ICAEW REPRESENTATION 60/15

DISCLOSURE INITIATIVE: PROPOSED AMENDMENTS TO IAS 7

ICAEW welcomes the opportunity to comment on ED/2014/6 *Disclosure Initiative – Proposed amendments to IAS 7* published by the International Accounting Standards Board (IASB) in December 2015, a copy of which is available from this link.

This response of 17 April 2015 has been prepared on behalf of ICAEW by the Financial Reporting Faculty. Recognised internationally as a leading authority on financial reporting, the Faculty, through its Financial Reporting Committee, is responsible for formulating ICAEW policy on financial reporting issues and makes submissions to standard setters and other external bodies on behalf of ICAEW. The Faculty provides an extensive range of services to its members including providing practical assistance with common financial reporting problems.

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MAJOR POINTS

The bigger picture

1. ICAEW welcomes the IASB's broad-based Disclosure Initiative and in general agrees with the approach taken by the IASB under the Disclosure Initiative of addressing, where possible, certain disclosure issues quickly, rather than awaiting the finalisation of the planned disclosure framework and revised conceptual framework. We would add, however, that in our opinion the development of a principle-based disclosure framework, which forms part of the revised conceptual framework, will be critical to the longer term aim of ensuring that disclosures are only introduced when they are needed, and that they are properly organised. Therefore we continue to strongly encourage the IASB to focus on finalising these two frameworks in a timely manner and undertake a more comprehensive review of existing disclosure requirements across all standards, whilst being mindful wherever appropriate of the current work of FASB and others in this area.

A step in the right direction

2. We support the IASB's decision to improve the information provided to users of financial statements on an entity's debt and liquidity. The proposed amendments are, in our view, a step in the right direction towards meeting investors' needs in this area. However, we do have some concerns, particularly in relation to the proposed 'financing activities' reconciliation, as discussed below.

RESPONSES TO SPECIFIC QUESTIONS

Question 1:

Do you agree with the proposed amendments (see paragraphs 44A and 50A)? Do you have any concerns about, or alternative suggestions for, any of the proposed amendments?

3. In principle we agree with the objective of the IASB's proposed amendments to IAS 7 *Statement of Cash Flows*. We note from the Basis for Conclusions that there has been a steady demand from investors for improved information about an entity's debt, including any changes in debt during the reporting period. Indeed, from a UK perspective, we understand that many UK investors, including those that invest globally, have long called for better disclosures in this area. The equivalent UK standard, FRS 1 *Cash Flow Statements*, requires disclosure of a note reconciling the movement of cash in the period with the movement in net debt, and we understand that many UK investors have lamented the lack of a similar disclosure requirement in IFRS.

4. Therefore, we consider the IASB's proposed new disclosures, particularly the 'financing activities' reconciliation (defined below), a step in the right direction. However, we believe there is scope for the IASB to go further in addressing investors' needs.

Proposed paragraph 44A – the 'financing activities' reconciliation

5. Proposed paragraph 44A sets out the requirements for a reconciliation of the amounts in the opening and closing statements of financial position for each item for which cash flows have been, or would be, classified as <u>financing activities</u> in the cash flow statement. While in principle we support this proposal as a reasonably limited amendment to the standard, we think the reconciliation is too prescriptive and may not ultimately provide investors with the information they need.

6. In particular, we are concerned that the proposed reconciliation, as defined, will not capture all the relevant components of an entity's debt. For example, IAS 7 does not determine how interest paid or received should be classified in an entity's cash flow statement. Instead, paragraph 33 outlines how these amounts could potentially be presented under operating, investing or financing activities. Therefore, interest paid or received that has been presented as operating or investing activities in the cash flow statement would not be picked up for the purpose of the proposed reconciliation. In this situation, the reconciliation would be incomplete and potentially misleading to users of the financial statements.

7. We also note from paragraph BC8 that the proposed reconciliation could be provided on a net basis, for example by deducting cash and cash equivalents balances. While we agree that an entity should be permitted to prepare the reconciliation on a net basis for the reasons discussed in paragraph BC8, we are concerned that deducting cash and cash equivalents balances without further disclosure may, in some cases, provide a misleading view to users of the financial statements (for example, if there are any restrictions on the availability of those cash and cash equivalents balances to settle an entity's debt).

8. In our view, it would be preferable for an entity to have greater flexibility to define (and disclose) what it considers 'net debt' and provide a reconciliation on that basis. This reconciliation should be accompanied by details of any concerns over the ability of the cash and cash equivalents balances to settle the entity's debts. We believe this would provide a more accurate and complete analysis of an entity's net debt position and therefore potentially be of more use to investors. Indeed, the very process of an entity defining and disclosing its own measure of net debt may provide interesting insights for investors. If an entity manages its debt on a gross, not net, basis then it should be permissible to provide information on that basis. In principle, this approach to disclosure is consistent with that required for capital in paragraphs 134 to 136 of IAS 1 *Presentation of Financial Statements* (substituting the phrase *net debt* for *capital*).

9. We have, in reviewing the proposals, considered the results of the UK Financial Reporting Council's Financial Reporting Lab project on net debt reconciliations. In our view, this project provides a very helpful analysis of best practice amongst those entities that are currently providing net debt reconciliations in their financial statements on a voluntary basis. It might be useful for the IASB to bear in mind this report when considering the feedback to this exposure draft.

