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The 100 Group

Financial Reporting Committee

Ms Michelle Sansom
Project Manager
IFRS Foundation
30 Cannon Street
London
EC4M 6XH

17 April 2015

Dear Ms Sansom

ED/2014/6 'Disclosure Initiative – Proposed amendments to IAS 7'

We welcome the opportunity to comment on the above proposals.

Who we are

The 100 Group of Finance Directors represents the views of the finance directors of FTSE 100 and several large UK private companies. Our member companies represent almost 90% of the market capitalisation of the UK FTSE 100 Index. Our aim is to contribute positively to the development of UK and international policy and practice on matters that affect our businesses, including taxation, financial reporting, corporate governance and capital market regulation. Whilst this letter expresses the views of The 100 Group of Finance Directors as a whole, those views are not necessarily those of our individual members or their respective employers.

Summary of our views

We broadly welcome the proposals, which are intended as a response to requests received from investors for improved disclosures about an entity's debt and liquidity, but we consider that they may not go far enough to satisfy their information needs. Our comments may be summarised as follows:

(a) we believe that the needs of investors would be better served if the Board was to require (or expressly permit) entities to present a *net* debt reconciliation;

(b) consistent with the disclosures about capital required by IAS 1 'Presentation of Financial Statements', we suggest the disclosures about debt and/or net debt should be based on what the entity's management considers to be the components of debt or net debt that they manage, i.e. on a 'management basis'.

(c) we consider that the proposed disclosures about restrictions on the ability to use cash and cash equivalents should apply only where management has identified an actual need to access the funds that are subject to the restrictions within the foreseeable future, i.e. where the disclosure will actually be relevant to an understanding of the entity's liquidity; and

(d) we agree that the amendments should be applied prospectively from their effective date and that no special transitional arrangements are necessary.

We believe that it is premature to consider the effects on the IFRS Taxonomy before a new or revised accounting standard has been finalised. We therefore do not welcome the publication of the proposed IFRS Taxonomy Update with this Exposure Draft and hope that this experiment will not be repeated.

Responses to specific questions

Question 1 – Disclosure Initiative amendments
This Exposure Draft of proposed amendments to IAS 7 forms part of the Disclosure Initiative. Its objectives are to improve: (a) information provided to users of financial statements about an entity's financing activities, excluding equity items; and (b) disclosures that help users of financial statements to understand the liquidity of an entity. Do you agree with the proposed amendments (see paragraphs 44A and 50A)? Do you have any concerns about, or alternative suggestions for, any of the proposed amendments?

(a) Financing activities, excluding equity items

We recognise that investors have called for improved disclosures within IFRSs about an entity's debt, including changes in debt during the reporting period. Whilst we broadly welcome the proposals, we believe that they are incomplete. In summary, we do not believe that the proposed disclosures will always encompass all changes in debt and we believe that the needs of investors would be better served if the Board was to require (or expressly permit) entities to present a *net* debt reconciliation.

<u>Components of debt</u>

We recognise that the Board sought to address investor needs without having to define 'debt' because it considered that finding a commonly agreed definition would be difficult and could delay the project.

In order to avoid having to define debt, the Board has effectively used 'financing activities, excluding equity items' as a proxy for debt. Accordingly, draft paragraph 44A proposes that entities shall be required to present a reconciliation of "the amounts in the opening and closing statements of financial position for each item for which cash flows have been, or would be classified as financing activities in the statement of cash flows, excluding equity items".

We are concerned that this may present an incomplete picture of the movements on debt. In particular, IAS 7 permits interest paid or received to be presented within operating, investing or financing activities. Where interest paid or received is presented within operating or investing activities any interest balances within the statement of financial position would not be included within the reconciliation proposed in draft paragraph 44A.

Under the heading 'Definition of debt and/or net debt', we propose an alternative approach that would not require the Board to reach any commonly agreed definitions.

