International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

11 May 2015

Dear Sir/Madam,

Re: Exposure Draft *Disclosure Initiative (Proposed amendments to IAS 7)*

On behalf of the European Financial Reporting Advisory Group (EFRAG), I am writing to comment on the Exposure Draft ED/2014/6 *Disclosure Initiative (Proposed amendments to IAS 7)* (the 'Amendments').

This letter is intended to contribute to the IASB's due process and does not necessarily indicate the conclusions that would be reached by EFRAG in its capacity as advisor to the European Commission on endorsement of definitive IFRS in the European Union and European Economic Area.

Our detailed comments and responses to the questions in the Exposure Draft are set out in the Appendix. To summarise EFRAG:

a) supports the objective of providing disclosures on movements in debt but is concerned that the IASB is proposing a piecemeal and prescriptive requirement without first setting clear principle-based objectives for the disclosures; and

b) disagrees with the proposal to introduce supplementary disclosures on restrictions on cash and cash equivalent balances.

In EFRAG's view, there is a need to introduce disclosures on movements in debt to meet the request of users for a net debt reconciliation. However, EFRAG recommends that the IASB first establish the objectives for the disclosures and then derives the requirements from these objectives, while allowing entities to determine the most appropriate way to provide the required information.

EFRAG does not support the proposed disclosures relating to restrictions on cash and cash equivalent balances because EFRAG believes that the proposed amendments lack a clear objective, and the requirements are not clear and largely overlap with existing guidance. Instead, EFRAG recommends that the IASB clarify existing guidance rather than introducing supplementary guidance.

Finally, and on a broader note, EFRAG encourages the IASB to reconsider the purposes and use of the statement of cash flows for financial institutions (such as banks and insurers) that seems to be of limited relevance for users.

If you would like to discuss our comments further, please do not hesitate to contact Hocine Kebli, Alejandro Saenz, Giorgio Acunzo or me.

Yours faithfully,

Roger Marshall
Acting President of the EFRAG Board.

APPENDIX

EFRAG's responses to the questions raised in the ED

Question 1 – Disclosure Initiative amendments

This Exposure Draft of proposed amendments to IAS 7 forms part of the Disclosure Initiative. Its objectives are to improve:

(a) information provided to users of financial statements about an entity's financing activities, excluding equity items; and

(b) disclosures that help users of financial statements to understand the liquidity of an entity.

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?

EFRAG's response

EFRAG supports the objective of providing disclosures on movements in debt but is concerned that the IASB is proposing piecemeal and prescriptive requirements without first setting clear principle-based objectives for the disclosures. EFRAG recommends that the IASB first establish the objectives for the disclosures and then bases the requirements on these; while allowing entities to determine the most appropriate way to provide the required information.

EFRAG disagrees with the proposal to introduce supplementary disclosures on restrictions on cash and cash equivalent balances as the proposed amendments lack a clear objective, they are not clear and largely overlap with existing guidance. We recommend that the IASB clarify existing guidance rather than introducing supplementary guidance.

Lastly, and on a broader note, EFRAG encourages the IASB to reconsider the purpose of the statement of cash flows for financial institutions (such as banks and insurers) as feedback from users shows that they place minimal value on information contained in the statement of cash flows because it is inadequate to depict their business.

1 EFRAG observes that the Amendments contain two distinct components as they propose to:

(a) introduce a requirement to disclose a reconciliation of components of financing activities; and

(b) aim to improve disclosures about restrictions on cash and cash equivalents.

2 EFRAG's comments on these proposals are presented in the subsections below as they have different objectives.

Reconciliation of components of financing activities

3 EFRAG agrees that there is a need to provide disclosures on movements in debt to meet the request of users for a net debt reconciliation.

4 However, EFRAG is concerned that the IASB is proposing to introduce additional and prescriptive disclosure requirements on a piecemeal basis without first setting a clear principle-based objective for the disclosures.

