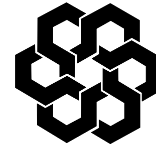

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International Accounting Standards Board

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These notes are based on the staff papers prepared for the IASB. Paragraph numbers correspond to paragraph numbers used in the IASB papers. However, because these notes are less detailed, some paragraph numbers are not used.

INFORMATION FOR OBSERVERS

Board Meeting:	**16 September 2008, London**
Project:	**Disclosures**
Subject:	**IFRS 7 *Financial Instruments: Disclosures,* Liquidity risk (Agenda paper 2A)**

INTRODUCTION

1. IFRS 7 was issued in 2005 with mandatory application for annual periods beginning on or after 1 January 2007. Although the Board encouraged early application, most entities implemented the requirements for the first time in 2007.

2. Market conditions have increased the focus on the need for transparency about the significance of financial instruments to an entity's financial position, performance, and cash flows (especially by financial institutions). In effect, IFRS 7 has been 'stress-tested' in the first year of widespread application.

3. Over the past 5 months, some Board members and staff have discussed experiences with (a) the implementation of IFRS 7 with many preparers and auditors of financial statements and (b) the use of the information produced with some users of financial statements.

4. Our discussions indicate that the approach and framework of IFRS 7 are working well in current market conditions. However, in some areas there is diversity in how (and how

well) the requirements are being applied. Moreover, in other areas, there may be an opportunity to enhance current requirements (notably fair value measurement disclosures).

5. Some of the diversity arose from the operational and systems challenges related to applying a new standard. As a result, some of that diversity will be reduced as entities refine disclosures in future reporting periods. However, the IASB may still need to amend particular wording in the Standard to clarify the requirements.

6. This paper does not address those possible minor wording changes to IFRS 7 that may be required in due course (for example, as part of the Annual Improvements project). Moreover, this paper does not address possible enhancements to fair value measurement disclosures (agenda paper 2B).

7. This paper addresses a recurring issue identified in all of our discussions with constituents – that is, the liquidity risk disclosures required by IFRS 7.

8. This paper asks the Board to change the current requirements and provides possible approaches to changing them. This paper also provides a staff recommendation.

9. Based on discussions with preparers, auditors and some users of financial statements the staff noted that there was widespread diversity in how the liquidity risk disclosure requirements were interpreted and applied in 2007. Diversity in practice is further supported by reports prepared by the larger accounting firms on the first-time adoption of IFRS 7.

10. At these discussions, constituents expressed that particular aspects of those requirements proved to be difficult and costly to implement. In addition, there were many questions about whether the minimum quantitative requirements:

    (a) are consistent with the approach taken in IFRS 7 to disclosing risks arising from financial instruments. That approach is to report information that is used internally by management to manage risk (paragraph 34 of IFRS 7), or

    (b) meet the principle set out in paragraph 31 of IFRS 7. That principle is to disclose information that enables users of its financial statements to evaluate the nature and

extent of risks arising from financial instruments to which the entity is exposed at the reporting date.

11. This paper sets out:

    (a) a summary of the liquidity risk disclosure requirements in IFRS 7 (paragraphs 12 – 26 of this paper)

    (b) a summary of how those requirements were applied in 2007 (paragraphs 27 – 31)

    (c) issues arising from the application of those requirements (paragraphs 32 – 36)

    (d) possible approaches for addressing those issues (paragraphs 37 – 50), and

    (e) a staff recommendation (paragraphs 51 – 58).

SUMMARY OF LIQUIDITY RISK DISCLOSURE REQUIREMENTS IN IFRS 7

Overall objective of the Standard

12. Paragraph 1 of IFRS 7 states the objective of the Standard - for entities to provide disclosures in their financial statements that enable users to evaluate:

    (a) the significance of financial instruments for the entity's financial position and performance; and

    (b) the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the end of the reporting period, and how the entity manages those risks.

Qualitative and quantitative disclosures about the nature and extent of risks

13. To meet part (b) of the overall objective, IFRS 7 requires both qualitative and quantitative disclosures for each type of risk arising from financial instruments. (Those risks generally include liquidity risk, credit risk and market risk.) The requirements include minimum levels of disclosures that apply to all entities for each type of risk.

