

11 June 2015

Mr Hans Hoogervorst
Chairman
International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
UNITED KINGDOM

Dear Hans,

AOSSG comments on IASB Exposure Draft ED/2015/1
Classification of Liabilities

The Asian-Oceanian Standard-Setters Group (AOSSG) is pleased to provide comments on the IASB ED/2015/1 *Classification of Liabilities*. In formulating its views, the AOSSG sought the views of its constituents within each jurisdiction.

The AOSSG currently has 26 member standard-setters from the Asian-Oceanian region: Australia, Brunei, Cambodia, China, Dubai, Hong Kong, India, Indonesia, Iraq, Japan, Kazakhstan, Korea, Macao, Malaysia, Mongolia, Nepal, New Zealand, Pakistan, Philippines, Saudi Arabia, Singapore, Sri Lanka, Syria, Thailand, Uzbekistan, and Vietnam.

To the extent feasible, this submission to the IASB reflects in broad terms the collective views of AOSSG members. Each member standard-setter may also choose to make a separate submission that is consistent or otherwise with aspects of this submission. The intention of the AOSSG is to enhance the input to the IASB from the Asian-Oceanian region and not to prevent the IASB from receiving the variety of views that individual member standard-setters may hold. This submission has been circulated to all AOSSG members for their feedback after having initially been developed through the AOSSG Financial Statement Presentation and Disclosure Working Group.

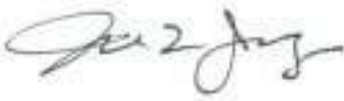
Overall, all AOSSG members generally support the proposed amendments outlined in Questions 1(a), 1(b) and 3; most AOSSG members support the proposed amendment outlined in Question 2 but provide some suggestions to strengthen the proposed amendment; and most AOSSG members do not support the proposal to delete the term 'unconditional' from paragraph 69(d) of IAS 1 *Presentation of Financial Statements* as outlined in Question 1(c).

The views of the AOSSG are explained in more detail in the Appendix. If you have any questions regarding any matters in this submission, please contact either one of us.

Yours sincerely,



Clement Chan
AOSSG Chair



Jee In Jang
AOSSG Financial Statement Presentation and Disclosure Working Group Leader

APPENDIX 1

Detailed comments on IASB ED/2015/1 Classification of Liabilities - 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'.

Do you agree with the proposed amendments? Why or why not?

1. All AOSSG members generally support the proposed amendments as outlined in Questions 1(a) and 1(b).
2. However, most members do not support the proposal to delete the term 'unconditional' [as outlined in Question 1(c)]. These members consider that deleting the term 'unconditional' might bring about unintended consequences given that this term has paramount significance in determining a liability's classification. These members' concerns are explained in the paragraphs below.

- (a) Uncertain rights depending on future events

If the IASB were to delete the term 'unconditional', it would become unclear whether it is the IASB's intention that an entity merely needs to have a 'right' at the end of the reporting period to classify the liability as non-current regardless of whether the entity is able to comply with covenants at a future date. This may be particularly relevant in the case of annual review clauses contained in loan agreements that give the financial institutions the potential to recall the loan.

In addition, there may be instances where it is difficult to assess whether an entity has complied with the liability conditions (e.g. debt covenants) at the reporting date. A breach of debt covenant indicated by a calculation subsequent to the reporting period may or may not point to the existence of the breach at the end of the reporting period.

(b) No perfect right to defer the settlement

In some member jurisdictions, certain loan agreements specify a repayment schedule over time in excess of one year and include an overriding repayment on demand clause, which gives lenders the right to demand repayment at any time at their sole discretion and irrespective of whether a default event has occurred. In this case, some members consider that such loans should be classified as current and deleting the term ‘unconditional’ would lead entities to disregard the repayment on demand clause.

