UK Endorsement Board

IAS 1 *Presentation of Financial Statements* Narrow Scope Amendments 2020 and 2022

Executive Summary

Project Type	Endorsement Project
Project Scope	Limited (Narrow Scope Amendments)
Purpose of the paper	
International Accounting Standards Board (IASB) issued its Amendments to IAS 1 *Non-current Liabilities with Covenants* in October 2022. The purpose of this paper is to provide an update to the Board on the link between the IASB's IAS 1 *Presentation of Financial Statements* Narrow Scope Amendments issued in 2020 and in 2022.	
Summary of the Issue	
On 31 October 2022 the IASB published amendments to IAS 1 *Non-current Liabilities with Covenants* (the 2022 Amendments). These amendments address stakeholders' feedback on the January 2020 amendments to IAS 1 *Classification of Liabilities as Current or Non-current*[1] (the 2020 Amendments). Both Amendments have an effective date of 1 January 2024 and neither has been endorsed for use in the UK. This paper provides information on: the background to, and summary of, the 2020 Amendments; the Board's influencing activities on the 2022 Amendments; and the new requirements in the final version of the 2022 Amendments that were not part of the Exposure Draft. The Secretariat considers that the 2020 and 2022 Amendments will need to be assessed for adoption together, and if appropriate adopted simultaneously, given their interaction. This paper sets out a tentative timeline for the project.	

1 Classification of Liabilities as Current or Non-current (Amendments to IAS 1) (ifrs.org)

Decisions for the Board	
The Board is not asked to make any decisions. The following questions are relevant for the Board's discussion:	
1.	Do Board members have any questions or comments on the Background (paragraphs 1 – 30)?
2.	Does the Board have any comment on the proposed next steps, including developing an approach based on assessing the two sets of amendments together (paragraphs 31) and the tentative timeline for the project (paragraph 33)?
3.	Do Board members agree that a consolidated text, incorporating both the 2020 and 2022 amendments, would be useful as they consider the two sets of amendments (paragraph 34)?
Recommendation	
•	N/A
Appendices	
Appendix A:	Key paragraphs from the 2020 Amendments
Appendix B:	The IASB's proposals in its ED, the UKEB's response in our comment letter, and the tentative decisions made by the IASB
Appendix C:	Key paragraphs from the 2022 Amendments

Background

The objective

1. On 31 October 2022 the IASB published amendments to IAS 1 *Non-current Liabilities with Covenants*[2] (the 2022 Amendments). These amendments address stakeholders' feedback on the classification of liabilities as current or non-current when applying requirements introduced in January 2020 amendments to IAS 1 *Classification of Liabilities as Current or Non-current*[3] (the 2020 Amendments) that are not yet in effect.

2. The amendments are focused on clarifying the classification of liabilities as current or non-current. So, while quite narrow and limited in scope, they have the potential to impact virtually every company preparing financial statements in accordance with international accounting standards. The classification of liabilities communicates important information to users about the likely pressures on the working capital of companies and can impact important metrics such as solvency and liquidity.

3. Both sets of Amendments now have an effective date of 1 January 2024 and neither has been adopted for use in the UK. The Board was not formed when the 2020 Amendments were developed but it actively influenced the 2022 Amendments.

4. This paper provides an overview of the requirements of each of the Amendments. We also outline stakeholder views that we are aware of at this point in time.

The 2020 amendments to IAS 1: *Classification of Liabilities as Current or Non-current*

Overview

5. In January 2020, the IASB issued narrow scope amendments to IAS 1 *Classification of Liabilities as Current or Non-current*. Appendix A reproduces the paragraphs from the 2020 Amendments.

6. The amendments are focussed on clarifying one of the criterion in IAS 1 for classifying a liability as non-current: the requirement for an entity to have the right to defer settlement of the liability for at least 12 months after the reporting period.

