Presenting certain items on the statement of cash flows

Extract, PSA Discussion Group Report on the Public Meeting – November 10, 2022

The submission was positioned as an application of existing standards in preparing general-purpose financial statements for a public sector entity applying the PSA Handbook as its primary source of GAAP. The submission raised two issues regarding how public sector entities should present the cash flows relating to public private partnerships and the asset retirement obligations in the statement of cash flows. A third issue asked whether restricted cash should be included in cash and cash equivalents; in cash flows from investing activities; or in cash flows from operating, investing, capital, or financing activities, as appropriate to the nature of the restrictions.

The issues stem from:

- Existing reporting model standard Section PS 1201 (and the Exposure Draft, "Financial Statement Presentation, Proposed Section PS 1202") do not specify how certain transactions are to be presented in the cash flow statement.
- Existing Section PS 1201 and proposed new Section PS 1202 do not go into the detail necessary to address the presentation questions raised because they are not focused solely on the cash flow statement.
- International Accounting Standard (IAS) 7 *Statement of Cash Flows* and International Publics Sector Accounting Standard (IPSAS) 2, *Cash Flow Statements*, have separate standards and include more detailed guidance on the cash flow statement, providing presentation requirements for many specific items.

Issue 1 – How should public sector entities reflect cash flows related to public private partnership arrangements (3Ps) in the statement of cash flows, in cash flows from capital activities, or cash flows from financing activities?

The issue asked the Group to consider whether cash flows related to operations or maintenance for infrastructure assets should be presented in cash flows from capital activities (View A) or from financing activities (View B).

A Group member clarified that the starting point for 3Ps is not acquiring infrastructure or securing alternate financing for capital but managing risk. So, accounting disclosures must help in evaluating if the 3P was successful: Was it effective? Did it transfer risk, etc.? This would include breaking out the cash flows into capital, financing, operating, and maintenance as appropriate. Another Group member countered that smaller governments may use 3Ps as a financing tool.The Group discussed the various components that can be introduced on 3Ps. A Group member outlined the several possible components of a 3P arrangement, such as design, build, finance, operate, and maintain (DBFOM). Some Group members noted that the benefit derived from 3Ps, such as from DBFOM arrangements, have become more common. They shared that such arrangements in procuring public infrastructure are beneficial in sharing the risks in terms of financing and construction, from design and planning to long-term maintenance, for example. Two Group members thought there was some appeal to splitting cash flows into such components, but acknowledged the additional complexity and decreased understandability for users.

Most Group members supported View B. They indicated that 3P cash flows should be presented as financing activities because the main motivation for a 3P arrangement is to access an alternative financing model for infrastructure. They noted the following:

- In many instances, governments cannot afford to purchase or replace their infrastructure. Certain projects require significant investments that public sector entities cannot self-finance. Governments often use 3Ps to help finance such projects and so this would represent a financing activity.
- Section PS 1201 links financing activities with the cash repayment of debt. Many 3P arrangements explicitly provide for repayment, which would support designating 3P cash flows being from financing activities.
- If the 3P project's ultimate intent is to offer a public service, then this would represent an activity to finance the delivery costs of a public service.
- The transfer of risks in the development of infrastructure assets may be transferred from the public sector to the private sector partner. A Group member noted that Section PS 3160, *Public Private Partnerships*, clearly addresses discount rates and estimating the liability, which seems most relevant to a financing activity.
- Section PS 3160 establishes that a public entity recognizes a liability when it recognizes an infrastructure asset. In addition, the type of consideration provided to the private sector partner determines whether the public sector entity recognizes a financial liability (financial liability model) or a performance obligation (user-pay model).[1]

The details and components of 3P agreements must be considered in determining whether the cash flows derived from the infrastructure asset should be presented as financing or capital activities. One Group member noted the existence of balloon payments in some arrangements, which may imply more of a capital activity (i.e., acquisition of infrastructure). Other arrangements involve service payments over several years, which may more closely resemble a financing activity. Another member agreed, indicating the substance of an arrangement may make a third view more appropriate (i.e., splitting the cash flows related to the 3P according to their objective and substance). Cost-benefit of splitting would be a consideration, as would the degree of transparency provided to readers.

Issue 2 – How should public sector entities present cash flows related to asset retirement obligations (AROs) in the statement of cash flows?

The Group was asked to consider whether cash flows related to AROs should be presented in cash flows from capital activities (View A) or from operating activities (View B).

Most Group members supported View A:

- An ARO would form part of the cost of capital items and should be presented as part of capital activities.
- In circumstances where the asset may still be in productive use, the cash flows would be capital activities in nature and should be presented as such.
- While Section PS 1201 is generic, it better suits the cash flows related to AROs as a capital activity.

[1] Section PS 3160 provides several recognition and disclosure considerations. However, the standard does not explicitly clarify how cash flows related to the infrastructure asset should be presented in the statement of cash flows.

- Constitutes as a capital activity because AROs only arise because an entity has a tangible capital asset. They are not driven by activities from ongoing operations.

Some Group members noted circumstances where View B may have merit or suggested other considerations:

- If an asset is fully depreciated, cash flows may be better reflected as cash derived from operating activities.

The nature of the business/activity of the entity holding the asset might be relevant to the classification of the ARO cash flows. For example, the cash flows of AROs related to defence assets might be classified differently if the assets are used on the battlefield (i.e., in operations), versus used in training (i.e., capital activities). Splitting the cash flows from the ARO may have merit. At inception, the ARO cash flows are considered related to capital activities. However, the interest accretion over time is reflected in the operating statement and thus in cash flow from operating activities over time.

Issue 3 – Should restricted cash be included in cash and cash equivalents on the statement of cash flow?

The Group was asked to consider three views:

- View A: Restricted cash should be included in cash and cash equivalents on the statement of cash flow.
- View B: Changes in restricted cash in the accounting period should be presented in cash flows from investing activities.
- View C: Changes in restricted cash in the accounting period should be presented in cash flows from operating, investing, capital, or financing activities, as appropriate to the nature of the restrictions.

Most Group members supported View C, that restricted cash would not be included in the cash and cash equivalents balance reconciled in the statement of cash flows.

However, many Group members offered thoughts on where View A or B may also apply. Comments included:

- Restricted cash should be identified separately on the statement of financial position, as this would be useful to users of financial statements. However, Section PS 3100, *Restricted Assets and Revenues*, does not allow restricted amounts to be presented separately.
- Disclosure of the restrictions and what the cash must be used for in the notes and schedules would be good accountability information.
- Separately reporting cash flows related to restricted cash in the categories of cash flow activities that best reflect the restrictions would provide good cash flow information for users.
- The presentation of the details of the restrictions may be a matter of public interest that should be disclosed and presented appropriately on statement of cash flow;
- One Group member noted support for View A, referring to the IFRS Interpretations Committee's April 2022, APA12A: Finalisation of agenda decision. This decision concluded that restricted cash is still considered to be cash, even if the entity does not have the intention for use in the short term.
- Another Group member reflected that Section PS 1201 does not clearly define cash and noted it is logical to include all items that by their nature comprise cash, even if their use is restricted. Cash is cash. Restricted cash should be reported as part of the cash and cash equivalents balance that is reconciled to on the statement of cash flow.

- A Group member felt that cash flows related to restricted cash should be reflected in investing activities as changes in cash are investing activities.
- Still another Group member questioned if the complexity associated with View C is justifiable or if the user might better understand that all cash, including restricted cash, was included in the cash and cash equivalents balances reconciled to in the statement of cash flows.

The Group encouraged PSAB to provide further guidance on the presentation of items in the statement of cash flows, including restricted cash.