STAFF PAPER

July 2022

IASB Meeting

Project	Non-current Liabilities with Covenants (IAS 1)	
Paper topic	Effective date and due process	
CONTACT(S)	Gustavo Olinda	golinda@ifrs.org

Introduction and purpose

1. In June 2022, the International Accounting Standards Board (IASB) decided to finalise its proposed amendments to IAS 1 *Presentation of Financial Statements* published in the Exposure Draft *Non-current Liabilities with Covenants*, with some changes to the proposals.

2. The purpose of this paper is to:

   (a) ask the IASB whether it agrees with our recommendation with respect to the effective date for the amendments to IAS 1;

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

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

   (d) ask whether any IASB member intends to dissent from the amendments.

Structure of the paper

3. This paper is structured as follows:

   (a) summary of the amendments (paragraphs 5–16);

   (b) effective date (paragraphs 17–21); and

(c) due process steps and permission for balloting (paragraphs 22–29):

(i) re-exposure;

(ii) intention to dissent;

(iii) confirmation of due process steps; and

(iv) proposed timetable for balloting and publication.

4. There are two appendices to this paper:

(a) Appendix A—Extracts from the *Due Process Handbook*; and

(b) Appendix B—Actions taken to meet the due process requirements.

Summary of the amendments

Background

5. IAS 1 requires that, for an entity to classify a liability as non-current, the entity must have the right at the reporting date to defer settlement of the liability for at least 12 months after that date (right to defer settlement).

6. In January 2020, the IASB issued *Classification of Liabilities as Current or Non-current* (2020 amendments). The 2020 amendments clarified aspects of how entities classify liabilities as current or non-current; in particular, how an entity assesses whether it has the right to defer settlement of a liability when that right is subject to compliance with conditions (hereafter, covenants) within 12 months after the reporting date.

7. In December 2020, responding to questions from stakeholders, the IFRS Interpretations Committee (Committee) published a tentative agenda decision explaining how to apply the 2020 amendments to particular fact patterns. The tentative agenda decision explained that, applying the 2020 amendments, an entity does not have the right to defer settlement of a liability—and thus classifies the liability as current—when the entity would not have complied with covenants based on its circumstances at the reporting date, even if compliance with such covenants were required only within 12 months after that date.

8. Respondents to the tentative agenda decision raised concerns about the outcomes and potential consequences of the 2020 amendments in some situations. The Committee

reported this feedback to the IASB, highlighting new information that the IASB had not considered when developing the 2020 amendments.

Proposals in the Exposure Draft

9. Having considered the new information, the IASB decided to propose narrow-scope amendments to IAS 1. The proposed amendments aimed to improve the information an entity provides when its right to defer settlement of a liability is subject to compliance with covenants within 12 months after the reporting date, in addition to addressing stakeholders' concerns about the outcomes of applying the 2020 amendments.

10. The proposals in the Exposure Draft covered three main areas:

    (a) *classification of liabilities as current or non-current*—the IASB proposed to specify that covenants with which an entity must comply only after the reporting date would not affect classification of a liability as current or non-current. In addition, the IASB proposed to clarify situations in which an entity would not have a right to defer settlement.

    (b) *disclosure of information about covenants*—the IASB proposed to require an entity to disclose information that enables investors to assess the risk that the liability could become repayable within 12 months, including:

        (i) the covenants (their nature and date on which the entity must comply with them);

        (ii) whether the entity would have complied with the covenants at the reporting date; and

        (iii) whether and how the entity expects to comply with the covenants in the future.

    (c) *separate presentation*—the IASB proposed to require an entity to present separately, in its statement of financial position, non-current liabilities subject to compliance with covenants within 12 months after the reporting date.

11. The proposed amendments would also defer the effective date of the 2020 amendments so that entities would not be required to change their assessment of the classification of liabilities before the proposed amendments would be in effect.

IASB's tentative decisions

12. In June 2022, in response to comments received the IASB tentatively decided to finalise the proposals in the Exposure Draft, with some changes to these proposals.