7. The genesis of the 2020 Amendments were submissions received by the IFRS Interpretations Committee in the early 2010s requesting clarification of the criteria for the classification of a liability as either current or non-current. The issues

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2 [IASB-IAS2022-1 – Final Amendment: Non-current Liabilities with Covenants - Amendment to IAS 1 (ifrs.org)]
3 [Classification of Liabilities as Current or Non-current (Amendments to IAS 1) (ifrs.org)]

concerned whether the classification requirements of paragraph 69(d) of IAS 1 were consistent with the circumstances detailed in paragraph 73.

8. The submitters considered that these two paragraphs were asymmetrical and requested further guidance on the classification of different types of debt as either current or non-current. In their view, having an unconditional right to defer settlement (specified in paragraph 69(d)) was irreconcilable with having the discretion to refinance or roll over an obligation (specified in paragraph 73).

9. Following outreach on this topic, the Interpretations Committee recommended a proposed amendment to IAS 1 as part of the 2010-2012 Cycle Annual Improvements to IFRS Standards to clarify that the refinancing arrangement detailed in paragraph 73 of the Standard should only result in a non-current classification if the arrangement was with the same lender and on the same or similar terms. That proposal included guidance on the nature of 'same or similar terms' that was linked to the derecognition requirements for financial liabilities in IFRS 9 *Financial Instruments*.

10. Many respondents raised concerns about the proposed amendments and at its March 2013 meeting the IASB agreed not to proceed with the proposed amendments and began to develop alternative amendments.

11. An Exposure Draft *Classification of Liabilities* was issued in 2015[4]. The IASB received a substantial amount of feedback that led to significant revisions over the next 5 years with the final amendments being published in 2020.

12. The amendments:

    a) specify that an entity's right to defer settlement must exist at the end of the reporting period (Paragraphs 69(d), 72A and 73);

    b) clarify that classification is unaffected by management's intentions or expectations about whether the entity will exercise its right to defer settlement (Paragraph 75A);

    c) clarify how lending conditions affect classification (Paragraph 72A); and

    d) clarify requirements for classifying liabilities an entity will or may settle by issuing its own equity instruments (Paragraph 76A).

13. As the Board is aware, Paragraph 72A subsequently caused concern with stakeholders (see below) which led to the 2022 Amendments.

14. We are not currently aware of any significant concerns with other elements of these amendments, bearing in mind that they are not yet effective. This was also confirmed at the October 2022 UKEB's Preparers Advisory Group meeting where,

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4 Exposure Draft: Classification of Liabilities—Proposed Amendments to IAS 1 (ifrs.org)

with the exception of the Paragraph 72A matter, no significant concerns were raised.

Stakeholder concerns with Paragraph 72A of the 2020 Amendments

15. In 2021, stakeholder concerns about Paragraph 72A led to consideration by the IFRS Interpretations Committee (Interpretations Committee) of the application of the 2020 amendments. Specifically, the Interpretations Committee considered classification of a liability as current or non-current when a company's right to defer settlement is subject to compliance with covenants within 12 months of the reporting date and the company is not compliant with such covenants at the reporting date.

16. This led to the Interpretations Committee issuing a tentative agenda decision (TAD) which stated that as the company would not have a right to defer settlement of the liability it would present the related liability as a current liability in its balance sheet. Respondents to the TAD were critical of the conclusion and highlighted unintended consequences arising from the 2020 Amendments and the TAD.

17. The IASB's response was a tentative decision to amend IAS 1 with respect to classification (as current or non-current), presentation and disclosures of liabilities where an entity's right to defer settlement for at least 12 months is subject to the entity complying with conditions after the reporting period. This was subsequently published as IASB Exposure Draft (ED) *Non-current Liabilities with Covenants* in November 2021.

18. In the ED, the IASB proposed to amend IAS 1 to specify that "specific conditions", with which a company must comply after the reporting date, do not affect the classification of a liability as current or non-current at that date. Instead, a company would be required to:

    a) present non-current liabilities with covenants separately on the face of its balance sheet; and

    b) disclose information in the notes about the covenants with which it must comply within 12 months of the reporting date.

