IFRS® Accounting

# Staff paper

Agenda reference: 6

# Accounting Standards Advisory Forum meeting

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| Date | **March 2025** |
| Project | **Statement of Cash Flows and Related Matters** |
| Topic | **Initial Research Findings** |


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# Purpose of this session

- Provide a summary of the initial research findings in the project on Statement of Cash Flows and Related Matters
- Discuss initial analysis and next steps for the project in the light of the findings

# Questions for ASAF members

1. Do you have any questions or comments on the findings from our initial research?
2. Considering the initial research findings, to help the IASB consider the next steps in the project:
   a) do you agree with the topics identified as stakeholder priorities?
   b) do you think there are any detailed topics we have missed?
   c) which topics do you think would most benefit from being assessed together because of their interconnected nature?
   d) do you have any comments on the key factors we plan to consider in deciding the next steps for the project?

# Information for ASAF members

# Background

- At the December ASAF meeting we reported preliminary findings from our initial research which included:
  - feedback from the Capital Markets Advisory Committee and the Global Preparers Forum meetings in November 2024 and at the joint meeting in June 2024
  - analysis of the financial statements of a sample of companies that apply IFRS Accounting Standards
- We have now completed our initial research and reported the overall findings to the IASB at its March 2025 meeting
- After considering the initial research the IASB will decide next steps for the project

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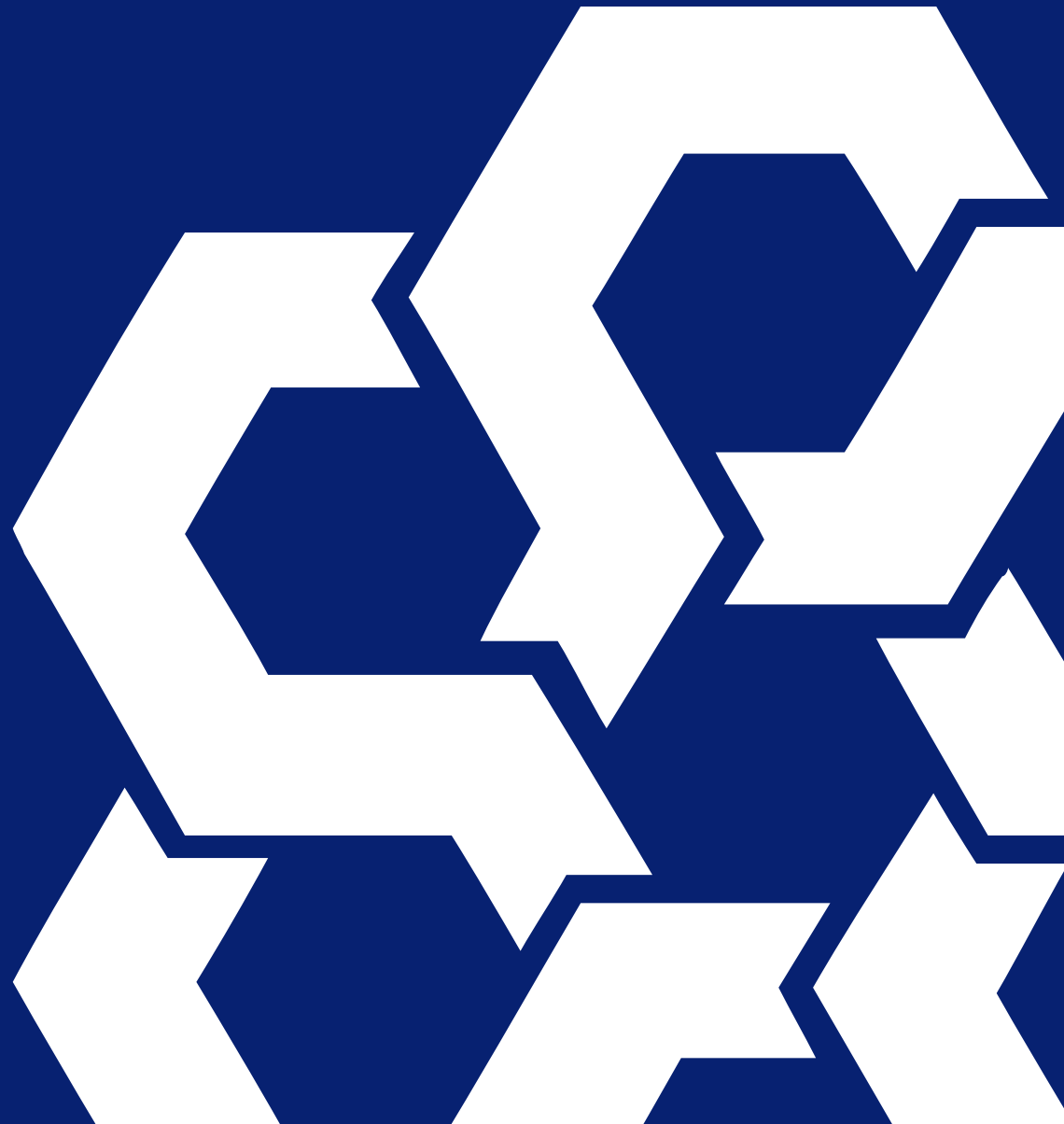
# Initial research findings



