STAFF PAPER

July 2021

IASB Meeting

Project	**Classification of Debt with Covenants as Current or Non-current (IAS 1)**
Paper topic	Transition, Early Application and Due Process

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Introduction

1. At its meeting in June 2021, the International Accounting Standards Board (Board) tentatively decided to propose narrow-scope amendments to IAS 1 *Presentation of Financial Statements*. The proposed amendments would modify the requirements introduced by *Classification of Liabilities as Current or Non-current* (2020 amendments) on how an entity classifies debt and other financial liabilities as current or non-current in particular circumstances. The proposed amendments would:

   (a) specify that conditions with which an entity must comply *after* the reporting period do not affect classification of a liability as current or non-current at the end of the reporting period;

   (b) add presentation and disclosure requirements for non-current liabilities subject to conditions in the next 12 months; and

   (c) clarify situations in which an entity does not have a right to defer settlement for at least 12 months after the reporting period.

2. The proposed amendments would also defer the effective date of the 2020 amendments to no earlier than 1 January 2024.

3. Appendix B to this paper reproduces excerpts from the June 2021 IASB *Update* summarising the Board's tentative decisions with respect to the proposed amendments.

4. The objective of this paper is to:

   (a) ask the Board whether it agrees with our recommendations on transition and early application of the proposed amendments;

   (b) set out the steps in the IFRS Foundation *Due Process Handbook* that the Board has taken in developing the proposed amendments;

   (c) ask the Board to confirm it is satisfied that it has complied with the applicable due process requirements; and

   (d) ask whether any Board member intends to dissent from the publication of the Exposure Draft.

Structure of the paper

5. This paper is structured as follows:

   (a) Transition, effective date and early application (paragraphs 7–13); and

   (b) Due process steps and permission for balloting (paragraphs 14–18).

6. This paper includes two appendices:

   (a) Appendix A—Due process steps taken in developing the proposed amendments; and

   (b) Appendix B—Excerpts from the June 2021 IASB *Update*.

Transition, effective date and early application

Transition

7. IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* requires an entity to retrospectively apply a change in accounting policy upon the initial application of an IFRS Standard that does not include specific transition requirements, except to the extent it is impracticable to do so.

8. In our view the Board should require entities to apply the proposed amendments retrospectively in accordance with IAS 8.[1] In our view, the benefits of retrospective application would outweigh the costs because:

   (a) classifying liabilities as current or non-current on the same basis in current and prior periods would result in more comparable, and thus more useful, information for users of financial statements; and

   (b) applying the amendments retrospectively would not be onerous for preparers:

      (i) the amendments affect only requirements on presentation and disclosure, not recognition and measurement, of liabilities;

      (ii) feedback on the tentative agenda decision *Classification of Debt with Covenants as Current or Non-current* suggest that many entities already classify liabilities as current or non-current in a manner consistent with the requirements in the proposed amendments, and thus might not need to change classification of liabilities;[2] and

      (iii) paragraph 41 of IAS 1 requires an entity to reclassify comparative amounts when the entity changes the presentation or classification of items in its financial statements, unless reclassification is impracticable—therefore, entities would be required to change classification in prior periods even if the Board were not to require retrospective application.

9. We see no reason to provide an exemption for first-time adopters (as defined in IFRS 1 *First-time Adoption of International Financial Reporting Standards*).

Staff recommendation

10. We recommend that the Board:

   (a) require entities to apply the proposed amendments retrospectively in accordance with IAS 8; and

   (b) not provide an exemption for first-time adopters.

[1] The 2020 amendments also require retrospective application in accordance with IAS 8.

[2] See Agenda Paper 12C for the Board June 2021 meeting for further information.

Effective date and early application

11. We will discuss the effective date at the time of finalising the amendments, should the Board decide to proceed with them.

12. The amendments, if finalised, will enhance the information entities provide about the conditionality associated with an entity's right to defer settlement of liabilities classified as non-current. We therefore see no reason to prohibit an entity from applying the proposed amendments earlier than the effective date.

Staff recommendation

13. We recommend permitting an entity to apply the amendments earlier than their effective date.

Due process steps and permission for balloting

Comment period

14. Paragraph 6.7 of the *Due Process Handbook* states that the Board 'normally allows a minimum period of 120 days for comment on an exposure draft'. However, if the matter is narrow in scope and urgent, the Board may consider a shorter comment period.

15. The proposed amendments are narrow in scope but, in our view, not so urgent that they would warrant a comment period of less than 120 days. We therefore recommend a comment period of no less than 120 days for the Exposure Draft on the proposed amendments.

Intention to dissent

16. In accordance with paragraph 6.9 of the *Due Process Handbook*, we are asking whether any Board member intends to dissent from the publication of the Exposure Draft.

Proposed timetable for balloting and publication

17. We plan to begin the balloting process in the near future and expect the Exposure Draft to be published in the fourth quarter of 2021.

Confirmation of due process steps

18. Appendix A sets out the required due process steps in developing and publishing an Exposure Draft together with the status of, and any planned action for, these steps. We note that the applicable due process steps to date for balloting of the Exposure Draft have been completed.