14. The purpose of specifying minimum disclosure requirements is set out in paragraph BC42 of IFRS 7. The purpose was to enhance comparability between entities because entities

view and manage risk in different ways and to overcome the situation in which an entity undertakes limited management of risk. Minimum risk disclosures 'provide a common benchmark for financial statement users and are expected to be relatively easy for entities to prepare.'

15. Qualitative disclosure requirements are set out in paragraph 33 of IFRS 7. In summary, an entity must disclose:

    (a) its exposure to risks and how those risks arise; and

    (b) how it manages and measures those risks.

16. Quantitative disclosure requirements are set out in paragraph 34 of IFRS 7. In summary, for each type of risk, an entity must disclose summary quantitative information about its exposure to that risk at the reporting date, based on the information provided internally to key management personnel (as defined in IAS 24 *Related Party Disclosures*).

17. In paragraph BC47 of IFRS 7, the Board concluded that quantitative disclosures should be based on how the entity views and manages its risk i.e. using the information provided to key management personnel (for example, its board of directors or chief executive officer) because that approach:

    (a) provides a useful insight into how the entity views and manages risk;

    (b) results in information that has more predictive value;

    (c) is more effective in adapting to changes in risk measurement and management techniques and developments in the external environment;

    (d) has practical advantages for preparers of financial statements, because it allows them to use the data they use in managing risk; and

    (e) is consistent with the approach used in IFRS 8 *Segment Reporting*.

This approach often is referred to as the 'through the eyes of management' principle.

Liquidity risk disclosures

18. IFRS 7 defines liquidity risk as ‘the risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities.’

19. The relevant disclosures for liquidity risk are set out in paragraph 39 of IFRS 7. An entity shall disclose:

    (a) a maturity analysis for financial liabilities that shows the remaining contractual maturities; and

    (b) a description of how it manages the liquidity risk inherent in (a).

20. For Board members’ convenience, the staff has included in the appendix to this paper the Application Guidance (B11-B16), the Implementation Guidance (IG30-IG31) and the Basis for Conclusions (BC57-58) that accompany the liquidity risk disclosure requirements.

21. The quantitative disclosure in paragraph 39(a) (in conjunction with the relevant application guidance) of IFRS 7 is based on a ‘worst case scenario.’ For example, a financial liability is included in the maturity analysis:

    (a) based on the **earliest date** on which the entity can be required to pay, when the counterparty has a choice of when an amount is paid (paragraph B12)

    (b) at the **maximum amount** that the entity can be required to pay (i.e. the contractual undiscounted cash flows of the liability (paragraph B14))

22. In the Basis for Conclusions, the Board acknowledged that the disclosures present a worst case scenario. The Board noted that by definition, liquidity risk is the risk that the entity will encounter difficulty in meeting commitments associated with financial liabilities. Liquidity risk arises because of the *possibility* that the entity could be required to pay its liabilities earlier than expected. This possibility is often remote.

23. However, the Board further acknowledged that the disclosure requirements do not reveal the expected maturity of liabilities, which may be very different from contractual maturities. Therefore, to achieve a more balanced disclosure ‘package’, the Board decided to require qualitative disclosures that describe how the entity manages the liquidity risk that is quantified in the maturity analysis (paragraph 39(b)). Non-mandatory

guidance regarding qualitative disclosures of liquidity risk is located in the Implementation Guidance (paragraphs IG30-31).

24. For example, paragraph IG30 states that if an entity manages liquidity risk on the basis of expected maturity dates, it might disclose a maturity analysis of the expected maturity dates of financial liabilities and financial assets. Moreover, paragraph IG31 suggests some factors that the entity could consider disclosing to describe how it manages liquidity risk. These include whether the entity expects:

    (a) some of its liabilities to be paid later than the earliest date on which the entity can be required to pay (as may be the case for customer deposits placed with a bank)

    (b) some of its undrawn loan commitments not to be drawn

25. The staff thinks that the qualitative requirements are intended to 'reconcile' the maturity analysis (i.e., a worst case scenario notion) with how an entity actually manages liquidity risk.