Classification as current or non-current

13. The IASB tentatively decided:

    (a) to finalise the proposals on classification of liabilities as current or non-current—that is, the IASB tentatively decided to confirm that only covenants with which an entity must comply on or before the reporting date would affect a liability's classification as current or non-current.

    (b) not to finalise the proposed clarification about situations in which an entity would have no right to defer settlement. Instead, the IASB tentatively decided to specify that the proposed requirements on classification of liabilities as current or non-current apply only to liabilities arising from loan arrangements.

Disclosure of information about covenants

14. The IASB tentatively decided to finalise the proposal to require an entity to disclose information about non-current liabilities with covenants, with some modifications. Specifically, the IASB tentatively decided to require that, when an entity classifies liabilities arising from loan arrangements as non-current and those liabilities are subject to covenants, the entity is required to disclose information that enables investors to assess the risk that the liabilities could become repayable within 12 months, including:

    (a) information about the covenants with which the entity is required to comply (such as the nature of the covenants and the date on which the entity must comply with them).

(b) facts and circumstances that indicate the entity may have difficulty complying with covenants when it is required to do so—for example, the entity having acted during or after the reporting period to avoid or mitigate a potential breach. Such facts and circumstances could also include the fact that the entity would not have complied with the covenants based on its circumstances at the reporting date.

Separate presentation

15. The IASB tentatively decided not to finalise the proposal to require an entity to present separately non-current liabilities with covenants but, instead, to require an entity to disclose the carrying amount of such liabilities in the notes.

Transition and effective date deferral

16. The IASB tentatively decided:

(a) to require an entity to apply the amendments retrospectively in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

(b) to allow an entity to adopt early the amendments or the 2020 amendments, but only if the entity adopts the amendments and the 2020 amendments at the same time.

(c) to defer the effective date of the 2020 amendments to align it with the effective date of the amendments.

Effective date

17. Paragraph 6.35 of the *Due Process Handbook* explains that the effective date of any amendment is set so that (a) jurisdictions have sufficient time to incorporate the new requirements into their legal systems; and (b) those applying IFRS Accounting Standards have sufficient time to prepare for the new requirements.

18. The IASB generally allows at least 12–18 months between the issuance of a new Accounting Standard or amendment and its effective date. If the IASB agrees with our recommendations set out in this paper, we expect the IASB to issue the amendments during the fourth quarter of 2022.

19. In our view, entities would have sufficient time to prepare for the new requirements if the IASB were to set an effective date of annual reporting periods beginning on or after 1 January 2024—ie 12 months after the end of the fourth quarter of 2022. This is because:

    (a) the amendments affect only the classification of liabilities arising from loan arrangements with covenants as current or non-current and the information the entity discloses about such covenants—they do not affect the recognition and measurement of liabilities.

    (b) based on feedback from stakeholders obtained throughout this project, we expect that most entities will not be required to change the classification of liabilities arising from loan arrangements as current or non-current as a result of the amendments.

    (c) in applying the amendments, entities would have to identify covenants in their loan arrangements and determine which information to disclose about such covenants. However, entities are already expected to closely monitor their compliance with covenants, and therefore the information required by the amendments might already be available. Further, we expect that entities might already be disclosing some information about covenants applying existing requirements in IFRS Accounting Standards.[1]

20. In our view such an effective date would also allow jurisdictions sufficient time to incorporate the new requirements into their legal systems. We therefore recommend that the IASB require entities to apply the amendments for annual reporting periods beginning on or after 1 January 2024.

21. As explained in paragraph 16(c) of this paper, the IASB tentatively decided to defer the effective date of the 2020 amendments to align it with the effective date of the amendments. Therefore, if the IASB agrees with our recommendation, the effective date for the 2020 amendments would be deferred to 1 January 2024.

[1] For example, in meeting the disclosure requirements about liquidity risk in IFRS 7 *Financial Instruments: Disclosures*.