# Planned initial research activities

- The objective of the initial research was to gather evidence of **the nature and extent** of the perceived deficiencies related to the topics identified in the agenda consultation and confirmed by the academic literature review
- We have **not yet assessed the feasibility** of standard setting for each possible topic
- Initial research included:
  - Consultative group meetings
  - Financial statement analysis
  - Individual stakeholder meetings
  - Review of NSS projects
  - Review previous IASB projects, existing Standards and firm guidance

# Overall initial research findings

- **Feedback confirmed the list of topics initially identified** and we obtained a more detailed understanding of each topic (findings by topic are summarised in slides 10–16)
- Matters highlighted by investors & analysts included non-cash transactions and disaggregation
- Matters highlighted by preparers, auditors, regulators and National Standard Setters included application guidance on classification and cash equivalents
- Both investors and preparers use a ‘free cash flow’ type measure, though specific definitions vary
- Statement of cash flows for financial institutions has limited use

# Topics of initial research

The following slides 10–16 summarise findings from initial research by topic

The Key topics include:

1. Requirements for classifying cash flows
2. Disaggregation of cash flow information
3. Definition of cash and cash equivalents
4. Effects of non-cash transactions
5. Method of reporting operating cash flows
6. Information about commonly used cash flow measures
7. Statement of cash flows for financial institutions

# 1. Classification

## Key research findings

- Most users and preparers classify cash flows differently from IAS 7 for their analyses, usually based around a version of free cash flow, but still find the IAS 7 classification useful
- Most users use specific line items to form their own views of operating and free cash flows
- Some seek alignment to categories in IFRS 18
- Many preparers, firms and regulators find definitions of categories challenging to apply for some transactions and identify frequent errors
- Review of financial statements shows diversity in classification is often not visible

## Possible detailed topics

- **Definitions of categories and subtotals (including alignment with IFRS 18)**
- **Consistent application of categories**

### Interconnections

- **Classification** and **disaggregation** affect the relationship between **free cash flow** and the SCF
- The **definition of cash equivalents** affects the structure of the SCF and the line items presented

# 2. Disaggregation

## Key research findings

- Many users say more disaggregation would be useful for specific items (e.g. growth versus maintenance capex, segmental cash flows, effects of business combinations, working capital)
- However, some preparers identify challenges with disaggregating some items (e.g. growth versus maintenance highly judgemental, group cash flows difficult to allocate to segments, non-cash element of working capital a challenge)
- There is interaction with existing guidance, other standards and ongoing projects
- A few preparers seek more guidance on aggregating cash flow information

## Possible detailed topics

- **Specific information users seek that is often not disaggregated**

## Interconnections

- Some users seek **disaggregated** information about **non-cash** changes to some assets and liabilities reflected in items presented in the SCF (e.g. non-cash changes to working capital)

