September 2024
ASAF

Statement of Cash Flows

Research Findings

Disclaimer
This slide deck has been prepared by the staff of the Canadian Accounting Standards Board (AcSB) to facilitate a discussion and does not represent the views of the AcSB. Comments on the application of IFRS Accounting Standards do not purport to set out acceptable or unacceptable application of IFRS Accounting Standards.

Research Project Background

International Accounting Standards Board (IASB)

- In April 2022, the IASB added a project on the Statement of Cash Flows and Related Matters to its research pipeline based on its analysis of feedback on its Third Agenda Consultation.
- As part of its initial work on this project, the IASB will consider whether the project should aim to comprehensively review IAS 7 *Statement of Cash Flows* or make more targeted improvements.

Canadian Accounting Standards Board (AcSB)

- In June 2023, the AcSB started a research project aimed at examining the usefulness of the Statement of Cash Flows and identifying whether there are other cash flow measures more relevant to financial statement users.
- These slides summarize the AcSB staff's research findings and potential solutions that the IASB could explore when considering whether to undertake a comprehensive review of IAS 7 or make more targeted improvements.

Note: Research pipeline projects are projects that the IASB expects to start before its next five-yearly agenda consultation (i.e., within its 2022-2027 current workplan).

What Improvements Could Be Made to the Statement of Cash Flows?

Identifying Information Gaps

What we have heard

1. The Statement of Cash Flows can be improved by communicating other relevant measures more commonly used by the user community.
2. There are benefits to reporting cash flows from operating activities using the direct method or the indirect method. However, the indirect method could be supplemented with additional direct method disclosures to make it more informative to users.
3. For banks and insurance companies, the Statement of Cash Flows provides limited useful information given the focus on solvency (specific regulatory requirements must be met), and the fact that cash plays a different role in their business models compared to non-financial companies. However, the Statement of Cash Flows is not irrelevant. Therefore, only targeted improvements should be considered given that the Statement of Cash Flows will not be heavily relied upon by users in the financial services sector.

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What Improvements Could Be Made to the Statement of Cash Flows? (Cont'd)

Other issues

1. There needs to be more transparency to non-cash transactions (for example, supply chain financing).
2. There is diversity in practice regarding how specific types of transactions are classified (for example, business combinations, factoring of trade receivables, and sale and leaseback transactions).
   - Comparability is an issue, so guidance is needed.
   - That said, classification as operating, investing or financing activities could depend on the nature of the transaction.
3. There is inconsistency with what entities consider as working capital.

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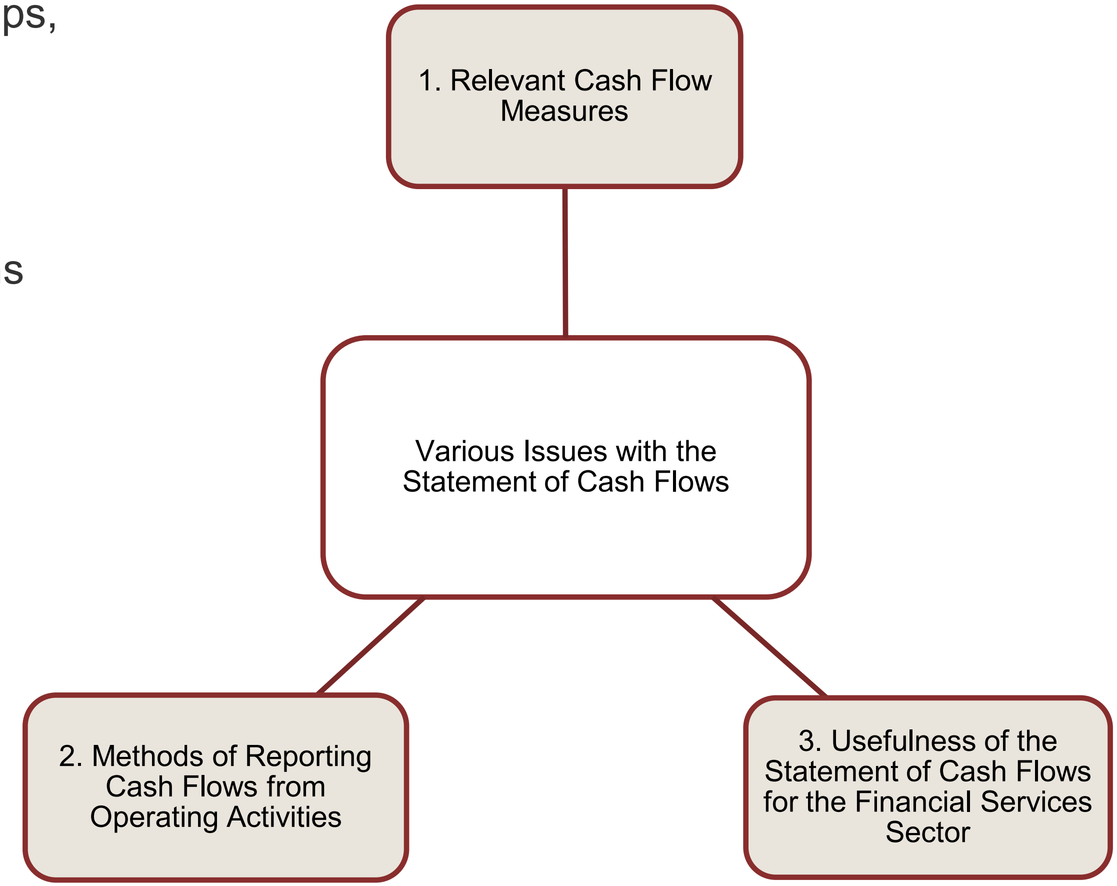
Deeper Dive into Specific Topic Areas

Reflecting on the information gaps, we first looked at three areas to understand:

1. Why is there a problem?
2. Are there potential solutions worth exploring?



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Relevant Cash Flow Measures

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Information Gathered

We performed research to determine what other relevant cash flow measures companies may report to their users, and what users may consider in addition to cash flows from operating activities. This research included sampling companies in Canada and beyond to understand what might be reported in annual reports and investor packages, and consulting with our User Advisory Committee.

