Australian Government
Australian Accounting Standards Board

Research Report

Statement of Cash Flows and Related Matters – Australian Listed Entities

September 2025

AASB Research Report 25

Australian Government
Australian Accounting Standards Board

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AASB Research Reports and Suggested Citation

The AASB Research Centre publishes research reports to promote thought leadership in accounting and reporting through rigorous analysis and research aimed at informing stakeholders and advancing the quality of corporate reporting.

The suggested citation for the complete report is:

Tran H, Lee E, Chang M and Hanlon D (2025) 'Statement of Cash Flows and Related Matters – Australian Listed Entities', *AASB Research Report 25* (September 2025).

ISBN: **978-1-7641059-2-7**

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Executive Summary

In response to feedback received from the 2022 International Accounting Standards Board (IASB) Third Agenda Consultation, the IASB commenced a project on the statement of cash flows to explore potential improvements to IAS 7 *Statement of Cash Flows*.

This research report provides findings from an analysis of the annual reports of the top 50 entities listed on the Australian Securities Exchange (ASX), hereinafter the ASX top 50, in 2023. The findings are as follows:

a) **Methods of reporting operating cash flows**: 72% of entities presented the direct method cash flow statements and the reconciliation of profit to net operating cash flows (i.e. indirect method) in the notes to the financial statements. The remaining 28% used the indirect method to present their statement of cash flows;

b) **Cash and cash equivalents**: 40% of the entities did not provide disaggregated information on the amounts of cash and cash equivalents. In addition, 62% and 2% of the entities defined short-term maturity to be a period of three months and 12 months, respectively, while 36% sampled entities did not disclose or define their short-term threshold;

c) **Classification**: There was inconsistency in the classification of cash flow items, particularly cash receipts and payments related to interest and dividends. Among the sampled entities disclosing dividends paid, almost 98% classified them within financing activities. Furthermore, there was wide variation in the classification of interest paid, interest received and dividends received;

d) **Encouraged voluntary disclosures**: Most entities disclosed information on undrawn borrowing facilities. However, voluntary disclosures of information about cash flows intended to increase and maintain operating capacity, as well as segmental cash flows were less common; and

e) **Free cash flow (FCF)**: 52% of entities disclosed FCF, reflecting its importance in annual reports. However, how FCF was determined and where it was disclosed in the annual report varied.

These findings provide additional evidence that there is diversity in practice on how cash flow statements and related information are presented and disclosed. They support and reinforce the need for revisions to IAS 7 to improve consistency and the usefulness of cash flow related information, thereby better meeting user needs.

1. Introduction

1.1 Background

IAS 7 *Statement of Cash Flows*[1] sets out requirements on the presentation of cash flow statements and disclosures of related information to meet the needs of financial statement users (IFRS Foundation, 2016). Since its issuance in 1992, the standard has evolved through several amendments driven by the needs to address deficiencies and respond to stakeholder feedback. A notable amendment is the 2016 *Disclosure Initiative* (Amendments to IAS 7),[2] which requires entities to disclose changes in liabilities arising from financing activities. Additionally, the ongoing work by the International Accounting Standards Board (IASB), such as the amendments to the statement of cash flows under IFRS 18 *Presentation and Disclosure in Financial Statements*, reflects its continued efforts to improve the usefulness of cash flow information. Many national standard setters, including the European Financial Reporting Advisory Group (EFRAG) (EFRAG 2024a), the UK Financial Reporting Council (UK FRC) (UK FRC 2016, 2017, 2020a, 2020b), the Canadian Accounting Standards Board (AcSB) (EFRAG 2024b; IASB 2024e) and the Accounting Regulatory Department of the Ministry of Finance of China (AOSSG 2023), have also conducted research and published reports or discussion papers, providing input into the ongoing deliberations on the future direction for improvements to the statement of cash flows and related matters.

In 2022, the IASB conducted its third agenda consultation to gather stakeholder feedback on its strategic direction and work plan for the period 2022–2026. The feedback revealed several concerns regarding the statement of cash flows and suggested that the IASB should undertake a revision of IAS 7 (IASB 2022a). In particular, stakeholders raised concerns about inconsistencies in the classifications of cash inflows and outflows, such as the classifications of interest received/paid and dividends received. Some also highlighted that certain financing arrangements, such as supply chain financing and reverse factoring, require clearer guidance on how they should be presented and classified in the statement of cash flows. Additionally, users noted the need for improved presentation and disclosure of cash flow information to better understand movements in working capital and operating cash flows. Specifically, they requested clearer information on cash inflows and outflows related to growth and maintenance capital expenditures (CAPEX), as well as details of non-cash transactions. Many stakeholders also noted challenges in applying the definition of cash equivalents under AASB 107/IAS 7, as evidenced by the inconsistent disclosures made by entities. Furthermore, there were mixed views on whether the direct and/or indirect method should be used to report operating cash flows.

Consequently, based on the feedback received, the IASB decided to add the statement of cash flows

[1] AASB 107 *Statement of Cash Flows* incorporates the requirements of IAS 7 *Statement of Cash Flows*.
[2] *Disclosure Initiative* (Amendments to IAS 7) is effective for annual periods beginning on or after 1 January 2017. <https://www.ifrs.org/projects/completed-projects/2016/disclosure-initiative-amendments-to-ias-7/>, accessed 1 November 2024.

project to its research pipeline and subsequently commenced the project in 2024. The aim of the IASB's project is to explore either possible targeted amendments or potentially conduct a comprehensive review to improve the relevance and comparability of cash flow statements, subject to further research and stakeholder input.

1.2 Scope and Purpose

The AASB research project on cash flow statements comprises two stages. The first stage involves analysing annual reports to identify key issues related to AASB 107/IAS 7, such as differences in disclosure or presentation of certain cash flow items. The second stage involves interviewing users, preparers and auditors to gain deeper insights into current challenges and concerns related to cash flow reporting.

This research report primarily focuses on the first stage, where the annual reports of the ASX top 50 in 2023 were reviewed, with attention paid to the following five key topics:[3]

a) Direct and indirect methods;
b) Cash and cash equivalents;
c) Classification of operating, investing and financing activities;
d) Encouraged voluntary disclosures; and
e) Free cash flow (FCF).

2. Sample selection and method

The research method involves reviewing and analysing the statement of cash flows and related cash flow information in the annual reports of the ASX top 50 by market capitalisation for the 2023 financial year (i.e. the financial year ending on 30 June 2023, 30 September 2023 or 31 December 2023). Annual reports were obtained from Morningstar DatAnalysis Premium. The Appendix provides detailed information on the 50 firms in the sample (as at the time of data collection for this report - April 2024).

Table 1 below describes the industry breakdown of the sample, which covers 12 industries. Firms in financial services account for 20% of the sample, while firms in mining, materials and construction; and health care equipment and services make up 18% and 12%, respectively. Together, these three industry groups make up 50% of the sample.

