4-20-2014

Balance Sheet Presentation under IAS 1 and U.S. GAAP

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April 20, 2014

HNR 499-01

International Accounting Standard 1: Presentation of Financial Statements (IAS 1) is the international standard for all financial statements that are prepared using International Financial Reporting Standards (IFRS). It lays out the guidelines for preparing all financial statements and lists the minimum content requirements, including the balance sheet, which is known under IFRS as the statement of financial position. While IAS 1 has many similarities to the United States Generally Accepted Accounting Principles (U.S. GAAP) in regards to the presentation of the statement of financial position, a few significant differences cause variances in how some financial instruments are reported. Three of these differences are in the layout and classification of the statement of financial position, presentation of long-term debt, and the classification of deferred tax assets and liabilities. BP and Marathon are two major oil and gas companies whose financial statements display these differences, with one entity preparing its statements according to IFRS (International Financial Reporting Standards) and IAS 1, and the other according to U.S. GAAP. While their financial statements present information regarding each company's financial position, there are still some differences that exist between IFRS and U.S GAAP in how that information is presented. Even though there are some fundamental differences between these two reporting standards, both aim to fairly present a company's financial position and the eventual goal is to eliminate this problem through the currently proposed FASB/International Accounting Standards Board (IASB) Convergence Project.

Under IAS 1, the classification of assets and liabilities on the statement of financial position is essential. According to IAS 1 paragraph 60, a company is required to present current and noncurrent assets and current and noncurrent liabilities, each as a separate classification in the company's statement of financial position (IASB, 2011). Under IAS 1 in paragraphs 63 and 64, there is an exception to the current/noncurrent classification requirement, as entities are able to present their statement of financial position based on liquidity or based on a mixture of liquidity and the current/noncurrent classification, as these presentations can provide a more relevant presentation of financial information (IASB, 2011). Lastly, IAS 1 in paragraph 54 provides a list of minimum items of assets and liabilities that must be included in the presentation of the financial statement of position, some of which are property, plant and equipment, intangible assets, and trade and other payables (IASB, 2011). This is unlike U.S. GAAP, as there is no specific requirement that states companies must classify their balance sheet. However, according to the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) 210-10-05-04, most entities display separate classifications of their current and noncurrent assets and liabilities even though it is not required by the FASB (FASB, 2013a). In fact, according to FASB ASC 205-10-S99-5, it is common for entities in specialized industries, such as insurance companies and banks, to prepare unclassified balance sheets, as classification is not relevant for every reporting entity (FASB, 2013b). Unlike IAS 1, U.S. GAAP also does not provide a list of minimum items that need to be included in balance sheet presentation, although relevant information to help understand an entities' financial position needs to be included in the statement. The primary issue here is that IAS 1 provides more specific guidance than U.S. GAAP regarding the presentation of the balance sheet in terms of classification and the items to be included, which has long been a source of debate and controversy amongst the financial world.

Although there is controversy regarding the overall presentation and classification of the statement of financial position between IFRS and U.S. GAAP, there are specific items on the statement that are reported and classified differently. One of these is the presentation of long-term debt as current or noncurrent in the case of violation of the debt agreement. Under IAS 1 paragraph 74, if an entity violates a condition of their long term debt agreement on or before the end of the reporting period and that violation causes that liability to become payable on demand, the liability is classified as current (IASB, 2011). This liability is classified as current no matter what, even if the lender agrees to not demand payment after the end of the reporting period, as entities do not have an unconditional right to defer the settlement of their violation for at least 12 months after the violation date (IASB, 2011). Specified in paragraph 75, there is only one exception to this specification of IAS 1, and that is if a grace period exists. If the lender of the debt agrees to provide a grace period ending at least 12 months after the reporting period. In this grace period, the entity has to correct their violation and the lender is unable to demand immediate repayment of the debt (IASB, 2011). Under FASB ASC 470-10-45-11, entities have to classify long-term debt as current that is or will be callable by the creditor due to violation of the debt agreement at the balance sheet date, not the end of the reporting period, or if the violation was resolved within a specific grace period. (FASB, 2009) Like IAS 1, the FASB ASC lists exceptions to this current classification. If a creditor waives or loses their ability to demand repayment for more than a year from the balance sheet date or if it is probable that a violation will be cured within a specified grace period, then the debt can still be classified as noncurrent, as opposed to a less favorable current classification (FASB, 2009). While both sets of standards have specific requirements regarding callable debt and violations of debt agreements, and agree on the classification due to such violations, IAS 1 has a more rigid requirement in regards to classification, while the FASB's ASC allows for more flexibility in these situations.