<u>Net debt reconciliation</u>

Whilst investors would find a reconciliation of gross debt useful, in our experience they would prefer a reconciliation of net debt. Indeed, an overwhelming majority of our member FTSE-100 companies already provide a net debt reconciliation in their IFRS financial statements on a voluntary basis. We believe that the principal reasons for this are that:

(i) net debt is a key indicator in the context of overall capital management ('cash and cash equivalents' as defined under IAS 7 is too narrow a measure for this purpose as it encompasses only short-term cash deposits and bank overdrafts repayable on demand);

(ii) investors find this information useful (research carried out in 2012 by the UK's Financial Reporting Lab showed that a large majority of investors use a net debt reconciliation in their analysis of a company); and

(iii) companies were required to present a net debt reconciliation under UK GAAP and saw value in continuing to provide this information to investors following their adoption of IFRS.

Whilst we appreciate that the Board may have some concerns about a net debt reconciliation, there is no doubt in our mind that this would more fully meet the needs of investors. We therefore suggest that the Board revisits the idea of a net debt reconciliation (perhaps with a sub-total at the gross debt level) or makes it clear in the revised standard that the required gross debt reconciliation may be incorporated within a net debt reconciliation.

Definition of 'debt' and/or 'net debt'

We consider that disclosures concerning debt and/or net debt are closely related to disclosures regarding the management of capital (many companies include debt or net debt in their definition of capital). Disclosure requirements regarding the management of capital are set out in IAS 1 'Presentation of Financial Statements' (IAS 1.134-136). IAS 1 does not seek to define 'capital' and it is made clear in the Basis for Conclusions that "this disclosure is intended to give entities the opportunity to describe how they view the components of capital they manage, if this is different from what IFRSs define as equity" (IAS 1.BC91). Moreover, the Illustrative Examples to IAS 1 contain an example of capital disclosure that includes within capital a measure of net debt (IAS 1. IE10).

We therefore suggest that the disclosure requirements concerning debt and/or net debt are similarly based on what the entity's management considers to be the components of debt or net debt that they manage, i.e. on a 'management basis'.

Whilst the UK's Financial Reporting Lab did find that some investors favour a standard definition of net debt, others acknowledged that the investor community itself does not have a standard definition of net debt and what they are looking for is sufficient disclosure to enable them to understand what is included and excluded from the entity's measure in order that they can include the appropriate amounts in their own analytical models. Some investors support the management basis because they particularly value information about how management views and manages its debt and/or net debt position.

Reconciling items

We recommend that paragraph 44A(b) should be amended to require separate disclosure of the effect of changes in foreign exchange rates. Such changes can be significant and separate disclosure of them is required in the statement of cash flows (IAS 7.28).

(b) Disclosures about liquidity

IAS 7 already requires that "an entity shall disclose, together with a commentary by management, the amount of significant cash and cash equivalent balances held by the entity that are *not available* for use by the group" (IAS 7.48). Examples given include balances held by a subsidiary that operates in a country where exchange controls or other legal restrictions apply when the balances are not available for general use by the parent or other subsidiaries (IAS 7.49)

Draft paragraph 50A proposes that "an entity shall consider matters such as *restrictions* that affect the decisions of an entity to use cash and cash equivalent balances, including tax liabilities that would arise on the repatriation of foreign cash and cash equivalent balances" and disclose such matters if they are relevant to an understanding of the liquidity of an entity.

We agree in principle that disclosure of material restrictions on the ability to use cash and cash equivalents in one entity to meet funding requirements in another provides useful information to investors. Indeed, we agree with the view expressed by the Global Preparers' Forum that the disclosure should be broader than cash and cash equivalents, i.e. encompass cash balances with an original maturity of more than three months and certain marketable

securities. Whilst the IASB acknowledges this view in paragraph BC13 but does not appear to have addressed it in the proposals.

We are concerned that draft paragraph 50A may be interpreted as a requirement to routinely provide disclosures about restrictions on the use of cash and cash equivalents, including the tax liabilities that would arise if it were necessary to repatriate funds held overseas. We believe that such disclosure is neither relevant nor practicable until such time as management has identified an actual need to access the restricted funds within the foreseeable future.

If cash can be repatriated and there is no cost-effective alternative but to do so, the cash will be repatriated. Management should consider the potential tax consequences in its assessment of whether the business remains a going concern, i.e. whether the net amount that would be repatriated would be sufficient to meet the entity's funding requirements.

