IFRS

STAFF PAPER

June 2019

IFRS® Interpretations Committee meeting

Project	**Changes in liabilities arising from financing activities (IAS 7)**
Paper topic	Updated proposed wording of the tentative agenda decision

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Introduction

1. This addendum to Agenda Paper 5 sets out updated proposed wording of the tentative agenda decision to reflect the discussions at the Committee's meeting on 11 June 2019.

2. The paper includes both:

   (a) clean version of the updated proposed tentative agenda decision (pages 2-5 of this paper); and

   (b) a mark-up version showing changes from that proposed in Agenda Paper 5 (pages 6-9 of this paper).

Proposed wording of the tentative agenda decision (updated)

Disclosure of changes in liabilities arising from financing activities (IAS 7 *Statement of Cash Flows*)

The Committee received a request from users of financial statements (investors) about the disclosure requirements in IAS 7 relating to changes in liabilities from financing activities. Specifically, investors asked whether application of the disclosure requirements in paragraphs 44B-44E of IAS 7 leads an entity to provide disclosures that enable investors to evaluate changes in liabilities arising from financing activities.

Meeting the disclosure objective (Paragraph 44A of IAS 7)

Paragraph 44A of IAS 7 requires an entity to provide 'disclosures that enable investors to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes.' To the extent necessary to satisfy this objective, paragraph 44B specifies that an entity discloses 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.

The Board explained in paragraph BC16 that it developed the disclosure objective in paragraph 44A to reflect the needs of investors, including those summarised in paragraph BC10. The Board also noted in paragraph BC18 that when considering whether it has fulfilled the objective in paragraph 44A, an entity takes into consideration the extent to which information of changes in liabilities arising from financing activities provides relevant information to investors, considering the needs of investor summarised in paragraph BC10. These needs are:

(a) to check their understanding of the entity's cash flows and use that understanding to improve their confidence in forecasting the entity's future cash flows;

(b) to provide information about the entity's sources of finance and how those sources have been used over time; and

(c) to help them understand the entity's exposure to risks associated with financing.

Consequently, the Committee concluded that, in meeting the disclosure objective in paragraph 44A of IAS 7, an entity considers whether its disclosures enable investors to check their understanding of the entity's cash flows, to provide information about the entity's sources of finance and to help them understand the entity's exposure to risks associated with financing as described in paragraph BC10.

Reconciling between the opening and closing balances of liabilities arising from financing activities

Paragraph 44D states that '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. When an entity discloses such a reconciliation, it shall provide sufficient information to enable investors to link items included in the reconciliation to the statement of financial position and the statement of cash flows.'

Consequently, when an entity discloses a reconciliation as described in paragraph 44D, the Committee observed that the entity provides information that enables investors to link items included in the reconciliation to other areas of the financial statements. In doing this, an entity applies:

(a) paragraph 44C to identify liabilities arising from financing activities and use them as the basis of the reconciliation. Paragraph 44C defines these liabilities as '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.' If an entity also chooses to define, and reconcile, a different 'net debt' measure, this does not remove the requirement to identify the entity's liabilities arising from financing activities as defined in paragraph 44C.

(b) paragraph 44E to disclose changes in liabilities arising from financing activities separately from changes in any other assets and liabilities. Paragraph 44E states '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.'

(c) paragraph 44D of IAS 7 to provide sufficient information to enable investors to link the items included in the reconciliation to amounts reported in the statement of financial position and the statement of cash flows, or related notes. An entity develops disclosures that enable investors to link (i) the opening and closing balances of the liabilities arising from financing activities reported in the reconciliation, to (ii) amounts reported in the entity's statement of financial position (or related notes) regarding those liabilities.