3. If the IASB were to proceed with the proposal to delete the term ‘unconditional’, some members suggest that the IASB puts in place a clear definition of a ‘right’ so that the new requirement would not be interpreted differently from the current requirement (as explained in paragraph BC19 of the ED the proposed amendment seeks to clarify existing requirements and should not result in a change in accounting policy). Adding a definition should lead the IASB to (i) clarify whether a ‘right’ exists only after all preconditions of a liability are met at the end of the reporting period; and (ii) clarify whether a lender’s rights, such as a right to invalidate the borrower’s right to defer settlement, at reporting date should be taken into consideration under the proposals.
4. One member considers there is a need to refine ‘the right to roll over an obligation under an existing loan facility’ in the proposed paragraph 72R(a) to clearly reflect the IASB’s intention as articulated in paragraph BC11 of the ED. That is, emphasis should be made on "the existing loan facility that directly relates to the loan being classified". This member agrees that the right of rollover, which is an exception to the classification principle in paragraph 69, should be restricted to such limited circumstances in which the rolled-over obligation is akin to an extension of the loan being classified. It also appears aligned with the concurrent removal of references to ‘refinance’ that could be strictly interpreted as precluding rights to defer settlement under any other existing loan facilities. This member therefore recommends incorporating the text in paragraph BC11 of the ED into paragraph 72R(a) of the ED.
5. Another member suggests that ‘management intent’, so long as it is backed by a right, should be considered in reclassifying a non-current liability to a current liability. This member has a concern that liabilities are being classified as non-current under the proposals while they should be classified as current when on the basis of management intent. For example, if an entity would otherwise have the ability to defer repayment beyond 12 months after reporting date, but has publicly announced it will be repaying the liability in the next 6 months, the member considers current classification is necessary.
6. One member considers that the current IAS 1 requirements and the proposed amendment in the ED do not sufficiently reflect the economic substance of the prevailing practice of this member jurisdiction. In this jurisdiction, loan covenants may provide a right to the lender to recall loans in the event of a breach, but in practice the loans are never recalled immediately. The lender has a legal right to recall the loan only upon occurrence of a ‘default event’ and upon the failure to rectify the breach, as specified by the lender (if any). In practice, however, lenders are required to prove to judicial authorities that every reasonable opportunity has been given to the borrower to make good the situation.

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?

7. Most AOSSG members generally support the proposed amendment outlined in Question 2 but some members would like to provide some suggestions to strengthen the proposed amendments.
8. One member recommends that the IASB incorporates an example to illustrate whether a liability that will be refinanced using the proceeds of a new loan after the reporting period that has been agreed with a new lender at the reporting date would constitute settlement of the liability by the transfer of cash or other assets. Although paragraph BC11 of the ED clarifies that paragraph 73 of IAS 1 applies to an existing loan facility, it is unclear whether liabilities which are off-set as a choice of settlement are addressed in the amendments. Therefore, this member considers that further explanation could be provided on whether liabilities which are off-set are considered outflow of resources in terms of ‘other assets’ (i.e. extinguishment of liability is equivalent with offsetting of accounts receivable with the same counterparty acting as both the supplier/creditor and customer to the entity). This member believes that additional clarification is also needed for cases in which liabilities are written-off or given a waiver. To clarify the meaning of ‘settlement’, this member also suggests relocating the proposed new sentence in paragraph 69(d) as follows:

Current liabilities

69 An entity shall classify a liability as current when:

...

- (d) **it does not have ~~an unconditional~~ a right at the end of the reporting period to defer settlement of the liability for at least twelve months after the reporting period (see paragraph 73 72R). Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect its classification.**

For the purposes of classification as current or non-current, settlement of a liability refers to the transfer to the counterparty of cash, equity instruments, other assets or services that results in the extinguishment of the liability. *(In the ED, the IASB proposed to add this new sentence after the following sentence.)*

An entity shall classify all other liabilities as non-current.

9. One member would like to clarify whether settlement by equity instruments would affect the classification of liability as current or non-current. This member notes that paragraph 69(d) of the IAS 1 states that “terms of a liability that could, at the option of the counterparty, result

in its settlement by the issue of equity instruments do not affect its classification” and, in particular, the following IAS 1 existing paragraphs respectively state that:

BC38G IAS 1 and the Framework state that information about the liquidity and solvency positions of an entity is useful to users. **The terms ‘liquidity’ and ‘solvency’ are associated with the availability of cash to an entity. Issuing equity does not result in an outflow of cash or other assets of the entity** (*emphasis added in bold*).

BC38H The Board concluded that **classifying the liability on the basis of the requirements to transfer cash or other assets rather than on settlement better reflects the liquidity and solvency position of an entity** (*emphasis added in bold*), and therefore it decided to amend IAS 1 accordingly.

This member points out that the paragraphs mentioned directly above seem to be inconsistent with the proposed additional wording in paragraph 69, which states “for the purposes of classification, settlement of liability refers to the transfer to the counterparty of cash, **equity instruments** (*emphasis added*), other assets or services”. This member considers that further clarity to resolve the above seeming inconsistency with paragraph 69 would be necessary.

10. Another member observes that the proposed clarification on settlement could create tension with the existing guidance in paragraph 69(d) on equity conversion optionality of the counterparty. This member is concerned that it is unclear whether the latter should override the former, which lacks merits. Specifically, it does not appear that there are compelling reasons for conversion optionality of the counterparty to affect the current/non-current classification differently from mandatory conversion that does not meet the ‘fixed-for-fixed’ criterion for equity classification under IAS 32 *Financial Instruments: Presentation*, given that the entity does not have the right to defer the transfer of equity instruments for the settlement of the liability in both cases. This member therefore recommends that the IASB should consider removing the aforesaid existing guidance in paragraph 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?

11. All AOSSG members generally agree with the proposed transition arrangements.