26. IFRS 7 applies to all types of entities. However, paragraph 39(d)(i) of IFRS 4 *Insurance Contracts* applies to contracts in the scope of that Standard. That paragraph exempts insurers from applying paragraph 39(a) of IFRS 7 to insurance liabilities if the insurer instead discloses information about the estimated timing of net cash outflows resulting from recognised insurance liabilities.

SUMMARY OF HOW THE LIQUIDITY DISCLOSURE REQUIREMENTS WERE APPLIED IN 2007

27. There was diversity in how the IFRS 7 liquidity disclosure requirements were applied in 2007. The following summary relates principally to banks because most of the analysis performed by the accounting firms[1] has focused on that industry. However, staff discussions and anecdotal evidence indicates that there is similar diversity in application for non-financial entities.

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[1] Accounting for Change: transparency in the midst of turmoil* A survey of banks' 2007 annual reports, PwC, 2008
Focus on transparency, trends in the presentation of financial statements and disclosure of information by European banks, KPMG, 2008
IFRS 7 in the Banking Industry, Ernst & Young, 2008

Quantitative disclosures

28. As noted previously, IFRS 7 requires a quantitative maturity analysis for financial liabilities that shows the remaining contractual maturities at undiscounted amounts.

29. Based on discussions with preparers, auditors and some users of financial statements and analysis performed by the accounting firms, the following summary illustrates how this requirement was applied by different entities. This summary is organised by (a) the items included in the maturity analysis, (b) the amounts included, and (c) the time buckets in which the items were included.

    (a) the **items included** in the maturity analysis of different entities ranged from:

    i. all financial liabilities (including derivatives)

    ii. non-derivative financial liabilities only

    iii. non-derivative financial liabilities and some derivative financial liabilities (for example, only trading derivatives)

    iv. only on-balance sheet financial liabilities

    v. all on-balance sheet financial liabilities and some (but not all) off-balance sheet financial liabilities

    vi. some combination of the above but excluding perpetual financial liabilities

    vii. inclusion of some non-financial items (for example, embedded derivative liabilities in a non-financial host contract that is outside the scope of IAS 39)

    viii. some contracts for the delivery of non-cash financial assets or non-financial assets (for example, financial liabilities that are settled by delivery of the entity's own shares and non-financial contracts that are in the scope of IAS 39)

    ix. something else (and possibly unable to tell from the disclosures)

    (b) the **amount included** in the maturity analysis of different entities ranged from:

    i. undiscounted cash flows

   ii. discounted cash flows

   iii. both discounted and undiscounted cash flows

   iv. undiscounted cash flows for non-derivative financial liabilities and discounted cash flows for derivative financial liabilities

   v. something else (and possibly unable to tell from the disclosures)

(c) the **time buckets** in which the items were included of different entities ranged from:

   i. contractual maturity

   ii. expected maturity

   iii. contractual maturity for all non-derivative financial liabilities but something else for derivative financial liabilities

   iv. contractual maturities for non-derivative financial liabilities and expected maturity for derivative financial liabilities and customer deposits

   v. inclusion of particular items in an 'undetermined' bucket (for example, customer deposits and/or perpetual financial liabilities)

   vi. something else (and possibly unable to tell from the disclosures)

Qualitative disclosures

30. As previously noted, IFRS 7 requires qualitative disclosures that describe how the entity manages the liquidity risk that is quantified in the maturity analysis (paragraph 39(b)) to provide a balanced view of the entity's exposure to liquidity risk.

31. Once again, disclosures made to comply with this requirement varied greatly. Application ranged from:

   (a) extensive disclosure of additional quantitative data (for example, expected cash flows arising from financial liabilities, assets available to meet liquidity requirements, key liquidity ratios used by senior management to manage liquidity, stress testing data/

sensitivity analysis) as well as qualitative descriptions of controls and contingency plans; to

(b) generic descriptions of liquidity risk and basic risk management policies but nothing else.

ISSUES ARISING FROM THE APPLICATION OF THE LIQUIDITY RISK DISCLOSURES

32. The following primary issues were identified in our discussions with constituents.

The inability to make the required quantitative disclosures and questions about what is actually required

33. Making the required quantitative disclosure generally is straightforward for non-derivative financial liabilities (with the possible exception of perpetual instruments because there is no guidance about which time bucket those instruments should be included in).