Until such time as a need to access the funds is identified, it will not usually be practicable to quantify the potential tax liabilities. For example, the tax liabilities may depend on which country the cash balances will be remitted to (it would not be appropriate always to assume that remittance will be to the parent company as it may be to a fellow subsidiary in another jurisdiction) and also on the timing of the payments.

We therefore recommend that the disclosures in paragraph 50A should apply only where management has identified an *actual* need to access the funds that are subject to the restrictions within the foreseeable future, i.e. where the disclosure will actually be relevant to an understanding of the entity's liquidity.

Question 2 – Transition provisions
Do you agree with the proposed transition provisions for the amendments to IAS 7 as described in this Exposure Draft (see paragraph 59)? If not, why and what alternative do you propose?

We agree that the amendments should be applied prospectively from their effective date (with early application permitted). We also agree that it is not necessary to have any specific transitional arrangements.

Question 3 – IFRS Taxonomy
Do the proposed IFRS Taxonomy changes appropriately reflect the disclosures that are set out in the proposed amendments to IAS 7 and the accompanying illustrative example? In particular: (a) are the amendments reflected at a sufficient level of detail? (b) should any line items or members be added or removed? (c) do the proposed labels of elements faithfully represent their meaning? (d) do you agree that the proposed list of elements to be added to the IFRS Taxonomy should be limited to the information required by the proposed amendments to IAS 7 or presented in the illustrative examples to IAS 7?

For the reasons set out in our answer to Question 4, we do not believe that it is appropriate to consider the effects on the IFRS Taxonomy at the exposure draft stage, i.e. before a new or revised accounting standard has been finalised. We have, however, considered the proposed changes to the IFRS Taxonomy included within the Exposure Draft.

We are generally content with the proposed changes to the IFRS Taxonomy except for one, which happens to illustrate rather well one of the problems with reporting using XBRL with its focus on quantitative disclosures and inability to deal adequately with qualitative disclosures.

Paragraph 10 of the proposed changes to the IFRS Taxonomy seems to require disclosure of the amount of tax liabilities that would arise on the repatriation of foreign cash and cash equivalents. We believe that this quantitative disclosure should not be introduced into the IFRS Taxonomy because it seems to us to be more prescriptive than the proposed new paragraph 50A of IAS 7.

As a general principle, we believe that it is important that the Board guards against the risk that proposed changes to the IFRS Taxonomy may unintentionally interpret or contradict accounting standards.

Question 4 – IFRS Taxonomy due process
As referenced in paragraph BC20, the IASB is holding a trial of a proposal to change the IFRS Taxonomy due process. Although not constituting a formal public consultation of the IFRS Taxonomy due process, views are sought on the following: (a) do you agree with the publication of the proposed IFRS Taxonomy Update at the same time that an Exposure Draft is issued? (b) do you find the form and content of the proposed IFRS Taxonomy Update useful? If not, why and what alternative or changes do you propose?

The IFRS Taxonomy is the means by which the disclosure requirements of accounting standards are codified into XBRL. We therefore believe that it is premature to consider the effects on the IFRS Taxonomy at the exposure draft stage, i.e. before a new or revised accounting standard has been finalised. We do not welcome the publication of the proposed IFRS Taxonomy Update with this Exposure Draft and hope that this experiment will not be repeated.

When amendments are made to the IFRS Taxonomy it is necessary for XBRL software providers to update their software and assist their customers in implementing the changes. With these practicalities in mind, we recommend that the amendments to the IFRS Taxonomy should be made on a regular cycle rather than on a piecemeal basis following the finalisation of each new or revised accounting standard in order that software providers can issue regular updates to their products.

On the assumption that there is usually a period of at least 12 months between the publication of a new or revised accounting standard and its mandatory adoption date, we suggest an annual cycle such that proposed changes to the IFRS Taxonomy should be published no later than during the fourth quarter of each year with a view to publishing the finalised changes no later than during the second quarter of the following year. In this way, the consequential changes to XBRL software could be effected in good time ahead of reporting in accordance with new or revised accounting standards.

Feedback

Please feel free to contact me through the 100 Group's website, www.the100group.co.uk, should you wish to discuss our comments.

Yours sincerely

Russ Houlden
Chairman
Financial Reporting Committee
The 100 Group of Finance Directors