10. Other matters that have come to our attention on review of the proposed reconciliation are as follows:

- It is not clear from proposed paragraph 44A that an entity can prepare the proposed reconciliation on a net basis. We believe at the very least, bearing in mind our comments in paragraphs 7 and 8 above, that the principle described in paragraph BC8 should be brought forward to the body of the standard.
- It would be useful to include a cross reference to paragraphs 43-44 of IAS 7 (relating to non-cash transactions) alongside proposed paragraph 44A b(iii), which outlines the 'other non-cash changes' within the proposed reconciliation.
- It would be helpful to clarify the level of granularity required by the IASB when it refers to 'each item' of the opening and closing statements of financial position. For example, whether it means the individual line items on the statement of financial positions or the notes to the accounts.

Proposed paragraph 50A - Liquidity

11. Proposed paragraph 50A extends the existing IAS 7 disclosures on liquidity by requiring details of any restrictions that affect the decisions of an entity to use its cash and cash equivalents balances. We support the intention of this proposal. However, it is not entirely clear how it interacts with the existing IAS 7 paragraphs 48 and 49 (which require disclosure on cash and cash equivalents 'not available' for use by the group), paragraph 50 (which encourages additional disclosure that may be relevant to an understanding of liquidity) or the IFRS 7 disclosure requirements on liquidity risk.

12. In our view, the various disclosure requirements described above are symptomatic of the haphazard fashion in which some disclosure requirements have evolved over time. We would strongly recommend that avoiding situations of this type should be an objective of the IASB's Principles of Disclosure project.

13. In the short term, and for the purposes of this narrow scope amendment to IAS 7, it would be helpful for the IASB to provide examples of the particular situations that would be covered by existing paragraphs 48 and 49 compared to proposed paragraph 50A. Further guidance in the Basis of Conclusions would also be useful, particularly on how the various liquidity disclosure requirements interact.

Question 2:

Do you agree with the proposed transition provisions for the amendments to IAS 7 as described in the Exposure Draft (see paragraph 59)?

14. Paragraph BC17 states that the amendments to IAS 7 'should be applied prospectively from its effective date with early application permitted'. We agree with this approach. However, this is not clearly reflected in the wording of proposed paragraph 59. Furthermore, it is not entirely clear from either BC17 or proposed paragraph 59 whether an entity is required to provide comparatives in the year of adoption. In our view, comparative figures in the year of adoption are not necessary and should be optional, although we would expect most entities to have the necessary information. Nevertheless, it is important for the IASB to clarify the transitional provisions, including whether or not comparatives will be required.

Question 3:

Do the proposed IFRS Taxonomy changes appropriately reflect the disclosures that are set out in the proposed amendments to IAS 7 and the accompanying illustrative example? In particular:

(a) are the amendments reflected at a sufficient level of detail?
(b) should any line items or members be added or removed?
(c) do the proposed labels of elements faithfully represent their meaning?
(d) do you agree that the proposed list of elements to be added to the IFRS Taxonomy should be limited to information required by the proposed amendments to IAS 7 or presented in the illustrative examples in IAS 7?

15. While we offer no comments on the details of the proposed taxonomy changes, we believe it will be helpful to offer some observations on the structure and approach taken by the IFRS Taxonomy at a more fundamental level.

16. The current IFRS taxonomy takes the standards as its starting point, and we understand why that is so. But the purpose of the taxonomy is to convert financial reports made under IFRS into XBRL, not to convert the standards themselves into XBRL. Therefore we suggest that the data model for the taxonomy should come from financial reports which correctly implement IFRS. Put simply, the taxonomy would work better if it were more 'report-centred', rather than 'standard-centred'.

17. We believe a more comprehensive IFRS taxonomy, built upon a full data model of the information than normally appears in accounts, would be a realistic and worthwhile aim. Such a taxonomy, designed to represent the range of real-world financial statements made under IFRS in a variety of different countries, would greatly reduce the need to rely upon extension taxonomies. This in turn would make the tagging of accounts more truly consistent and comparable across different entities and jurisdictions. That, after all, is a key purpose of XBRL.

Question 4:

As referenced in paragraph BC20, the IASB is holding a trial of a proposal to change the IFRS Taxonomy due process. Although not constituting a formal public consultation of the IFRS Taxonomy due process, views are sought on the following:

(a) do you agree with the publication of the proposed IFRS Taxonomy Update at the same time that an Exposure Draft is issued?
(b) do you find the form and content of the proposed IFRS Taxonomy Update useful?

If not, why and what alternative or changes do you propose?

18. No, we do not agree with the publication of a proposed IFRS Taxonomy Update at the same time that an Exposure Draft is issued. In our view, amendments to accounting standards and IFRS Taxonomy will, in most cases, be reviewed by very different groups of stakeholders. We are concerned that combining the amendments may result in confusion and reduce overall awareness of proposed changes to the IFRS Taxonomy.

19. In addition, we have some concerns over timing. For example, we assume that the proposed IFRS Taxonomy Update would need to be revisited if subsequent changes were made to the amendments set out in the Exposure Draft. In our view, a more effective and efficient approach would be to issue the proposed IFRS Taxonomy Update as a separate consultation shortly after the IASB Board has issued a conclusion in principle on any proposed amendments.