34. That is not the case for derivative financial liabilities. For example:

(a) gross undiscounted cash flow data often are not produced in any management or other reporting system (for example, such data are irrelevant for net-settled trading derivatives)

(b) for derivatives that require gross settlement (such as a foreign currency swap) the guidance in paragraph B14 requires the entity to disclose only the gross undiscounted cash **outflow**. That mandatory disclosure ignores the cash (or other asset) inflow. Some entities include the inflows, arguing that otherwise the disclosure is meaningless because in the event of financial difficulty most such derivatives will be net-settled.

(c) for some derivatives (such as interest rate swaps), it is unclear what amounts should be included in the maturity analysis. That is, it is unclear whether an entity should include (i) only expected cash flows in the future time periods that result in a net cash outflow (in that case, some time buckets will be empty), (ii) net cash outflows and net

cash inflows (if the swap is in a financial liability position overall), or (iii) something else.

(d) the treatment of written options is unclear. Paragraph B12 states that when the counterparty has a choice of when an amount is paid, the liability is included in the maturity analysis on the basis of the earliest date on which the entity can be required to pay. Paragraph B16 states that when an amount payable is not fixed, the amount disclosed is determined by reference to the conditions existing at the reporting date. It is unclear whether applying these two paragraphs means that if the option has no intrinsic value based on forward stock prices (i.e., the option's strike price is higher than the price of the stock), then the amount in the maturity table should be zero or something else. That question applies equally to recognised options and unrecognised options (such as loan commitments and financial guarantees).

35. There also is confusion about whether the quantitative disclosures must be provided for embedded financial liability derivatives if the hybrid contract is something other than a financial liability (and, if so, how to do the disclosure because the embedded derivative is imputed and does not itself have a contractual cash flow), and financial liabilities that will be settled by delivery of an entity's own shares. In both situations, there will be no outflow of cash or other financial asset of the entity.

Purpose and usefulness of the required quantitative disclosures

36. Many entities manage liquidity on the basis of expectations. That includes expectations about whether existing funding will require refinancing or whether the entity's obligations will be satisfied with existing assets. Therefore, it is argued (by more or less everyone we have spoken with) that basing the minimum required quantitative disclosures on contractual undiscounted data (i.e., worst case):

(a) is inconsistent with the approach taken in IFRS 7 to disclosing risks arising from financial instruments. That approach is to report information that is used internally by management to manage risk,

(b) is difficult and costly to do for some financial instruments, and

(c) does not meet the principle set out in paragraph 31 of IFRS 7. That principle is to disclose information that enables users of its financial statements to evaluate the nature and extent of risks arising from financial instruments to which the entity is exposed at the reporting date.

POSSIBLE APPROACHES TO ADDRESSING THOSE ISSUES

37. At a minimum, the staff believes that the Board needs to clarify the treatment of particular instruments – notably (a) derivative instruments and (b) liabilities in the scope of IAS 39 that do not result in the delivery of cash or other financial assets of the entity. However, the Board could also take this opportunity to reconsider the minimum quantitative liquidity requirements for all financial liabilities.

Alternative approaches

38. The staff has identified two possible approaches to respond to some or all of the issues discussed above:

    Approach 1: Maintain the existing quantitative disclosure requirements (i.e., a worst case scenario notion) for non-derivative financial liabilities but require different quantitative disclosures for derivatives. Quantitative disclosures for derivatives would be based on how the entity manages risk and the entity's expectations (<u>not</u> contractual maturities). Also, Approach 1 places greater emphasis on the need for, and purpose of, the qualitative disclosures.

    Approach 2: The same as Approach 1 except an entity would be allowed to disclose a quantitative maturity analysis based on the entity's expectations for any non-derivative financial liabilities if that is how the entity manages risk. If the maturity analysis for non-derivative financial liabilities is based on expectations, an entity would not be required to provide an analysis based on contractual maturities for those items. All other non-derivative financial liabilities would be disclosed based on contractual maturities.

