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STAFF PAPER

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IASB Meeting

Project	**Disclosure Initiative**		
Paper topic	Amendments to IAS 7—Disclosure about restrictions on cash and cash equivalents		

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Objective

1. The objective of this paper is to discuss improving disclosures about restrictions on cash and cash equivalents.

Summary of staff recommendations

2. This paper recommends that the IASB should include as part of its Exposure Draft of Amendments to IAS 7 *Statement of Cash Flows,* an amendment to paragraph 48 of IAS 7. This amendment would require, in addition to disclosures of restricted cash and cash equivalents, disclosure of the costs that would be incurred if the cash or cash equivalents were remitted as earnings (including a distribution of profits) to a parent entity.

Background

3. The proposed amendment to IAS 7 is part of the Disclosure Initiative project. At its meeting in March 2014 the IASB considered whether disclosures about cash and cash equivalents should be improved. This followed feedback from investors that disclosures are required to understand:

   (a) what cash is immediately available for the repayment of debt;

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(b) the restrictions on cash, and/or the costs associated with repatriation of cash, where there are foreign exchange controls or tax implications; and

(c) what cash is held for regulatory purposes.

4. At that meeting the IASB tentatively decided to consider amendments to IAS 7 to improve disclosures about restrictions on cash.

Understanding the request from investors

Outreach

5. As reported to the IASB at its meeting in March 2014, we undertook a survey in January 2014 designed to obtain information to help the IASB understand what information users seek when reviewing cash flow information and how they use that information. As part of the survey we asked questions about disclosures related to cash. We first sought to identify whether users encounter situations in which there is a significant restriction on an entity's ability to access or move cash, or a significant cost in doing so resulting from such a restriction. For respondents that did encounter this situation, we asked if they could access the information they needed to assess the risks and/or cost related to any restriction on movement of cash. The results of the survey supported the need to improve disclosures on cash restrictions, with respondents noting a particular concern in relation to the cost of repatriation of cash across different tax jurisdictions.

6. In preparing the agenda paper for the March 2014 meeting, we discussed the concerns with the Capital Markets Advisory Council (CMAC) and the European Financial Reporting Group User Panel, who supported the need to improve disclosures regarding cash.

Why do users find this information useful?

7. Investors noted that when performing analysis of leverage they sometimes 'discount' the cash and cash equivalents as reported in the consolidated financial statements. The 'discount' represents an estimate of the costs that may be associated with repatriation of funds. By discounting the cash, investors consider that they obtain a better assessment of the liquidity of the entity.

8. It might also be noted that there has been some press discussion recently of cases in which a parent entity has retained cash balances in a foreign jurisdiction and met ongoing liquidity needs through external borrowing, instead of remitting earnings held overseas. This has been referred to as 'local restrictions preventing an efficient intercompany movement of funds'.

Existing disclosures about cash and cash equivalents

9. IAS 7 requires disclosure of:

   (a) the components of cash and cash equivalents; (paragraph 45); and

   (b) the amount of significant cash and cash equivalents held by the entity that is not available for use by the group (paragraph 48).

10. IFRS 12 *Disclosure of Interests in Other Entities* requires an entity to disclose information that enables users of its consolidated financial statements to evaluate the nature and extent of significant restrictions on its ability to access or use assets, and settle liabilities, of the group. This includes restrictions on the ability of a parent or its subsidiaries to transfer cash or other assets to (or from) other entities within the group.

11. In addition IFRS 7 *Financial Instruments: Disclosures* contains disclosures regarding liquidity. These disclosures address the maturity of financial liabilities and provide a description of how an entity manages the liquidity risk inherent in its financial liabilities.

12. IAS 1 *Presentation of Financial Statements* paragraph 66(d) requires an entity to classify an asset as current when:

> "… the asset is cash or a cash equivalent (as defined in IAS 7) unless the asset is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period."

13. Although cash and cash equivalents may be classified as current, it is important to understand the effects of any restrictions that are placed on the timing or use of those assets.

14. As noted, at the IASB meeting in March 2014, although the disclosures set out above are related to the concerns that have been expressed, they do not specifically address the circumstance in which the cash is unrestricted but there is a cost associated with repatriation of cash (such as a tax charge) that results in an entity making the economic decision not remit the earnings.

15. In addition to the disclosures above, we have considered whether the restrictions that relate to income taxes on undistributed earnings of subsidiaries could be considered to be a contingent liability in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. Our analysis is that income tax on undistributed earnings does not met the definition of a contingent liability, because the remittance of the undistributed earnings (and therefore any costs such as taxes on remittance) are within the control of the entity.

