



International Organization of Securities Commissions
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المنظمة الدولية لهيئات الأوراق المالية

14 March 2022

International Accounting Standards Board
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

Our Ref: 2022/O/C1/IASB/MS/2.

RE: Exposure Draft | Non-current Liabilities with Covenants - Proposed Amendments to IAS 1

Dear International Accounting Standards Board (IASB or the “Board”) Members,

The International Organization of Securities Commissions (IOSCO) Committee on Issuer Accounting, Auditing and Disclosure (Committee 1) thanks you for the opportunity to provide our comments on the Exposure Draft | Non-current Liabilities with Covenants - Proposed Amendments to IAS 1 (Amendments to IAS 1)

IOSCO is committed to promoting the integrity of the international markets through promotion of high-quality accounting standards, including rigorous application and enforcement. Members of Committee 1 seek to further IOSCO's mission through thoughtful consideration of accounting and disclosure concerns and pursuit of improved transparency of global financial reporting. The comments we have provided herein reflect the general consensus among the members of Committee 1 and are not intended to include all of the comments that might be provided by individual securities regulator members on behalf of their respective jurisdictions.

General Observations

Members of Committee 1 (“members” or “we”) appreciate the Board’s willingness to revisit the topic of non-current liabilities with covenants considering emerging stakeholder feedback.

Overall, we support the Board’s effort to improve the information an entity provides about liabilities with covenants, in addition to addressing stakeholders’ concerns about how an entity classifies those liabilities as current or non-current.



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Classification & Disclosure

Classification

Classification Boundary

Most members agree with the classification proposal (i.e., an entity would classify liabilities as current or non-current based on its compliance with covenants required only *on or before* the reporting date).¹

In addition, members believe the Conceptual Framework for Financial Reporting does not prohibit the inclusion of forward-looking information in the notes to the financial statements. We observe, for example, in accordance with IAS 1 *Presentation of Financial Statements* (IAS 1), management assesses an entity's ability to continue as a going concern and uses, among other things, forward-looking information to make this assessment.² We do not believe the requirement in paragraph 76ZA(b)(iii) would be inconsistent with IFRS or cause undue burden on management.

A few members disagree with the proposals and believe that specified conditions with which an entity must comply within twelve months *after* the reporting period should affect the classification of a liability as current or non-current at the end of the reporting period.³ These members acknowledge the rationale included paragraph BC16 in the Basis for Conclusions but nonetheless believe consideration of forward-looking information has the potential to produce more relevant information to investors.

Management Expectations

Notwithstanding the above, some members recommend that the Board clarify the interaction between paragraph 69(a) and paragraph 69(d) of IAS 1. Since IAS 1.69(a) uses the term “expects” some consider that a view could arise that management expectations regarding compliance with a future debt covenant test are relevant for classification purposes.

¹ Specifically, specified conditions with which an entity must comply within twelve months after the reporting period have *no* effect on whether an entity has, at the end of the reporting period, a right to defer settlement of a liability for at least twelve months after the reporting period. Such conditions would therefore have *no* effect on the classification of a liability as current or non-current.

² Similar requirements exist under US GAAP (e.g., (ASC Subtopic 205-40).

³ Specifically, these members believe specified conditions with which an entity must comply within twelve months after the reporting period, especially in those circumstances where the issuer considers that it is highly likely that it will not comply with those conditions so the financial liability would be repayable unless the borrower provides a waiver, *should* affect whether an entity has, at the end of the reporting period, a right to defer settlement of a liability for at least twelve months after the reporting period.



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Specified Conditions

Considering the wide range of “specified conditions” an entity might need to comply with (i.e., a range of potential financial and non-financial conditions), a few members suggest the Board either clarify the scope of “specified conditions” or define the term. Without this clarity, these members expect diversity in practice to arise.

Other Conditional Settlement Terms

When reading paragraph 72C(b) and related the Basis for Conclusions (paragraphs BC18 - BC20), there is confusion on what transactions are captured by these paragraphs, and therefore fall outside the scope of 72B.⁴ For example, many members observe common features of debt agreements include provisions relating to “change of control” and “timely submission of audited financial statements” – which is an event or outcome that is arguably unaffected by the entity’s future actions.

We encourage the Board not to use the notion of “unaffected by the entity’s future actions”, as there is a substantial risk that the proposed wording will cause confusion and divergent interpretation. Instead, we recommend the Board to either:

- revise the condition to state that an obligation to repay because of a discrete event⁵ occurring *after* the end of the reporting period does not affect classification at the end of the reporting period⁶, or
- if the Board chooses not to revise the condition, then to clarify what is meant by a “future event or outcome...is unaffected by the entity’s future actions” and consider application guidance in the body of the standard. For example, is a liability with various settlement outcomes, some of which the entity might influence or affect by their future actions qualify for consideration under paragraph 72B?

⁴ An entity’s right to defer settlement of a liability for at least twelve months after the reporting period may be subject to the entity complying with specified conditions (often referred to as ‘covenants’).

⁵ Examples of discrete events *after* the reporting period may include: change of control, change of management, Initial Public Offering, de-listing event, change of law, weather condition, commodity conditions, timely submission of audited financial statements.