[3] These five priority areas are chosen to be consistent with the feedback highlighted as part of the IASB's agenda consultation documents (IASB 2021, 2022a, 2022b).

Table 1. Types of Industry

Industry	No. of entities	%
Financial services	10	20
Mining, materials & construction	9	18
Healthcare equipment & services	6	12
Energy & utilities	5	10
Retail	4	8
Real estate investment trust (REITs)	3	6
Media & entertainment	3	6
Insurance	3	6
Manufacturing	2	4
Software & services	2	4
Logistics & transportation	2	4
Telecommunication	1	2

3. Findings

3.1 Direct and indirect methods

Background

There has been a longstanding debate over whether the direct or indirect method of presenting operating cash flows provides better information, as each method has its distinct benefits and drawbacks (Krishnan and Largay 2000; Clinch et al. 2002; Bradbury 2011; Hales and Orpurt 2013). The direct method has been credited with practical benefits, such as helping entities resolve liquidity issues and making cash flow reports more user-friendly for managers without technical accounting expertise (Trout et al. 1993).[4] Some academic evidence also supports the view that the direct method provides useful information. For example, Orpurt and Zang (2009) found that the direct method enhances the ability to predict future cash flows. Farshadfar and Monem (2013) emphasised that the direct method provides granular information, unavailable through the indirect method, that enables users to make more informed decisions. Clacher et al. (2013) also found that the direct method provides incremental value relevance post-IFRS adoption in 2005, though they did not compare it to the indirect method. This aligns with the recommendation in paragraph 19 of AASB 107/IAS 7, which encourages entities to report cash flows from operating activities using the direct method.

However, not all research evidence agrees that direct method is superior to the indirect method. The literature presents mixed findings on the value relevance of the direct method. For example, Clinch et al. (2002), examining Australian companies from 1992–1997, concluded that the direct

[4] Trout et al. (1993:23) demonstrated the usefulness of the direct cash flow statement for Chicago Central Pacific Railroad to manage its liquidity crisis: "*Collecting the direct cash flow information and implementing the report provided meaningful insights into cash issues within the company. Also, the direct method made the report user friendly for managers with little technical accounting training.*"

method did not offer additional value beyond the indirect method for industrial firms, as market participants primarily rely on aggregate cash flow information rather than individual components. Kent and Birt (2021) showed that the information provided by the indirect presentation is as useful as the direct presentation; nonetheless, the latter is more helpful in certain situations, such as for entities with lower earnings quality or small-sized entities.

Before the adoption of International Financial Reporting Standards (IFRS),[5] Australian Accounting Standards mandated the presentation of operating cash flows using the direct method under paragraph 6.1 of AASB 1026 *Statement of Cash Flows* (initially published in 1991 and revised in 1997). Entities were also required to provide a reconciliation of cash flows arising from operating activities to operating profit or loss after income tax as reported in the profit or loss account. AASB 1026 emphasised that the direct method provided information not otherwise available in the other financial statements, offering a useful basis for estimating future cash flows (paragraph 6.2.2 of AASB 1026).

Following the adoption of IAS 7 (incorporated in AASB 107), Australian entities can choose to present their statement of cash flows using either the direct or indirect method. However, if the direct method is used, under paragraph 16 of AASB 1054 *Australian Additional Disclosures*, entities must provide a reconciliation of the net cash flow from operating activities to profit or loss. Given Australia's historical practice of requiring the direct method for presenting the statement of cash flows, along with the reconciliation of cash flows from operating activities to operating profit or loss after income tax (i.e. indirect method), many entities have continued the practice.

Nonetheless, the indirect method remains the dominant approach globally, particularly in the United States (US) and Europe, where the direct method is rarely used due to its complexity, higher costs and the need for significant changes to accounting systems (IASB and FASB 2011; Farshadfar and Monem 2013). For example, in contrast to the Australian market, only 2-3 % of US entities use the direct method (Krishnan and Largay 2000). Similarly, EFRAG (2024a) highlights the challenges of the direct method in Europe, noting that accounting systems are generally tailored to the indirect method and significant costs would be required to switch to the direct approach. Supporters of the indirect method highlight its ease of preparation and lower costs, arguing that the additional detail provided by the direct method does not always justify the increased effort and cost (Golub and Huffman 1984; Krishnan and Largay 2000; Hales and Orpurt 2013).

To gauge the current practice in Australia regarding the use of direct and/or indirect methods, the following sections outline the findings on whether direct and/or indirect methods are used among the ASX top 50.

[5] Australia has officially adopted IFRS since 1 January 2005 (IFRS Foundation 2017)

The use of the direct and indirect methods in Australia

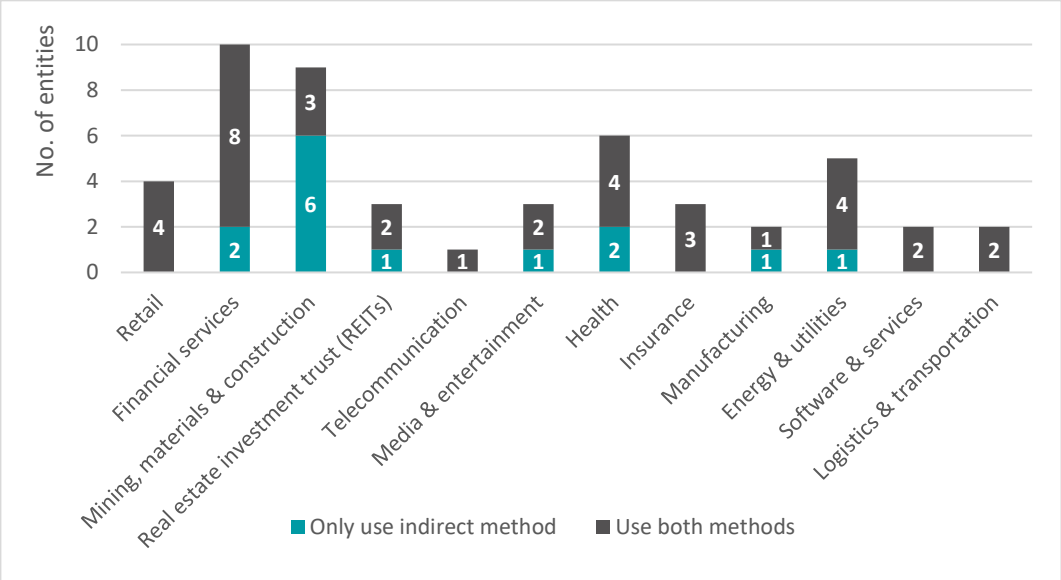
Table 2 shows that 72% of entities presented both the direct and indirect methods for reporting operating cash flows. That is, the direct method was used in the cash flow statements, while the reconciliation of profit to net operating cash flows under the indirect method was often disclosed in the notes to the financial statements. In contrast, 14 entities (28%) used the indirect method to present their cash flow statements. Of these, 13 entities are cross listed on exchanges in the US, Europe and South Africa apart from the ASX.

