125%	105%	86%
Interest cover[3]	>150%	162%	307%
Loan to value[4]	<70-80%	46%	53%

[1]Net assets: definition of net assets in banking facilities vary, the most stretching excludes minority interest. [2]Gearing: net debt as a %age of shareholders' funds. [3]Interest cover: Recurring PBIT plus crystallised historic revaluation surpluses as a %age of net cash interest payable. [4]Loan to value: Loan as a %age of specific portfolios of assets, tested separately for each bank facility. The figure above is total secured debt to secured assets.

7.0 Pensions accounting – an example

We have referred to pensions as creating difficulties in the context of the cohesiveness principle. They also give rise to debate amongst CRUF members.

In our view, the current year pension costs of current employees should be treated and shown as part of employment costs and as operating components. For companies without DB schemes, that may be the end of it: an accrued cost for DC contributions payable by the employer and/or, where applicable, additional social security taxes paid in respect of state provision.

With DB schemes, many of us believe that there is also a financing component. Work is obtained in the current and in previous periods, but part of the cost of that work is deferred and often for very long periods. This applies whether the scheme is funded or not.

If one accepts this logic, for effective comparison between firms that pay for their current labour in different ways, the operating charge should be restricted for DB schemes to the current year service cost for current employees (for example, a mortality estimate revision that changes the defined benefit obligation in respect of current employees for previous years' work and previous employees who may well have left the firm many years ago has nothing to do with the costs of conducting the firm's current operations). On that basis, the single category approach is inappropriate, as noted in Section 3.2 above.

However, the treatment of pensions in the context of FSP has been overtaken by separate discussions at the Board on post employment benefits. The Board's decision in January 2009 to disaggregate changes in the defined benefit obligation and in plan assets into employment, financing and remeasurement components to be recognised in the income statement would deal at high level with this concern, and those of us who believe pensions give rise to both operating and

financing effects would support the board's decision at the March 2009 meeting that pensions must be separated into three line items:

a. Service cost

b. Interest cost on the obligation

c. All other changes

Similarly in the Statement of Cashflows many of us would like to see deficit reduction payments identified separately outside operating cashflows. If the agreement with the pension scheme does not separately identify the deficit reduction component of payments, the company should assume that it is the excess of cash paid over the current service cost.

Consideration of the details of the board's discussion and conclusions on this subject will be addressed separately from this FSP submission.

Appendix 3 - Cashflow statements - suggested layout – indirect method

This example is included to show how the indirect reconciliation could be improved and integrated with a direct method cashflow, which is the approach generally favoured in Europe.

Many CRUF members in Australia and the US would approach the problem the other way round, with a direct cashflow starting from Cash Received from Customers accompanied by an indirect reconciliation similar to that shown below.

The Statement ends with a Net Debt Reconciliation, something that many of us would like to see included whichever cashflow format is finally adopted.

Illustration of an improved Indirect Cashflow format

Indirect format for the first section (calculating pre-tax Operating Cashflow) and then direct format for the rest.

BUSINESS				
Cash received from customers		DIRECT	**XXX**	*This should also be shown as a separate line in the Receivables note and reconciled to Sales*
EBIT			**XXX**	*This should match the P&L prior to exceptional items (it should also be before non-cash fair value movements)*
Add back	Amortization & depreciation	INDIRECT	X	*Details in individual notes*
EBITDA			**XXX**	
Adjust for	Non-cash revenues and costs included in EBIT (e.g. option expenses, pension service costs, income from Associates/JVs, profit/loss on sales of assets, etc)		<X>/X	*Identify in sufficient detail so that the unexplained rump is small (set hard limit?) and the identified items can be traced to other note disclosure – see comments about reconciliations*
	<Increase>/decrease in provisions and other operating prepayments and accruals		<X>/X	*Details in individual B/S notes – same comment re rump*
	Cash <receipts>/payments relating to operating items not adjusted for above (e.g. ongoing pension contributions?)			*Deficit reduction payments should be disclosed separately (see below)*
	<Increase>/decrease in Working Capital (Show breakdown for Inventories, Receivables and Payables NB exclude "Other" from this analysis)		<X>/X	*Should match B/S notes exactly*
Operating cashflow			**XXX**	*S/be split to show Continuing and Discontinued*