Our research identified three cash flow measures that would be helpful to provide in the financial statements:

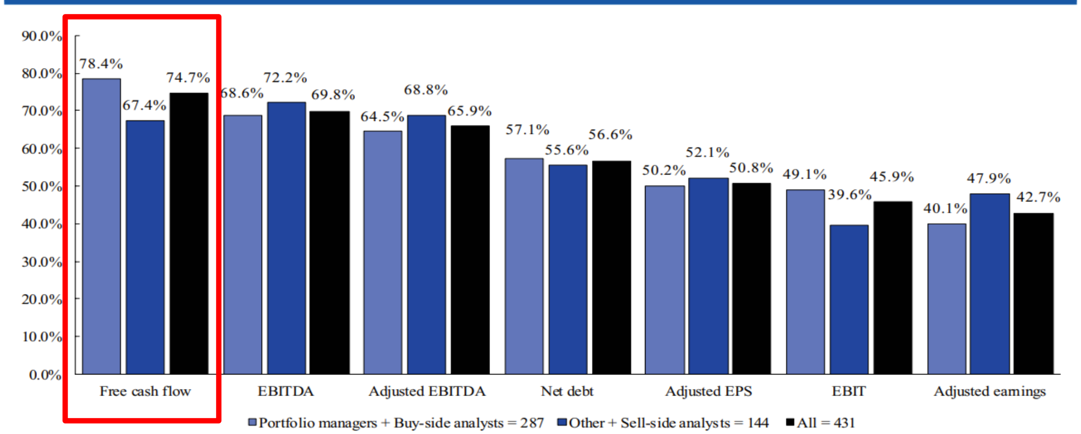
1. Free cash flow – improve comparability to how this measure is calculated.
2. Capital expenditures – require disclosure of an entity's capital expenditures or operating expenditures to understand sustaining and expansion activities, as applicable to capital intensive or service-type entities.
3. Alternative measure to cash equivalents – the definition of cash equivalents in IAS 7 may not be appropriate in today's market.

Our findings are described in slides 8–15.

1. Free Cash Flow Measure

- In a study conducted by the CFA Institute in 2016, a member survey revealed that for “buy-side analyst and portfolio manager” respondents, free cash flow is the most used non-GAAP financial measure, followed by EBITDA.

Figure 2.4. Investor Use of Different NGFMs



Source: CFA Institute, Investor Uses, Expectations, and Concerns of Non-GAAP Financial Measures, September 2016

- Securities regulators in Canada and the U.S. have also often cited free cash flow as a common non-GAAP measure.
- Many credit rating agencies, such as Moody’s Investors Services, S&P Global Ratings and Fitch Ratings, consider free cash flow in their rating methodologies.

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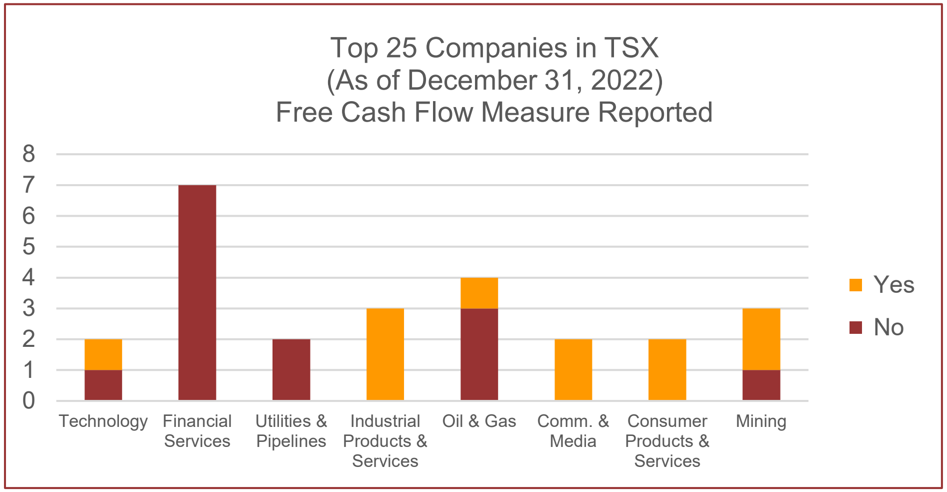
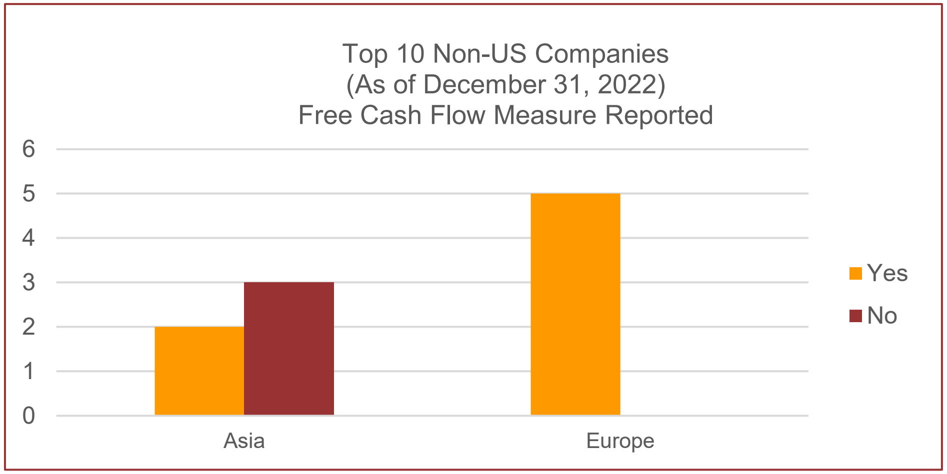
Free Cash Flow Reported – Sampled Companies in Canada & Beyond

Observations

- In Canada, certain sectors such as industrial products, consumer products, communications and mining commonly report free cash flow measures. Financial services was distinctly different from other sectors.
- Of the top 10 largest non-U.S. companies, a majority also report a free cash flow measure.
- Free cash flow could be generally understood as: Operating cash flow minus capital expenditures.* However, there is diversity in the computation of free cash flow.





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* Source: Investopedia

Diversity in Free Cash Flow Calculation – Canadian Examples

Communications & Media

This company uses this free cash flow measure because it helps assess its ability, over the long term, to create value for shareholders as it represents cash available to repay debt, pay common dividends and fund share repurchases and acquisitions.

Reconciliation of Net Cash Provided by Operating Activities to Free Cash Flow

	Three months ended December 31,		Year ended December 31,	
(millions of U.S. dollars)	**2022**	2021	**2022**	2021
Net cash provided by operating activities	**676**	397	**1,915**	1,773
Capital expenditures	**(135)**	(123)	**(595)**	(487)
Other investing activities	**1**	25	**88**	81
Payments of lease principal	**(15)**	(44)	**(65)**	(109)
Dividends paid on preference shares	**(1)**	-	**(3)**	(2)
Free cash flow	**526**	255	**1,340**	1,256

Consumer Products & Services

This company believes that free cash flow is the appropriate measure in assessing the company's cash available for additional financing and investing activities.

Free Cash Flow(2)

	2022 (52 weeks)			
For the years ended December 31, 2022 and January 1, 2022 (millions of Canadian dollars)	**Retail**	**Financial Services**	**Eliminations(i)**	**Total**
Cash flows from (used in) operating activities	**$ 5,133**	**$ (444)**	**$ 66**	**$ 4,755**
Less:				
Capital investments	**1,538**	**33**	**—**	**1,571**
Interest paid	**278**	**—**	**66**	**344**
Lease payments, net	**1,312**	**—**	**—**	**1,312**
Free cash flow(2)	**$ 2,005**	**$ (477)**	**$ —**	**$ 1,528**

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Diversity in Free Cash Flow Calculation – Canadian Examples (Continued)

Industrial Products and Services

This company describes free cash flow as a useful measure of liquidity as it demonstrates the company's ability to generate cash for debt obligations and for discretionary uses such as payment of dividends, share repurchases and strategic opportunities.

