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International Financial Reporting Standard<sup>®</sup>

# Disclosure Initiative

Amendments to IAS 7

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# **Disclosure Initiative**

(Amendments to IAS 7)

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## Amendments to IAS 7 *Statement of Cash Flows*

Paragraphs 44A–44E and the related heading is added. Paragraph 60 is also added.

### Changes in liabilities arising from financing activities

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- 44A** An entity shall provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes.
- 44B** To the extent necessary to satisfy the requirement in paragraph 44A, an entity shall disclose the following changes in liabilities arising from financing activities:
- (a) changes from financing cash flows;
  - (b) changes arising from obtaining or losing control of subsidiaries or other businesses;
  - (c) the effect of changes in foreign exchange rates;
  - (d) changes in fair values; and
  - (e) other changes.
- 44C** Liabilities arising from financing activities are liabilities for which cash flows were, or future cash flows will be, classified in the statement of cash flows as cash flows from financing activities. In addition, the disclosure requirement in paragraph 44A also applies to changes in financial assets (for example, assets that hedge liabilities arising from financing activities) if cash flows from those financial assets were, or future cash flows will be, included in cash flows from financing activities.
- 44D** One way to fulfil the disclosure requirement in paragraph 44A is by providing a reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities, including the changes identified in paragraph 44B. Where an entity discloses such a reconciliation, it shall provide sufficient information to enable users of the financial statements to link items included in the reconciliation to the statement of financial position and the statement of cash flows.
- 44E** If an entity provides the disclosure required by paragraph 44A in combination with disclosures of changes in other assets and liabilities, it shall disclose the changes in liabilities arising from financing activities separately from changes in those other assets and liabilities.

## Effective date

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- 60 *Disclosure Initiative* (Amendments to IAS 7), issued in January 2016, added paragraphs 44A–44E. An entity shall apply those amendments for annual periods beginning on or after 1 January 2017. Earlier application is permitted. When the entity first applies those amendments, it is not required to provide comparative information for preceding periods.

## **Approval by the Board of *Disclosure Initiative* (Amendments to IAS 7) issued in January 2016**

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*Disclosure Initiative* (Amendments to IAS 7) was approved for issue by thirteen of the fourteen members of the International Accounting Standards Board. Mr Ochi dissented. His dissenting opinion is set out after the Basis for Conclusions.

Hans Hoogervorst

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Martin Edelmann

Patrick Finnegan

Amaro Gomes

Gary Kabureck

Suzanne Lloyd

Takatsugu Ochi

Darrel Scott

Chungwoo Suh

Mary Tokar

Wei-Guo Zhang

## Amendments to the Basis for Conclusions on IAS 7 *Statement of Cash Flows*

Paragraphs BC9-BC27 and their related headings are added.
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### Changes in liabilities arising from financing activities (paragraphs 44A–44E)

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#### Background to the January 2016 Amendments

- BC9 In January 2016 the Board amended IAS 7 to require entities to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities. The amendments were in response to requests from users, including those received at the Board's *Financial Reporting Disclosure Discussion Forum* in January 2013 and reflected in the resulting Feedback Statement ('the Feedback Statement'), which was issued in May 2013. Users highlighted that understanding an entity's cash flows is critical to their analysis and that there is a need for improved disclosures about an entity's debt, including changes in debt during the reporting period. The Feedback Statement noted that users had been consistently asking for the Board to introduce a requirement for entities to disclose and explain a net debt reconciliation.
- BC10 In early 2014, to understand the reasons for their requests for more disclosure about net debt, the Board undertook a survey of investors. The survey sought information about why investors seek to understand the changes in debt between the beginning and the end of a reporting period. The survey also sought input on disclosures about cash and cash equivalents. On the basis of the survey, the Board identified that investors use a net debt reconciliation in their analysis of the entity:
- (a) to check their understanding of the entity's cash flows, because it provides a reconciliation between the statement of financial position and the statement of cash flows;
  - (b) to improve their confidence in forecasting the entity's future cash flows when they can use a reconciliation to check their understanding of the entity's cash flows;
  - (c) to provide information about the entity's sources of finance and how those sources have been used over time; and
  - (d) to help them understand the entity's exposure to risks associated with financing.
- BC11 The survey helped the Board to understand why investors were calling for improved disclosures about changes in debt during the reporting period. The Board noted that one challenge in responding to this need was that debt is not defined or required to be disclosed in current IFRS Standards. The Board noted that finding a commonly agreed definition of debt would be difficult. However, the Board decided that it could use the definition of financing activities in IAS 7.