In addition to a controversy over the presentation of long-term debt, a difference exists in the presentation and classification of deferred tax asset and liabilities. IAS 1 only devotes paragraph 56 to the discussion of the presentation and classification of deferred tax assets and liabilities. This paragraph states that "When an entity presents current and non-current assets, and current and non-current liabilities, as separate classifications in its statement of financial position, it shall not classify deferred tax assets (liabilities) as current assets (liabilities)" (IASB, 2011). Entities that have adopted IFRS and classify their statement of financial position, based on the current and noncurrent classification, have to report deferred tax assets and liabilities as noncurrent. Unlike other requirements laid out in IAS 1, there is no exception to this classification or presentation given. Under U.S. GAAP, the treatment of deferred tax assets and liabilities is very different. Under ASC 740-10-45-4, these deferred tax accounts are separated into a current and noncurrent portion, which are determined based on the classification of the asset or liability used for financial reporting purposes (FASB, 2010). For example, accelerated depreciation reported on the tax return in excess of the straight-line on the income statement, is a noncurrent deferred tax liability because depreciation is associated with a fixed asset, which is always classified as noncurrent on a balance sheet. ASC 740 also discusses the valuation allowance, which modifies deferred tax assets, while IAS 1 makes no mention if noncurrent deferred tax assets are altered by such an allowance. In this case, the FASB ASC provides more detail and guidance regarding the treatment and classification of deferred tax assets and liabilities, while IAS 1 only provides a single paragraph that merely states these items are to not be classified as current.

Within the oil and gas industry, the first company I chose to look at was British Petroleum (BP), an international oil and gas company based out of the United Kingdom. As an international entity, the company prepares its financial statements according to IFRS, particularly according to IAS 1. I focused on their December 31, 2013 year-end balance sheet or statement of financial position. As an entity that prepares their financial statements according to IFRS, the first thing I noticed about BP's statement of financial position was that it was called the balance sheet, the term commonly used under U.S. GAAP. Although not required under IAS 1, BP lists its noncurrent assets before its current assets on balance sheet, a presentation preference among many international companies. In addition to this, the company lists out all of the required items under IAS 1, paragraph 54, which include property, plant, and equipment, intangible assets, and provisions but do not provide labeled subtotals for current or noncurrent assets or liabilities, a requirement laid out in U.S. GAAP but not specified at all in IAS 1 (Grant Thornton, 2013). In addition, it is obvious that BP is a company that prepares its financial statements according to IFRS, as the company explicitly classifies current and noncurrent assets and liabilities. There are individual classifications on the balance sheet, something that is clearly laid out in IAS 1, but not required by U.S. GAAP. Lastly, in BP's 2013 balance sheet, their deferred tax assets of $985 million, and their deferred tax liabilities of $17,439 million are reported at their gross amounts as noncurrent assets and liabilities (BP, 2014). The net amount of $16,454 million is only shown in the notes to the financial statements (BP, 2014). Overall, solely based on the classifications of assets and liabilities, the addition of the required items, and the presentation of deferred tax assets and liabilities, it is clear that BP is a company that prepares their financial statements according to IFRS and IAS 1.