In millions	*Year ended December 31,*	**2022**
Net cash provided by operating activities	$	**6,667**
Net cash used in investing activities		**(2,510)**
Net cash provided before financing activities		**4,157**
Adjustments:		
Cash income taxes for merger transaction-related payments and cash receipts (1)		**102**
Transaction-related costs (2)		**–**
Advance for acquisition (3)		**–**
Refund of advance for acquisition (3)		**–**
Merger termination fee (3)		**–**
Acquisition, net of cash acquired (4)		**–**
Total adjustments	$	**102**
Free cash flow	$	**4,259**

Mining

This company uses this measure because management believes this to be a useful indicator of its ability to operate without reliance on additional borrowing or usage of existing cash.

RECONCILIATION OF NET CASH PROVIDED BY OPERATING ACTIVITIES TO FREE CASH FLOW

	For the three months ended		For the years ended		
($ millions)	**12/31/22**	**9/30/22**	**12/31/22**	**12/31/21**	**12/31/20**
Net cash provided by operating activities	**795**	758	**3,481**	4,378	5,417
Capital expenditures	**(891)**	(792)	**(3,049)**	(2,435)	(2,054)
Free cash flow	**(96)**	(34)	**432**	1,943	3,363

RECONCILIATION OF THE CLASSIFICATION OF CAPITAL EXPENDITURES

	For the three months ended		For the years ended		
($ millions)	**12/31/22**	**9/30/22**	**12/31/22**	**12/31/21**	**12/31/20**
Minesite sustaining capital expenditures	**557**	571	**2,071**	1,673	1,559
Project capital expenditures	**324**	213	**949**	747	471
Capitalized interest	**10**	8	**29**	15	24
Total consolidated capital expenditures	**891**	792	**3,049**	2,435	2,054

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2. Capital Expenditures Measure

Input from the AcSB's User Advisory Committee

- Information that segregates capital expenditures between those for sustaining operations and those for growth is important to users when analyzing a company's performance.
  - This information facilitates an understanding of whether a company's actions are consistent with its business plan (for example, a company that plans for growth, but makes no investments in capital expenditures, may be a concern).
  - For mergers and acquisitions, it is also helpful to understand whether the transaction is for growth or maintaining operations.
- Even if the information is subjective, users would rather management present its view in the financial statements and then users can make their own adjustments accordingly.
- This information is also important for non-capital-intensive companies, except that the focus would be on non-capital expenditures (for example, growth in human capital for service-type companies reflected through higher selling, general and administrative expenses).

Disclosure of Capital Expenditures

Observations

- IAS 7 encourages this type of disclosure but does not require it (IAS 7.50–51).
- We sampled 25 companies in Canada and found that the disclosure of capital expenditures between maintaining vs. growing operations is not commonly found.
- To the right are two examples of disclosures identified. The level of detail provided varies.

Mining

(millions of US dollars)	2022	2021
Cash used in investing activities	(2,901)	(1,807)
Sustaining capital expenditures	1,449	1,247
Mine development and pre-stripping capital expenditures	234	156
Borrowing costs on property, plant and equipment	(37)	(29)
Other [1]	12	(64)
Net changes in non-cash working capital [1]	44	(101)
Growth capital	(1,199)	(598)

1 Included in investing activities as per the consolidated statement of cash flows.

Oil & Gas

Net capital expenditures for 2022 were $5,471 million compared with $4,908 million for 2021. Net capital expenditures for 2022 included base capital expenditures [(1)] of $3,956 million and strategic growth capital expenditures [(1)] of $1,045 million, in accordance with the Company's capital budget. The Company also completed strategic acquisitions [(1)] of $470 million during 2022.

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3. Cash Equivalents vs. Other Measure

Observations

- A Discussion Paper titled *Improving the Statement of Cash Flows* suggested that the Statement of Cash Flows should be required to report inflows and outflows of cash, rather than cash and cash equivalents, and that the Statement of Cash Flows should contain a separate section that reports cash flows relating to the management of liquid resources.*
- We sampled the top 25 entities in the TSX and observed a few entities providing a liquidity measure that communicates the resources available to meet liquidity needs, which includes items beyond cash and cash equivalents.

Oil & Gas

LIQUIDITY

Liquidity is a non-GAAP financial measure that represents the availability of readily available undrawn bank credit facilities, cash and cash equivalents, and other highly liquid assets to meet short-term funding requirements and to assist in assessing the Company's financial position. The Company's calculation of liquidity is presented below.

($ millions)		**2022**		2021		2020
Undrawn bank credit facilities	**$**	**5,520**	$	6,098	$	4,958
Cash and cash equivalents		**920**		744		184
Investments		**491**		309		305
Liquidity	**$**	**6,931**	$	7,151	$	5,447

Consumer Products & Services

Available liquidities. This measure represents Cash and cash equivalents plus amounts available under our term revolving unsecured operating credit facility. This measure is considered useful to evaluate our ability to meet our liquidity needs for the foreseeable future.

The table below reconciles Cash and cash equivalents, as per IFRS, with available liquidities:

(in millions of US dollars)	**As at April 24, 2022**	As at April 25, 2021	As at April 26, 2020
Cash and cash equivalents	**2,143.9**	3,015.8	3,641.5
Add: Unused portion of the term revolving unsecured credit facility	**2,525.0**	2,525.0	1,025.0
Less: Letters of credit reducing the amount that may be borrowed on the term revolving unsecured operating credit facility	**(6.7)**	(6.8)	(11.9)
Available liquidities	**4,662.2**	5,534.0	4,654.6

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* Source: "Improving the Statement of Cash Flows", A Discussion Paper prepared by staff of the UK Financial Reporting Council, October 2016

Cash Equivalents vs. Other Measure (Continued)

- We also observed that, because of the highly regulated environment that financial institutions operate within, their disclosures on how they manage their liquidity risks are extensive. Liquid assets are a common disclosure found in the MD&A of Canadian banks to explain what they hold to meet their liquidity requirements. For example:

