

STAFF PAPER

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IASB Meeting

Project	Disclosure Initiative		
Paper topic	Amendments to IAS 1: net debt		
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Introduction

1. *The Discussion Forum: Financial Reporting Disclosure Feedback Statement* (the ‘Feedback Statement’) suggested that the IASB should assess whether to add a requirement around the disclosure of ‘net debt’ as part of the possible short-term amendments to IAS 1 *Presentation of Financial Statements*.

Background

2. During the Agenda Consultation several users asked the IASB to give urgency to improving the disclosure requirements in IFRS. As well as suggesting that we look at ways of removing ‘clutter’ in financial statements, we were asked to add some disclosure requirements that users considered would allow related information to be connected. They considered that providing clarity could be achieved by adding what they considered to be more meaningful disclosures. The most commonly requested additional requirements related to net debt.
3. IFRS does not explicitly require a disclosure of ‘net debt’ and ‘net debt’ is not defined in IFRS.
4. The IASB has considered this matter before. The Financial Statement Presentation (FSP) project explored the topic of ‘net debt’. The staff draft for that project proposed requiring an analysis of changes in specific line items which

typically constitute what users of financial statements sometimes refer to as net debt. The FSP project described net debt in the following way:

255 An entity shall provide an analysis of changes for the following line items in a single note and include a total for these items:

- a) cash;**
- b) short-term investments;**
- c) finance leases; and**
- d) each line item in the debt category**

5. The FSP project included the following language in the ‘debt category’:

86 Liabilities that are borrowing arrangements entered into for the purpose of obtaining (or repaying) capital and the related income effects shall be classified in the debt category.

6. The IASB suspended this project and, accordingly, has not taken this matter further. Perhaps as a reaction to this suspension, the Capital Markets Advisory Committee, respondents to the Agenda Consultation and investors with whom our investor liaison staff have interacted have asked the IASB to consider adding a requirement separately. The matter of net debt was raised again in the disclosure Discussion Forum and related survey. The staff therefore thought that the IASB should assess whether adding a new requirement should be included as part of the Amendments to IAS 1 project under the Disclosure Initiative.

Views heard

User requests

7. Some users have told us that disclosures about net debt are very important to them. For example, the following was noted in the Financial Reporting Lab report on ‘Net debt reconciliations’:¹

A strong majority of investors indicate they use a NDR [net debt reconciliation] or reconciliation of net cash flows to net debt in their analysis when one is presented, and given the importance, attempt to construct them when they are not.

...

The reconciliations can provide insight on the company’s definition of net debt, the cash and non-cash drivers of changes in net debt, the effect of hedging activities on debt, and the measurement of debt for accounting purposes, which are all important to these two analytical objectives.

8. A September 2009 paper from the FSP project highlighted that:²

A number of user and preparer groups in Europe (mainly the UK and France) have asked that an entity be required to present a net debt reconciliation in its financial statements. In addition, a number of respondents to the discussion paper asked that this project address presentation of net debt. Those who support this disclosure believe that:

- a) It would provide a broader measure of a business’s liquidity, solvency, and financial flexibility than that provided solely by the movement in cash balances in the statement of cash flows.

¹ <http://www.frc.org.uk/getattachment/b3878472-c07a-45a3-b8b6-dcb538f53bd9/FRC-Lab-project-report-Net-Debt-Reconciliations.aspx>

² <http://www.ifrs.org/Meetings/MeetingDocs/IASB/2009/September/18th/FSP-0909-AP14C-obs.pdf>

- b) It would provide more complete information for assessing future cash flows, as cash flow information should be analyzed along with profit or loss and statement of financial position accounts.
- c) It would provide a clear picture of an entity's debt position, which would help a user of the financial statements determine the entity's credit risk profile.

Practice

9. Some entities reporting under IFRS currently provide net debt disclosures. However, anecdotal evidence suggests that whether entities decide to make a net debt disclosure varies by jurisdiction. Feedback from the September 2013 World Standard Setters (WSS) meeting and Accounting Standards Advisory Forum (ASAF) meeting indicated that only some jurisdictions have entities that disclose net debt, or historically have had disclosure requirements about net debt. It was, for example, a disclosure requirement in UK GAAP, which seems likely to be a factor that has led to net debt being reported more frequently in the UK than some other countries.
10. For those entities that currently make some form of net debt disclosure, we understand that the type and extent of the disclosure varies. We therefore think that there could be a number of different formats for net debt disclosures, including:
- (a) a disaggregation of net debt at the end of the period;
 - (b) a roll-forward disclosure of net debt showing net debt at the beginning of the period, reconciled to the net debt at the end of the period; and/or
 - (c) a reconciliation of net cash flows to net debt.
11. The WSS and ASAF meetings highlighted differing views as to whether the information about net debt should be required (ie, is it useful) and whether requiring a disclosure of net debt is necessary at this stage in the Disclosure Initiative project—and, specifically, whether it was appropriate within the Amendments to IAS 1 project.

12. To summarise, although net debt and net debt reconciliations are reported by some companies the nature of those disclosures vary. There does not seem to be a common understanding of what information should be provided by such disclosures.

Staff analysis

Scope of the Amendments to IAS 1 project

13. As mentioned, so far we have been considering looking into the topic of net debt as part of the short-term Amendments to IAS 1 project.
14. We note that the scope of the Amendments to IAS 1 work is narrow. Most of the proposed amendments are to address what we perceive to be overly literal interpretations of the language in IAS 1. This work is seen as a ‘quick win’ under the Disclosure Initiative, to build on the current momentum for improving behaviours with regards to disclosure and to address some of the problems we have heard. Consequently, we are aiming to publish an Exposure Draft in the first quarter of 2014.

Work that would need to be undertaken

15. We think that if the IASB wants to address the topic of net debt there are a number of questions that would need to be answered, such as:
- (a) should net debt be defined in IFRS?
 - (b) should net debt disclosures be specifically required in IFRS?
 - (c) what should be the nature and form of any disclosure of net debt? For example, disaggregation and/or reconciliation.
16. We think that there is merit in examining net debt disclosure requirements. However, to do so would require more research and outreach. We are simply not in a position to be able to provide sufficient analysis to support an IASB decision at this time. Including net debt disclosures in the Amendments to IAS 1 project could jeopardise our projected timeline and slow the momentum for change in the area of disclosures we are trying to achieve.

Conclusion

17. We think that any amendments made about net debt would require more extensive outreach to better understand the issue and to provide a full analysis on the topic.
18. In addition, if net debt was to be explicitly required or defined in IFRS, it would be introducing a new requirement. We therefore think that amendments regarding a net debt disclosure would be more than clarifying. Consequently, we think that such amendments is outside the scope of the Amendments to IAS 1 project.
19. However, we do note the medium-term project under the Disclosure Initiative for research into IAS 1, IAS 7 *Statement of Cash Flows* and IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* and the FSP project to, in essence, create a ‘Disclosure Framework’. We think that a consideration of a net debt disclosure would be much better placed as part of that project.

Staff recommendation and question 1

We recommend that the IASB not include any proposal to amend IFRS in relation to net debt disclosure in the package of proposed amendments to IAS 1 planned for exposure in the first quarter of 2014.

Does the IASB agree?

Staff recommendation and question 2

We recommend considering a net debt disclosure as part of the medium-term project under the Disclosure Initiative as explained in paragraph 19.

Does the IASB agree?