30 Cannon Street, London EC4M 6XH, United Kingdom
Tel: +44 (0)20 7246 6410 Fax: +44 (0)20 7246 6411
E-mail: iasb@iasb.org Website: www.iasb.org

International
Accounting Standards
Board

INFORMATION FOR OBSERVERS

Board Meeting: **January 2009, London**

Project: **Annual Improvements 2009**

Subject: **Comment analysis – IAS 7 *Statement of Cash Flows***
Classification of expenditures on unrecognised assets
(Agenda Paper 6D)

INTRODUCTION

1 In the 2008 Annual Improvements ED, the Board addressed an issue relating to the classification of cash flows from expenditures on unrecognised assets.

2 The Board proposed amending IAS 7 to state explicitly that only an expenditure that results in a recognised asset can be classified as a cash flow from investing activities.

BACKGROUND

3 In 2008 the International Financial Reporting Interpretations Committee (IFRIC) reported to the Board that practice differs for the classification of cash flows for expenditures incurred with the objective of generating future cash flows when those expenditures are not recognised as assets in accordance with IFRSs. Some entities classify such expenditures as cash flows from operating activities and others classify them as investing activities.

4 Examples of such expenditures are those for exploration and evaluation activities, which IFRS 6 *Exploration for and Evaluation of Mineral Resources* permits to be recognised as either an asset or an expense depending on the entity's previous accounting policies for those expenditures.

5 The IFRIC noted that expenditures on advertising and promotional activities, staff training, and research and development could also raise the same issue.

6 The IFRIC decided not to add this issue to its agenda but recommended that the Board amend IAS 7.

STAFF ANALYSIS

7 The Board received 60 comment letters on the 2008 Annual Improvements of which 27 dealt with IAS 7.

8 The staff notes that the vast majority of respondents either disagreed with the proposed amendment or agreed, but expressed concerns.

9 Those who disagreed or expressed strong concern believe that there should not be a systematic link between the Statement of Financial Position and the Statement of Cash Flow. They believe that achieving consistency between the cash flow statement and the statement of financial position would not faithfully represent the economic substance of operations. They take the example of extractive activities where unrecognised assets are nonetheless in the nature of investing activities. Constituents claim that this is how the market views these expenditures.

10 Other minor concerns are as follows:

- Current wording in IAS 7.16 could be improved to take into account assets such as inventory, prepayments and assets held for rental,
- Constituents were concerned that the proposed wording in the 2008 AIP ED could be misleading regarding the treatment of subsequent expenditures. Constituents asked for guidance on the treatment of

subsequent expenditures for "initially" recognised assets as referred to in the proposed amendments to IAS 7.16.

- IAS 7.32 should be amended to reflect the change in IAS 23, *Borrowing costs*.

11 As regards the subject of the consistency between statements – issue that most constituents disagree on - the staff is of the opinion that financial statements need to be consistent.

12 The staff refers to the Discussion Paper "Preliminary views on Financial Statement Presentation" where paragraph 1.11 clearly states "users have asked for improved linkages between and amongst statements. The issue was addressed by the Board and paragraph 2.5 thus asserts that "An entity should present information in its financial statements in a way that portrays a cohesive financial picture of its activities.

13 As regards the three other minor issues, the staff proposes changes be made to the existing wording.

STAFF RECOMMENDATION

14 The staff is of the opinion that the treatment of items in the statement of financial position and the cash flow statement should be consistent.

15 As regards the other issues, the staff believes that, as a short term solution, wording could be changed and proposes amendment in the appendix to the paper.

QUESTION FOR THE BOARD

16 Does the Board agree with the staff recommendation as regards the classification issue?

17 Does the Board agree with the proposed wording for other minor issues?

Appendix 1

Proposed amendment to IAS 7 *Statement of cash flows*

All proposed changes are to the Exposure Draft of proposed *Improvements to IFRSs*, published in August 2008 (new text is double underlined and deleted text is double struck through).

Presentation of a statement of cash flows

Investing activities

16 The separate disclosure of cash flows arising from investing activities is important because the cash flows represent the extent to which expenditures have been made for resources ~~intended to generate future income and cash flows~~ that are ~~initially~~ recognised as long-term assets and other investments not included in cash equivalents ~~assets~~ in the statement of financial position. Examples of cash flows arising from investing activities are:

(a) ...

32. The total amount of interest capitalised in accordance with IAS 23 Borrowing Costs ~~paid during a period~~ is disclosed in the statement of cash flows ~~whether it has been recognised as an expense in profit or loss or capitalised in accordance with IAS 23 Borrowing Costs~~ as investing activities.