After looking at an international oil and gas company that prepares its financial statements according to IFRS, I analyzed an American oil and gas company that prepares its financial statement in accordance with U.S. GAAP. The one I chose to examine was Marathon Petroleum Corporation, based out of Findlay, Ohio. Like BP, the focus is on the December 31, 2013 fiscal year end balance sheet. The most obvious distinction is that Marathon not only lists current assets and liabilities before noncurrent assets and liabilities, but they also provide subtotals for its current assets and liabilities. However, Marathon does not provide a separate classification for noncurrent assets and liabilities, the company simply lists these noncurrent instruments after the current asset and liability subtotals (Marathon, 2014). These subtotals and classifications are not required by U.S. GAAP, but are commonplace as these can provide more relevance to the financial information being provided (Grant Thornton, 2010). In addition to these differences regarding classification, Marathon reports the net amount of its deferred tax assets and liabilities. The gross amount of their deferred tax assets was $569 million and their gross deferred tax liabilities were $3,241 million, which means they reported a net deferred tax liability of $2,672 million (sum of portion of other noncurrent assets, portion of accrued taxes and deferred income taxes) on the consolidated balance sheet (Marathon, 2014). This was all recorded as noncurrent, meaning the liabilities they were associated with were noncurrent. Lastly, one other brief difference I noticed was that Marathon disclosed more information regarding shareholder's equity like the number of common shares issues and authorized, par value of common and preferred shares, and the number of shares held in treasury, which is not explicitly required under U.S. GAAP. The 2012 balance sheet of Marathon is obviously prepared using U.S. GAAP as fewer classifications are used, more equity detail is provided on the face of the balance sheet, and the net amount of their deferred tax liabilities are reported rather than the gross amount. Please see Exhibit 1 and 2 for a visual comparison of the asset and equity sections of the balance sheet of both Marathon and BP.

Multiple differences between GAAP and IFRS have been noted within the standards themselves and within actual financial statements, but there is currently a proposal that will effectively converge GAAP and IFRS into one set of standards. In April 2004, the FASB and

IASB began a joint project on financial statement presentation, with the hopes of converging IFRS and U.S. GAAP (McLain and McLelland, 2008). The goal of this project is to no longer have two sets of financial reporting standards, but to have one global standards that will help enhance comparability and comprehension of financial statements for all users. In 2008, the Securities and Exchange Commission (SEC) released a proposed road map that detailed the transition from GAAP to IFRS, which will require a significant investment of time and money for corporations and accounting firms to prepare for one of most substantial financial reporting changes in the history of the U.S. This initial road map estimated that the 2014 would be year IFRS would be first by U.S. companies, but later on in 2010, the SEC noted that 2015 would be the earliest date the single standard would be used (Carpenter and Mahoney, 2011). One of the greatest changes under this Convergence Project would be the face of the financial statements and the new classifications. Firstly, there would be a new definition of a complete set of financial statements, which includes a statement of financial position, a statement of comprehensive income, a statement of cash flows prepared by the direct method with a separate reconciliation of operating income to operating cash flows, a statement of changes in equity, notes, and comparative information for items in the current financial statements (Carpenter and Mahoney, 2011). U.S. companies would now be required to issue their balance sheet as a statement of financial position and a statement of comprehensive income, and not an income statement. These new statements have different classifications and subcategories that would help to better organize the financial information. However, "Several projects have been partially completed and others were discontinued. In some cases, there was no consensus between the boards and different standards were created. To date some projects are still in process" (Rivera et al, 2014). It is currently 2014 and some convergence between the two standards has been achieved, but it does appear that there will be one global reporting standard beginning in a year or less. The intentions behind the project are good and progressive, but completion has been difficult due to the project's magnitude and complexity. Please see Exhibit 3 and 4 for a template of the proposed financial statements and an example of a statement of financial position under the Convergence Project.

Overall, IAS 1 and the FASB ASC have many similarities regarding the presentation of assets and liabilities on the statement of financial position and naturally, there are some differences in the classification of specific assets and liabilities. The three differences highlighted were the overall presentation and layout of the statement of financial position, the presentation of long term debt due to violation (callable debt), and the classification of deferred tax assets and liabilities, some of which were examined through the 2013 financial statements of BP and Marathon. Most of these differences are quite small and insignificant, but will inevitably disappear in the near future as the FASB and IASB Convergence Project continues to move towards a single global reporting standard. There will no longer be the debate over which set of standards to use to best represent an entity's financial position and users will be able to compare domestic and international companies alike.