Questions for the Board

1. **Transition**—does the Board agree with our recommendation to:
   a. require entities to apply the proposed amendments retrospectively in accordance with IAS 8; and
   b. not provide an exemption for first-time adopters?
2. **Early application—**does the Board agree with our recommendation to permit an entity to apply the proposed amendments earlier than the effective date?
3. **Comment period**—does the Board agree with our recommendation to allow a comment period of no less than 120 days for the Exposure Draft?
4. **Dissent**—does any Board member intend to dissent from publication of the Exposure Draft?
5. **Permission to ballot**—is the Board satisfied that it has complied with the applicable due process steps and that it should begin the balloting process for the Exposure Draft?

Appendix A—Due process steps taken in developing the proposed amendments

A1. The following table summarises the required due process steps taken in developing the proposed amendments. The table does not list all the optional steps.

Step	Actions
Board meetings are held in public, with papers available for observers. All decisions are made in public sessions	• The Board discussed the matter at its meetings in June 2021 (see Agenda Papers 12B and 12C) and July 2021 (this Agenda Paper). • The IFRS Interpretations Committee (Committee) discussed the matter at its meeting in April 2021 (see Agenda Paper 3).
Consultation with the Trustees and the Advisory Council	• The Trustees and Advisory Council will be updated on the project as part of their discussions of the Board's technical activities.
Analysis of likely effects of the forthcoming Standard or major amendment, for example, initial costs or ongoing associated costs	• The proposed amendments would: (a) enhance the information entities provide about the conditionality associated with an entity's right to defer settlement of liabilities classified as non-current; and (b) resolve stakeholders' concerns about the costs associated with some of the potential consequences of applying the 2020 amendments—such as the costs of possibly renegotiating lending terms or seeking to obtain a waiver. • We expect the costs of disclosing additional information to not outweigh (a) the benefits of the proposed amendments, and (b) the reduction of costs associated with applying the 2020 amendments. • Because the amendments are narrow in scope, we see no need to have a separate effects analysis.
Outreach meetings with stakeholders	• In developing the proposed amendments, the Board considered feedback from a few investors and analysts about (a) the outcomes and potential consequences of applying the 2020 amendments, and (b) what they view as useful information about liabilities subject to conditions in the next 12 months. The Board also considered feedback from Committee members and in comment letters sent in response to the Committee's tentative agenda decision on the topic.

Finalisation	
Due process steps reviewed by the IASB	• This paper asks the Board to review the due process steps for the project.
The Exposure Draft has an appropriate comment period	• This paper seeks the Board's approval for a comment period of no less than 120 days. The proposed comment period is in line with the minimum period specified in paragraph 6.7 of the *Due Process Handbook* and, therefore, no special approval is required from the Due Process Oversight Committee.
Drafting	
Drafting quality assurance steps are adequate	• The translations, editorial and taxonomy teams will review drafts during the balloting process.
Publication	
Exposure Draft published	• The Exposure Draft will be made available on the project website when published.
Press release to announce publication of the Exposure Draft	• A press release will be published on our website with the Exposure Draft.

Appendix B—Excerpts from June 2021 IASB *Update*

B1. This appendix reproduces excerpts from the June 2021 IASB *Update* summarising the Board's tentative decisions with respect to the proposed amendments.

Classification of Debt with Covenants as Current or Non-current (IAS 1) (Agenda Papers 12B–12C)

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Classification and disclosure

The Board tentatively decided to amend IAS 1 so that:

a. it specifies that if the right to defer settlement for at least 12 months is subject to an entity complying with conditions after the reporting period, then those conditions would not affect whether the right to defer settlement exists at the end of the reporting period (the reporting date) for the purposes of classifying a liability as current or non-current; and
b. for non-current liabilities subject to conditions, an entity is required to disclose information about:
    i. the conditions (for example, the nature of and date by which the entity must comply with the condition);
    ii. whether the entity would comply with the conditions based on its circumstances at the reporting date; and
    iii. whether and how the entity expects to comply with the conditions by the date on which they are contractually required to be tested.

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Separate presentation

The Board tentatively decided to amend IAS 1 to require that an entity present separately in its statement of financial position 'non-current liabilities subject to conditions in the next 12 months'. This line item would include liabilities classified as non-current for which the right to defer settlement for at least 12 months is subject to the entity complying with conditions after the reporting date.

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Further clarification

The Board tentatively decided to amend IAS 1 to clarify that an entity does not have a right to defer settlement at the reporting date when the related liability could become repayable within 12 months:

a. at the discretion of the counterparty or a third party (for example, when a loan is callable by the lender at any time without cause); or
b. if an uncertain future event occurs (or does not occur) and the event’s occurrence (or non-occurrence) is unaffected by the entity’s future actions (for example, when the liability is a financial guarantee or insurance contract liability).

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Deferral of the effective date of the 2020 amendments

The Board tentatively decided to amend IAS 1 to defer the effective date of the 2020 amendments to no earlier than 1 January 2024.

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