5 EFRAG believes that the IASB should establish clear objectives for the reconciliation, to assist entities in making judgements when identifying the relevant components of their liabilities to reconcile in their particular circumstances and allow flexibility for entities to determine the most appropriate way to disclose the information. This would also avoid undue costs for those entities that already provide more extensive information in their financial statements.

6 EFRAG believes that such objectives could encompass:

(a) identifying the items included in the reconciled components;

(b) reconciling movements in items in the statement of financial position to movements in the statement of cash flows; and

(c) explaining non-cash movements.

7 EFRAG also suggests that the information indicated in paragraph 44A should be characterised as one of the possible ways to provide the information, but not as a prescriptive requirement. Other presentations (including narratives) could meet the objective and entities should be able to exercise judgement to determine the most appropriate way to meet the disclosure objective and provide additional information that is relevant for their investors. This will enable entities to include additional components of debt that are not captured by the proposed disclosure requirements and, for instance, to provide the reconciliation on a net basis.

8 Flexibility in the choice would also be consistent with recent Standards that require use of a tabular format '*unless another format is considered as more appropriate*'[1]. EFRAG also notes that this would be consistent with the statement in the Basis for Conclusions that the Amendments should not prevent disclosures being provided on a net basis. In EFRAG's view, entities that already provide consistent information on a voluntary basis should be allowed to maintain their practice.

9 If the IASB decides to finalise the proposals, EFRAG has a number of concerns and recommends that the following aspects of the Amendments are clarified.

<u>Each item</u>

10 The IASB should clarify the meaning of the term 'each item' in paragraph 44A as it is not clear whether it relates to individual line items or whether it could also represent a more specific level of aggregation or disaggregation of information presented on the face of the statement of financial position. For instance, it is unclear whether:

(a) the current and non-current portions of a liability should be reconciled separately or can be aggregated;

(b) accrued interest expenses should be reconciled separately from the liability they relate to;

[1] For instance: IFRS 7 *Financial Instruments: Disclosures*; IFRS 12 *Disclosure of Interests in Other Entities*; IFRS 13 *Fair Value Measurement*.

(c) items showing a nil amount in the statement of financial position are required be reconciled (if movements have occurred over the period); and

(d) how the proposals would apply for instance to items with a low or nil balance at reporting date, but that have material turnover during the reporting period (e.g. concentration accounts).

<u>Items classified as financing activities</u>

11 The use of classification in the statement of cash flows as the qualifying characteristic for inclusion in the reconciliation raises questions about the treatment of items for which the classification is not specified (for instance cash flows from interest paid and received can be classified either as operating or financing cash flows). Users of financial statements are interested in understanding how these items affect debt (e.g. rolling up of interest costs, movements related to interest accruals and whether cash flows are classified within financing activities).

<u>Illustrative example</u>

12 EFRAG believes that the proposed illustrative example is simplistic and does not include some of the components commonly found in similar reconciliations (such as accrued interests, advanced payments, changes in fair value of derivative). EFRAG recommends expanding the illustrative example to cover a broader set of circumstances.

13 EFRAG also observes that the proposed amendments to the illustrative example in IAS 7 *Statement of Cash Flows* introduce a 'long-term debt' total that is not defined or required to be disclosed in current IFRS or even under the Amendments. EFRAG recommends that elements to be added to the illustrative example should be limited to items that can be linked directly to existing authoritative IFRS literature, and therefore suggests changing the heading (e.g. 'total' or 'total reconciled components of financing activities').

Disclosures about restrictions on cash and cash equivalents

14 EFRAG agrees that there is a need for improved disclosures related to liquidity of an entity, including improved disclosures on cash and cash equivalents, and narrative disclosures about liquidity risk.

15 However, EFRAG does not support the Amendments because we believe that the IASB should clarify the existing requirements in IFRS rather than introducing supplementary disclosure requirements into IAS 7.

16 In our view, the proposed guidance in paragraph 50A largely overlaps with requirements that exist in other IFRS on liquidity and on restrictions in the access or use of assets to settle liabilities (for instance paragraph 48 of IAS 7, paragraph 13(a) of IFRS 12 *Disclosure of Interests in Other Entities*; paragraphs 34(a) and 39 in IFRS 7 *Financial Instruments: Disclosures*, and IAS 1 *Presentation of Financial Statements*). It is unclear how the Amendments would improve the already existing disclosures.