Appendix

Exhibit 1 – Presentation Preferences of Assets section of Balance Sheet

Example from BP

Non-current assets	
	Property, plant and equipment
	Goodwill
	Intangible assets
	Investments in jointly controlled entities
	Investments in associates
	Other investments
	Fixed assets
	Loans
	Trade and other receivables
	Derivative financial instruments
	Prepayments
	Deferred tax assets
	Defined benefit pension plan surpluses
Current assets	
	Loans
	Inventories
	Trade and other receivables
	Derivative financial instruments
	Prepayments
	Current tax receivable
	Other investments
	Cash and cash equivalents
Assets classified as held for sale	
Total assets	

Example from Marathon

Assets	
Current assets:	
	Cash and cash equivalents
	Receivables, less allowance for doubtful accounts of $9 and $10
	Inventories
	Other current assets
	Total current assets
Equity method investments	
Property, plant and equipment, net	
Goodwill	
Other noncurrent assets	
	Total assets

Exhibit 2 – Presentation Preferences of Equity section of Balance Sheet

Example from BP

Equity	
	BP shareholders' equity
	Non-controlling interests
Total equity	

Example from Marathon

Equity	
MPC stockholders' equity:	
	Preferred stock, no shares issued and outstanding (par value $0.01 per share, 30 million shares authorized)
	Common stock:
	Issued - 362 million and 361 million shares (par value $0.01 per share, 1 billion shares authorized)
	Held in treasury, at cost - 65 million and 28 million shares
	Additional paid-in capital
	Retained earnings
	Accumulated other comprehensive loss
	Total MPC stockholders' equity
Noncontrolling interests	
	Total equity
	Total liabilities and equity

Exhibit 3 – Proposed Financial Statements

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		
	Multicategory transaction section	**Multicategory 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	

Template retrieved from *The Convergence Project: The Matter of Financial Statement Presentation* by Brian W. Carpenter and Daniel P. Mahoney

Exhibit 4 – Example of Statement of Financial Position under the Convergence Project

Exhibit 2 Hutch Manufacturing Co.
Consolidated Balance Sheets

	2007	2006
BUSINESS		
Operating assets and liabilities		
Short term		
Receivables	$68,000	$54,000
Less: Allowance for bad debts	(2,000)	(1,000)
Inventories	26,000	20,000
Prepaid expenses	19,000	24,000
Short-term assets	111,000	97,000
Accounts payable	(19,000)	(16,000)
Accrued liabilities and other	(56,000)	(74,000)
Short-term liabilities	(75,000)	(90,000)
Long term		
Property, plant, and equipment	34,000	24,000
Less: Accumulated depreciation	(9,000)	(6,000)
Goodwill	20,000	25,000
Intangibles	82,000	82,000
Less: Accumulated amortization	(21,000)	(14,000)
Other assets and liabilities, net	(5,000)	(3,000)
Net long-term assets	101,000	108,000
Net operating assets	$137,000	$115,000
Investing assets and liabilities		
Long term		
Available-for-sale securities	2,000	3,000
Investment in affiliate – equity method	6,000	5,000
Total investing assets	$8,000	$8,000
Net business assets	$145,000	$123,000
FINANCING		
Financing assets		
Short term		
Cash	92,000	94,000
Total financing assets	92,000	94,000
Financing liabilities		
Short term		
Dividends payable	(3,000)	(3,000)
Short-term debt and current portion of long-term	(14,000)	(1,000)
Short-term financing liabilities	(17,000)	(4,000)
Long term		
Long-term debt	(71,000)	(49,000)
Long-term financing liabilities	(71,000)	(49,000)
Net financing assets	$4,000	$41,000
INCOME TAXES		
Short term		
Income tax payable	(8,000)	(12,000)
Long term		
Deferred tax assets, net	10,500	13,500
Net income tax assets	$2,500	$1,500
DISCONTINUED OPERATIONS		
Assets classified as held for sale	20,000	22,000
Liabilities classified as held for sale	(8,000)	(8,000)
Net assets held for sale	$12,000	$14,000
EQUITY		
Common stock and additional paid in capital	(47,000)	(40,000)
Treasury stock	142,000	97,000
Retained earnings	(250,750)	(228,000)
Accumulated other comprehensive income	(7,750)	(8,500)
Total equity	$(163,500)	$(179,500)

Retrieved from *Shaking Up Financial Statement Presentation* by Guy McClain and Andrew J. McLelland

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