19. The Board engaged in influencing activities, including stakeholder outreach and desk-based research, and submitted a comment letter in response to that ED.

The 2022 Amendments *to IAS 1: Non-current Liabilities with Covenants*

20. On 31 October 2022 the IASB published amendments to IAS 1 *Non-current Liabilities with Covenants* (2022 Amendments).

21. Appendix B summarises the IASB's proposals in its ED, the UKEB's response in its comment letter[5], and the final amendment published by the IASB. We are pleased to note that many of the changes made in the published final amendment align with recommendations in the UKEB comment letter.

22. Appendix C reproduces the primary paragraphs from the 2022 Amendments including those referenced below.

New additions to the final 2022 Amendments

23. The term "covenant" has been defined in paragraph 72B (as conditions specified in a loan arrangement) and is subsequently used in paragraph 74 (not reproduced) replacing the words "condition of". This clarification is consistent with the recommendation in the UKEB comment letter.

24. More significantly, the disclosure requirements have been substantially rewritten (Paragraph 76ZA). The UKEB comment letter supported the objective of enhancing disclosure in the notes to provide useful information that enables users of financial statements to assess the risk that a liability classified as non-current could become repayable within twelve months. However, we suggested that a number of the proposed requirements were deleted as we did not consider that they were directly relevant to the disclosure objective. Those requirements were deleted and replaced with different requirements.

25. The revised disclosure requirements are that where a company has non-current liabilities subject to covenants in the next twelve months, the company shall disclose information in the notes that enables users of financial statements to understand the risk that the liabilities could become repayable within twelve months after the reporting period, including:

    a) information about the covenants (including the nature of the covenants and when the entity is required to comply with them) and the carrying amount of related liabilities.

    b) facts and circumstances, if any, that indicate the entity may have difficulty complying with the covenants—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 if they were to be assessed for compliance based on the entity's circumstances at the end of the reporting period.

[5] IFRS - Exposure Draft and comment letters: Non-current Liabilities with Covenants

26. Finally, the IASB has clarified in Paragraph 139U that a company would need to adopt both sets of amendments at the same time. Again, this is consistent with the recommendations in the UKEB comment letter.

27. We undertook brief preliminary outreach with both the Preparers Advisory Group and the Accounting Firms & Institutes Advisory Group in the same week that the Amendment was published.

28. Members of the Preparers Advisory Group noted some preliminary concerns with the new additions to the 2022 Amendments, including:

    a) The intended meaning of "loan arrangement" in paragraph 72B.

    b) The extent of the disclosure expected in accordance with paragraph 76ZA(a) and the application of materiality.

    c) The interpretation of "may have" in paragraph 76ZA(b), and the type of threshold it implies.

29. However, no one raised any of these as fatal flaws with the Amendments.

30. Members of the Accounting Firms & Institutes Advisory Group indicated broad agreement that the amendments were a significant improvement, and that the matters identified at the Preparers Advisory Group would most likely be resolved through the implementation phase.

Question for the Board
1. Do Board members have any questions or comments on the Background (paragraphs 1 – 30)?

Next steps

Endorsement

31. As the 2022 Amendments amend the 2020 Amendments in a significant way, the Secretariat considers that both sets of amendments should be assessed for adoption together and, if appropriate, adopted simultaneously. This will also enable the concurrent implementation of those two sets of amendments by companies, as envisaged by the IASB.

32. The Secretariat expects to continue outreach and desk-based research to identify any concerns with the 2020 and/or 2022 Amendments until the end of 2022 with the aim of developing an approach to the endorsement project.

33. A Project Initiation Plan, including the findings and a project timeline, is currently scheduled to be presented at the January 2023 Board meeting. Broadly, this would permit a Draft Endorsement Criteria Assessment (DECA) to be discussed at the Board's February 2023 meeting. This should allow for final adoption to be completed by Q4 2023.

