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ED/2015/1 Disclosure Initiative - Proposed amendments to IAS 1

Grant Thornton International Ltd is pleased to comment on the International Accounting Standards Board's (the Board) Exposure Draft ED/2015/1 *Classification of Liabilities- Proposed amendments to IAS 1* (the ED). We have considered the ED, as well as the accompanying draft Basis for Conclusions.

We support the Board's objectives and believe that the proposed amendments will help clarify that classification of liabilities as either current or non-current is based on the rights that are in existence at the end of the reporting period. However, we also believe the amendments could benefit from further refinement in a number of areas in order to better promote their consistent application and that additional illustrative examples should be provided to address some of the challenges that have arisen in practice. Ultimately, we feel that classification of liabilities is a topic which would benefit from a more comprehensive review in due course.

Our specific responses to the ED's Invitation to Comment are set out in the Appendix.

If you have any questions on our response, or wish us to amplify our comments, please contact our Global Head of IFRS, Andrew Watchman (andrew.watchman@gti.gt.com or telephone + 44 207 391 9510).

Yours sincerely,

Kenneth C. Sharp

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Responses to Invitation to Comment questions

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?

We agree with the proposed amendment (a) on the understanding that 'right' has the same meaning as 'discretion' in this context such that the proposed amendment represents a clarification that is not expected to lead to a change in practice.

We agree with the proposed amendment (b) and the guiding principle that only rights in place at the reporting date should affect the classification of a liability. With respect to the rights in place at the reporting date, the final sentence of the example provided in IAS 1.72R(b) should be amended further to clarify that the lender only has to waive its right to immediate repayment resulting from the specific breach (or breaches) that occurred either at or before the end of the reporting period. The existing wording may lead some constituents to incorrectly conclude that the liability is classified as current if the lender could demand repayment within the 12 month grace period under any circumstances, including in the event of future breaches of covenant tests falling within that 12 month period. We also believe that the clarity of the proposed amendments would be enhanced if they included examples illustrating:

- that covenant breaches occurring between the end of the reporting period and the date the financial statements are authorised for issue are non-adjusting events that do not affect classification at the end of the reporting period;
- whether non-current classification is appropriate if a lender agrees before the end of the reporting period to waive a covenant breach but specifies requirements to rectify the breach, or inserts an additional covenant test, within twelve months after the reporting period; and
- whether, when assessing the scenario described in the preceding bullet point, an entity should consider the likelihood that it will be able to rectify the breach and/or meet the additional covenant test.

With respect to amendment (c) and the proposed removal of the word 'unconditional' from IAS 1.69(d), we agree with the Board's reasoning as explained in paragraph BC2. However, we are also aware of a perception that this change could weaken the existing requirement and lead to increased diversity in practice as entities seek to avoid classifying liabilities as current. We believe this risk might be mitigated by incorporating the situational language of BC2 directly into IAS 1.69(d) to better convey the intended meaning.

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 instruments, other assets or services' to paragraph 69 of the Standard.

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

We find the additional clarification proposed for the end of paragraph 69, as presently worded, is ambiguous with respect to whether the reference to the transfer of 'equity instruments' is referring to equity instruments of the entity, or investments in equity instruments of other entities held as assets. We believe that classification should be based on expected outflows of resources such as cash and financial or other assets. Also, IAS 1.69(d) explains that terms of a liability that could, at the option of the counterparty, result in settlement by the issue of the entity's own equity instruments should not affect its classification.

This could be clarified by inserting '(other than the entity's own equity instruments)' after the reference to equity instruments in the proposed amendment. .

Question 3 – Transition arrangements

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

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

We agree with the proposed transition arrangements.

Other comments

We believe the proposed amendments could also be improved by providing guidance with respect to the definition of a rollover. At present the Standard (in BC12) states only that a rollover is an 'extension' of an existing loan facility. Entities may face challenges identifying the point at which modifications are so significant that they can no longer be seen as an extension of an existing loan facility, but are more accurately characterised as a settlement and refinancing. We believe there are strong arguments in favour of providing a formal link to the extinguishment guidance contained in IFRS 9/IAS 39.