Table 2. Direct and indirect methods to present the operating cash flows

Method	No. of entities	%
Direct (primary statement of cash flows) and indirect methods (notes)	36	72
Indirect method only	14	28

Figure 1 shows that entities presenting operating cash flows using only the indirect method come from diverse sectors, including financial services; mining, materials and construction; real estate investment trust (REITs); media and entertainment; health; manufacturing; and energy and utilities. Given the dispersion of industries using the indirect method, this suggests that the choice to present cash flow statements using the indirect method is not primarily influenced by industry-specific factors.

Figure 1. Industry breakdown for methods used



The starting point for the indirect method

The indirect method for reporting cash flows from operating activities starts with profit or loss and adjusts for the effects of a non-cash nature, any deferrals or accruals of past or future operating cash receipts or payments, and items of income or expense associated with investing or financing cash

flows (paragraph 18 of AASB 107/ IAS 7). Although the illustrative examples in AASB 107/IAS 7 use profit before taxation to demonstrate the use of the indirect method, neither AASB 107/IAS 7 nor AASB 1054 prescribes which specific profit or loss figure (e.g. net profit/loss before tax, net profit/loss after tax, or profit and loss from continuing operations) should be used for the reconciliation (KPMG 2019a). As a result, variation in practice has emerged.

Table 3 shows that 46 entities (92%) used net profit/loss after tax as the starting point, while one entity (from the healthcare sector) used net profit/loss before tax and three entities (financial services, mining and software services sectors) used profit/loss from continuing operations.

Table 3. Starting point for the indirect method

Starting point	No. of entities	%
Net Profit/Loss before tax	1	2
Net Profit /Loss after tax	46	92
Profit/Loss from continuing operations	3	6

It is important to note that AASB 18/IFRS 18 recently amended paragraph 18(b) of AASB 107/IAS 7 to require operating profit[6] as the starting point for the indirect method cash flow statements in 2024 (IASB 2024d). As such, the amendment may have resolved concerns about the variation in practice, where entities used different profit measures, such as profit before or after tax, as the starting point for reconciliation.

3.2 Cash and cash equivalents (CCE)

Background

AASB 107/IAS 7 defines *cash* as cash on hand and demand deposits, while *cash equivalents* are short-term, highly liquid investments that can be easily converted into known amounts of cash with insignificant risk of changes in value (paragraph 6 of AASB 107/IAS 7). This definition emphasises that cash and cash equivalents are not held for investment purposes but to meet short-term cash commitments, highlighting their role in managing immediate liquidity needs. Furthermore, paragraph 7 of AASB 107/IAS 7 suggests, though does not prescribe, that short-term maturity is typically three months or less from the date of acquisition.

Paragraph 8 of AASB 107/IAS 7 also identifies circumstances where bank borrowings may be included as cash and cash equivalents. For instance, while bank borrowings are generally classified as financing activities, bank overdrafts that are repayable on demand and form an integral part of an entity's cash management strategy can be included as cash equivalents.

In terms of disclosure requirements, paragraph 45 of AASB 107/IAS 7 requires entities to disclose the

[6] Paragraph 70 of AASB 18/IFRS 18 clarifies that operating profit or loss comprises all income and expenses classified in the operating category.

specific components of cash and cash equivalents and reconcile these amounts in the statement of cash flows with those reported in the statement of financial position. Additionally, paragraph 48 of AASB 107/IAS 7 requires the disclosure of any restrictions on using cash and cash equivalents, such as funds that are not readily available due to legal or contractual constraints.

Despite these requirements, there is diversity in practice when determining cash and cash equivalents. A key issue lies in the subjective interpretation of the definition of cash equivalent, particularly the meaning of terms such as 'short-term', 'highly liquid' and 'insignificant risk', which leads to inconsistencies in assessing what qualifies as cash and cash equivalents. Presentation challenges also arise when items such as bank overdrafts and restricted cash are included in cash and cash equivalents but are not adequately disclosed, potentially obscuring information about the entity's liquidity position.

Disclosures of cash equivalents

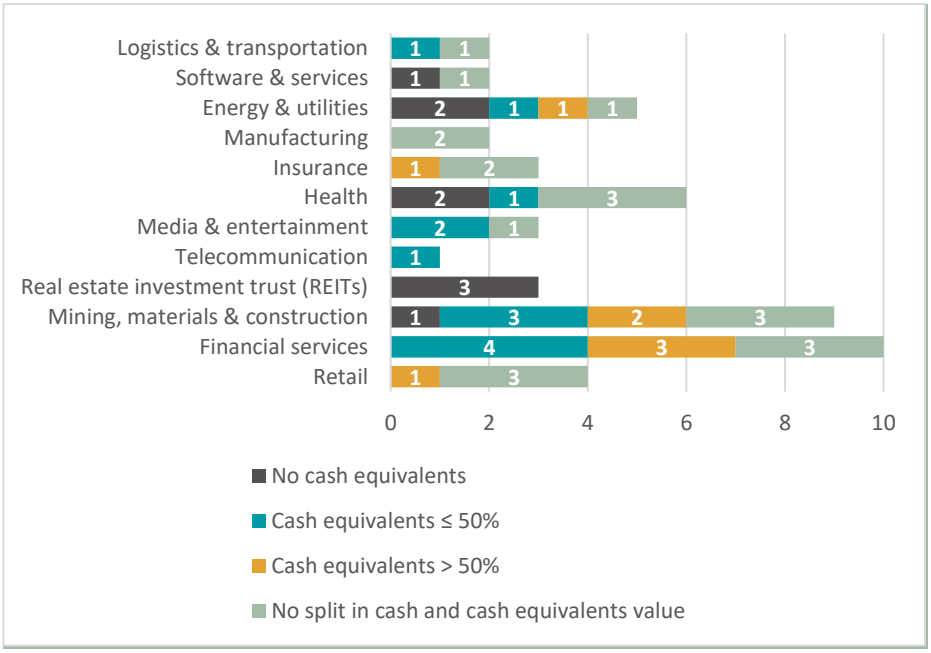
Table 4 and Figure 2 below present the proportion of cash equivalents (i.e. cash equivalents relative to the total of cash and cash equivalents) as disclosed in the notes to the financial statements, along with the corresponding industry breakdown of the sampled entities. Among the 50 entities reviewed, 30 entities (60%) reported the breakdown of their cash and cash equivalents components, either by presenting separate line items or through narrative disclosure. Of these 30 entities, eight entities (16%) reported that cash equivalents comprised more than 50% of their total cash and cash equivalents; while 13 entities (26%) that cash equivalents comprised 50% or less. The remaining nine entities disclosed that they held no cash equivalents (i.e. zero balance).