# 3. Cash and cash equivalents definition

## Key research findings

- Many preparers, firms and regulators find the definition of cash equivalents challenging to apply and seek more application guidance
- Some preparers (especially in specific jurisdictions) seek more alignment of cash equivalents with investments used internally for cash management
- However, most users prefer a definition closer to cash and do not raise issues with cash equivalents
- Some stakeholders question whether the statement should reconcile to cash or something else (e.g. net debt)

## Possible detailed topics

- **Definition of cash equivalents/objective of the statement of cash flows**
- **Consistent application**

## Interconnections

- The **definition of cash equivalents** affects the structure of the SCF and the line items presented
- The **definition of cash equivalents** affects the scope of **non-cash** transactions

# 4. Non-cash effects of some transactions

## Key research findings

- Many users said information about non-cash transactions was important for understanding movements in working capital and operating cash flows but can be difficult to locate (e.g. effects of leases, acquisitions and factoring)
- Preparers said there are some limitations on the availability of some information about the non-cash effects of some transactions (e.g. difficult to identify non-cash changes in some working capital items)
- Some said more guidance on agency relationships would be helpful

## Possible detailed topics

- **Information about non-cash changes to assets and liabilities**
- **Improved accessibility of disclosures about non-cash transactions**

### Interconnections

- The **definition of cash equivalents** affects **non-cash** transactions scope
- A few said sufficient information about **non-cash** changes, for example **disaggregation** of working capital would provide **direct method** information

# 5. Method of reporting operating cash flows

## Key research findings

- Many users and preparers said they use the indirect method, and many preparers expressed concerns over the cost or complexity of change
- Some users said information using the direct method is useful, particularly for some items because it provides more accurate information about earnings quality they otherwise must deduce and is more transparent
- Most preparers that use the direct method also disclose information using the indirect method
- IFRS 18 principles of useful structured summary raise a question over the choice of method

## Possible detailed topics

- **Specific direct method information that might provide sufficient benefits**
- **Guidance on deciding method**

## Interconnections

- A few said sufficient information about **non-cash** changes, for example **disaggregation** of working capital would provide **direct method** information

# 6. Information about common cash flow measures

## Key research findings

- Most users construct a FCF measure, sometimes users' adjustments consist of non-cash transactions (e.g. share based payments)
- Many preparers also manage cash internally using a similar FCF measure view
- Both users and preparers said having a standardised subtotal that could act as a starting point to reconcile FCF would help provide transparent information about FCF and allow users to make their own calculations
- Some said it would be useful to have disclosure requirements similar to MPMs in IFRS 18 for cash flow measures

## Possible detailed topics

- **Requirements similar to MPMs for cash flow measures**
- **Possible additional subtotals in the statement of cash flows**

## Interconnections

- **Classification** and **disaggregation** affect the relationship between **free cash flow** and the SCF
- FCF adjustments sometimes include **non-cash** transactions

# 7. Statement of cash flows for financial institutions

## Key research findings

- Most said the statement of cash flows has limited usefulness and useful information is mostly related to financing activities
- Some said the statement of cash flows has no usefulness for financial institutions and suggested the IASB consider exempting such entities from preparing the statement
- A few suggested replacing the statement of cash flows with an alternative
- A few suggested supplementary disclosures that might enhance the usefulness of the statement of cash flows for financial institutions

## Possible detailed topics

- **Potential for changes to classification, disaggregation or disclosure to improve usefulness for financial institutions**
- **Potential to scope out some entities**

## Interconnections

- Broad connection to all topics as any improvements to the statement of cash flows for other entities might improve the usefulness for financial institutions