Liquid Assets

(Canadian $ in millions)	As at October 31, 2022 Bank-owned assets	Other cash and securities received	Total gross assets (1)	Encumbered assets	Net unencumbered assets (2)	As at October 31, 2021 Net unencumbered assets (2)
Cash and cash equivalents	**87,466**	**–**	**87,466**	**87**	**87,379**	93,151
Deposits with other banks	**5,734**	**–**	**5,734**	**–**	**5,734**	8,303
Securities and securities borrowed or purchased under resale agreements						
Sovereigns / Central banks / Multilateral development banks	**143,094**	**101,481**	**244,575**	**132,635**	**111,940**	76,410
NHA mortgage-backed securities and U.S. agency mortgage-backed securities and collateralized mortgage obligations	**54,601**	**5,565**	**60,166**	**20,188**	**39,978**	40,422
Corporate and other debt	**22,560**	**19,328**	**41,888**	**8,190**	**33,698**	35,330
Corporate equity	**53,007**	**50,926**	**103,933**	**63,967**	**39,966**	48,509
Total securities and securities borrowed or purchased under resale agreements	**273,262**	**177,300**	**450,562**	**224,980**	**225,582**	200,671
NHA mortgage-backed securities (reported as loans at amortized cost) (3)	**21,881**	**–**	**21,881**	**5,277**	**16,604**	15,126
Total liquid assets	**388,343**	**177,300**	**565,643**	**230,344**	**335,299**	317,251

(1) Gross assets included bank-owned assets and cash and securities received from third parties.
(2) Net unencumbered liquid assets are defined as total gross assets less encumbered assets.
(3) Under IFRS, National Housing Act (NHA) mortgage-backed securities that include mortgages owned by BMO as the underlying collateral are classified as loans. Unencumbered NHA mortgage-backed securities have liquidity value and are included as liquid assets under BMO's Liquidity and Funding Risk Management Framework. This amount is shown as a separate line item, NHA mortgage-backed securities.

- These examples illustrate that the definition of cash equivalents in IAS 7 is often different compared to an entity's view of its liquid resources.

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Summary: Relevant Cash Flow Measures

Problems identified

- Various user groups (for example, buy-side, sell-side, portfolio managers, credit rating agencies) use free cash flow in their analysis, but there is diversity in the way this non-GAAP measure is computed and disclosed (slides 8–11).
- Information on expenditures for sustaining operations compared to growing operations is missing in the financial statements, and this is another key measure that users have expressed the need for more transparency (slides 12–13).
- The definition of cash equivalents in IAS 7 may not appropriately reflect what entities consider as liquid resources to meet their short-term requirements (slides 14–15).

Potential solutions to explore

- Extend the disclosure requirements in IFRS 18 *Presentation and Disclosure in Financial Statements* for management-defined performance measures to the Statement of Cash Flows. These requirements should add transparency to the computation of other cash flow measures and increase discipline in their use.
- Amend IAS 7 to require disclosing cash flows that represent increases in operating capacity and cash flows that are required to maintain operating capacity.
- Remove the concept of cash equivalents in IAS 7 and explore developing another measure for communicating what are an entity's available liquid assets or funding sources to meet its liquidity needs.

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Methods of Reporting Cash Flows from Operating Activities

Information Gathered

IAS 7 Requirements

Entities are allowed to report cash flows from operating activities using either:

a) the direct method, whereby major classes of gross cash receipts and gross cash payments are disclosed; or

b) the indirect method, whereby profit or loss is adjusted for the effects of transactions of a non-cash nature, any deferrals or accruals of past or future operating cash receipts or payments, and items of income or expense associated with investing or financing cash flows.

Academic Research

- We reviewed academic studies that examined reporting cash flows from operating activities using the direct method or indirect method.
- Archival academic literature has overall documented that the direct method is more useful to users than the indirect method, as it leads to better prediction of future firm performance. However, results from experimental studies that investigated how the reporting methods affect users' decisions show mixed conclusions.

Input from User Advisory Committee

- We sought input from users, and they expressed that there are pros and cons to each reporting method.
- We conducted a survey, and the results showed that providing supplemental information to the indirect method will enhance the usefulness of the Statement of Cash Flows.

Our findings are described in slides 19–30.

Academic Research: Literature Review

Overall, archival academic literature has documented that the direct method to report cash flows from operating activities is more useful to users than the indirect method, as it leads to better prediction of future firm performance (cash flows or earnings) and a stronger association with share prices.[1,2]

While the data analyzed mostly comes from the US, several studies have focused on Australia, where the direct method was mandatory until July 2007. These studies show that the direct method is value relevant both under the Australian Generally Accepted Accounting Principles and after the adoption of IFRS.[3] In addition, the direct method has been found to enhance the predictive ability of aggregate operating cash flows, using data from Australia.[4]

However, there is also evidence that the indirect method can be decision useful. Studies based on Australian[5] and Chinese[6] samples indicate that the indirect method is better than the direct method to forecast cash flows from operations.

In addition, some researchers call for a critical analysis of these results, arguing that academic research is statistical in nature and unlikely to lead to conclusive answers, especially with respect to cost-benefit considerations.[7]

Researchers also note that these studies entail self-selection and estimation problems as firms do not usually present their operating cash flows under both methods. It is therefore necessary to derive the other presentation method (not used by the entity), potentially causing estimation errors.[8]

More importantly, researchers note that these archival approaches do not address how investors use the information in their decision-making processes.[9,10]

Academic Research: Experimental Studies

There are few experimental studies that have investigated how the reporting methods affect users' decisions, and their results show mixed conclusions.

Decision usefulness

- Three studies directly examine the decision usefulness of the direct versus indirect method for users' lending decisions.
- These studies either show that the direct method leads to more consistent decisions or that there is no difference between the two methods,[11,12] and that most of the subjects obtains their information from other financial statements than the Statement of Cash Flows.[13]

Forecasting

- As for forecasting, a recent experimental study demonstrates that there are benefits for the indirect method, as it leads to lower forecasting errors in the presence of nonrecurring accrued expenses.[14]
- Results also show that there is no difference in forecasting errors between participants provided with the indirect method and those provided with the indirect and the direct method (while the combination of the two methods lead to less forecasting errors than the direct method only).

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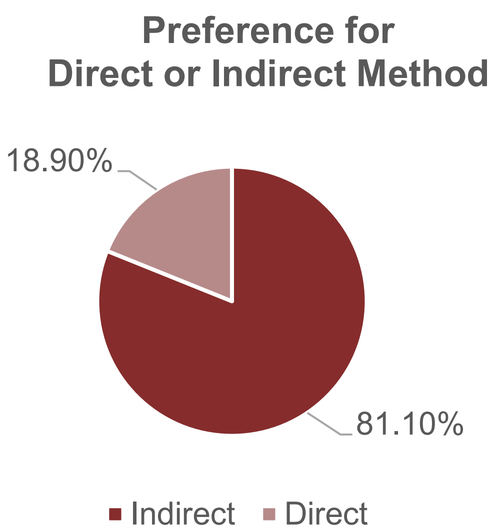
Academic Research: Comment Letters



- Focusing more specifically on standard-setting activities, an academic paper analyzing the comment letters received to the joint FASB-IASB Discussion Paper *Preliminary Views on Financial Statement Presentation* issued in 2008 shows a strong support for the indirect method.[15]
- Of the 180 comment letters that commented on the direct or indirect method, 81.1% expressed a preference for the indirect method.
- Results also show stronger support for the direct method in countries where this method is or has been mandated in the past. For example, 75% (3 out of 4 letters) of New Zealander respondents favored the direct method, while only 20% (3 out of 15 letters) of Canadian respondents expressed the same opinion.
- While substantially more preparers responded than users (153 vs 27 respondents), only 15.7% of preparers and 37% of users preferred the direct method.

