



Organización Internacional de Comisiones de Valores
International Organisation of Securities Commissions
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15 June 2015

International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

RE: Exposure Draft: *Classification of Liabilities, Proposed amendments to IAS 1*

Our Reference: 2015/JE/C1/IASB/69

Dear IASB Members:

The International Organization of Securities Commissions (IOSCO) Committee on Issuer Accounting, Audit and Disclosure (Committee 1 or C1) thanks you for the opportunity to provide our comments regarding the International Accounting Standards Board (IASB or the Board) Exposure Draft: *Classification of Liabilities, Proposed amendments to IAS 1 (the Exposure Draft or ED)*.

IOSCO is committed to promoting the integrity of 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 a 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 are supportive of the Board's overall objective to clarify the criteria for the classification of a liability as either current or non-current.

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Question 1—Classification based on the entity’s rights at the end of the reporting period

The IASB proposes clarifying that the classification of liabilities as either current or non-current should be based on the entity’s rights at the end of the reporting period. To make that clear, the IASB proposes:

- (a) replacing ‘discretion’ in paragraph 73 of the Standard with ‘right’ to align it with the requirements of paragraph 69(d) of the Standard;
- (b) making it explicit in paragraphs 69(d) and 73 of the Standard that only rights in place at the reporting date should affect this classification of a liability; and
- (c) deleting ‘unconditional’ from paragraph 69(d) of the Standard so that ‘an unconditional right’ is replaced by ‘a right’.

Do you agree with the proposed amendments? Why or why not?

Rights versus Management Expectations

Members raise the question of whether the Board’s intention to focus only on rights in place at the reporting date also incorporates any aspect of management intentions and expectations and believe additional clarity should be provided. The removal of the word “expects” from paragraph 72(a) appears to link classification solely to a right to roll-over debt at the end of the reporting period and disregards the impact of any right to settle the debt early. In contrast, paragraph 69(a) will remain unchanged to indicate that an entity shall classify a liability as current when it expects to settle the liability in its normal operating cycle. Because this may create some question as to the principle to be followed in paragraph 69, Members believe the following points should be addressed:

- Further clarify whether or not paragraph 69(a) is meant to: (i) require an entity to classify any liability as current if it intends to settle it within 12 months after the reporting period even when the entity has the right, as of the end of the reporting period, to settle the liability after 12 months; or (ii) only is intended to apply to working capital items as suggested in paragraph 70 of IAS 1, exclusive of current portions of long-term debt.
- If the Board is making a distinction in paragraph 69 between how debt and working capital items should be evaluated for current and non-current classification through the amendments to IAS 1, Members believe additional discussion should be provided in the Basis of Conclusion as to the conceptual reasons for this distinction so it is clear what types of liabilities should only be evaluated based on a right to defer repayment as opposed to an expectation to make repayment.

Disclosure about Management Intentions

While members note the concerns the Board expressed in paragraph BC16 about “... too much emphasis on management intentions and expectations”, without considering any expectations of timing of cash flows, an entity may be required to classify a liability as noncurrent which it fully expects and has evidence to support at period end that the liability will be settled in the next 12 months notwithstanding a right to roll-over or defer settlement exists. Members are concerned that this could result in less relevant information to investors unless the presentation on the face of the statement of position is supplemented with footnote disclosure describing the expected current uses

of cash that may exceed the amount presented as current on the face of the statement of position. For example, an entity may need to settle its debt shortly after the end of the reporting period rather than exercise its right to roll-over the debt because the terms and conditions of the roll-over right are no longer at market terms or such terms have become uneconomic compared to other means of financing which the entity is sourcing (e.g., equity or other debt offering). An entity may also have cause to settle debt in order to execute an anticipated transaction that is highly likely to occur within a short time after the reporting date and for which it has publicly disclosed at period end. Members recommend the Basis of Conclusions provide how the proposed amendment is consistent with the objective of financial reporting which includes providing useful information about the amount, timing and uncertainty of future net cash inflows of the entity.¹

Conditional Rights and Rights of Counterparties

Members believe that it is necessary to provide more explicit guidance within the body of the standard of how conditional rights and the rights of the counter party should be evaluated under the amendments to IAS 1. Members considered the following common examples:

- An entity has the right to roll over an existing debt on July 1 (presuming a December 31 year-end), but to do so also must satisfy a liquidity covenant on July 1 that is more stringent than the covenant under the existing debt that the entity is in compliance with as at December 31, but management does not expect to comply with the liquidity covenant to roll over the debt as at July 1, the proposed amendments would appear to require the entity to classify the current debt as non-current.
- An entity has a right to defer settlement of the debt at least 12 months from the end of the reporting period but, as is common, has quarterly covenants that it must satisfy or else the lender may exercise its right to demand payment currently. Does the concept of looking at the rights as of the end of the reporting period also look at contingent rights of the lender during the forthcoming 12 months and if so, how might an entity overcome the lender's contingent right to demand payment currently if a quarterly covenant is violated?