In addition, as shown in Table 4, 20 entities (40%) did not disaggregate the amounts of cash and cash equivalents. The reasons for the absence of disaggregated disclosure are unknown; it is possible that the amounts were considered immaterial. However, regardless of the reason, the lack of disaggregation may make it challenging for users to clearly understand the composition and the specific amounts of each component within cash and cash equivalents.

Table 4. Proportion of cash equivalents

Disaggregation of cash and cash equivalents	Cash equivalents relative to the total of cash and cash equivalents	No. of entities	%
Yes	0	9	18
	≤ 50% cash and cash equivalents	13	26
	> 50% cash and cash equivalents	8	16
No	N/A (Not provided)	20	40

Figure 2. Industry breakdown of cash & cash equivalents



Threshold of short-term maturity

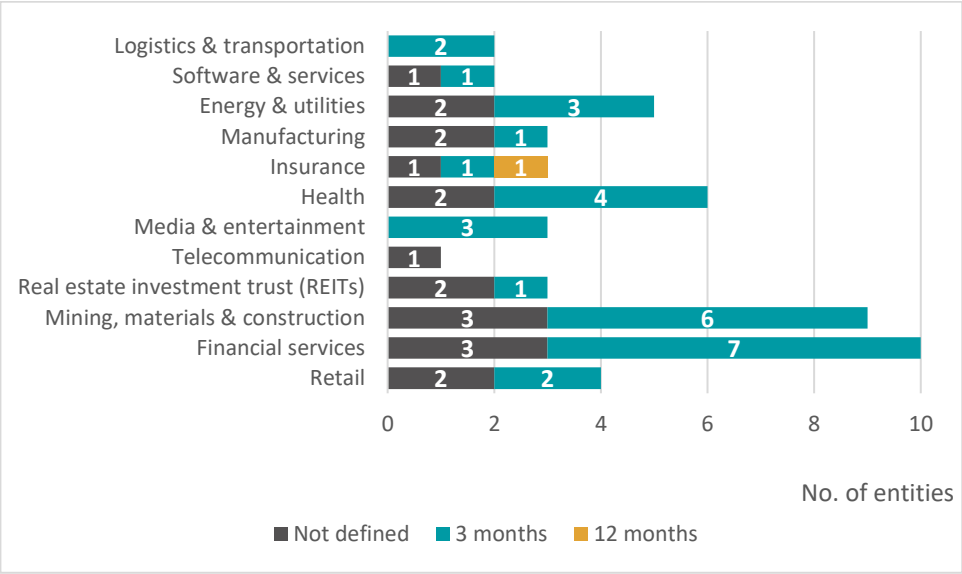
Under paragraphs 6 and 7 of AASB 107/IAS 7, cash equivalents are short-term maturity, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. However, the standard does not prescribe a specific threshold for what constitutes 'short-term' maturity; instead, it suggests that "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" (AASB 107/IAS7, paragraph 7, emphasis added).

Table 5 and Figure 3 present the disclosures by the ASX top 50 regarding the duration they consider as 'short-term' within the notes to the financial statements describing accounting policies for cash and cash equivalents. As shown in Table 5, 62% of the entities defined short-term maturity to be a period of three months. This three-month threshold was applied across all industries except telecommunications. Notably, one insurance entity defined short-term maturity as 12 months. The remaining 18 entities did not provide information about how they defined short-term maturity, which may lead users to question how cash and cash equivalents are determined and limit their ability to adjust the reported amounts for their own decision-making purposes.

Table 5. Threshold of short-term maturity in the accounting policy of cash and cash equivalents

Threshold of short-term maturity	No. of entities	%
3 months	31	62
12 months	1	2
N/A (Not defined)	18	36

Figure 3. Industry breakdown for the liquidity threshold



Overall, close to two-thirds of the entities adopted three-month duration as the threshold for short-term maturity, aligning with the suggestion in AASB 107/IAS 7. However, it remains unclear whether this three-month threshold continues to be appropriate in the current business environment, particularly given evolving business models in recent decades, and whether it should be reconsidered or revised. In addition, it is worth noting that over one-third of the entities did not explicitly disclose their definition of short-term maturity in their accounting policies. While AASB 101/IAS 1 *Presentation of Financial Statements* includes a general requirement for entities to disclose significant accounting policies, the absence of such disclosure is understandable, as AASB 107/IAS 7 does not explicitly mandate it. Nonetheless, including this information would enhance the transparency and clarity in the disclosure about cash equivalents. Given the significant number of entities omitting this detail, an explicit disclosure requirement may be warranted to improve consistency and comparability across financial statements.

3.3 Classification of operating, investing and financing

Background

Entities are required to classify cash flows into operating, investing and financing categories (paragraph 10 of AASB 107/IAS 7) in the statement of cash flows. However, classifying cash flows into the categories is not always straightforward. For example, an annual review conducted by the UK FRC (2022) revealed several entities restating cash flow statements due to errors in classifying operating, investing and financing activities, indicating that the classification can be complex and may require significant judgement in certain circumstances. Some stakeholders have also requested the standard setter to reconsider and revise the classification requirements.

Table 6 below highlights some general issues and feedback raised concerning the classification of cash flows.

Table 6. Common classification issues

Issues	Sources
1. Definition of operating activities	UK FRC (2016, 2017)
2. Classification of cash outflows to acquire property, plant and equipment	UK FRC (2016, 2017)
3. Classification of maintenance and growth CAPEX	UK FRC (2017); IASB (2024b)
4. Lease-related cash flows	UK FRC (2022)
5. Inconsistent categorisation for similar items	UK FRC (2022)
6. Classification of cash flows from interest and dividends	UK FRC (2016); IASB (2023a, 2024a)
7. Income tax cash flows	UK FRC (2016, 2017); FASB (2023)

Paragraph 6 of AASB 107/IAS 7 defines *operating activities* as "the principal revenue-producing activities of the entity and other activities that are not investing or financing activities". Some stakeholders have suggested that this definition should be revisited to establish clearer principles, rather than serving as a residual or default classification (UK FRC 2016, 2017). The UK FRC (2017) also suggested that cash outflows to acquire property, plant and equipment (PPE) should be classified as operating activities, rather than investing activities, given that such expenditures are integral to an entity's business operations.

In addition, some stakeholders have provided feedback that the standard should be updated to require more detailed disclosures in the cash flow statement regarding the classification of maintenance and growth CAPEX, including the extent to which expenditure on non-current assets represents replacement or expansion (UK FRC 2017; IASB 2024b). This feedback aligns with paragraph 50 of AASB 107/IAS 7, which encourages entities to provide such information. However, as discussed in Section 3.4 of this report, it remains unclear how such disclosures should be made, and few, if any, entities currently provide such information.