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User Advisory Committee

In addition to the diverse views documented by the academic literature, we have heard mixed feedback on the two methods currently allowed under IFRS Accounting Standards to report cash flows from operating activities.

	Indirect Method	Direct Method
Pros	• Reconciles net income to cash flows from operating activities (useful for credit investors in their cash flow ratio analysis and for equity investors in their valuation modelling). • Provides insights into working capital changes and reinvestments in working capital. • Helps identify non-cash items, some of which may be non-recurring items (for example, stock-based compensation). • Easier to prepare as information derived from line items in the Statement of Financial Position and Statement(s) of Financial Performance.	• More intuitive to understand because provides information on actual cash transactions. • Provides better disaggregation of the main streams of cash flows (for example, receipts from customers, payments to suppliers and payments to employees) to communicate an entity's sources and uses of cash. • Offers a detailed view of cash inflows and outflows, making it easier for analysts to assess the quality of earnings. • Enhances the ability to forecast future cash flows by revealing trends in specific categories of cash receipts and payments.
Cons	• Less intuitive to understand given the reconciling items between net income and cash flows from operating activities. • Can be less transparent as actual cash flows are within the adjustments, so additional analysis needed to fully understand. • Less disaggregated information, making it hard to identify main streams of cash flows (for example, receipts from customers, payments to suppliers, and payments to employees) and understand an entity's sources and uses of cash. • Provides less detail on the specifics of cash movements, such as who the cash was received from or paid to, making the analysis of operational efficiency more complex.	• Does not reconcile net income to cash flows from operating activities, making it difficult to understand the relationship between a measure of operating performance and cash generation. • Does not identify working capital changes and reinvestment needs in working capital. • Does not provide insights into non-cash items or non-recurring items. • More costly to prepare because system changes required to capture information to provide under the direct method.

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Conducting Survey on Other Reporting Options

Based on the mixed feedback received, we conducted a survey on the following five options to determine if there is a particular option that would better suit users' needs:

1. Require the direct method only, with format enhancements showing sources and uses of cash.
2. Require the direct method in the primary financial statements, with a reconciliation to net income in the notes.
3. Require the indirect method only.
4. Require the indirect method in the primary financial statements, with supplemental disclosures of certain direct method information.
5. Keep a choice between using the direct method and indirect method but requiring improvements to each method.

Results: 13 survey responses were received from the AcSB's User Advisory Committee. The results are summarized on slide 24, with further details on slides 25–29.

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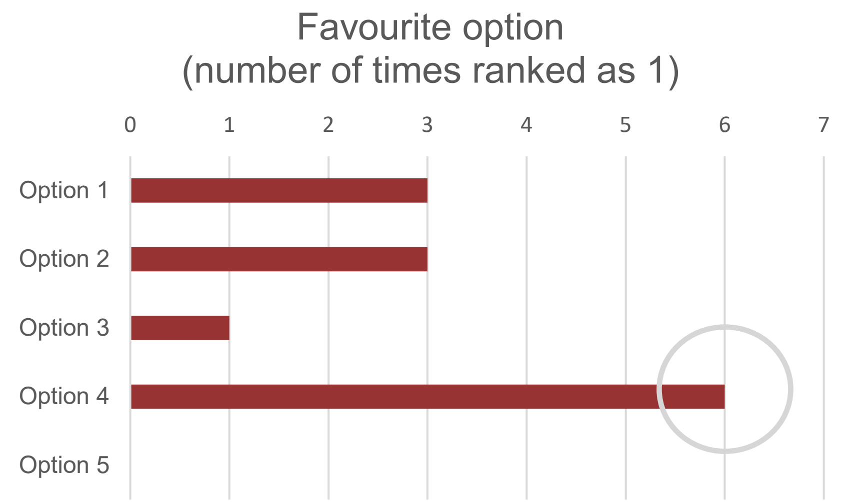
Summary of Survey Results

Observations

- Option 4 was the preferred option because users thought the information provided by the indirect method is important to be on the face of the Statement of Cash Flows. They supported complementing the indirect method with supplemental disclosures of certain direct method information.
- Some users did prefer the direct method, as shown by the rankings of options 1 and 2, which confirms that there is a mix of preference for indirect and direct methods of reporting.
- It is interesting to note that users do not prefer a choice in reporting methods, even if both methods were improved (option 5). However, we think the mixed preference makes it challenging to eliminate either option that currently exists in IAS 7.
- 92% of respondents indicated that IAS 7 should be amended to change the way cash flows from operating activities are reported.



Legend: Options with Description	
1	Require the direct method only, with format enhancements showing sources and uses of cash.
2	Require the direct method in the primary financial statements, with a reconciliation to net income in the notes.
3	Require the indirect method only.
4	Require the indirect method in the primary financial statements, with supplemental disclosures of certain direct method information.
5	Keep a choice between using the direct method and indirect method but requiring with improvements to each method.

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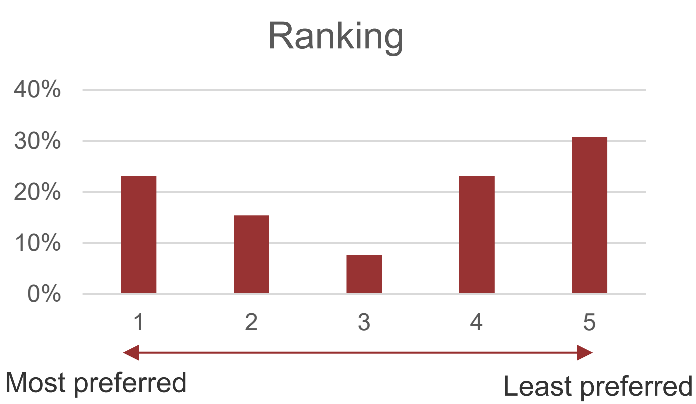
Details of Survey Results

Option 1: Require the direct method only, with format enhancements showing sources and uses of cash

Feedback received

- **Mixed feedback**
- Ranked as first choice by 23% respondents
- Ranked as last choice by 31% respondents



