

Association of Accounting Technicians response to EFRAG Draft Comment Letter on Exposure Draft ED/2015/1 Classification of Liabilities – Proposed amendments to IAS1

Association of Accounting Technicians response to EFRAG Draft Comment Letter on Exposure Draft ED/2015/1 “Classification of Liabilities – Proposed amendments to IAS 1”

1. Introduction

- 1.1. The Association of Accounting Technicians (AAT) is pleased to have the opportunity to respond to EFRAG’s draft comment letter to the International Accounting Standards Board (IASB), released on 24 March 2015 (the letter).
- 1.2. AAT is submitting this response on behalf of our membership and from the wider public benefit of achieving sound and effective administration of taxes.
- 1.3. AAT has added comment in order to add value or highlight aspects that need to be considered further.
- 1.4. AAT has focussed on the operational elements of the proposals and has provided opinion on the practicalities in implementing the measures outlined.
- 1.5. Furthermore, the comments made reflect the potential impact that the proposed changes could have on businesses, many of whom employ AAT members or would be represented by our operationally skilled members in practice.

2. Executive summary

- 2.1. The IASB issued an exposure draft ED/2015/1 *Classification of Liabilities – Proposed amendments to IAS 1* on 10 February 2015.
- 2.2. The exposure draft seeks to clarify how an unconditional right to defer settlement of a liability outlined in para 69(d) of IAS 1 is reconciled with an entity having the discretion to refinance or roll over an obligation outlined in para 73 of IAS 1.
- 2.3. The IASB is also proposing to require that the amendments made to the Standard are applied retrospectively by reporting entities.
- 2.4. EFRAG has drafted a response to the IASB on its exposure draft and has invited comments on the draft comment letter by 10 June 2015.
- 2.5. AAT agrees with the responses in the draft comment letter relating to ED/2015/1 *Classification of Liabilities – Proposed amendments to IAS 1* (5.1, below). AAT supports EFRAGs suggestion that to avoid unintended consequences the IASB should clarify the guidance in para 69(d) (5.2, below).
- 2.6. AAT agrees with EFRAGs suggestion that the IASB undertakes additional research as to whether current guidance always provides the most relevant information when rights to defer settlement of a liability are not substantive as at the reporting date (**Error! Reference source not found.**, below).

3. AAT response to the draft comment letter on exposure draft ED/2015/1 “Classification of Liabilities – Proposed amendments to IAS 1”

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’.

- 3.1. AAT supports EFRAG’s response to this question on page 5 of the IASBs exposure draft.
- 3.2. Furthermore, AAT also considers that the IASB’s proposal to amend IAS 1 by removing inconsistent terms will make the Standard clearer.
- 3.3. AAT also supports EFRAG’s comment regarding the fact that only rights in place at the reporting date should affect the classification of the liability in para 5 (page 2) of the letter.
- 3.4. AAT agrees with the comprehensive example outlined at para 8 (page 3) of the letter. However, the example cites a ‘reporting period’ (being 31 March in para 8(a)) and a ‘reporting date’ being the year-end date of 31 December.
- 3.5. AAT recommends referring to the period-ended 31 March as the ‘interim reporting period’ or ‘interim period’ to avoid any ambiguity between ‘reporting period’ and ‘reporting date’ in the example. It would also be consistent with the terminology used in IAS 34 *Interim Financial Reporting*.
- 3.6. AAT accepts that it would be helpful if the IASB was to include additional application examples to address the situations outlined in the example in paras 8(a) and (b) (page 3) of the letter where different parties may view a breach of covenants as taking place at the reporting date or as at the interim reporting period.
- 3.7. It is AAT’s view that including additional application-guidance should serve to reduce the scope for divergent practices to emerge, particularly where the use of professional judgements are required.
- 3.8. The comments made in para 3.3 (above) are also relevant to EFRAG’s comments concerning the ‘existence of a right’ which are outlined in paras 11 and 12 (page 3) of the letter where classification of liabilities may be based on rights that are not substantive.
- 3.9. In addition AAT supports EFRAG’s suggestion in para 12 (page 3) of the letter that the IASB further explores these aspects to determine whether the current guidance does provide the most relevant information. As professional judgement would undoubtedly be needed to determine whether a reporting entity would fail to comply with the terms of any conditions attached to liabilities, the Standard would benefit from additional application guidance in such instances to reduce the scope for divergent practices emerging.

Question 2 – Linking settlement with 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?

- 3.10. AAT supports the response EFRAG made in its draft comment letter at para 16 (page 4) of the letter for the reasons given. AAT considers that it is important that unintended consequences are avoided as far as possible and agree that adding in the text “*by the transfer to the counterparty of cash, equity instruments, other assets or services*” makes it clear that a transfer of resources embodying economic benefits to another entity gives rise to a settlement of a liability and distinguishes this action from merely rolling over an obligation (which, of course, is not a settlement of a liability).
- 3.11. AAT, also, agrees with EFRAG in respect of the point raised relating to the convertible debt example in paras 18, 18 (a) and 18 (b) (page 4 of the letter). It is evident that unintended consequences are present due to the additional wording proposed in para 69 (para 13, page 4, the letter) which appears to contradict the wording in para 69(d) of the Standard (para 17(a), page 4, the letter).
- 3.12. The suggested re-drafting of para 69 (para 20, page 5, the letter), would be welcomed by the IASB to enable appropriate classification of the liability as current or non-current in the financial statements where the lender can opt for settlement of the liability in equity instruments as the proposed wording in para 69 would conflict with the existing wording in para 69(d).

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?

- 3.13. AAT agrees with the response in EFRAGs draft comment letter (paras 21 and 22, page 5) on the basis that the requirements in IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* as retrospective changes to financial statements enable the financial statements to be both comparable and consistent (characteristics which are both vital to users’ of the financial statements in order to arrive at reasoned and balanced conclusions about the financial affairs of a reporting entity).

4. Conclusion

- 4.1. AAT agrees with the responses as set out in the draft comment letter relating to ED/2015/1 *Classification of Liabilities – Proposed amendments to IAS 1*.
- 4.2. AAT also supports EFRAG’s suggestion for the IASB to include additional guidance in the standard where rights to defer settlement of a liability are subject to conditions which occur and are assessed after the reporting period (paras 6 and 7, page 3, the letter).
- 4.3. AAT, further, supports EFRAG’s suggestion that to avoid unintended consequences the IASB should clarify the guidance in para 69(d) (para 5 on page 1, the draft letter) for liabilities which can be settled, at the option of the counterparty, in an entity’s own equity instruments (paras 17, 18 and 19 of the letter).
- 4.4. AAT agrees with EFRAG’s suggestion that the IASB undertakes additional research as to whether current guidance always provides the most relevant information when rights to defer settlement of a liability are not substantive as at the reporting date (para 12 of the letter).

5. About AAT

- 5.1. AAT is a professional accountancy body with over 49,800 full and fellow members and 78,400 student and affiliate members worldwide¹. Of the full and fellow members, there are over 4,100 Members in Practice who provide accountancy and taxation services to individuals, not-for-profit organisations and the full range of business types.
- 5.2. AAT is a registered charity whose objectives are to advance public education and promote the study of the practice, theory and techniques of accountancy and the prevention of crime and promotion of the sound administration of the law.

6. Further information

If you have any questions or would like to discuss any of the points in more detail then please contact AAT at:

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¹ Figures correct as at 31 March 2015