39. The following is a summary of the two approaches compared with existing IFRS 7 requirements:

Quantitative disclosures	**Derivatives**	**Non-derivatives**
Existing IFRS 7	Based on contractual maturities (undiscounted amounts)	
Approach 1	Based on how the entity manages risk	Based on contractual maturities (undiscounted amounts)
Approach 2	Based on how the entity manages risk	Based on how the entity manages risk or contractual maturities (undiscounted amounts)

40. The staff also would recommend that the quantitative disclosures in either approach apply only to liabilities in the scope of IAS 39 that are settled by cash or another financial asset of the entity. This would exclude (a) embedded derivatives separately accounted for (other than those for which the hybrid contract is a financial liability–in that case the entire liability should be included in the disclosure) and (b) financial liabilities that are settled by delivering an entity's own shares.

41. Although these financial liabilities are included in the definition of liquidity risk, the staff believes that including them is unhelpful to users of financial statements in understanding the liquidity information provided.

42. The staff thinks that liquidity risk arises when an entity encounters difficulty in meeting its obligations to deliver cash or other financial asset of the entity. An embedded derivative does not itself have a contractual cash flow. Moreover, although an entity might encounter difficulties in issuing its own shares (e.g. difficulties in obtaining shareholder approval or other regulatory restrictions), the staff believes this risk is different from liquidity risk. Such risk does not arise because the entity has difficulty in meeting its financial liabilities; it arises because the entity has difficulty issuing its own shares.

Analysis of Approaches

Approach 1

43. Approach 1 would maintain the current quantitative disclosure requirements described in paragraph 39(a) of IFRS 7 for non-derivative financial liabilities, but require different disclosure requirements for derivative instruments.

44. Currently, the requirements for non-derivative and derivative instruments are the same. However, in paragraph B15, the Board acknowledges that an entity may wish to disclose the analysis of derivative instruments separately from that of non-derivative instruments.

45. Approach 1 would require an entity to make separate disclosures about the liquidity implications of derivative instruments. These disclosures would be based on how the entity manages the liquidity risk arising from such instruments. For example, for a trading portfolio, a bank might disclose the total fair value of derivatives that are liabilities, interaction between the net derivative position (asset/liability) and master netting agreements for positions with major counterparties, and how such exposures are managed and controlled. For derivatives such as loan commitments, an entity might disclose a projected cash flow scenario analysis under different stress scenarios, and discuss the liquidity risk consequences of draw downs. For all derivative positions (and also non-derivative financial liabilities), an entity might disclose any significant credit contingent features that result in accelerated repayment, and any situations that the close-out values differ significantly from the fair value.

46. The staff believes this approach resolves many issues relating to quantitative disclosures for derivative instruments. As noted previously, quantitative disclosures for derivative instruments based on contractual maturities:

    (a) are difficult to prepare (some entities do not prepare data based on contractual maturities for derivatives because that is not how they manage liquidity risk), and arguably

    (b) do not provide useful information to users

47. Approach 1 would also strengthen the emphasis on the qualitative disclosure requirements in paragraph 39(b) of IFRS 7 by:

(a) more clearly articulating the relationship between quantitative and qualitative disclosures, and

(b) moving some of the disclosure requirements from implementation guidance (for example, disclosure about liquid and near-liquid financial assets that may be used to pay down funding) to application guidance to ensure entities do not perceive these requirements as supplementary.

48. (Under either Approach, the staff would seek further input from users of financial statements in terms of improving the application guidance about qualitative disclosures.)

Approach 2

49. Approach 2 is similar to Approach 1. However, an entity would be allowed to disclose a quantitative maturity analysis based on expectations for any non-derivative financial liabilities if that is the way the entity manages liquidity risk. If such a disclosure was made, an entity would not be required to provide an analysis based on contractual maturities for such items. However, if the entity does not manage liquidity risk based on expectations, the entity should disclose (by default) a quantitative maturity analysis for all non-derivative items based on contractual maturities. This Approach provides the entity with the option to disclose based on expectations if that is how it manages liquidity risk. It also ensures that all entities provide a minimum quantitative disclosure for non-derivative financial liabilities. However, Approach 2 does not restrict an entity from disclosing all its derivative and non-derivative liabilities based on expectations if that is how it manages liquidity risk.

