

Brief facts of the enquiry:

An Insurance Company (the Company) has arranged a guarantee in favor of the regulator to meet the regulatory requirement through a commercial bank against which the saving account has been provided as collateral/cash margin and at any point of time the bank balances under lien can be released by providing another collateral as security acceptable to the bank. The guarantee is in favor of the regulator for an indefinite period.

The Company needed guidance as to what is the most appropriate way of presenting the bank balances under lien or subject to encumbrance in the Statement of Financial Position and the Statement of Cash flows in accordance with the Financial Reporting Standards as applicable in Pakistan, whether such balances can be presented as part of 'Cash and Bank' with disclosure providing details of lien or need to be disclosed as separate line item on the face of the balance sheet or to be clubbed in 'Other receivables' in the Statement of Financial Position."

It was requested to the Board to provide clarity, in context of given fact pattern, on most appropriate way of presenting bank balances under lien in the Statement of Financial Position and Statement of Cash Flows.

Opinion:

As per facts pattern provided by Company, the Company has arranged a guarantee in favour of the regulator to meet the regulatory requirement through a commercial bank against which the bank balance held with such bank has been provided as collateral/cash margin. At any point of time, the bank balance under lien can be released by Bank after Company has provided another collateral as security acceptable to the bank. Without Company providing an alternative collateral acceptable to Bank, the Company cannot withdraw / transfer amounts from such bank account.

In the following paragraphs, it is evaluated whether the Company's bank account balance meets the definition of 'cash' or 'cash equivalents' as per paragraph 6 and 7 of IAS 7.

Definition of Cash and whether Company's bank account meets the definition of 'cash' as per IAS 7

Paragraph 6 of IAS 7 defines 'Cash' as follows:

"Cash comprises cash on hand and demand deposits."

(Italic and emphasis ours)

The term 'demand deposit' has not been defined in IAS 7 or other IFRS Accounting Standards. Therefore, for this purpose, simple dictionary meaning of Demand Deposits was extracted from Oxford dictionary which is as follows:

"A deposit of money that can be withdrawn without prior notice, e.g. in a current account."

Further, Collins Dictionary also provides following definition of demand deposit:

"A bank deposit from which withdrawals may be made without notice"

(Italic and emphasis ours)

By above definition, a demand deposit must allow the account holder to withdraw funds freely at any time. However, in this case, the bank balances under lien can only be accessed by providing alternative collateral acceptable to the bank. This restriction prevents the entity from withdrawing funds freely, which is a key characteristic of a demand deposit. As a result, it does not meet definition of 'Cash' laid down in IAS 7.

Opinion Issued by the Accounting Standards Board
Bank Balance under lien

Definition of 'Cash equivalents' as per IAS 7 and whether Company's bank account meets the definition of 'cash equivalents'

Paragraph 6 of IAS 7 defines 'Cash equivalents' as follows:

"Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value."

Paragraph 7 of IAS 7 explains 'Cash equivalents' as follows:

"Cash equivalents are held for the purpose of meeting short-term cash commitments rather than for investment or other purposes. For an investment to qualify as a cash equivalent it must be readily convertible to a known amount of cash and be subject to an insignificant risk of changes in value. Therefore, an investment normally qualifies as a cash equivalent only when it has a short maturity of, say, three months or less from the date of acquisition. Equity investments are excluded from cash equivalents unless they are, in substance, cash equivalents, for example in the case of preferred shares acquired within a short period of their maturity and with a specified redemption date."

The definition under IAS 7 emphasizes that cash equivalents must be both readily convertible to cash and subject to

However, in the instant case, the bank balances under lien can only be accessed and used by Company after providing alternative collateral acceptable to the bank. Hence, as bank balance under lien is not readily available.

In view of above, the Company's balance in bank account does not meet definition of cash equivalents as provided in IAS 7.

The Board considered to guidance issued by large accounting firms world-wide for above areas.

The Board also considered guidance contained in Accounting Standards for Private Enterprises issued by Canadian Accounting Standards Board on the topic of Cash and Cash Equivalents as reproduced below:

Extracts from General Accounting Section 1540 of Accounting Standards for Private Enterprises issued by Canadian Accounting Standards Board

Paragraphs .06 and .07 of General Accounting Section 1540 contained in Accounting Standards for Private Enterprises issued by Canadian Accounting Standards Board respectively define 'cash' and explain whether restricted cash balance can qualify as 'cash and cash equivalent' or not. These paragraphs state as follows:

".06 Cash comprises cash on hand and demand deposits."

".07 Cash subject to restrictions that prevent its use for current purposes, such as compensating balances required in accordance with lending arrangements, would not be included among cash and cash equivalents....."

The Board noted that above pronouncement also requires that cash subject to restrictions that prevent its use for current purposes, would not be included among cash and cash equivalents.

The Board's conclusion

The Board concluded as follows:

As per IAS 7, *Cash comprises cash on hand and demand deposits*. A demand deposit, by definition, must allow the account holder to withdraw funds freely at any time. However, in this case, access to the bank balances under lien is contingent upon Company providing alternative collateral acceptable to the bank. This restriction prevents immediate withdrawal, contradicting the fundamental characteristic of a demand deposit. Consequently, bank balance of Company does not meet definition of cash, as it is not readily accessible and withdrawable by the Company without prior notice and provision of an alternative collateral by the Company to the Bank.

Under IAS 7, cash equivalents represent short term, highly liquid investments that are readily convertible to known amounts of cash and subject to an insignificant risk of value changes. As per paragraph 7 of IAS 7, an investment normally qualifies as a cash equivalent only when it has a short maturity of, say, three months or less from the date of acquisition.

As per information received, Company's bank balance under lien is held against a guarantee for an indefinite period, and therefore, as such, it cannot be used to meet short-term commitments.

Accordingly, such balance cannot be said to be realizable within a period of 3 months or lesser period, and therefore does not meet definition of cash equivalents under IAS 7.

In view of restriction by Bank on use / withdrawal from the Company's Bank balance by the Company, Company's bank balance does not meet the definition of '*Cash*' or '*Cash and cash equivalents*' in terms of *IAS 7 Statement of Cash Flows*. Therefore, balance of Company's bank account should be presented separately from "Cash and Bank Balances" in the Statement of Financial Position as 'Other financial assets' or with another appropriate nomenclature in line with requirements of paragraphs 54 and 57 of IAS 1. Further, such balance should also be excluded from "Cash and Cash Equivalents" in the Statement of Cash Flows.

Caveat

- the analysis and conclusion are specific to the described fact pattern and should not be applied universally to all scenarios involving bank balances under lien. Each case must be evaluated based on its unique facts to ensure compliance with IAS 7 and other applicable standards.
- this analysis is based solely on the requirements of IAS 7, and with the presumption that it would not affect any determinations made under Insurance laws or regulations.
- the opinion expressed in this matter, should not be applied where restricted bank balances are accessible/usable for liquidity management on a day-to-day basis.

(Issued in May 29, 2025)

Disclaimer

The Board believes that the enquired matter, transaction or arrangement has been or will be made considering the legal, ethical and moral requirements. The comments and opinion are based on the facts and circumstances provided by the enquirer. The comments and opinion may change if the facts and the circumstances change. An opinion may also change due to subsequent change in law, pronouncements made by the Institute and other relevant changes. The Institute, its staff and the Board will have no liability in connection with such opinion and this opinion is not a 'legal advice'.