It therefore decided to propose a requirement to disclose a reconciliation between the amounts in the opening and the amounts in the closing statements of financial position for liabilities for which cash flows were, or future cash flows will be, classified as financing activities in the statement of cash flows.

BC12 IAS 7 defines financing activities as activities that result in changes in the size and composition of the contributed equity and borrowings of the entity. The Board proposed that a reconciliation of liabilities arising from financing activities would provide the information about debt that users of financial statements were requesting.

BC13 In December 2014 the Board published an Exposure Draft *Disclosure Initiative* (Proposed amendments to IAS 7) ('the 2014 Exposure Draft') seeking views on the proposals for a reconciliation of liabilities arising from financing activities.

### **Feedback on the proposals set out in the Exposure Draft**

BC14 The feedback received on the 2014 Exposure Draft provided evidence that the disclosure would provide users of financial statements with the information they were seeking in order to analyse an entity's cash flows. The Board decided to finalise the amendments to IAS 7 ('the 2016 Amendments'); paragraphs BC15–BC24 set out how the Board responded to the feedback received on the 2014 Exposure Draft.

#### **The objective of the disclosure**

BC15 Feedback on the 2014 Exposure Draft noted that the proposal did not set out a disclosure objective, and consequently it was not sufficiently clear how entities would determine the most appropriate way to provide the required disclosure. The Board agreed with this feedback and included an objective within the requirement set out in paragraph 44A of the 2016 Amendments.

BC16 In setting the disclosure objective the Board decided the objective should reflect the needs of the users of financial statements, including those summarised in paragraph BC10.

#### **Application of the 2016 Amendments to financial institutions**

BC17 Some respondents to the 2014 Exposure Draft from financial institutions stated that the proposals would provide little or no relevant information to users of their financial statements because:

- (a) only some of the sources of finance for a financial institution are classified as 'financing activities' (for example, deposits from customers provide finance but in practice the resulting cash flows are typically classified as operating cash flows). A reconciliation may therefore provide an incomplete picture of the changes in the financing structure of a financial institution; and
- (b) other disclosure requirements (for example, comprehensive regulatory disclosure requirements) may already result in sufficient disclosure about an entity's financing structure.

BC18 After taking into consideration the feedback from respondents from financial institutions, the Board decided that the disclosure requirement could be

satisfied in various ways, and not only by providing a reconciliation. The Board noted that when an entity is considering whether it has fulfilled the disclosure requirement, it should take into consideration:

- (a) the extent to which information about changes in liabilities arising from financing activities provides relevant information to its users, considering the needs of users summarised in paragraph BC10; and
- (b) whether the entity is satisfying the disclosure requirement through other disclosures included in the financial statements.

BC19 The Board therefore decided that a reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities is one way to fulfil the disclosure requirement but should not be a mandatory format.

### **Information that supplements the disclosures**

BC20 Some respondents to the 2014 Exposure Draft expressed a concern that the proposals in the Exposure Draft were too restrictive because, in their view:

- (a) the proposed disclosure would not include liabilities that an entity considers to be sources of finance although the entity does not classify them as financing activities (for example, pension liabilities); and
- (b) entities that already provided a net debt reconciliation (a reconciliation of movements in a net balance comprising debt less cash and cash equivalents) would be prevented from providing such a reconciliation, even if users would find it useful.

BC21 The Board did not intend to prevent entities from providing information required by paragraph 44A in a format that combines it with information about changes in other assets and liabilities. For example, an entity could provide that information as part of a net debt reconciliation, as described in paragraph BC20(b). To ensure users can identify the information required by paragraph 44A, the format selected needs to distinguish that information from information about changes in other assets and liabilities. In finalising the 2016 Amendments, the Board clarified these points in paragraph 44E.