17 In the absence of a clear objective for the proposed disclosures, it is not obvious what other circumstances (other than when there are tax liabilities that would arise on repatriation of foreign cash and cash equivalents, the example provided in paragraph 50A) result in cash or cash equivalents being 'restricted'. For instance, it is unclear whether internal policies on working capital, planned investment or higher cost of fund raising can be considered a 'restriction', or if restrictions are limited to constraints imposed by third parties.

18 Furthermore, EFRAG does not believe that the statement of cash flows can provide relevant information about liquidity risk when applied to the consolidated financial information of a group. This is because consolidated financial statements do not provide information about the location and the availability of assets, including cash items, and liabilities within the group (as identified in the alternative view put forward by Mr Takatsugu Ochi).

19 Therefore, EFRAG does not believe that the proposed amendments could be improved to meet that stated objective. If it is the intention of the IASB to improve disclosures about the entity's cash position and liquidity risk, we recommend a more holistic approach across all IFRS with clear disclosure objectives and consistent requirements derived from such objectives.

Other Comments

20 One a broader note, EFRAG believes that it would be worthwhile for the IASB to reconsider the purpose and use of statement of cash flows for financial institutions (such as banks and insurers). Feedback received from users shows that they place limited value on information contained in the statement of cash flows because it is inadequate to depict the business model of a financial institution and does not take into account the complexity of liquidity and funding management nor acknowledge the level of liquidity disclosures already provided by them.

21 In this regard, EFRAG is conducting some research on *Cash Flow Statements for Financial Institutions*, which aims at addressing this issue.

Question 2 – Transition provisions

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

If not, why and what alternative do you propose?

EFRAG's response

EFRAG agrees with the proposed transition requirements.

22 EFRAG is generally in favour of retrospective application of amendments and standards as this enhances comparability. However, EFRAG observes that the Amendments do not affect recognition and measurement and only supplement existing disclosures in the financial statements. Therefore, EFRAG considers that the benefit of retrospective application would be limited compared to the cost of providing the information.

23 Consequently, EFRAG agrees with the IASB's proposed requirements to apply the Amendments prospectively. However, we recommend the IASB to clearly state, in paragraph 59 of the ED, that an entity shall apply the proposed Amendments *prospectively* as from their effective date. In the current drafting the word 'prospectively' (as referred to in paragraph BC17 in the basis for conclusions) is missing.

Question 3 – IFRS Taxonomy

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?

Question 4 – IFRS Taxonomy due process

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?

EFRAG's response

EFRAG reiterates its previously expressed view that the IFRS Taxonomy should not be integrated into the IASB standard setting process but kept as a separate activity of the IFRS Foundation, as it may take the IASB away from a principle-based approach to standard setting. Consistent with this position, EFRAG does not intend to assess the proposed changes to the IFRS Taxonomy relating to the Amendments.

24 In its final comment letter in response to the Report of the Trustees' Strategy Review for public consultation *IFRSs as the Global Standard*, sent in August 2011, EFRAG expressed the view that the IASB should not integrate the development of the IFRS taxonomy in the IASB standard-setting process, but it should be kept as a separate activity of the IFRS Foundation.

25 We understand that the benefit of the integration in the IASB due process is that the IASB would consider, from the outset, the impact of its decisions on how the standards are represented in the IFRS Taxonomy and their usability for end-users of financial data with access to XBRL data. We also concur that a formal methodology for considering developing the IFRS Taxonomy alongside the development of the Standard could be established.

26 However we continue to caution the IASB that integrating the development of the Taxonomy in the standard setting process may take the IASB away from a principle-based approach, more particularly in the area of disclosures; since the IASB has decided to make disclosures more principle-based by indicating the objective of the disclosures, rather than a prescriptive list of disclosures.

27 Consistent with this position EFRAG does not intend to assess the proposed changes to the IFRS Taxonomy relating to the Amendments.