# Initial analysis and next steps

# Initial analysis of findings

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|---|---|
| **No topics ruled out** | We think feedback suggests the project should explore the feasibility and the extent of possible benefits of resolving the possible reporting deficiencies in each of the research topics |
| **Some topics might require small changes** | Considering the individual questions that arose we think some of the topics might involve issues that could be resolved by small changes without looking at the Standard wholistically. For example, focusing on the individual topics or resolving only specific questions |
| **But others might require more significant change** | Given the total number of topics identified, the connections between some of them, and the potential for complexity, we think the IASB might need to consider more significant changes to fully resolve some possible reporting deficiencies |
| **Some differing priorities** | There are some topics that are higher priority for some stakeholder groups than others. For example, the defintion of cash equivalents is a high priority for many preparers, accounting firms, and NSS but is not a priority for users. It is also an area where some seek fundamental change while others seek only clarifying guidance |
| **Balance of timing, satisfactory resolution and disruption** | There is feedback that the project should move quickly to resolve ‘quick wins’, however the IASB will need to carefully consider the balance between timing, sufficiently resolving the possible reporting deficiencies and minimising disruption |

# Next steps

- The IASB will discuss the project plan in May including:
  - which of the detailed topics identified in the initial research the IASB should assess for feasibility and extent of possible benefits of resolving related issues; and
  - how possible approaches to the order of the assessment might balance various stakeholder priorities, potential complexities of solutions, and the result on the possible length of the project
- As part of that assessment the IASB will consider interaction with other active projects (e.g. PIR Leases, BCDGI, Intangible Assets)

# Key factors to consider in deciding project plan

## Stakeholder priorities

Considering how to best meet user information needs while considering the needs of the other stakeholders

## Potential complexity of solutions

Understanding the potential for complexity will help assess which approaches might be more efficient, for example:

- approaches to one topic might affect the approach on another topic and there might be approaches that resolve connected problems;
- change management for some possible approaches might be more challenging; or
- some approaches might involve greater technical challenges

# Applying the key factors

- The factors are not intended to result in a definitive ranking of topics but rather to give the IASB information needed to assess the next steps in the project. For example:
    - Information about non-cash transactions is a high priority for investors but some preparers identified potential limitations to available information. Defining the scope of non-cash transactions might be technically complex, and additional requirements would interact with other topics (e.g. cash equivalents definition). Developing guidance to make existing disclosures more accessible might be less complex. The extent of the potential complexity and the information sufficient to meet stakeholder needs is unknown until such approaches are explored.
    - Feedback on common cash flow measures (e.g. free cash flow) is generally aligned towards building on the guidance for MPMs in IFRS 18, an approach that is not expected to be complex nor highly connected to other topics.
- Based on the assessment of the factors the IASB could decide whether it is more efficient to first explore the feasibility and benefits of solutions for topics with a higher potential complexity to resolve these uncertainties, or to make early progress by first exploring those with more aligned stakeholder priorities and less potential for complexity.

# Initial assessment using factors (1/2)

| Topic | Detailed topics identified in findings | Investor priority | Preparer & others priority | Potential complexity |
|---|---|---|---|---|
| **Classification (see slide 10)** | Definitions of categories and subtotals | | ✓ | **High** |
| | Consistent application of categories | | ✓ | **Low** |
| **Disaggregation (see slide 11)** | Specific information users seek that is often not disaggregated | ✓ | | **Moderate** |
| **Cash equivalents (see slide 12)** | Definition of cash equivalents/objective of the statement of cash flows | | ✓ | **High** |
| | Consistent application of definition | | ✓ | **Low** |
| **Non-cash (see slide 13)** | Non-cash transactions economically similar to cash transactions | ✓ | | **High** |
| | Improved accessibility of currently disclosed non-cash information | ✓ | | **Low** |

# Initial assessment using factors (2/2)

| Topic | Detailed topics identified in findings | Investor priority | Preparer & others priority | Potential complexity |
|---|---|---|---|---|
| **Presentation method (see slide 14)** | Specific direct method information that might provide sufficient benefits | | | **Moderate** |
| | Guidance on deciding method | | | **Low** |
| **Common cash flow measures (see slide 15)** | Requirements similar to MPMs for cash flow measures | ✓ | ✓ | **Low** |
| | Possible additional subtotals in the statement of cash flows | ✓ | ✓ | **Moderate** |
| **Financial Institutions (see slide 16)** | Potential for changes to classification, disaggregation or disclosure to improve usefulness for financial institutions | | | **Moderate** |
| | Potential for scope out for some entities | | | **High** |

# Questions for ASAF members

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