Furthermore, the classification of lease-related cash flows following the introduction of the new lease standard AASB 16/IFRS 16 *Leases* remains a subject of debate (UK FRC 2022) for both lessees (KPMG 2019b) and lessors (PWC 2021). For lessees, AASB 16/IFRS 16 eliminates the previous distinction between operating and finance leases, requiring almost all leases to be recognised on the balance sheet as right-of-use assets with corresponding lease liabilities. As a result, lessees must now allocate their lease payments into principal and interest components. The principal portion is classified as a financing activity, while the interest portion can be classified as either operating or financing activity, depending on the entity's accounting policy and the requirements of AASB 107/IAS 7. Variable lease payments, such as those based on future sales or usage rather than an index or rate, and payments for short-term or low-value leases not included in the lease liability should be classified as operating activities.

For lessors, however, lease accounting remains largely unchanged from previous standards, with leases still classified as either operating or finance leases. This creates a divergence in how lease cash flows are presented by lessees and lessors. Some stakeholders have also noted that it is debatable whether cash flows related to the acquisition of PPE intended to be routinely held for rent and subsequent sale should be classified as investing or operating activities (PWC 2021). Additionally, the UK FRC (2022) observed inconsistent categorisation of items with similar nature or substance. For example, cash flows related to lease interest payments were classified as financing activities, whereas cash flows related to interest on borrowings were categorised as operating activities.

Stakeholders have also recently raised concerns regarding the introduction of new categories for presenting income and expenses in the statement of profit or loss under AASB 18/IFRS 18, specifically, operating, investing and financing categories (EFRAG 2024a; IASB 2025). Despite using the same labels, these categories are not currently aligned with those used in the statement of cash flows under AASB 107/IAS 7 in some cases. As a result, inconsistencies can arise. For instance, income and expenses related to the use of PPE are classified as operating activities in the profit or loss statement under AASB 18/IFRS 18, whereas the cash flows associated with acquiring PPE are classified as investing activities in the statement of cash flows.

The discussion above provides several examples of stakeholder concerns regarding the classification in the statement of cash flows. This research specifically focuses on the classification of cash flows related to interest, dividends and income tax. This area is particularly relevant given the introduction of AASB 18/IFRS 18, which is effective for annual reporting periods beginning on or after 1 January 2027, with earlier application permitted. AASB 18/IFRS 18 introduces new requirements that affect how interest and dividends paid and received are presented in the statement of cash flows. Under the amendments to AASB 107/IAS 7 resulting from AASB 18/IFRS 18, these cash flows must now be classified consistently with the presentation of the related income and expenses in the statement of profit or loss. This change removes previous classification flexibility and aims to improve consistency across financial statements. Additionally, income tax cash flows are generally classified as operating activities unless they can be specifically identified with investing or financing transactions, requiring entities to exercise judgement. As such, this research aims to investigate how interest and dividends, and income tax cash flows have been classified in practice.

Classification of cash flows from interest and dividends

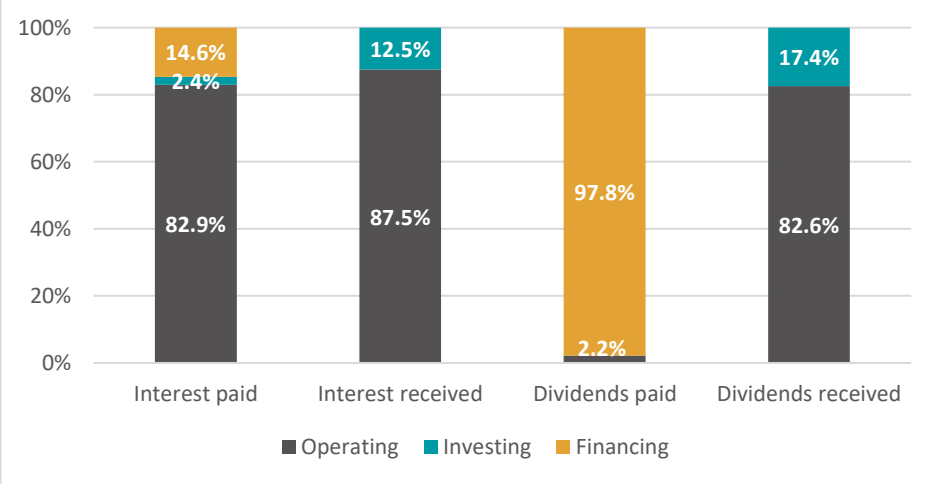
Paragraphs 33 and 34 of AASB 107/IAS 7 currently require an entity to disclose cash flows from interest and dividends separately but allow entities to classify: (1) interest and dividends paid as either operating or financing cash flows and (2) interest and dividends received as either operating or investing cash flows.[7] The implications of this classification choice have been extensively discussed in prior academic research (Charitou et al. 2018; Gordon et al. 2017; Baik et al. 2016). Research

[7] The amendments resulting from AASB 18/IFRS 18 are not yet effective, unless applied early.

generally shows that firms that classify interest payments outside of operating activity exhibit poorer future expected performance and lower disclosure quality than firms that classify interest payments as an operating activity. For example, Gordon et al. (2017) investigated the determinants and effects of classification flexibility for interest and dividends received or paid across 798 European firms. They identified key determinants such as capital market incentives (e.g. equity issuances), financial distress, leverage level and frequency of accessing the equity market. The study showed that firms with higher equity issuance activity and a greater likelihood of financial distress were more likely to rely on the classification choice to inflate operating cash flows. In contrast, firms with more analyst coverage and those cross-listed in the US are less likely to do so. The findings also indicated significant variation in classification across industries, with approximately 76%, 60% and 57% of firms classifying interest paid, interest received and dividends received, respectively, as operating activities.

Evidence from the ASX top 50 reveals that a total of 41, 40, 46 and 23 sampled entities disclosed interest paid, interest received, dividends paid and dividend received respectively in their statements of cash flows. Figure 4 further illustrates the variation in the classification of interest and dividend related cash flows within these disclosures. Notably, among the sampled entities disclosing dividends paid, almost 98% classified them as a financing activity. One mining entity classified dividends paid as both operating and financing: specifically, it classified "dividends paid to holders of non-controlling interests in subsidiaries" as an operating activity, while classifying "dividends paid to owners" as a financing activity. Some differences were also observed in the classification of cash flows for interest paid, interest received and dividends received. Nevertheless, those cash flows were mostly classified as operating activities.

Figure 4. Classification of interest- and dividends-related cash flows



Classification of income tax-related cash flow

Paragraph 35 of AASB 107/IAS 7 requires cash flows arising from taxes on income to be separately disclosed and classified as cash flows from operating activities unless they can be specifically identified with financing and investing activities.