Question 1 for the IASB
1. Effective date for the amendments to IAS 1—Does the IASB agree with our recommendation to require entities to apply the amendments for annual reporting periods beginning on or after 1 January 2024?

Due process steps and permission for balloting

Re-exposure

22. As noted in paragraphs 12–16 of this paper, the IASB has tentatively decided to finalise the proposals in the Exposure Draft with some changes to these proposals.

23. In the light of these changes, we considered the requirements in paragraphs 6.25–6.29 of the *Due Process Handbook* (reproduced in Appendix A to this paper) to assess whether the IASB should re-expose the amendments to IAS 1.

24. In our view, there is no need to re-expose the amendments because:

    (a) the IASB has undertaken the steps described in paragraph 6.25 of the *Due Process Handbook*;

    (b) it is unlikely that re-exposure would reveal new information or feedback not already considered by the IASB because:

        (i) most changes to the proposals were made to remove requirements proposed in the Exposure Draft or to narrow the scope of liabilities to which the requirements would apply. These changes were made in response to feedback received.

        (ii) the requirement for an entity to disclose 'facts and circumstances that indicate the entity may have difficulty complying with covenants when it is required to do so' is not a fundamental change from the proposals in the Exposure Draft. That requirement was introduced to replace disclosure proposals in response to feedback received.

    (c) as discussed in paragraph 19(a), the amendments do not affect recognition and measurement of liabilities.

25. Accordingly, we recommend finalising the amendments to IAS 1 without re-exposure.

Intention to dissent

26. In accordance with paragraph 6.23 of *Due Process Handbook*, we are asking whether any IASB member intends to dissent from the amendments to IAS 1.

Confirmation of due process steps

27. In our view the IASB has undertaken all the due process activities identified as being required in the *Due Process Handbook* and, thus, is able to finalise the amendments. Appendix B to this paper summarises the due process steps taken in developing the amendments to IAS 1—the applicable due process steps to date for issuing the amendments have been completed.

28. We request permission to start the balloting process if the IASB is satisfied that (a) it has been provided with sufficient analysis, and (b) has undertaken appropriate consultation and due process to support issuing the amendments.

Proposed timetable for balloting and publication

29. The balloting process for the amendments to IAS 1 will commence in the near term, with the amendments planned for issue in the fourth quarter of 2022.

Questions 2–4 for the IASB
2. **Re-exposure**—does the IASB agree with our recommendation in paragraph 25 of this paper not to re-expose the amendments to IAS 1?
3. **Dissent**—does any IASB member intend to dissent from the amendments to IAS 1?
4. **Permission to ballot**—is the IASB satisfied it has complied with the applicable due process requirements and that it has undertaken sufficient consultation and analysis to begin the balloting process for the amendments to IAS 1?

Appendix A—Extracts from the *Due Process Handbook*

6.25 In considering whether there is a need for re-exposure, the [IASB]:

(a) identifies substantial issues that emerged during the comment period on the exposure draft and that it had not previously considered;

(b) assesses the evidence that it has considered;

(c) determines whether it has sufficiently understood the issues, implications and likely effects of the new requirements and actively sought the views of interested parties; and

(d) considers whether the various viewpoints were appropriately aired in the exposure draft and adequately discussed and reviewed in the basis for conclusions.

6.26 It is inevitable that the final proposals will include changes from those originally proposed. The fact that there are changes does not compel the [IASB] to re-expose the proposals. The [IASB] needs to consider whether the revised proposals include any fundamental changes on which respondents have not had the opportunity to comment because they were not contemplated or discussed in the basis for conclusions accompanying the exposure draft. The [IASB] also needs to consider whether it will learn anything new by re-exposing the proposals. If the [IASB] is satisfied that the revised proposals respond to the feedback received and that it is unlikely that re-exposure will reveal any new concerns, it should proceed to finalise the proposed requirements.