50. Approach 2 is similar to the approach in IFRS 4 that allows an entity to disclose information about the estimated timing of the net cash outflows resulting from recognized insurance liabilities instead of based on contractual maturities. This Approach also is similar to the approach taken in the market risk disclosures in paragraph 40 and paragraph 41 of IFRS 7, whereby if an entity prepares a sensitivity analysis that reflects interdependencies between risk variables (e.g. value-at-risk), the entity may use that analysis in place of the minimum sensitivity analysis set out in paragraph 40 of IFRS 7.

STAFF RECOMMENDATION

51. The staff recommends Approach 2.

52. The staff believes that Approach 2 provides more useful and meaningful information than Approach 1 (and IFRS 7). Approach 1 (and IFRS 7) can result in information that has little, if anything, to do with the way that an entity manages liquidity risk for particular non-derivative financial liabilities.

53. Moreover, the staff does not believe that Approach 2 would result in reduced comparability among entities in terms of quantitative data about non-derivative financial liabilities. The staff notes that diversity in application is the main cause of incomparability. There is diversity in application of the existing requirements because (i) entities are unable to apply the requirements (ii) entities do not believe the resulting disclosures reflect how they manage liquidity risk.

54. Approach 2 sets out consistent minimum quantitative requirements for all entities (disclose based on expectations if that is how the entity manages liquidity risk, disclose contractual maturities otherwise). Thus, under Approach 2, any differences in resulting disclosures reflect differences in how an entity views and manages liquidity risk. The staff believes that such differences provide users with insight on how the entity views and manages liquidity risks. Approach 2 highlights these relevant differences rather than assumes that all entities manage liquidity risk the same way. In addition, the staff believes that within the same industry sector, one would expect entities to take a similar approach to liquidity risk management. Comparability is also likely to increase with the development of best disclosure practices within industry sectors.

55. The staff is also aware that the some mandatory minimum quantitative disclosure requirements i.e. requirements to disclose contractual maturities for derivative liabilities have deterred entities from providing more useful information. By placing greater emphasis on entities to disclose relevant information in Approach 2, it will become more apparent if they do not.

56. Moreover, Approach 2 is more consistent with the 'through the eyes of management' principle in IFRS 7. As stated in paragraph BC47 of IFRS 7, that approach provides more useful information with better predictive value, is more effective in adapting to change, and has practical advantages for preparers and their auditors.

57. The staff also notes that Approach 2 is consistent with IFRS 4. The staff believes that financial liabilities and insurance liabilities that meet the definition of a financial liability (and some that do not) share many common characteristics and thus should require similar liquidity disclosures. As discussed in paragraph BC215 of IFRS 4, simply disclosing cash flows does not necessarily help users gain an understanding of the characteristics of the cash flows.

58. If the Board agrees with the staff recommendation, the staff will prepare a pre-ballot draft of the proposed amendments.

QUESTIONS FOR THE BOARD

1) Does the Board agree with the staff recommendation: (a) to require an entity to make separate disclosures about the liquidity implications of derivative instruments based on how the entity manages the liquidity risk arising from such instruments, and (b) to disclose a quantitative maturity analysis based on the entity's expectations for any non-derivative financial liabilities if that is how the entity manages risk (and, if not, to disclose based on contractual maturities)? If so, please go to question 3 below.

2) If not, which other approach (Approach 1 or some other approach) does the Board wish to pursue and why?

3) Does the Board agree with the staff recommendation that the quantitative liquidity disclosure should apply only to liabilities in the scope of IAS 39 that are settled by cash or another financial asset of the entity (see paragraph 40 of this agenda paper)? If the Board does not agree with that recommendation, why and how should the quantitative liquidity disclosure requirements apply to such items?

APPENDIX

The following additional paragraphs in IFRS 7 discuss liquidity risk disclosures:

Appendix B
Application guidance

Contractual maturity analysis (paragraph 39(a))

B11 In preparing the contractual maturity analysis for financial liabilities required by paragraph 39(a), an entity uses its judgement to determine an appropriate number of time bands. For example, an entity might determine that the following time bands are appropriate:

(a) not later than one month;
(b) later than one month and not later than three months;
(c) later than three months and not later than one year; and
(d) later than one year and not later than five years.

