STAFF PAPER

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IASB® meeting

Project	**Classification of Liabilities as Current or Non-current**
Paper topic	Transition and early application

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Paper overview

1. The Exposure Draft *Classification of Liabilities* (Exposure Draft) proposed amendments to paragraphs 69-76 of IAS 1 *Presentation of Financial Statements*. Those paragraphs specify requirements for classifying liabilities as current or non-current.

2. This paper discusses proposals for transition and early application.

3. Comments were received on two matters:

   (a) *the proposal to require retrospective application.* Most respondents agreed with this proposal and the staff recommend no changes to it (see paragraphs 4–10).

   (b) *the analysis in paragraph BC19 of the Basis for Conclusions.* Some respondents disagreed with Board's conclusion that a reclassification resulting from initial application of the amendments would be more in the nature of a change in accounting estimate than a change in accounting policy. The staff recommend omitting this conclusion from the Basis for Conclusions on the final amendments (see paragraphs 11–17).

Background—Exposure Draft proposals

4. The Exposure Draft proposed that:

139Q …. An entity shall apply those amendments for annual periods beginning on or after [date to be inserted after exposure] retrospectively in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. Earlier application is permitted. If an entity applies those amendments for an earlier period it shall disclose that fact.

5. The Basis for Conclusions explained that:

BC19 The Board noted that requirements for transition arrangements are set out in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. That Standard requires that changes in accounting policies are generally applied retrospectively in accordance with paragraph 19(b) and changes in accounting estimates are applied prospectively in accordance with paragraph 36. The Board concluded that the proposals would not result in a *change* of accounting policy; instead the proposed amendment would clarify existing requirements about the classification of liabilities. Consequently, any resulting change in classification would be more in the nature of a change in accounting estimate which, in accordance with IAS 8, would warrant prospective application.

BC20 The Board concluded, however, that these proposals should nonetheless be applied retrospectively because:

(a) paragraph 41 of IAS 1 requires that, if an entity changes the presentation or classification of items in its financial statements, it shall reclassify comparative amounts unless reclassification is impracticable;

(b) the Board considered that the retrospective application of the proposed narrow-scope amendments would not be onerous, because they deal solely with classification, rather than recognition or measurement;

(c) the proposed narrow-scope amendments would clarify existing requirements rather than imposing additional requirements; and

(d) information about the classification of liabilities would be most useful if current and prior period information is presented on the same basis.

BC21 The Board proposes that early application should be permitted.

BC22 The Board also considered the effects of the amendments when an entity adopts IFRS for the first time and concluded that no exemption to the requirements of IFRS 1 *First-time Adoption of International Financial Reporting Standards* would be required.

Transition

Proposal to require retrospective application

Respondent feedback

6. Most respondents commented on proposed transition requirements, and most of those respondents agreed with the proposal to require retrospective application. Respondents agreeing with the proposal included the two regulators responding and one of the two groups representing users of financial statements.

7. Many respondents emphasised the importance of comparability of current and prior period information. Some agreed that, because the amendments would be clarifications, not new requirements, they should not be burdensome for preparers. A few respondents specifically noted that retrospective application would be feasible because it would not be affected by hindsight—the amendments would require an entity to classify liabilities by reference to its rights at the reporting date, not management expectations about future events.

8. Of the respondents who disagreed with the proposal to require retrospective application:
   (a) a few expressed concern that retrospective application might require the use of hindsight.
   (b) a few questioned whether the benefits of retrospective application would be sufficient to justify the cost and effort. A standard-setter noted that paragraph 41 of IAS 1 requires only reclassification of comparative amounts, not full retrospective application. An accounting firm suggested the information obtained by retrospective application might not be relevant, particularly if a liability was reclassified as non-current at the end of the previous period and then settled during the current period (or reclassified as current and then not settled). One group representing users of financial statements said its members would not be very interested in the amounts classified as short-term in prior periods.

(c) one group representing preparers of financial statements noted that restatement of comparative amounts could result in changes to previously reported performance indicators. The group was concerned that such changes might be misunderstood by investors.

(d) an accounting firm raised concerns that reclassifying prior period liabilities from non-current to current could trigger a current-period breach of covenants for other non-current liabilities, if at each reporting date the entity is required to have complied continuously with the covenants for several periods.