⁶ One member recommends the content included in paragraph BC20 of the Basis for Conclusions be included, in some form, in the body of the standard. This member believes that non-native English speakers may not appreciate the nuance between “affect” and “control” and therefore consider explanatory information in the body of the standard to be necessary. This member observes that paragraph 25 of IAS 32 considers an entity’s future net income as beyond the control of the entity. A fine line exists between an entity’s future actions being able to *affect* its future profitability but not *control* it. This member believes that the Board should clarify the distinction, and the application of this proposed IAS 1 guidance compared to the existing IAS 32 guidance.



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To avoid uncertainty, one member suggests the Board clarify whether the concept of “genuine” applies in the context of paragraph 72C(b). In their view, to minimize diversity, this concept should not apply.⁷

Grace Period

Some members suggest the Board explicitly clarify the interaction between paragraph 72B(b) and paragraph 75 of IAS 1 for situations where at the end of the reporting period an entity has received a waiver and is in a grace period ending *within* twelve months. Members consider that unless the period of grace covers at least twelve months *after* the reporting period, the entity shall classify the liability as current.

Disclosure

A few members suggest that paragraph 76ZA(b)(i) be clarified to explicitly require disclosure of the “nature and the date on which the entity must comply” rather than identifying such information as an example.

A few members disagree with the proposed disclosure requirement in paragraph 76ZA(b)(iii) because, among other things, they consider the disclosures to be speculative in nature and unlikely to result in entity-specific information. These members suggest the proposed disclosure be revised as follows:

76ZA(b)(iii) “any cyclical in the business, or other factors, relevant to understanding the ability of the entity to meet its covenant requirements during the 12 months following the reporting date.”

In addition, a few members consider the overall proposed disclosures to be better associated with disclosures regarding going concern or “close-call” situations and therefore consider the proposed disclosure, outside of such contexts, to be less meaningful to investors.⁸

Presentation

Disaggregation

While many members do not theoretically disagree with the “disaggregation” proposal⁹ contained in paragraph 76ZA(a) and acknowledge the rationale included in paragraph BC21 in the Basis for Conclusions, these members believe the proposed presentation may not achieve the desired objectives

⁷ The concept of “genuine” is considered in other standards such as IFRS 9, IFRS 16 *Leases* and IAS 32 *Financial Instruments - Presentation*. For example, IFRS 16.B42 and IAS 32.25.

⁸ For example, paragraph 25 of IAS 1 states “when management is aware, in making its assessment, of material uncertainties related to events or conditions that may cast significant doubt upon the entity’s ability to continue as a going concern, the entity shall disclose those uncertainties”.

⁹ Specifically, to present separately, in its statement of financial position, liabilities classified as non-current for which the entity’s right to defer settlement for at least twelve months after the reporting period is subject to compliance with specified conditions within twelve months after the reporting period.



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because, among other things, the conditions envisioned in paragraph 76ZA(a) are likely to exist in many entities, resulting in such presentation being pervasive and commonplace. For example, debt agreements subject to conditions (i.e., covenants), either financial or non-financial, where failure to meet a condition could result in the lender being able to demand repayment immediately are pervasive.

As a result, most members believe that absent basing the disaggregation on a characteristic *beyond* a contract containing a condition, such as a likelihood threshold of covenants being breached within twelve months or those debt contracts in which management believes are substantially uncertain of not breaching the covenant threshold, or some other characteristic, the disaggregation may not result in a meaningful distinction for investors.

Consistent with the views expressed in paragraph AV4 in the Exposure Draft, many members consider paragraph 55 of IAS 1 to contain sufficient requirements on disaggregation and do not believe additional requirements are necessary.¹⁰ However, several members believe guidance on the application of paragraph 55 of IAS 1 in the context of debt agreements with conditions (at the contract level) would be useful.

A few members consider separate presentation based on management expectations rather than those outlined in the proposals to provide more relevant information to investors.¹¹

Level of Disaggregation

Notwithstanding our comments above, some members observe that paragraph 76ZA(a) is unclear about the level of disaggregation. Specifically, does paragraph 76ZA(a) require separate presentation by:

- *Condition* – non-current liabilities with conditions and those without, resulting in two non-current line items, or
- *Contract* - contract level resulting in potentially several separate non-current line items.

If the Board retains the disaggregation proposal, these members recommend the level of disaggregation in paragraph 76ZA(a) be clarified. In making its determination regarding the level of disaggregation, the Board should consider not only the “human readable” layer of financial statements but also the increased

¹⁰ Among other things, these members observe that including a mandatory requirement for separate presentation is unnecessary for most entities that are at no material risk of breaching covenant requirements.

¹¹ Specifically, these members consider if the entity assesses that it is [highly] likely [or virtually certain] that it will *not* comply with the specified conditions within twelve months after the reporting period, so the liability is expected to become repayable unless the borrower provides a waiver, separate presentation of this liability (within the non-current liabilities) in the statement of financial position is appropriate. These members acknowledge the alternatives considered in paragraph BC22 of the Basis for Conclusion but are not supportive of these alternatives.



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prevalence of digital reporting and use of tagging as it allows for more line items (i.e., at the contract level) to be reported on the face of the financial statements as preparers are not constrained by page size.

We appreciate your thoughtful consideration of the views provided in this letter.

If you have any questions or need additional information, please do not hesitate to contact Cameron McInnis, Chair of the Accounting Subcommittee of Committee 1 at +1 416-593-3675 or myself. In case of any written communication, please mark a copy to me.

Yours sincerely,



Makoto Sonoda



Chair
Committee on Issuer, Accounting, Audit and Disclosure
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