

Thematic Review – Cash flows and liquidity disclosures

The FRC will conduct a thematic review of companies' disclosures of cash flows and liquidity risks, exploring in more detail issues identified in CRR's routine work and the themes of the Financial Reporting Lab's recently published report 'Disclosure on the sources and uses of cash'.

The FRC finds many examples of basic errors in the cash flow statement, often from a desktop review of the financial statements. This is unsatisfactory. Investors require reliable and thorough analysis of how cash is generated and spent, and the figures presented in the cash flow statement are used as the starting point for a number of performance measures.

The FRC's Lab reported in September 2019 that understanding the generation, availability, and use of cash is fundamental to investors. While the core disclosure which supports these investor needs is the cash flow statement, the Lab also found that some of the most helpful disclosures are outside the cash flow statement, for example, the notes and cash flow based metrics.

Certain sectors of the economy are currently under significant pressure and facing increased liquidity risk. The thematic will consider how the presentation of the cash flow statement and disclosures can help readers assess the ability of the company to generate cash flows and the cash flow needs of the company.

The FRC has identified the following specific areas where improvements can be made. It expects:

- Cash flow statements to follow the treatments prescribed in IAS 7, where provided, and to be free from basic errors;
- Disclosure of accounting policies for complex transactions where the cash flow presentation is judgemental and, where relevant, any significant accounting judgements applied in the cash flow statement;
- Company specific disclosures of liquidity risk consistent with disclosures given for going concern and the viability statement;
- Where material, disclosure of supplier financing arrangements, including the impact on cash flows and the presence of any concentrations of liquidity risk;
- Disclosure of what constitutes cash and cash equivalents, including any restrictions on the availability of cash; and
- Compliance with the ESMA Guidelines for cash flow based Alternative Performance Measures ('APMs').

Notes:

1. The objective of IAS 7, 'Statement of Cash Flows' is to require the provision of information about the historical changes in cash and cash equivalents of an entity by means of a statement of cash flows which classifies cash flows during the period from operating, investing and financing activities.
2. Paragraph 33 of IFRS 7, 'Financial Instruments: Disclosures' requires disclosure of information about liquidity risk including; the exposures to liquidity risk, how they arise, the objectives, policies and processes for managing the risk and any changes from the previous period.

3. The Lab project report “Disclosures on the sources and uses of cash” may be found at <https://www.frc.org.uk/news/september-2019/the-financial-reporting-lab-publishes-latest-repor>
4. The ESMA Guidelines on Alternative Performance Measures may be found at <https://www.esma.europa.eu/press-news/esma-news/esma-publishes-final-guidelines-alternative-performance-measures>