Staff analysis and conclusion

9. Concerns about reclassifications triggering breaches of covenants are also reported in paragraph 14 of Agenda Paper 29A *Classification of Liabilities as Current or Non-current—Equity settlement features*. The staff think that the Board could address these concerns by giving entities enough time to renegotiate covenants before implementing the proposed amendments. We would therefore consider the concerns when developing recommendations on the effective date of the amendments (to be discussed at a future meeting).

10. Other comments on the proposed transition arrangements are opinions on the relative costs and benefits of retrospective application. The balance of opinion supports the Board's view that the benefits would exceed the costs. On this basis, the staff conclude that the Board should require retrospective application. This conclusion is reflected in the staff recommendation in paragraph 18.

Paragraph BC19 of Basis for Conclusions

Respondent feedback

11. Some respondents disagreed with the analysis in paragraph BC19 of the Basis for Conclusions. They disagreed that a change in classification resulting from initial application of the proposed amendments would be more in the nature of a change in an accounting estimate than a change in accounting policy.

12. In addition, a few respondents specifically challenged the suggestion that clarifications of existing requirements do not lead to changes in accounting policy. One respondent noted that such a suggestion was inconsistent with conclusions the Board had reached when clarifying other requirements—for example in IFRIC® Interpretations.

13. Some respondents suggested rewriting paragraph BC19 to describe reclassification as a change in accounting policy. Others suggested omitting any reference to IAS 8—they thought retrospective application could be justified solely on the basis that IAS 1 requires an entity to reclassify comparative amounts when it reclassifies current period amounts.

Staff analysis

14. The staff think a reclassification resulting from initial application of the proposed amendments would be the result of a change in accounting policy, not a change in accounting estimate:

    (a) IAS 8 defines accounting policies as 'the specific principles, bases, conventions, rules and practices applied by an entity in preparing and presenting financial statements'. Paragraphs 69-76 of IAS 1 specify the principles entities apply in presenting liabilities. The proposed amendments to those paragraphs would change those principles.

    (b) IAS 8 describes a change in accounting estimate as an adjustment of the carrying amount of an asset or a liability that results from new information or new developments. The proposed amendments would not lead to any such adjustments.

15. Paragraph 19 of IAS 8 requires an entity to account for a change in accounting policy resulting from the initial application of an IFRS Standard:

    (a) in accordance with any specific transitional provisions in that Standard; or

    (b) retrospectively if there are no specific transitional provisions in the Standard.

16. Thus, to support a requirement for retrospective application of the proposed amendments, the Board need only explain why it thinks there is no need for alternative transitional provisions. The Board explains those reasons in paragraphs BC20 of the Exposure Draft.

Staff conclusion

17. The staff think the analysis in paragraph BC19 of the Exposure Draft should be omitted from the Basis for Conclusions accompanying the proposed amendments.

Staff recommendation and question for the Board

18. The staff recommend that, as proposed in the Exposure Draft, and for the reasons set out in paragraph BC20 of the Basis for conclusions on the Exposure Draft, the Board requires entities to apply the amendments retrospectively in accordance with IAS 8.

Question 1—Transition
Do you agree that, as proposed in the Exposure Draft, the Board should require entities to apply the amendments retrospectively in accordance with IAS 8?

Other matters

First-time adoption

19. In developing the Exposure Draft, the Board considered the effects of the amendments when an entity adopts IFRS for the first time and concluded that no exemption to the requirements of IFRS 1 *First-time Adoption of International Financial Reporting Standards* would be required. Respondents did not challenge this conclusion so the staff recommend no changes to the Exposure Draft proposals.

Question 2—First-time adoption
Do you agree that, as proposed in the Exposure Draft, the Board should provide no exemptions for entities adopting IFRS Standards for the first time?

Early application

20. The Exposure Draft proposed to permit entities to apply the amendments before their effective date (early application) and to require entities that apply the amendments early to disclose that fact. Respondents did not question these proposals so the staff recommend no changes to them.

Question 3—Early application
Do you agree that, as proposed in the Exposure Draft, the Board should permit early application, requiring entities that apply the amendments early to disclose that fact?