	20XY		
	Sources	**Uses**	**Total**
Operating activities			
Receipts from customers	443,822		443,822
Payments to suppliers		(322,635)	(322,635)
Payments to employees		(84,372)	(84,372)
Income tax paid		(7,337)	(7,337)
Net cash flows from operating activities	**443,822**	**(414,344)**	**29,478**
Investing activities			
Proceeds from sale of property, plant and equipment	4,975		4,975
Purchase of property, plant and equipment		(25,417)	(25,417)
Purchase of investment properties		(3,040)	(3,040)
Purchase of financial instruments		(680)	(680)
Proceeds from sale of financial instruments	820		820
Purchase of intangible assets		(1,467)	(1,467)
Acquisiton of a subsidiary, net of cash acquired	575		575
Interest received	625		625
Receipt of government grants	7,377		7,377
Net cash flows used in investing activities	**14,372**	**(30,604)**	**(16,232)**
Financing activities			
Proceeds from exercise of share options	437		437
Acquisition of non-controlling interests		(812)	(812)
Transaction costs of issue of shares		(80)	(80)
Payment of principal option of lease liabilities		(1,015)	(1,015)
Proceeds from borrowing	14,122		14,122
Repayment of borrowings		(5,080)	(5,080)
Interest paid		(2,667)	(2,667)
Dividends paid to equity holders of the parent		(4,947)	(4,947)
Dividends paid to non-controlling interests		(75)	(75)
Net cash flows from/ (used in) financial activities	**14,559**	**(14,676)**	**(117)**
Total sources/ (uses) of cash and cash equivalents	**472,753**	**(459,624)**	
Net increase in cash and cash equivalents			13,129
Net foreign exchange difference			848
Cash and cash equivalents at January 1			30,665
Cash and cash equivalents at December 31			**44,642**

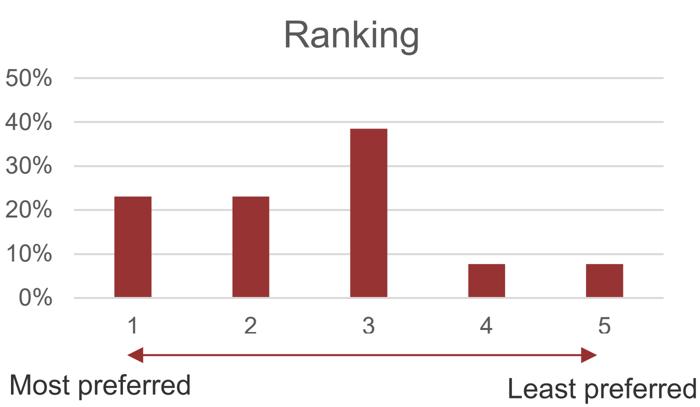
Direct method of reporting for cash flows from operating activites and explicitly showing columns for sources and uses of cash across all three categories of cash flows

Details of Survey Results

Option 2: Require the direct method in the primary financial statements, with a reconciliation to net income in the notes

Feedback received

- **Option having some support**
- Ranked as first choice by 23% respondents
- Ranked as second choice by 23% respondents
- Ranked as third choice by 38% respondents



	Notes	2023 $M	2022 $M
Cash flow from operating activities			
Cash was provided from:			
Receipts from customers		593.3	287.0
Interest received		3.2	0.3
		596.5	287.3
Cash was applied to:			
Payments to suppliers and employees		(213.5)	(134.6)
Income tax paid/(received)		-	-
Interest paid		(57.9)	(51.5)
		(271.4)	(186.1)
Net cash flow from operating activities	6	325.1	101.2

6. Reconciliation of profit after taxation with cash flow from operating activities

	2023 $M	2022 $M
Profit after taxation	43.2	191.6
Non-cash items		
Depreciation	145.3	113.1
Deferred taxation expense	(19.2)	(22.1)
Share-based payments	0.1	-
Fixed asset write-offs and impairment	5.1	6.9
Reversal of fixed asset impairment	(1.0)	-
Equity-accounted (earnings)/loss from associate and joint ventures	(11.1)	12.8
Property, plant and equipment fair value revaluation	15.6	1.4
Investment property fair value decrease/(increase)	139.7	(204.4)
Derivatives fair value (increase)/decrease	0.7	(1.7)
Items not classified as operating activities		
Gain on asset disposals	3.4	-
Decrease/(increase) in provisions and property, plant and equipment retentions and payables	(39.4)	25.5
(Increase)/decrease in investment property retentions and payables	(16.4)	1.2
Increase in investment property lease incentives and receivables	(12.5)	(11.4)
Items recognised directly in equity	0.5	0.9
Movement in working capital		
(Increase)/decrease in trade and other receivables	(23.1)	(3.1)
(Increase)/decrease in taxation receivable	20.2	(0.7)
(Decrease)/increase in accounts payable and provisions	73.8	(9.3)
Increase in other term liabilities	0.2	0.5
Net cash flow from operating activities	325.1	101.2

Details of Survey Results

Option 3: Require the indirect method only

Consolidated Statements of Cash Flows

53 and 52 Weeks Ended (in millions of Canadian dollars)	**May 7, 2022**	May 1, 2021
Operations		
Net earnings	**$ 811.3**	$ 764.2
Adjustments for:		
Depreciation	**872.3**	768.7
Income tax expense	**270.3**	265.9
Finance costs, net (Note 22)	**282.1**	269.4
Amortization of intangibles	**94.8**	75.6
Net gain on disposal of assets	**(23.1)**	(37.1)
Net gain on lease terminations	**(47.0)**	-
Impairment (reversals) losses of non-financial assets, net	**(7.4)**	1.6
Amortization of deferred items	**1.8**	2.2
Equity in earnings of other entities, net of distributions received	**9.5**	35.7
Employee future benefits	**(12.0)**	(8.4)
Decrease in long-term provisions	**(0.7)**	(10.5)
Equity based compensation	**14.6**	11.8
Net change in non-cash working capital	**(46.8)**	(80.9)
Income taxes paid, net	**(112.6)**	(198.6)
Cash flows from operating activities	**2,107.1**	1,859.6

Feedback received

- **Option in the middle**
- Ranked as second choice by 23% respondents
- Ranked as third choice by 23% respondents
- Ranked as fourth choice by 38% respondents

Details of Survey Results

Option 4: Require the indirect method in the primary financial statements, with supplemental disclosures of certain direct method information

Note X - Supplemental cash flow disclsoures

Below are supplemental gross inflows and outflows of the company for the year ended

	20XY	
Cash received from customers	$ 1,000,000	*Note: potential new disclosure*
Cash paid to suppliers	(500,000)	*Note: potential new disclosure*
Cash paid to employees	(200,000)	*Note: potential new disclosure*
Cash paid for income taxes	(50,000)	*Note: currently required by IAS 7*
Cash paid for interest	(20,000)	*Note: currently required by IAS 7*

Feedback received

- **Preferred option**
- Ranked as first choice by 46% respondents
- Ranked as second choice by 31% respondents