Direct format

Operating cashflow			**XXX**	*S/be split to show Continuing and Discontinued*
	Cash <receipts>/payments relating to exceptional operating items			*Details in individual notes*
CASH INVESTED IN OPERATING ASSETS				
Net cash invested in PPE			<X>	*Disaggregate costs & disposal proceeds separately in B/S notes*
Net cash invested in Intangibles			<X>	*(including spending on capitalized R&D)*
ACQUISITIONS AND DISPOSALS				
Cash spent on Acquisitions of subsidiaries			<X>	*NB need to capture the debt acquired with subsidiaries (also debt / cash on disposal of subsidiaries) – either on the face of the Statement or in the accompanying notes – see Net debt reconciliation*
Proceeds from disposal of subsidiaries			X	
Operating cashflow net of investment spending			**XXX**	
RETURNS ON INVESTMENTS AND SERVICING OF FINANCE				
	Cash interest received & paid including finance leases	<X>/X		*Disaggregate separately in notes*
	Dividends paid on non-equity finance	<X>		
	Dividends received from Associates, JVs and other equity investments	X		*NB NOTE THAT ASSOCs AND JVs SHOULD NOT BE INCLUDED WITHIN OPERATING* *Disaggregate separately in notes*
Aggregate financial cashflows			**XX**	

Tax paid on operating activities			**<X>**	*Details in tax note*
Net Cashflow for Ordinary Equity			**XXX**	***Equivalent to Free Cashflow for Equity***
Dividends paid to ordinary shareholders			**<XX>**	
CASH INVESTED IN NON-GROUP ENTITIES				
	Net investment in Associates and JVs	<X>/X		*Disaggregate separately in notes*
	Net investment in equities	<X>/X		*Disaggregate separately in notes*
Aggregate investment in non-group entities			**XX**	
Net cashflow before financing and changes in liquid resources			**XXX**	
CASH PAID TO SETTLE NON-DEBT OBLIGATIONS CLASSIFIED AS FINANCING				
Cash payments / receipts relating to hedge transactions			**XX**	*Disaggregate separately in notes so that users can see premia paid/received and the cash impact of margin / closing positions*
Pensions	**Total cash paid to pension funds** **Less amount expensed in operating** **Operating cash payment under/over expensed** **Deficit reduction payment**	**X** **<X>** **<X>**	**XX**	*Effect: include deficit reduction payments, but not ongoing cash payments (see above for them) – if a precise deficit reduction payment is not known the operating cashflow should be assumed to equal the current service cost*
EQUITY FINANCING				
Proceeds from issue of ordinary shares			**X**	*Details in equity note*
Cash expended on buying back ordinary shares			**<X>**	*Details in equity note*
Change in Net Debt			**XXX**	

NET DEBT RECONCILIATION				
Increase / decrease in cash and cash equivalents			**X**	
Cash acquired with subsidiaries / given up with disposals			**X**	
Increase / decrease in marketable securities			**X**	
CHANGES IN DEBT INCLUDED WITHIN FINANCING				*Disaggregate issue proceeds and repayments*
Issuance/redemption of commercial paper		<X>/X		
Issuance/redemption of debt over 1 year		<X>/X		
Issuance/redemption of other non-equity finance over 1 year		<X>/X		
Debt acquired or disposed of with acquisitions or disposals		<X>/X		
			XXX	
Finance leases				
New finance leases		X		
Capital repayments relating to finance leases		<X>		
			XXX	
Change in Net Debt			**XXX**	
Opening Net Debt			X	
FX translation differences			**<X>/X**	
Impact of restating debt and derivatives to fair value			**<X>/X**	
Closing Net Debt			**XXX**	