6.27 The more extensive and fundamental the changes from the exposure draft and current practice the more likely the proposals should be re-exposed. However, the [IASB] needs to weigh the cost of delaying improvements to financial reporting against the relative urgency for the need to change and what additional steps it has taken to consult since the exposure draft was published. The use of consultative groups or targeted consultation can give the [IASB] information to support a decision to finalise a proposal without the need for re-exposure.

6.28 The [IASB] should give more weight to changes in recognition and measurement than disclosure when considering whether re-exposure is necessary.

6.29 The [IASB]'s decision on whether to publish its revised proposals for another round of comment is made in a [IASB] meeting. If the [IASB] decides that re-exposure is necessary, the due process to be followed is the same as for the first exposure draft. However, because it is not the first exposure of the proposed IFRS [Accounting] Standard, it may be appropriate to have a shortened comment period, particularly if the [IASB] is seeking comments on only specific aspects of the revised exposure draft, while recognising that respondents may not limit their comments to these aspects. The public comment period for such documents will normally be at least 90 days.

Appendix B—Actions taken to meet the due process requirements

Step	Required / Optional	Actions
Consideration of information gathered during consultation		
The IASB posts all of the comment letters that are received in relation to the Exposure Draft on the project pages.	Required	All comment letters received by the IASB (84 comment letters) have been posted on the project website here: https://www.ifrs.org/projects/work-plan/classification-of-debt-with-covenants-as-current-or-non-current-ias-1/exposure-draft-and-comment-letters/#view-the-comment-letters
The IASB and the IFRS Interpretations Committee (Committee) meetings are held in public, with papers being available for observers. All decisions are made in public sessions.	Required	The IASB discussed our analysis and recommendations on the matters identified in the feedback to the Exposure Draft at its June 2022 meeting. *(see Agenda Papers 12A–D for that meeting)* All staff papers above are publicly available. The project webpage has up-to-date information about all technical papers related to the project: https://www.ifrs.org/projects/work-plan/classification-of-debt-with-covenants-as-current-or-non-current-ias-1/#project-history
Analysis of likely effects of the forthcoming Standard or major amendment, for example, costs or ongoing associated costs.	Required	The IASB considered the likely effects of the amendments at each stage of their development. The basis for conclusion on the amendments will include the IASB's views on these effects.
Round-table and outreach meetings to promote debate and hear views on proposals that are published for public comment	Optional	The proposed amendments were discussed with members of: (i) the Global Preparers Forum at its March 2022 meeting *(see Agenda Paper 2 for that meeting)*; (ii) the Capital Markets Advisory Committee at its March 2022 meeting *(see Agenda Paper 3 for that meeting)*; and (iii) the Accounting Standards Advisory Forum at its March 2022 meeting *(see Agenda Paper 2 for that meeting)*.
Finalisation		
Due process steps are reviewed by the IASB.	Required	This step will be met by this Agenda Paper.
Need for re-exposure of a Standard is considered.	Required	Paragraphs 22–25 of this paper discuss re-exposure. We recommend the IASB not re-expose the amendments.

The IASB sets an effective date for the Standard, considering the need for effective implementation, generally providing at least one year.	Required	Paragraphs 17–21 of this paper discuss the effective date. We recommend an effective date of annual reporting periods beginning on or after 1 January 2024.
Drafting		
Drafting quality assurance steps are adequate.	Required	To be completed in due course. The Translations, Taxonomy and Editorial teams will review the pre-ballot draft. We intend to send a draft of the amendments to external parties for review before finalisation. This process allows external parties to review and report back to the staff on the clarity and understandability of the draft.
Publication		
News release to announce the final Standard.	Required	To be completed in due course. A news release will be published with the amendments.
A Feedback Statement is provided which provides high level executive summaries of the Standard and explains how the IASB has responded to the comments received.	Required	Not considered necessary because these amendments are narrow in scope. According to paragraph 6.38 of the *Due Process Handbook*, a Feedback Statement is required for all new IFRS Accounting Standards and major amendments. The Basis for Conclusions on the amendments will explain how the IASB has responded to the main comments received.
Standard is published.	Required	The amendments will be made available on our website when published.