### **Financial assets**

BC22 Some respondents to the 2014 Exposure Draft asked the Board to clarify whether changes in financial assets held to hedge financial liabilities could also be included in the disclosure required by the 2016 Amendments. The Board noted that paragraph G.2 of the Guidance on implementing IFRS 9 *Financial Instruments* states that cash flows arising from a hedging instrument are classified as operating, investing or financing activities, on the basis of the classification of the cash flows arising from the hedged item. Consequently, the Board clarified in paragraph 44C that changes in financial assets held to hedge financial liabilities are included in the disclosure required by paragraph 44A.

### **Cost-benefit considerations**

BC23 The Board considered the feedback received on perceived costs and benefits in finalising the 2016 Amendments. The Board noted that there will be initial costs

for preparers to update information technology systems to enable changes in liabilities arising from financing activities to be tracked and collated. The Board also acknowledged that disclosing additional information could result in costs relating to extending the existing internal controls and audit processes of the entity. However, the Board noted that much of the information is already available to preparers. It also noted that the 2016 Amendments do not change the recognition or measurement for liabilities arising from financing activities; instead, they track changes in those items. Consequently, the Board concluded that it does not foresee any significant ongoing cost related to providing this information, and that the informational benefits to users of financial statements would outweigh the costs.

### **Illustrative example**

- BC24 Some respondents to the 2014 Exposure Draft stated that the example proposed within the Exposure Draft was too simplistic and might not help preparers in disclosing relevant information, because in practice the reconciliation would be more detailed. To address this feedback, the Board inserted a further example in the illustrative examples accompanying IAS 7.

### **Other disclosures**

- BC25 To supplement the current disclosure requirements in paragraph 48 of IAS 7 the 2014 Exposure Draft proposed additional disclosure requirements about an entity's liquidity such as restrictions that affect an entity's decision to use cash and cash equivalent balances. However, in the light of the responses, the Board decided that further work is needed before it can determine whether and how to finalise requirements arising from that proposal. The Board decided to continue that work without delaying the improvements to financial reporting that it expects will result from adding paragraphs 44A–44E to IAS 7. The Board may also, in due course, consider adding to its technical work programme a project that would look at liquidity disclosures more broadly.

### **Transition and effective date**

#### **Amendments to IAS 7**

- BC26 The Board concluded that timely application of the 2016 Amendments would respond to a long-standing request from users of financial statements. Thus, the Board decided that the 2016 Amendments should be applied for annual reporting periods beginning on or after 1 January 2017, with early application permitted.
- BC27 Because the 2016 Amendments were issued in January 2016, which is less than one year before the beginning of the period when some entities could be required to apply them, the Board exempted entities from providing comparative information when they first apply the amendments.

## Dissenting opinion

### Dissent of Mr Takatsugu Ochi from *Disclosure Initiative* (Amendments to IAS 7)

- DO1 Mr Ochi voted against the publication of *Disclosure Initiative* (Amendments to IAS 7) (the 2016 Amendments). The reasons for his dissent are set out below.
- DO2 Mr Ochi believes that financial statements that reflect the 2016 Amendments may provide incomplete information about an entity's management of liquidity. The objective of the 2016 Amendments is to require disclosures that enable users to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. However, Mr Ochi thinks that users of financial statements are seeking clearer information about entities' management of liquidity risk. Consequently, he thinks that the information provided by the 2016 Amendments will not meet users' needs. Mr Ochi thinks that the Board has issued these amendments without setting a clear vision of overall improvements to the disclosure about an entity's liquidity risk management. He thinks that this could confuse and mislead users of financial statements.
- DO3 The objective mentioned in paragraph DO2 refers to liabilities arising from financing activities. Paragraph 44C specifies that those liabilities are liabilities for which cash flows were, or future cash flows will be, classified in the statement of cash flows as cash flows from financing activities. However, Mr Ochi thinks that specifying the scope of the disclosure requirement in this way does not capture the information that users need. This is because changes in liabilities arising from financing activities are different from the information used to assess liquidity risk management. Because IAS 7 permits an entity to classify some cash flows (such as interest payments) as either operating or financing, the understanding of what constitutes changes in liabilities arising from financing activities may vary among preparers. In Mr Ochi's view, preparers may have a more precise understanding about what constitutes information on liquidity risk than simply understanding changes in liabilities arising from financing activities.
- DO4 Mr Ochi also thinks that if an entity provides the disclosures required by paragraph 44A in combination with disclosure of changes in the amount of cash and cash equivalents and does not disclose information about the location and availability of the cash and cash equivalents, the disclosure is sometimes irrelevant to how an entity manages liquidity. If users expect to obtain a full picture of an entity's liquidity risk management as a result of the 2016 Amendments, they may be confused and misled.
- DO5 Mr Ochi thinks that providing the disclosure may require excessive work and hence may be inefficient from a preparer's point of view. He notes that the Board may conduct research regarding the effectiveness of IAS 7. Because he regards IAS 7 as having some significant shortcomings, he believes that issuing amendments based on the existing statement of cash flows is not a worthwhile endeavour. He also thinks that it could reduce the clarity of the statement of cash flows.