As shown in Table 7, cash flows arising from taxes on income were classified as operating cash flows by 82% the ASX top 50. Only one entity (2%) allocated tax-related cash flow across both the operating and investing activities, classifying income tax refunds related to the disposal of subsidiaries as investing cash flows. Another entity (2%) did not provide any disclosure regarding cash flows related to income tax.

Table 7. Classification of income tax-related cash flows

Classification	Number of entities	%
Operating	41	82
Operating and investing	1	2
Disclose separately in the supplemental cash flow information section (not being classified under operating, investing or financing labels in cash flow statements)	7	14
N/A (no disclosure)	1	2

In addition, the evidence from the ASX top 50 shows that when entities used only the indirect method in reporting cash flows from operating activities, income tax-related cash flows may be either: (1) disclosed separately as a line item in the cash flows from operating activities; or (2) disclosed separately in the supplemental cash flow information (not using operating, investing or financing labels). These variations suggest that enhanced disclosure requirements may be warranted to ensure users can better access information on income tax-related cash flows.

3.4 Encouraged voluntary disclosures

Background

The term *encouraged voluntary disclosures* refers to additional information that AASB 107/IAS 7 does not mandate but encourages entities to provide. Paragraph 50 of AASB 107/IAS 7 currently encourages entities to voluntarily disclose additional relevant information that help users in understanding an entity's financial position and liquidity. Such disclosures may include: (a) undrawn borrowing facilities; (b) cash flows related to increased and maintained operating capacity; and (c) cash flows of reportable segments.[8]

Table 8. Encouraged voluntary disclosures under AASB 107/IAS 7

	Undrawn borrowings (paragraph 50(a))	**Cash flows to grow and maintain operating capacity** (paragraph 50(c))	**Cash flows of reportable segments** (paragraph 50(d))
Disclosures made by the ASX top 50	Almost all entities disclosed (92%)	Limited disclosure (4%)	No disclosure

[8] See paragraph 50(a)-(d) of AASB 107/IAS 7.

Undrawn borrowings

Disclosures about undrawn borrowing facilities provide key information on liquidity and information relating to cash availability. The disclosure is required in AASB 7/IFRS 7 *Financial Instruments Disclosures,* where paragraph 39(c) of AASB 7/IFRS 7 mandates that entities to disclose how they manage liquidity risk, which may include details about undrawn borrowing facilities. Additionally, paragraph 50(a) of AASB 107/IAS 7 encourages entities to report "the amount of undrawn borrowing facilities that may be available for future operating activities and to settle capital commitments, indicating any restrictions on the use of these facilities".

The findings from this research show that 92% of the entities provided some form of liquidity risk management disclosures in the notes to their financial statements, which is unsurprising given the disclosure requirement under paragraph 39(c) of AASB 7/IFRS 7. However, it remains unclear whether these disclosures provide sufficient information for users to assess related cash flow information. Accordingly, further research may be warranted to determine whether such disclosures adequately meet user needs.

Cash flows to grow and maintain operating capacity

AASB 107/IAS 7 also encourages entities to disclose the aggregate amount of cash flows that represent increases in operating capacity (i.e. *growth* CAPEX) separately from those cash flows that are required to maintain operating capacity (i.e. *maintenance* CAPEX). The distinction between maintenance CAPEX and growth CAPEX is crucial (Liang and Linsmeier 2025). While maintenance CAPEX is essential to preserve a business's operating capacity for ongoing operations, users want to understand whether an entity has allocated spending to growth CAPEX, which reflects the entity's strategic intent to expand the business and operations (IASB 2024b).

However, practical guidance on defining and determining growth and maintenance CAPEX is limited, and there is a lack of guidance on how to disclose such information. Although such disaggregated information would be beneficial, concerns remain that preparers may face practical challenges in distinguishing between growth and maintenance CAPEX, as they often overlap and are interrelated (IASB 2024c).

The findings from this research show that disclosures about cash flows relating to growth and maintenance CAPEX are limited in the financial reports of the ASX top 50. Only two entities disclosed information regarding the replacement and expansion of CAPEX in the financial review section (i.e. management commentary) of their annual report rather than in the financial statements:

> $27.2m in assets (PPE) mostly related to data center capacity expansion, and IT infrastructure investments to enhance scalability, reliability and security (WiseTech Global 2023:102).
>
> Our capital expenditure of $7.1 billion was comprised of $1.0 billion of growth, $1.6 billion of replacement, $4.3 billion of sustaining and $0.2 billion of decarbonisation capital (in addition to

> $0.2 billion of decarbonisation spend in operating costs). We expect to spend around $4.0 billion each year on sustaining capital; spend in 2023 included the smelter and refinery rebuild at Kennecott ($0.3 billion) and targeted investment in asset health in Iron Ore and Aluminium. We funded our capital expenditure from operating activities and generally expect to continue funding our capital program from internal sources (Rio Tinto 2023:27).

WiseTech's CAPEX cash outflow of AUD27.2 million was primarily for growth CAPEX to enhance technological capacity and increase operational capacity. However, this investment not only aimed for expansion (scalability) but also related to the quality and security of its information technology and data infrastructure.

Compared to WiseTech, Rio Tinto's CAPEX in 2023 was presented in greater detail, broken down into four specific categories: growth, replacement, sustaining and decarbonisation. Growth CAPEX (USD1 billion) was allocated for expanding operation and production capacity while replacement CAPEX (USD1.6 billion) was used to substitute outdated and/or faulty assets, preventing reductions in operational efficiency. Sustaining CAPEX (USD4.3 billion) was spent to "ensure the integrity of assets[9]" (Rio Tinto 2023:204) and decarbonisation CAPEX (USD0.2 billion) reflected investing cash flow directly towards sustainability commitments, such as increased usage of "renewable power, electrifying processing and running electric mobile fleets" (Rio Tinto 2024:8). Furthermore, the company highlighted that its CAPEX was funded from internal sources generated through operating activities rather than relying on external financing. This detailed disclosure of CAPEX categories, alongside information about the funding sources, provides insights for investors to assess the entity's capital allocation and liquidity management.

Cash flows of reportable segments

The requirements for segment reporting are addressed in AASB 8/IFRS 8 *Operating Segments*. However, some studies have noted that segment disclosures are insufficient (Barneto and Ouvrard 2015; Kajüter and Nienhaus 2017) and have highlighted the usefulness of segmental cash flow information for users and lenders (Street and Stanga 1989; IASB 2024b). For example, Street and Stanga (1989) noted that the segmental cash flow information would be highly relevant to the lending decisions of banks. Nevertheless, the findings of this research show that none of the ASX top 50 provided such disclosures, as shown in Table 8. Segment reporting often prioritises other financial metrics, particularly earnings-related performance indicators (e.g. revenue, other comprehensive income, and earnings before interest, taxes, depreciation and amortisation) over cash flow information. Given that the IASB has included segment reporting in its research projects pipeline following its third agenda consultation, and subject to the forthcoming agenda consultation, a revision of segment reporting requirements is warranted. This revision should consider whether, and if so, how, segmental cash flow information should be disclosed.

