

INVITATION TO COMMENT ON EFRAG'S ASSESSMENTS ON CLASSIFICATION OF LIABILITIES AS CURRENT OR NON-CURRENT

Once filled in, this form should be submitted by 7 December 2020 using the 'Comment publication link' available at the bottom of the respective news item. All open consultations can be found on EFRAG's web site: [Open consultations: express your views](#).

EFRAG has been asked by the European Commission to provide it with advice and supporting material on Classification of Liabilities as Current or Non-current (the Amendments). In order to do so, EFRAG has been carrying out an assessment of the Amendments against the technical criteria for endorsement set out in Regulation (EC) No 1606/2002 and has also been assessing the costs and benefits that would arise from their implementation in the European Union (the EU) and European Economic Area.

A summary of the Amendments is set out in Appendix 1.1 of the accompanying Draft Letter to the European Commission regarding endorsement of the Amendments.

Before finalising its assessment, EFRAG would welcome your views on the issues set out below. Please note that all responses received will be placed on the public record, unless the respondent requests confidentiality. In the interests of transparency, EFRAG will wish to discuss the responses it receives in a public meeting, so it is preferable that all responses can be published.

EFRAG's initial assessments, summarised in this questionnaire, will be updated for comments received from constituents when EFRAG is in the process of finalising its Letter to the European Commission regarding endorsement of the Amendments.

Your details

1 Please provide the following details:

(a) Your name or, if you are responding on behalf of an organisation or company, its name:

Mazars

(b) Are you a:

Preparer

User

Other (please specify)

International audit firm

(c) Please provide a short description of your activity:

Mazars is an international, integrated and independent firm, specialising in audit, accountancy, advisory, tax and legal services. Operating in more than 90 countries and territories, the firm draws on the expertise of 24,400 professionals to assist major international groups, SMEs, private investors and public bodies at every stage in their development, and has a global revenue of 1.8bn EUR

(d) Country where you are located:

Mazars is an international audit firm with Headquarters in France

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EFRAG's initial assessment with respect to the technical criteria for endorsement

2 EFRAG's initial assessment of the Amendments is that they meet the technical criteria for endorsement. In other words, the Amendments are not contrary to the principle of true and fair view and meet the criteria of understandability, relevance, reliability, comparability and lead to prudent accounting. EFRAG's reasoning is set out in Appendix 2.1 of the accompanying Draft Letter to the European Commission regarding endorsement of the Amendments.

(a) Do you agree with this assessment?

Yes No

If you do not agree, please provide your arguments and what you believe the implications of this could be for EFRAG's endorsement advice.

While we agree with the objectives of the amendment to provide clarifications on the classification principles of liabilities as current or non-current, in order to help consistent application of IAS 1 provisions, we believe that paragraph 72A fails to meet the criteria of understandability and relevance.

Indeed, paragraph 72A states that when an entity's right to defer settlement of a liability for at least 12 months after the reporting date is subject to the entity complying with specified conditions, that right exists only if the entity complies with the conditions at the end of the reporting period, even if the compliance with the conditions is only tested at a later date.

We believe that this paragraph fails to consider the reasons why both lender and the entity have agreed to test the compliance with the conditions at a later date, and that ignoring those reasons when assessing whether the conditions are met at reporting date could lead to irrelevant classification of the liabilities.

This has been highlighted by the current discussions at the IFRS Interpretations Committee and the examples provided in the tentative agenda decision.

For instance, an entity acting in the hospitality industry in a ski resort usually has a better financial position at 30 June, after the high activity season, than at 31 December. Let's assume that the lender and the entity have agreed that the gearing ratio at each 30 June shall remain below a specified threshold, otherwise the loan will become repayable on demand. Applying paragraph 72A would lead the liability to be classified as non-current in the interim financial statements and as current in the annual financial statements, even in situations where the probability that the gearing condition will not be met at the next 30 June is remote. We believe that the change of classification of the liability depending on the reporting date is neither relevant nor understandable for users.

Another example is case 3 in the tentative agenda decision published in the IFRIC Update in December 2020: the covenant of the loan requires a working capital ratio above 1.0 at 31 December 20X1 and above 1.1 at 30 June 20X2 and at each 30 June thereafter. If the covenant is not met, the loan becomes repayable on demand. In the fact pattern described, the working capital ratio is 1.05 at 31 December 20X1, and the entity expects the ratio to be above 1.1 at 30 June 20X2. The IFRS Interpretations Committee has tentatively concluded that the liability shall be classified as current as at 31 December 20X1 because according to paragraph 72A, the entity does not have the right to defer settlement for at least 12 months if the ratio required for the next covenant-testing date (30 June 20X2) is not met at 31 December 20X1. This conclusion ignores the rationale for the agreement between the entity and the lender, and the fact that there is no breach or anticipated breach in the loan contract as at 31 December 20X1.