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Details of Survey Results

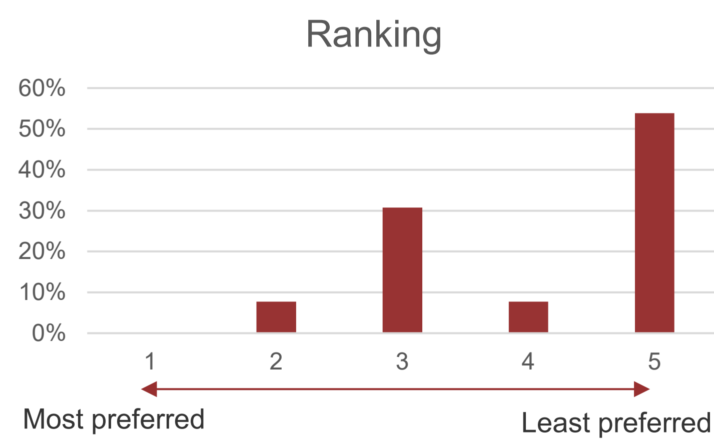
Option 5: Keep a choice between using the direct method and indirect method but require improvements to each method

The improvements could be those described in:

- Option 1 (*require the direct method only, with format enhancements showing columns for sources and uses of cash*);
- Option 2 (*require the direct method in the primary financial statements, with a reconciliation to net income in the notes*); and
- Option 4 (*require the indirect method in the primary financial statements, with supplemental disclosures of certain direct method information*).

Feedback received

- **Least preferred option**
- Ranked as last choice by 54% respondents)



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Other Comments from Users

Input from the AcSB's User Advisory Committee

- Although the direct method may be better in theory, most users thought that the indirect method provides valuable information (for example, changes in non-cash items and in working capital). The indirect method is also useful to predict recurrent and future cash flows.
- The indirect method is more prevalent in Canada. Therefore, users accustomed to the indirect method expressed concerns that the direct method might not provide sufficient benefits to justify a change and noted that their models are based off the indirect method. Although providing supplemental direct method information is helpful, users understand that there are costs involved from entities to provide this information.
- A few users also noted that in some sectors, the direct method is used. Therefore, these users thought that having a choice in IAS 7 on the method to report cash flows from operating activities is reasonable as the same method is generally used within a sector or subsector.
- Finally, users indicated that they prefer information to be included in the primary financial statements rather than in the notes because the databases they use often capture information more accurately from the primary financial statements than from the notes.

Summary: Methods of Reporting Cash Flows from Operations

Problems identified

- Academic studies and user feedback point to diverse views on the usefulness of the current reporting options allowed under IAS 7. Some prefer the direct method, while others argue that the indirect method is better (slides 19–21).
- Based on the survey conducted, there is support to enhance the information provided under the indirect and direct method. Most of the AcSB's User Advisory Committee members prefer the indirect method supplemented with certain direct method information (slides 22–30).

Potential solutions to explore

- Keep the current choice between the direct and the indirect method.
- Based on data from our jurisdiction that predominantly uses the indirect method, explore requiring supplemental disclosures of certain direct method information to complement the indirect method. Some entities may already provide this information via other standards like cash flow information disclosed in reconciliations of insurance contracts.

Usefulness of the Statement of Cash Flows for Financial Services Sector

Information Gathered

We conducted interviews with users and preparers from the financial services sector to better understand why there is a general view that the Statement of Cash Flows is not useful.

We also searched for any relevant academic research that examined whether the Statement of Cash Flows in the financial services sector provided useful information.

Our findings are described in slides 34–40.

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Why is the Statement of Cash Flows of Limited Use to the Financial Services Sector?

- We understand from analysts that, given the strong regulatory nature of the financial services sector, the focus on solvency is greater than on liquidity.
  - In addition to maintaining regulatory capital ratios, banks can access central banks or capital markets for cash, as long as they are solvent. Therefore, there is less focus on a bank's cash position.
  - Insurers must also maintain regulatory capital ratios. While an insurance company could have liquidity problems due to mispricing of a risk, it would usually adjust premiums for subsequent products underwritten (or be required to do so by its regulator) before liquidity potentially becomes an issue.
- We have also heard that the Statement of Cash Flows is not representative of the underlying nature of the banking and insurance businesses.
  - There are too many adjustments that must be made to the Statement of Cash Flows for it to be useful for analysts in this sector.
  - The Statement(s) of Financial Performance better reflects the economics of this sector because it uses accrual accounting, which explains why it is preferred by analysts to evaluate entities in this sector.
  - Slide 35 describes the unique business models of banks and insurers.

Understanding the Role of Cash in the Business Models of Banks and Insurers

Banks

Cash movements are not helpful in understanding how a bank's decisions will affect its future profitability and ability to generate cash. Elements that have a negative impact on cash flows (e.g., increase in loans), may be beneficial to future returns and vice versa.

In addition, several non-cash elements (for example, provision for credit losses), are crucial to understand the risk a bank is undertaking and the impact on its returns.

The banking sector is also not capital-intensive like other industries.

As a result, the Statement of Financial Position and Statement(s) of Financial Performance are more useful than the Statement of Cash Flows to understand the composition and the quality of assets and liabilities, and the bank's future profitability.

Insurers

In the insurance sector, the timing of cash movements is unique. Cash inflows (premiums) and outflows (claims) are clustered: premiums can be received upfront, and claims paid out later.

For life insurers, net income is highly volatile due to the long tail nature of the assets and liabilities and their sensitivity to changes in actuarial assumptions and interest rates. Entities report core earnings, an income metric that is more representative of the long-term trends and expected returns.

While it is less extreme than for life insurers, cash movements can also be volatile in the property and casualty business due to long tail claims. However, the expense is provisioned over time in the Statement(s) of Financial Performance.

Consequently, users focus on the Statement(s) of Financial Performance rather than the Statement of Cash Flows as it better represents the run rate of the business.

Financial Services Entities: Key Metrics

In Canada, analysts also noted the following key metrics for financial services entities:

The most relevant metrics followed by analysts of the financial services sector are return on equity (ROE), earnings per share (EPS) and adjusted net income.

In terms of solvency, analysts are interested in the regulatory capital measures: common equity tier 1 capital (CET1), liquidity coverage ratio (LCR) or high-quality liquid assets (HQLA).

There is no free cash flow or distributable reserves metric in the financial services sector. The important metric is the dividend payout ratio, which is a function of adjusted net income. Cash generated is not important for future dividends, because dividends are regulated and depend on capital ratios being met. Capital ratios deteriorate if insufficient net income is generated (as it reduces retained earnings). Consequently, adjusted net income is a better indicator of future dividends than any cash flow measure.

All these metrics are based on income and the riskiness of the assets, and cash flows don't influence them.

However, analysts noted that there are inconsistencies observed in the non-GAAP measures provided by financial services entities in their MD&A. They think it could be helpful to require disclosures in the notes to the financial statements of these metrics, to add transparency and discipline in their use.