[9] Asset integrity management aims to maintain efficiency and accuracy in the operation of assets.

3.5 Free cash flow (FCF)

Background

Although many definitions of FCF exist, one of the earliest conceptualisations described it as "cash flow in excess of that required to fund all projects that have positive net present values when discounted at the relevant cost of capital" (Jensen 1986:323).

Extant literature highlights the incremental informational value of FCF in decision making. Prior research has examined the impact of FCF on firm valuation (Brush et al. 2000), firm performance (Kadioglu et al. 2017), audit pricing (Gul and Tsui 1997) and investment decision making (Carroll and Griffith 2001; Richardson 2006; Chen et al. 2016). Furthermore, research evidence shows that voluntary disclosure of FCF has grown significantly over time (Adhikari and Duru 2006; Adame et al 2023). For example, Adhikari and Duru (2006) documented that the number of entities voluntarily disclosing FCF increased nearly 15 times between 1994 and 2004, suggesting the growing importance of this information to users.

During the development of IFRS 18, the IASB received feedback highlighting that FCF is widely used by entities as a key performance metric. However, the IASB concluded that FCF is derived from the cash flow statement rather than the income statement, and, therefore, does not meet the criterion of being a subtotal of income and expenses. Consequently, FCF was excluded from the scope of IFRS 18's management performance measures (IASB 2023b).

The prevalence of FCF and industry breakdown

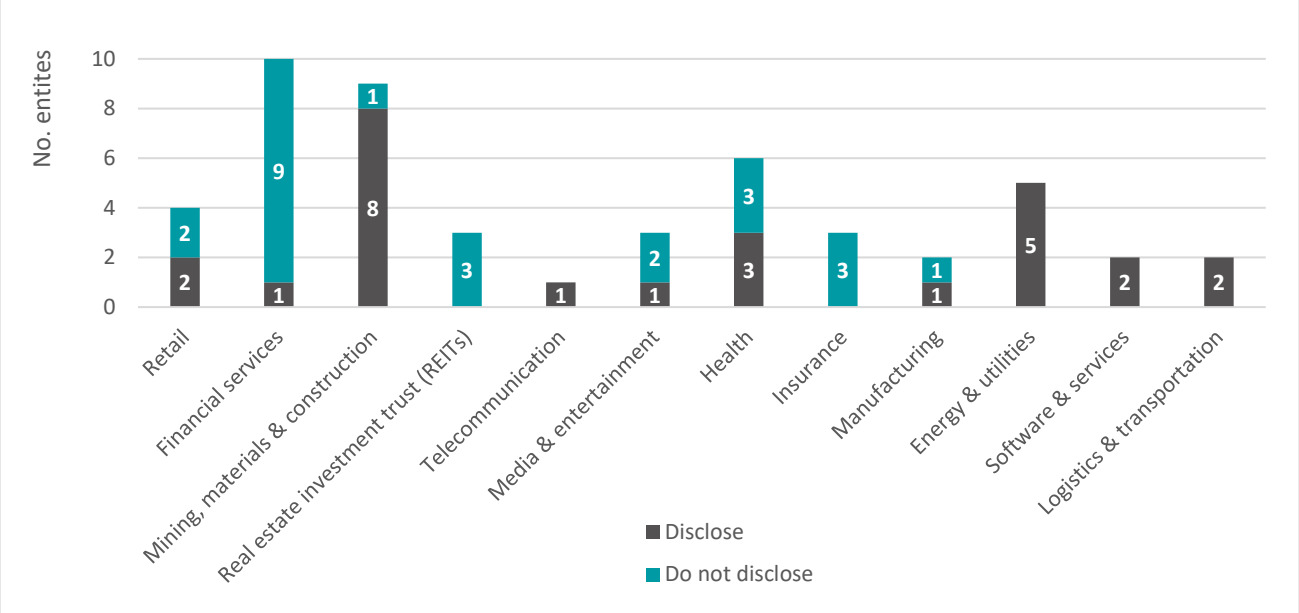
Table 9 presents the reporting of FCF in the annual reports of the ASX top 50. It should be highlighted that 52% of the entities disclosed FCF, although the nature and level of detail varied. For example, some entities provided the value of FCF but did not provide details on how FCF was calculated. In contrast, other entities provided more comprehensive disclosures, including the definition, components and calculation of FCF.

Table 9. Disclosure of FCF in annual reports

The disclosure of FCF	No. of entities	%
Disclose FCF	26	52
Do not disclose FCF	24	48

Figure 5 further illustrates that FCF disclosure was particularly prevalent in certain industries, such as energy and utilities (100%) and mining, materials and construction (89%), while it was less common in financial services (10%). Notably, no FCF disclosures were observed in REITs and insurance sectors within the sample.

Figure 5. Industry breakdown for FCF disclosure



The nature of FCF disclosure

Our review of the ASX top 50 shows that FCF was disclosed in different sections of the annual report. The sections include:

- Company's outlook
- Financial highlights
- Company's key performance indicators
- Director's report
- Business strategy and performance summary
- Segment's financial performance
- Financial position and capital management
- Capital allocation and management
- Strategy and value creation
- Remuneration report
- Letter to shareholders

The findings from this research indicate that the extent to which the FCF is mentioned, calculated and discussed varies considerably across entities and sectors. Prior research highlights that voluntary disclosure and forecasting of cash-based measures, including FCF, often aim to signal positive cash flow trends, growth potential and to satisfy investor demand for cash flow information (Wasley and Wu 2006). Consistent with these observations, some entities used FCF disclosures to demonstrate their strong financial position, particularly within strategic reports and directors' reports, as illustrated by the following examples:

> Strong free cash flow generation provides funding for market growth activities and R&D as well as the ability to reward shareholders with a growing dividend stream (Cochlear 2023:58)

> As a result of the strong production and gold price realized during the year, the Company generated Underlying EBITDA of $1.5 billion. This translated into operating cash flows of $1.4 billion (FY22: $1.6B)

> and underlying free cash flows of $359 million, highlighting the Company's continued ability to generate cash from operations while investing in its future (Northern Star 2023:28)

In addition, some entities disclosed that they used FCF information for an internal measure to allocate and manage capital efficiently, as reflected in the following excerpts:

> […] regularly monitors its capital requirements using various benchmarks, with the main internal measures being free cash flow and debt to EBITDA (Wesfarmers 2023:154)

> Our Capital Allocation framework prioritizes the use of free cash flow as follows: invest in organic growth; maintain a flexible balance sheet; and deploy excess capital to shareholders via a share buyback program (James Hardie 2023:105)

Furthermore, FCF was commonly linked to remuneration, in both short-term and long-term incentive plans:

> Short-term incentive plan free cash flow demonstrates how we convert underlying earnings to cash and provides further insight into how we are managing costs, efficiency and productivity (Rio Tinto 2023:130)

> The target range for the FCF measure in the Long-Term Incentive plans considers forecast financial performance over the three years in which the award is measured. This three-year forecast reflects near-term FCF growth generated by the business together with planned activities that deliver value over the longer term (Transurban Group 2023:101).