The Committee also observed that an entity applies judgement in determining the extent to which it disaggregates and explains the changes in liabilities arising from financing activities included in the reconciliation, considering the investor information needs described in paragraph BC10. In this respect, the Committee noted the following:

(a) in disaggregating liabilities arising from financing activities, and cash and non-cash changes in those liabilities, an entity applies paragraph 44B of IAS 7 and paragraph 30A of IAS 1 *Presentation of Financial Statements*. Paragraph 30A of IAS 1 states that 'an entity shall not reduce the understandability of its financial statements…by aggregating material items that have different natures or functions.' Accordingly, in considering the investor information needs in paragraph BC10, an entity discloses any individually material items separately in the reconciliation. This includes material classes of liability (or asset) arising from financing activities and material reconciling items (ie cash or non-cash changes).

(b) in explaining liabilities arising from financing activities, and cash and non-cash changes in those liabilities, an entity applies paragraph 44B of IAS 7 and paragraph 112(c) of IAS 1 *Presentation of Financial Statements*. Paragraph 112(c) of IAS 1 requires an entity to disclose 'information that is not presented elsewhere in the financial statements, but is relevant to an understanding of any of them.' Accordingly, in considering the investor information needs in paragraph BC10, an entity explains each class of liability (or asset) arising from financing activities included in the reconciliation and each reconciling item in a way that (i) provides information about its sources of finance, (ii) enables investors to check their understanding of the entity's cash flows, and (iii) enables investors to link items to the statement of financial position and the statement of cash flows, or related notes.

The Committee concluded that the requirements in IFRS Standards provide an adequate basis for an entity to disclose information about changes in liabilities arising from financing activities that enables investors to evaluate those changes. Accordingly, the Committee concluded that application of the requirements in paragraphs 44B–44E of IAS 7 leads to disclosure that meets the disclosure objective in paragraph 44A. Consequently, the Committee [decided] not to add this matter to its standard-setting agenda

Mark-up of proposed wording of the tentative agenda decision (updated)

Disclosure of changes in liabilities arising from financing activities (IAS 7 *Statement of Cash Flows*)

The ~~IFRS Interpretations~~ Committee ~~(Committee)~~ received a request from ~~has been informed by~~ users of financial statements (investors) about the disclosure requirements in IAS 7 ~~that disclosure~~ relating to changes in liabilities from financing activities ~~applying IAS 7 *Statement of Cash Flows*~~. Specifically, investors asked whether application of the disclosure requirements in paragraphs 44B-44E of IAS 7 leads an entity to provide disclosures that enable investors to evaluate changes in liabilities arising from financing activities. ~~does not always meet their information needs. In particular, investors highlighted shortcomings in the disclosure of a reconciliation between the opening and closing balances in the statement of financial position for liabilities arising from financing activities (IAS 7 reconciliation).~~

~~Investors said that IAS 7 reconciliations provided often do not enable them to evaluate changes in liabilities arising from financing activities. This is because the disclosures provided often:~~

~~(a) cannot be linked to other areas of the financial statements, such as the statement of financial position and the statement of cash flows;~~

~~(b) do not adequately disaggregate or explain (i) liabilities arising from financing activities or (ii) cash and non-cash changes in those liabilities; and~~

~~(c) contain errors.~~

~~In the light of that feedback, the Committee considered whether application of the existing requirements of IAS 7 leads to disclosure that meets investor information needs.~~

Meeting the disclosure objective (Paragraph 44A of IAS 7)

Paragraph 44A of IAS 7 requires an entity to provide 'disclosures that enable investors to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes.' To the extent necessary to satisfy this objective, paragraph 44B specifies that an entity discloses 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.

The Board explained in paragraph BC16 that it developed the disclosure objective in paragraph 44A to reflect the needs of investors, including those summarised in paragraph BC10. The Board also noted in paragraph BC18 that when considering whether it has fulfilled the objective in paragraph 44A, an entity takes into consideration the extent to which information of changes in liabilities arising from financing activities provides relevant information to investors, considering the needs of investor summarised in paragraph BC10. These needs are:

(a) to check their understanding of the entity's cash flows and use that understanding to improve their confidence in forecasting the entity's future cash flows;

(b) to provide information about the entity's sources of finance and how those sources have been used over time; and

(c) to help them understand the entity's exposure to risks associated with financing.