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Statement of Cash Flows – Limited Usefulness but not Irrelevant

While recognizing that the Statement of Cash Flows has limited usefulness in evaluating financial services entities, there is still value derived from this statement because of the following:

Insights on liquidity

- Although the focus on solvency is greater than on liquidity in the financial services sector, investors still need to assess for liquidity risk. The Statement of Cash Flows does provide some insights to an entity's liquidity position and a clear reconciliation of the cash balance.
- Regulators require entities to report on liquidity ratios, but often these are non-GAAP metrics (as noted earlier in slide 36) and they could benefit from added transparency and discipline in their use.

Validation tool

- The Statement(s) of Financial Performance is more relevant to understand the business; however, it relies on estimations, which could be prone to subjectivity and errors.
- The Statement of Cash Flows is useful for users, to validate some of these estimations.
- The Statement of Cash Flows is also appreciated by preparers as a control measure, to ensure that all the transactions have been appropriately recorded.

Relevant information

- While the Statement of Cash Flows is less important, it still provides relevant information, such as:
  - contingent consideration paid for acquisitions;
  - interest and dividends paid, which can be materially different from accruals;
  - capital raised less buybacks;
  - stock options exercised; and
  - certain working capital items.

Mixed activities

- Many insurers and banks have other activities such as material asset management arms.
- Analysts want to see the cash inflows and outflows for these activities. Therefore, the Statement of Cash Flows is relevant in such cases.

Statement of Cash Flows – Limited Usefulness but not Irrelevant

Input from preparers in the financial services sector

- Preparers noted that no questions are asked on the Statement of Cash Flows during earnings calls, which is an indication that this statement is not heavily relied upon by analysts.
- While acknowledging that the Statement of Cash Flows has limited use, preparers thought that entities in the financial services sector *should not* be exempted from producing this statement. It still provides complementary and validating information and is viewed as a control measure to have in place. Regulators will also likely continue requiring the Statement of Cash Flows.
- There were concerns around the benefits of developing a different Statement of Cash Flows for banks and insurers.
  - Users understand that the Statement of Cash Flows is not the main statement to analyze the performance of banks and insurers. Therefore, investing to change this statement may not result in better information since cash plays a different role in their business models.
  - There is also a scoping risk for entities that may have a mix of financing and/or insurance and other business activities, or for insurance entities reporting into non-insurance entities.
- Instead, it may be worth considering targeted improvements such as adding transparency to the computation of non-GAAP metrics and exploring whether some transactions are better classified in operating activities for banks and insurers. Another improvement could be to better link cash flow-related disclosures required by other standards to the Statement of Cash Flows (for example, cash flow information disclosed in reconciliations of insurance contracts).

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Shared Viewpoint Globally

The issues raised by Canadian users and preparers are echoed on the international stage. Comment letters to the joint FASB-IASB Discussion Paper *Preliminary Views on Financial Statement Presentation* issued in 2008, and participants to EFRAG consultations have raised the following points:*

Greater focus on solvency than liquidity	**Cash flows do not reflect the business**
• Cash and cash equivalents is not a relevant indicator of liquidity, especially since only historical information is provided. Capital ratios provide a more complete view on liquidity, as they consider liquid assets. • The Statement of Cash Flows has limited use in assessing liquidity and solvency risks, capital adequacy and the impact on dividends. • The frequency of publishing a Statement of Cash Flows on a quarterly or annual basis makes this statement less relevant since the solvency of a bank is challenged daily by the market.	• Performance for banks is not a main driver for the change in cash. • The Statement of Cash Flows does not provide information on the value-creation process. • Analysts ask for the recurring cash flows generated by the entity, a data point that cannot be deduced from the Statement of Cash Flows. • The disaggregation between operating, investing and financing is not meaningful for banks because assets and liabilities are often fungible due to the nature of their operations.

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* EFRAG. 2015. "The Statement of Cash Flows: Issues for the Financial Institutions" *EFRAG Short Discussion Series*

Academic Research: Literature Review

We have not identified an academic study that investigated the usefulness of the Statement of Cash Flows for Canadian entities in the financial services sector.

However, a research paper based on a sample of U.S. banks from 2004 to 2016 confirms the limited usefulness of the Statement of Cash Flows for banks.[16]

- Results suggest that the Statement of Cash Flows has limited incremental value relevance (and is much less relevant compared to industrial firms). Contrary to industrial firms, the distinction between operating, investing and financing is uninformative for the valuation of banks.
- Focusing on the 2008 financial crisis, this study finds no evidence that elements from the Statement of Cash Flows are useful to predict bank distress in the presence of standard predictors such as size, tier-1 capital ratio, non-performing loans or leverage.

The findings above are different compared to a prior U.S. study that found cash flows from operations of U.S. banks are value relevant by showing that they are predictive of future earnings and cash flows, and that they are positively associated with share prices.[17] However, that study did not compare banks to other sectors and only considered the information provided in the operating section and not the entirety of the Statement of Cash Flows.

Summary: Usefulness of the Statement of Cash Flows for Financial Services Sector

Problems identified

- The Statement of Cash Flows has limited usefulness in the financial services sector (slides 34–40):
  - There is greater focus on solvency than on liquidity given the regulatory requirements that need to be met to continue operating and declaring dividends.
  - Cash flows are also less relevant to understand the economics of the business in the financial services sector.
- While the Statement of Cash Flows has limited use, it does not mean that it is irrelevant.
- The benefits to users are likely not sufficient to justify the costs of developing a different Statement of Cash Flows for the financial services sector.

Potential solutions to explore

- As recommended on slide 16, extend similar disclosure requirements as the management-defined performance measures to the Statement of Cash Flows.
- Consider making targeted improvements to improve certain cash flow information reported by entities in the financial services sector such as exploring whether some transactions are better classified in operating activities for banks and insurers, and better linking cash flow-related disclosures required by other standards.

Overall Observations

IAS 7: Targeted Improvements or Comprehensive Review?

- Our research suggests that the Statement of Cash Flows provides useful information, except for the financial services sector. Therefore, a comprehensive review of IAS 7 is not needed.
- For the financial services sector, a comprehensive review to develop a different Statement of Cash Flows for banks and insurers is also not needed. The general view is that, while the Statement of Cash Flows has limited usefulness given the role of cash in the entity's business and the regulatory focus, the statement is not irrelevant.
- We think making targeted improvements to IAS 7 is more beneficial than performing a comprehensive review of the Standard. Our research identified that improvements are needed to:
  - bring visibility to other cash flow measures;
  - supplement the indirect method of reporting cash flows from operating activities with additional direct method information; and
  - improve certain cash flow information reported by the financial services sector.
- We acknowledge that there could be other targeted improvements to the Statement of Cash Flows to enhance comparability and address other specific issues (for example, see slide 4). Our research was limited to the three areas described in slide 5 at this time.

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Questions

1. Are the findings in this research consistent with what you are hearing in your jurisdiction?
2. Do you think targeted improvements should be made to IAS 7 instead of performing a comprehensive review of the Standard?

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Academic Research: Sources for Literature Review

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