Members suggest that the IASB clarify how conditional rights to defer settlement of, or roll over, debt at the end of the reporting period should be evaluated in determining classification when the right is contingent upon meeting lender requirements that either are not expected to be met or are outside the control of the entity and give the lender the right to require settlement. Also, Members believe it would be helpful to include the guidance in BC 4 in the body of the standard indicating that it is a matter of whether the entity complies with the condition as at the end of the reporting period that determines whether or how rights should be considered in determining classification.

Curing Breaches of Debt Provisions

Members note that paragraph 72R(b) indicates that when an entity breaches a provision in a long-term debt arrangement at the end of the reporting period, the debt would be classified as current unless the lender has agreed by the end of the reporting period to provide a period of grace ending at least twelve months after the reporting period. Some Members read the guidance in 72R(b) to mean that if the lender would have any right to demand payment within 12 months from the end of the reporting period, for example, if the lender has a right to call the debt due to an unrelated contingent event or if other debt covenants unrelated to the breached provision are violated, then the borrower would be precluded from classifying the debt as non-current. Specifically, the words "...and during which the lender cannot demand immediate repayment" included at the end of paragraph 72R(b). This would seem to make the year-end breach grace (or waiver) ineffective in

¹Conceptual Framework for Financial Reporting, Chapter 1

achieving current classification of the debt. Members suggest that the IASB clarify how such a situation would impact classification of debt.

Roll-over Terminology

Members note that paragraph 72R(a) retained the word “refinance” rather than “roll over”. It was not clear if this was indicating a distinction between the terms “refinance” and “roll over” or if they are interchangeable. We recommend the term “roll over” be used if there is a distinction or if there is not a distinction that should be made clear. If there is a distinction, Members believe this should be made clear by describing the distinction in the Basis of Conclusions.

Question 2 – Linking settlement with the outflow of resources

The IASB proposes making clear the link between the settlement of the liability and the outflow of resources from the entity by adding ‘by the transfer to the counterparty of cash, equity instrument, other assets or services’ to paragraph 69 of the Standard.

Do you agree with that proposal? Why or why not?

Committee 1 members note that paragraph 69(d), which precedes the new paragraph referred to in the question above regarding outflows of resources, uses the term ‘equity instruments’ in reference to equity of the entity/borrower. When reading the new paragraph inserted after paragraph 69(d), members observe the use of the same term, ‘equity instruments’, and wonder if the term in this case refers to the equity of the entity or, rather, refers instead to equity/debt securities that are held as financial assets by the entity/borrower. If the term in this newly inserted paragraph refers to equity of the entity, then members find the newly inserted paragraph to be in conflict with paragraph 69(d) that indicates that debt that can be settled “by the issue of equity instruments do not affect its classification”. Further, this inserted paragraph would seem to require instruments that can be settled by issuance of equity of the entity to require a presentation of the current portion of such obligations, which would be a change in IFRS.

If instead, the term ‘equity instruments’ used in the new paragraph inserted below 69(d) is meant to refer to securities that are financial assets, then members suggest the term be clarified in this new paragraph so that the reader can understand that the reference is to financial assets rather than an entity’s own equity. Members suggest that the IASB clarify this use of the term ‘equity instruments’ and if in doing so there is a change in the presentation of debt that can be settled by the issuance of equity securities of the entity/borrower, explanation of the basis for such a change should be included in the amendments.

Question 3 – Transition Provisions

The IASB proposes that the proposed amendments should be applied retrospectively.


Do you agree with that proposal? Why or why not?

Committee 1 members agree with the proposed transition provisions.

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We appreciate your thoughtful consideration of the comments raised in this letter. If you have any questions or need additional information on the recommendations and comments that we have provided, please do not hesitate to contact me at 202-551-5300.

Sincerely,



Julie A. Erhardt

Chair

IOSCO Committee on Issuer Accounting, Audit and Disclosure