Consequently, the Committee concluded that, in ~~to~~ meeting the disclosure objective in paragraph 44A of IAS 7, an entity considers whether its ~~must provide~~ disclosures ~~that~~ enable investors to check their understanding of the entity's cash flows, to provide information about the entity's sources of finance and to help them understand the entity's exposure to risks associated with financing as described in paragraph BC10.

Reconciling between the opening and closing balances of liabilities arising from financing ~~financial~~ activities

Paragraph 44D states that '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. When an entity discloses such a reconciliation, it shall provide sufficient information to enable investors to link items included in the reconciliation to the statement of financial position and the statement of cash flows.'

Consequently, when an entity discloses a reconciliation as described in paragraph 44D, the Committee observed that the entity provides information that enables investors to link items included in the reconciliation to other areas of the financial statements. In doing this, an entity applies:

(a) paragraph 44C to identify liabilities arising from financing activities and use them as the basis of the reconciliation. Paragraph 44C defines these liabilities as '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.' If an entity also chooses to define, and reconcile, a different 'net debt' measure, this does not remove the requirement to identify the entity's liabilities arising from financing activities as defined in paragraph 44C.

(b) paragraph 44E to disclose changes in liabilities arising from financing activities separately from changes in any other assets and liabilities. Paragraph 44E states '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.'

(c) paragraph 44D of IAS 7 to provide sufficient information to enable investors to link the items included in the reconciliation to amounts reported in the statement of financial position and the statement of cash flows, or related notes. <u>An entity develops disclosures that</u> ~~The information provided must~~ enable investors to link (i) the opening and closing balances of the liabilities arising from financing activities reported in the reconciliation, to (ii) amounts reported in the entity's statement of financial position (or related notes) regarding those liabilities. ~~An entity avoids errors in doing so.~~

The Committee also observed that an entity applies judgement in determining the extent to which it disaggregates and explains the changes in liabilities arising from financing activities included in the reconciliation, considering the investor information needs described in paragraph BC10. In this respect, the Committee noted the following:

(a) in disaggregating liabilities arising from financing activities, and cash and non-cash changes in those liabilities, an entity applies paragraph 44B of IAS 7 and paragraph 30A of IAS 1 *Presentation of Financial Statements*. Paragraph 30A of IAS 1 states that 'an entity shall not reduce the understandability of its financial statements…by aggregating material items that have different natures or functions.' Accordingly, in considering the investor information needs in paragraph BC10, an entity discloses any individually material items separately in the reconciliation. This includes material classes of liability (or asset) arising from financing activities and material reconciling items (ie cash or non-cash changes).

(b) in explaining liabilities arising from financing activities, and cash and non-cash changes in those liabilities, an entity applies paragraph 44B of IAS 7 and paragraph 112(c) of IAS 1 *Presentation of Financial Statements*. Paragraph 112(c) of IAS 1 requires an entity to disclose 'information that is not presented elsewhere in the financial statements, but is relevant to an understanding of any of them.' Accordingly, in considering the investor information needs in paragraph BC10, an entity explains each class of liability (or asset) arising from financing activities included in the reconciliation and each reconciling item in a way that (i) provides information about its sources of finance, (ii) enables investors to check their understanding of the entity's cash flows, and (iii) enables investors to link items to the statement of financial position and the statement of cash flows, or related notes.

The Committee concluded that the requirements in IFRS Standards provide an adequate basis for an entity to disclose information about changes in liabilities arising from financing activities that enables investors to evaluate those changes. <u>Accordingly, the Committee concluded that the application of the requirements in paragraphs 44B–44E of IAS 7 leads to disclosure that meets the disclosure objective in paragraph 44A.</u> Consequently, the Committee [decided] not to add this matter to its standard-setting agenda