B12 When a counter party has a choice of when an amount is paid, the liability is included on the basis of the earliest date on which the entity can be required to pay. For example, financial liabilities that an entity can be required to repay on demand (eg demand deposits) are included in the earliest time band.

B13 When an entity is committed to make amounts available in instalments, each instalment is allocated to the earliest period in which the entity can be required to pay. For example, an undrawn loan commitment is included in the time band containing the earliest date it can be drawn down.

B14 The amounts disclosed in the maturity analysis are the contractual undiscounted cash flows, for example:

(a) gross finance lease obligations (before deducting finance charges);
(b) prices specified in forward agreements to purchase financial assets for cash;
(c) net amounts for pay-floating/receive-fixed interest rate swaps for which net cash flows are exchanged;
(d) contractual amounts to be exchanged in a derivative financial instrument (eg a currency swap) for which gross cash flows are exchanged; and
(e) gross loan commitments.

Such undiscounted cash flows differ from the amount included in the statement of financial position because the amount in the statement of financial position is based on discounted cash flows.

B15 If appropriate, an entity shall disclose the analysis of derivative financial instruments separately from that of non-derivative financial instruments in the contractual maturity analysis for financial liabilities required by paragraph 39(a). For example, it would be

appropriate to distinguish cash flows from derivative financial instruments and non-derivative financial instruments if the cash flows arising from the derivative financial instruments are settled gross. This is because the gross cash outflow may be accompanied by a related inflow.

B16 When the amount payable is not fixed, the amount disclosed is determined by reference to the conditions existing at the end of the reporting period. For example, when the amount payable varies with changes in an index, the amount disclosed may be based on the level of the index at the end of the reporting period.

Basis for Conclusions on IFRS 7

Liquidity risk (paragraphs 39 and B11–B16)

BC57 The Board decided to require disclosure of a maturity analysis for financial liabilities showing the remaining earliest contractual maturities (paragraph 39(a) and paragraphs B11–B16 of Appendix B). Liquidity risk, ie the risk that the entity will encounter difficulty in meeting commitments associated with financial liabilities, arises because of the possibility (which may often be remote) that the entity could be required to pay its liabilities earlier than expected. The Board decided to require disclosure based on the earliest contractual maturity date because this disclosure shows a worst case scenario.

BC58 Some respondents expressed concerns that such a contractual maturity analysis does not reveal the expected maturity of liabilities, which, for some entities—eg banks with many demand deposits—may be very different. They suggested that a contractual maturity analysis alone does not provide information about the conditions expected in normal circumstances or how the entity manages deviations from expected maturity. Therefore, the Board decided to require a description of how the entity manages the liquidity risk portrayed by the contractual maturity analysis.

Guidance on Implementing IFRS 7

Liquidity risk (paragraphs 39 and B11)

Liquidity management (paragraph 39(b))

IG30 If an entity manages liquidity risk on the basis of expected maturity dates, it might disclose a maturity analysis of the expected maturity dates of both financial liabilities and financial assets. If an entity discloses such an expected maturity analysis, it might clarify that expected dates are based on estimates made by management, and explain how the estimates are determined and the principal reasons for differences from the contractual maturity analysis that is required by paragraph 39(a).

IG31 Paragraph 39(b) requires the entity to describe how it manages the liquidity risk inherent in the maturity analysis of financial liabilities required in paragraph 39(a). The factors that the entity might consider in providing this disclosure include, but are not limited to, whether the entity:

(a) expects some of its liabilities to be paid later than the earliest date on which the entity can be required to pay (as may be the case for customer deposits placed with a bank);

(b) expects some of its undrawn loan commitments not to be drawn;

(c) holds financial assets for which there is a liquid market and that are readily saleable to meet liquidity needs;

(d) has committed borrowing facilities (eg commercial paper facilities) or other lines of credit (eg stand-by credit facilities) that it can access to meet liquidity needs;

(e) holds financial assets for which there is not a liquid market, but which are expected to generate cash inflows (principal or interest) that will be available to meet cash outflows on liabilities;

(f) holds deposits at central banks to meet liquidity needs;

(g) has very diverse funding sources; or

(h) has a significant concentration of liquidity risk in either its assets or its funding sources.