2019

Statutory Reporting Quality

Information Note

Liquidity analysis in annual and half-yearly financial reports

IAASA
Irish Auditing & Accounting Supervisory Authority

MISSION

To contribute to Ireland having a strong regulatory environment in which to do business by supervising and promoting high quality financial reporting, auditing and effective regulation of the accounting profession in the public interest

INFORMATION NOTE

LIQUIDITY ANALYSIS IN ANNUAL AND HALF-YEARLY FINANCIAL REPORTS

1. Purpose of this Information Note

The purpose of this Information Note is to remind management and those charged with governance of the requirements in IFRS to disclose higher quality liquidity risk analysis in annual and half-yearly financial reports and, thereby, to contribute to the provision of useful financial information to users of those reports.

2. Introduction

Liquidity risk is defined in Appendix A of IFRS 7 *Financial Instruments: Disclosures* as:

> '*The risk that an entity will encounter difficulty in meeting obligations associated with financial liabilities that are settled by delivering cash or another financial assets.*'

Liquidity risk tables and the related liquidity risk disclosures (i.e. liquidity risk analysis) is a key metric for many users of financial statements. Liquidity risk analysis is essential information that enables users of the financial statements to gain an understanding of the timing of cash flows and changes therein that is associated with financial liabilities.

This Information Note is focused on a maturity analysis for non-derivative financial liabilities.

3. Liquidity risk reporting requirements

Paragraph 39 of IFRS 7 requires that an issuer shall disclose:

> ' *(a) a maturity analysis for non-derivative financial liabilities (including issued financial guarantee contracts) that shows the remaining contractual maturities;*
>
> *(b) a maturity analysis for derivative financial liabilities. The maturity analysis shall include the remaining contractual maturities for those derivative financial liabilities for which contractual maturities are essential for an understanding of the timing of the cash flows (see paragraph B11B); and*
>
> *(c) a description of how it manages the liquidity risk inherent in (a) and (b).*'

IFRS 7.BC57 states that:

> '*The Board decided to require disclosure of a maturity analysis for financial liabilities showing the remaining* ***earliest*** [bold emphasis added] *contractual maturities (paragraph 39(a) and paragraphs B11 – B16 of Appendix B).Liquidity risk, i.e. the risk that the entity will encounter difficulty in meeting commitments associated with financial liabilities, arises because of the possibility (which may often be remote) that the entity could be required to pay its liabilities earlier than expected. The Board decided to require disclosure based on the earliest contractual maturity date because this disclosure shows a* ***worst case scenario*** [bold emphasis added].'

IFRS 7.B10A to B11F and Illustrative Guidance paragraph IG31A are also relevant in this regard.

4. Evaluation of the level of compliance by issuers

In the course of our examination of the financial reports of financial institutions and debt issuers in recent years, we have raised matters regarding the presentation of the liquidity risk analysis of financial liabilities (i.e. quantitative and qualitative information). We have observed a varied level of compliance with the disclosure requirements of IFRS 7.39. However, we are disappointed to have detected recurring errors and non-compliance linked to the liquidity analysis disclosed by certain issuers.

It is a matter of concern to us that a cohort of issuers has disclosed liquidity analysis of non-derivative financial liabilities that, to varying degrees, limit users' understanding of liquidity risks and changes therein.

We have noted that the most common areas of non-compliance of liquidity risk reporting typically include one or more of the following:

(a) liabilities are not presented by the **earliest** contractual maturity date in which the entity can be required to pay (IFRS 7.BC11 refers) and are sometimes prepared on a best case scenario (i.e. the **latest** payment date);

(b) the omission of selected non-derivative financial liabilities from the liquidity tables;

(c) presentation of too few time bands and inappropriate aggregation of time bands that limits the usefulness of the liquidity analysis;

(d) time bands for financial liabilities maturities presented in the liquidity risk analysis table being inconsistent with cash flow patterns observed in the Statement of Cash Flows;

(e) material restatement of comparative amounts in liquidity analysis tables without the explanation and disclosure required (i.e. IAS 1.41 and IAS 8.49 refer); and

(f) boilerplate description as to how the entity manages the liquidity risk or omission of same.

5. Key messages to issuers

Liquidity analysis disclosure is a significant disclosure in the financial statements of issuers and particularly those of financial institutions and debt issuers.

We remind management and those charged with governance to exercise closer scrutiny in the preparation and review of liquidity risk analysis disclosures in the preparation of future financial statements.

Liquidity risk analysis should:

(a) disclose a maturity analysis for financial liabilities showing the remaining earliest contractual maturities;

(b) use an appropriate number of time bands;

(c) avoid boilerplate disclosures; and

(d) enable users of the financial statements to gain an understanding of the timing of cash flows and changes therein that is associated with financial liabilities.

We will continue to monitor issuers' disclosure of liquidity risk analysis as part of our on-going cycle of examinations.

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