Staff analysis

16. We have outlined above that investors are requesting improved information about cash and cash equivalents, specifically the costs associated with repatriation of cash where there are foreign exchange controls or tax implications.

17. Following the IASB's tentative decision at its meeting in March 2014 we have explored the following three options:

    (a) Option 1—do not provide additional disclosures (paragraph 18);

    (b) Option 2—amend IAS 7 to require disclosure of the costs that would be incurred if the cash or cash equivalents were remitted as earnings (including a distribution of profits) to a parent entity (paragraphs 19-25); and

    (c) Option 3—redefine 'cash' and 'cash equivalents' (paragraphs 26 and 27).

Option 1: do not provide additional disclosures

18. It was proposed to the IASB, at its meeting in March 2014, that the disclosure improvements on cash and cash equivalents should be considered as part of the Disclosure Initiative research project Principles of Disclosure. This was because

it was thought greater research is needed to understand users' requests and those requests required careful assessment. The IASB, however, asked the staff to consider short-term amendments to IAS 7 to improve disclosures about restrictions on cash. We have therefore sought to find a solution that would addresses the request from users regarding the restrictions over cash and/or the costs associated with repatriation of cash where there are foreign exchange controls or tax implications. However, we continue to hold the view that further research is required on disclosure improvements for cash and cash equivalents, and narrative disclosures about liquidity risk, as part of the Disclosure Initiative and/or any post-implementation review of IFRS 7.

Option 2: amend IAS 7 to require disclosures

19. To address the specific concern about disclosures of costs associated with repatriation of cash where there are foreign exchange controls or tax implications, we have identified a possible short-term amendment that could be proposed for IAS 7.

20. We think it is possible to amend paragraph 48 of IAS 7 to require, in addition to disclosures of restricted cash and cash equivalents, disclosure of the costs that would be incurred if the cash or cash equivalents were remitted as earnings (including a distribution of profits) to a parent entity.

21. As part of the amendment, the list of examples in paragraph 49 of IAS 7 could be amended to include the example of costs associated with repatriation of cash where there are foreign exchange controls or tax implications.

22. We also recommend that the amendment should clarify that the scope of the disclosure includes cash and cash equivalents held by a joint operation accounted for in accordance with IFRS 11 *Joint Arrangements,* if cash held by the joint operation is included in cash and cash equivalents of the reporting entity.

23. This amendment should satisfy investors' requests, because it will provide disclosures regarding the restrictions over cash and/or the costs associated with repatriation of cash where there are foreign exchange controls or tax implications. The amendments proposed would help investors to assess liquidity risks, but it is

possible that preparers may argue that the information being requested is sensitive and outside the scope of a narrow-scope amendment.

IFRS Taxonomy

24. The staff have not identified any significant issues with introducing the effects of this proposed amendment to IAS 7 into the IFRS Taxonomy. The staff have not identified any inconsistencies between this amendment and other Standards.

25. To update the IFRS Taxonomy, the staff propose to create an element for the disclosure of 'Cash and cash equivalents held by entity that are subject to legal and/or economic constraints', as mentioned in paragraph 21 of this paper.

Option 3: redefine cash & cash equivalents

26. IAS 7 defines cash and cash equivalents as:

> "..Cash equivalents are held for the purpose of meeting short-term cash commitments rather than for investment or other purposes. For an investment to qualify as a cash equivalent it must be readily convertible to a known amount of cash and be subject to an insignificant risk of changes in value. Therefore, an investment normally qualifies as a cash equivalent only when it has a short maturity of, say, three months or less from the date of acquisition. …"

27. The existing definition does not require the separate disclosure of cash held permanently in a subsidiary overseas and therefore does not distinguish cash or cash equivalents that are available, but that would be subject to cost if used to repay debt in a different jurisdiction. We considered whether restricted cash and cash equivalents, or cash and cash equivalents held that are subject to a cost if repatriated should be presented separately; however, we think such an amendment is outside the scope of a narrow-scope amendment.

Conclusion

28. In view of the above it is proposed that the narrow-scope amendment to IAS 7 should include additional disclosure of the costs that would be incurred if the cash

or cash equivalents were remitted as earnings (including a distribution of profits) to a parent entity.

29. This will address part of investors' concerns without inhibiting the research project.

Question 1
Does the IASB agree to proceed with option 2?