DO6 Mr Ochi also has a significant concern regarding the costs required to prepare the disclosure. Although the 2016 Amendments are disclosure-only amendments, all reporting entities will need to consider providing this disclosure. For this disclosure, an entity may be required to adjust items already presented as operating and financing activities in a statement of cash flows (for example, interest payments that are classified as operating activities), which may require system changes. Concurrently, an entity may also have to initiate system changes to prepare for applying IFRS 9 *Financial Instruments* and IFRS 15 *Revenue from Contracts with Customers* (both effective on 1 January 2018) as well as IFRS 16 *Leases* (effective on 1 January 2019). Mr Ochi believes that the costs that will be incurred by entities as a consequence of those other changes will be considerable and he thinks that this fact is not reflected in the conclusion the Board had reached as a consequence of its assessment of costs pertaining to this disclosure. Taking these matters into consideration, Mr Ochi believes that the costs of the 2016 Amendments will outweigh the benefits.

## Amendments to the Illustrative examples accompanying IAS 7 *Statement of Cash Flows*

Note E is added to the existing Illustrative Example A.

As explained in paragraph 1 of the illustrative example, the example shows only current period amounts. Corresponding amounts for the preceding period are required to be presented in accordance with IAS 1 *Presentation of Financial Statements*, except when an entity first applies paragraphs 44A–44E of IAS 7 (see paragraph 60 of IAS 7).

### Notes to the statement of cash flows (direct method and indirect method)

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#### E. Reconciliation of liabilities arising from financing activities

	20X1	Cash flows	Non-cash changes		20X2
			Acquisition	New leases	
Long-term borrowings	1,040	250	200	—	1,490
Lease liabilities	—	(90)	—	900	810
Long-term debt	<u>1,040</u>	<u>160</u>	<u>200</u>	<u>900</u>	<u>2,300</u>

A new example (Example C) is inserted after the existing Illustrative Examples A and B.

**C Reconciliation of liabilities arising from financing activities**

- 1 This example illustrates one possible way of providing the disclosures required by paragraphs 44A–44E.
- 2 The example shows only current period amounts. Corresponding amounts for the preceding period are required to be presented in accordance with IAS 1 *Presentation of Financial Statements*.

	20X1	Cash flows	Non-cash changes			20X2
			Acquisition	Foreign exchange movement	Fair value changes	
Long-term borrowings	22,000	(1,000)	—	—	—	21,000
Short-term borrowings	10,000	(500)	—	200	—	9,700
Lease liabilities	4,000	(800)	300	—	—	3,500
Assets held to hedge long-term borrowings	(675)	150	—	—	(25)	(550)
Total liabilities from financing activities	35,325	(2,150)	300	200	(25)	33,650

## Consequential amendment to the Guidance on implementing IAS 1 *Presentation of Financial Statements*

Paragraph IG10 is amended. New text is underlined.

### Part III: Illustrative examples of capital disclosures (paragraphs 134–136)

#### An entity that is not a regulated financial institution

IG10 The following example illustrates the application of paragraphs 134 and 135 for an entity that is not a financial institution and is not subject to an externally imposed capital requirement. In this example, the entity monitors capital using a debt-to-adjusted capital ratio. Other entities may use different methods to monitor capital. The example is also relatively simple. An entity decides, in the light of its circumstances, how much detail it provides to satisfy the requirements of paragraphs 134 and 135. In determining the form and content of the disclosure to satisfy those requirements, an entity also considers the disclosure requirements set out in paragraphs 44A–44E of IAS 7 *Statement of Cash Flows*.



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