We believe that paragraph 72A has anti-abuse merits: it requires to classify as current loans for which the lender and the entity agree, before reporting date, to test the covenant at a later date because they both know that the covenant will not be met at reporting date. By solving this issue, we strongly believe it creates unintended consequences leading to irrelevant classification of liabilities in specific circumstances.

- (b) Are there any issues that are not mentioned in Appendix 2.1 of the accompanying Draft Letter to the European Commission regarding endorsement of the Amendments that you believe EFRAG should take into account in its technical evaluation of the Amendments? If there are, what are those issues and why do you believe they are relevant to the evaluation?

The changes brought by paragraph 72A are not clearly described in paragraph 9 of Appendix 1.1 of the accompanying Draft Letter to the European Commission. In particular, paragraph 9(b) is not precise enough. Furthermore, the sentence seems not being complete (“(...) and instead adding a paragraph (IAS 1 paragraph 72A) to clarify that if an entity’s right to defer settlement is subject to compliance with specified conditions;”).

This lack of precision does not allow a sufficient understanding of the consequences of applying this paragraph in specific -but quite widespread- situations. Consequently, the assessment of relevance in paragraphs 7-9 of Appendix 2.1 only considers that the amendment provides more guidance on how to make the distinction between the current and non-current classification and therefore enhance relevance.

The lack of relevance of information resulting from the application of paragraph 72A in specific circumstances has not been analysed.

The European public good

- 3 In its assessment of the impact of the Amendments on the European public good, EFRAG has considered a number of issues that are addressed in Appendix 3.1 of the accompanying Draft Letter to the European Commission regarding endorsement of the Amendments.

Improvement in financial reporting

- 4 EFRAG has identified that in assessing whether the endorsement of the Amendments is conducive to the European public good it should consider whether the Amendments are an improvement over current requirements across the areas which have been subject to changes (see paragraphs 3 to 4 of Appendix 3.1 of the accompanying Draft Letter to the European Commission). To summarise, EFRAG’s initial assessment is that the Amendments are likely to improve the quality of financial reporting.

Do you agree with the assessment?

Yes No

If you do not agree, please provide your arguments and indicate how this could affect EFRAG’s endorsement advice.

The quality of financial reporting cannot be improved through amendments that fail to produce relevant information in widespread circumstances. See our comments to questions 2(a) and 2(b).

Costs and benefits

- 5 EFRAG is also assessing the costs that are likely to arise for preparers and for users on implementation of the Amendments in the EU, both in year one and in subsequent years. Some initial work has been carried out, and the responses to this invitation to comment will be used to complete the assessment.

The results of the initial assessment of costs are set out in paragraphs 6 to 11 of Appendix 3.1 of the accompanying Draft Letter to the European Commission regarding endorsement of the Amendments. To summarise, EFRAG's initial assessment is that the Amendments will not result in increased costs and that it is likely to be cost neutral.

Do you agree with this assessment?

Yes No

If you do not, please explain why you do not and (if possible) explain broadly what you believe the costs involved will be?

- 6 In addition, EFRAG is assessing the benefits that are likely to be derived from the Amendments. The results of the initial assessment of benefits are set out in paragraphs 12 to 13 of Appendix 3.1 of the accompanying Draft Letter to the European Commission regarding endorsement of the Amendments. To summarise, EFRAG's initial assessment is that users are likely to benefit from the Amendments as the information resulting from it will remove inconsistency and increase comparability between entities and therefore enhance their analysis.

Do you agree with this assessment?

Yes No

If you do not agree with this assessment, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

Paragraph 72A will produce in certain circumstances information that is not relevant for users, as it will lead to present as current liabilities for which the risk that they become repayable on demand is highly remote.

- 7 EFRAG's initial assessment is that the benefits to be derived from implementing the Amendments in the EU, as described in paragraph 6 above, are likely to outweigh the costs involved, as described in paragraph 5 above.

Do you agree with this assessment?

Yes No

If you do not agree with this assessment, please provide your arguments and indicate how this could affect EFRAG's endorsement advice.

See our answer to question 6 above

Overall assessment with respect to the European public good

- 8 EFRAG has initially concluded that endorsement of the Amendments would be conducive to the European public good (see paragraphs 15 to 18 of Appendix 3.1 of the accompanying Draft Letter to the European Commission).

Do you agree with this conclusion?

Yes No

If you do not agree, please explain your reasons.

We strongly believe that the situations where the outcome of applying paragraph 72A is not relevant are widespread and could impact negatively the presentation of the financial position of a large number of listed entities. While we agree it was necessary to provide more guidance in IAS 1 on how to assess the classification of liabilities as current or non-current, we believe this amendment fails to produce relevant outcome.