Diverse definition and measurement of FCF

While there is a common understanding of FCF as cash available for distribution and reinvestment and free from encumbrances (IFRS Foundation 2019), differences in its determination are evident, as shown in Table 10.

Table 10. Variation in the definition and measurement of FCF

Definition and measurement of FCF	Examples
Net operating cash flows less net investing cash flows	BHP Group (2023:94)
Operating cash flows less investing cash flows (net of acquisitions and disposals and major growth CAPEX) less lease liability payments	Santos (2023:153)
Normalised EBITDA less net movements in working capital, income tax paid and lease payments. (Normalised EBITDA = EBITDA adjusted to exclude impairment, business acquisition costs and finance costs.)	Reece Group (2023:27)
Cash flow generated after net CAPEX, finance costs and tax, but excluding the net cost of acquisitions and proceeds from business disposals	Brambles (2023:142)

The IASB (2021) has engaged in discussions regarding the potential standardisation of FCF determination. However, achieving such standardisation remains challenging because each entity defines and calculates FCF based on its own specific needs, historical practices and perspectives on what information is most useful. These variations stem from differences in business models, industry practices, management objectives and the diverse ways entities use FCF internally and externally. Consequently, there is no single, universally accepted definition or calculation method for FCF, which complicates efforts to establish a standardised approach.

4. Conclusion and limitations

Overall findings

This research report examines the presentation and disclosure of cash flow statements and related information in the annual reports of the ASX top 50 in 2023. Key findings are as follows:

- 72% of entities presented cash flows from operating activities using both direct and indirect methods;
- 40% of entities did not provide disaggregated information on the amounts of cash and cash equivalents. Additionally, many entities considered three months as the threshold for short-term maturity, aligning with the suggestion in AASB 107/IAS 7;
- There was inconsistency in the classification of cash flow items, particularly cash receipts and payments related to interest and dividends, across operating, investing and financing activities. Furthermore, the majority of entities classified cash flows arising from taxes on income as operating activities;
- Almost all entities reported undrawn borrowings; however almost all entities did not provide disaggregated cash flow information related to growth and maintenance CAPEX and none of sampled entities disclosed segmental cash flows; and
- FCF was commonly disclosed across entities; nonetheless, the extent to which the FCF was mentioned, calculated and discussed varied considerably across entities and sectors.

These findings support the recommendation that the IASB should conduct further work on improving IAS 7, particularly regarding the items discussed in this report.

Limitations

We acknowledge several limitations of this research. First, given the small sample size, our findings may not be generalisable to a larger population but, instead, offer insights for standard setters in their review of IAS 7 based on a subset of Australian entities. Notwithstanding the small sample, this investigation did cover a diverse range of industries. Second, the sample focused only on Australia's largest listed entities, which do not represent the full range of entities in the Australian economy,

such as not-for-profit, proprietary and small-/medium-sized entities. Third, the findings were solely drawn from reviewing and analysing the statement of cash flows and other related cash flow information extracted from annual reports. Investigating accounting narratives from annual reports, as a documentary analysis method, is widely used in accounting research (Campbell et al. 2009; Beattie 2014). However, this method has its own weaknesses regarding completeness, accuracy and bias in data (Ahmed 2010).

Acknowledging the above limitations, the AASB is currently conducting stage two of this research project. In the second research phase, in-depth semi-structured interviews are conducted with relevant stakeholders, including preparers, users and auditors, to identify what the deficiencies are in the cash flow statement or other related cash flow information. The triangulation between archival data obtained from the present report and insights obtained from those interviews is paramount to probe potential issues to be addressed by standard setters in the future.

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Appendix

The ASX top 50 entities reviewed in the year of 2023

No.	ASX code	Company name	Number of pages reviewed
1	BHP	BHP Group Limited	252
2	CBA	Commonwealth Bank of Australia	308
3	CSL	CSL Limited	176
4	NAB	National Australia bank Limited	280
5	WBC	Westpac Banking Corporation	334
6	ANZ	Australia and New Zealand Banking Group Ltd	222
7	FMG	Fortescue Ltd	184
8	WES	Wesfarmers Limited	193
9	MQG	Macquarie Group Limited	308
10	NEM	Newmont Corporation	222
11	SQ2	Block Inc.	239
12	GMG	Goodman Group	222
13	WDS	Woodside Energy Group Ltd	220
14	RIO	Rio Tinto Limited	360
15	TLS	Telstra Group Ltd	193
16	RMD	ResMed Inc	108
17	TCL	Transurban Group	234
18	WOW	Woolworths Group Limited	187
19	WTC	WiseTech Global Ltd	165
20	QBE	QBE Insurance Group Ltd	238
21	ALL	Aristocrat Leisure Limited	131
22	JHX	James Hardie Industries plc	203
23	STO	Santos Ltd	160
24	REA	Rea Group Ltd	132
25	NWS	News Corporation	146
26	BXB	Brambles Ltd	135
27	COL	Coles Group Ltd	139
28	COH	Cochlear Ltd	172
29	SUN	Suncorp Group Ltd	191
30	AMC	Amcor CDI	143
31	XRO	Xero Ltd	170
32	REH	Reece Ltd	100
33	NST	Northern Star Resources Ltd	176
34	SCG	Scentre Group	137
35	URW	Unibail-Rodamco-Westfield CDI	141
36	ORG	Origin Energy Ltd	201
37	IAG	Insurance Australia Group Ltd	156
38	CPU	Computershare Ltd	144

39	VAS	Vanguard Australian Shares Index Fund	55
40	SVW	Seven Group Holdings Ltd	173
41	S32	South32 Ltd	193
42	MEZ	Meridian Energy Ltd	321
43	SHL	Sonic Healthcare Ltd	158
44	MIN	Mineral Resources Ltd	261
45	FPH	Fisher & Paykel Healthcare Corporation Ltd	214
46	LNW	Light & Wonder, Inc.	121
47	CAR	CAR Group Limited	169
48	RHC	Ramsay Health Care Limited	152
49	ASX	ASX Limited	142
50	SOL	Washington H Soul Pattinson & Company Limited	196