34. The Secretariat is making enquiries as to whether the IASB intends to publish a consolidated text incorporating both the 2020 and 2022 Amendments. If not, we intend to prepare such a text so the Board can review the amendments in the round.

Questions for the Board
2. Does the Board have any comment on the proposed next steps, including developing an approach based on assessing the two sets of amendments together (paragraphs 31) and the tentative timeline for the project (paragraph 33)? 3. Do Board members agree that a consolidated text, incorporating both the 2020 and 2022 amendments, would be useful as they consider the two sets of amendments (paragraph 34)?

Appendix A: Key paragraphs from the 2020 Amendments

A1. Paragraph 69(d):

it does not have ~~an unconditional~~ the 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). 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~~.

A2. Paragraph 72A:

An entity's right to defer settlement of a liability for at least twelve months after the reporting period must have substance and, as illustrated in paragraphs 73–75, must exist at the end of the reporting period. If the right to defer settlement is subject to the entity complying with specified conditions, the right exists at the end of the reporting period only if the entity complies with those conditions at the end of the reporting period. The entity must comply with the conditions at the end of the reporting period even if the lender does not test compliance until a later date.

A3. Paragraph 73:

If an entity ~~expects, and~~ has the ~~discretion,~~ right, at the end of the reporting period, to ~~refinance or~~ roll over an obligation for at least twelve months after the reporting period under an existing loan facility, it classifies the obligation as non-current, even if it would otherwise be due within a shorter period. ~~However, when refinancing or rolling over the obligation is not at the discretion of the entity (for example, there is no arrangement for refinancing)~~ If the entity has no such right, the entity does not consider the potential to refinance the obligation and classifies the obligation as current.

A4. Paragraph 75A:

Classification of a liability is unaffected by the likelihood that the entity will exercise its right to defer settlement of the liability for at least twelve months after the reporting period. If a liability meets the criteria in paragraph 69 for classification as non-current, it is classified as non-current even if management intends or expects the entity to settle the liability within twelve months after the reporting period, or even if the entity settles the liability between the end of the reporting period and the date the financial statements are authorised for issue. However, in either of those circumstances, the entity may need to disclose information about the timing of settlement to enable users of its financial statements to understand the impact of the liability on the entity's financial position (see paragraphs 17(c) and 76(d)).

A5. Paragraph 76A and B:

For the purpose of classifying a liability as current or non-current, settlement refers to a transfer to the counterparty that results in the extinguishment of the liability. The transfer could be of:

(a) cash or other economic resources—for example, goods or services; or

(b) the entity's own equity instruments, unless paragraph 76B applies.

Terms of a liability that could, at the option of the counterparty, result in its settlement by the transfer of the entity's own equity instruments do not affect its classification as current or non-current if, applying IAS 32 *Financial Instruments: Presentation*, the entity classifies the option as an equity instrument, recognising it separately from the liability as an equity component of a compound financial instrument.

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Appendix B IASB's proposals in its ED, the UKEB's response in our comment letter, and the tentative decisions made by the IASB

IASB proposal	UKEB final position[1]	Final Amendment
That the classification of a liability as current or non-current should be based on conditions that exist at the end of the reporting period, even if that compliance is only tested later.	We agreed in principle with this approach. However, we believed that "specified conditions" either needed to be defined or the term "condition" should be used. We also recommended some redrafting for clarity.	The IASB retained this proposal but has been some rewording in the final standard to enhance clarity of the paragraph
When an entity classifies a liability subject to conditions as non-current, it would be required to disclose information in the notes that enables users of financial statements to assess the risk that the liability could become repayable within twelve months.	We supported the objective of enhancing disclosure in the notes to provide useful information that enables users of financial statements to assess the risk that a liability classified as non-current could become repayable within twelve months. However, we suggested that a number of the proposed requirements were deleted as we did not consider that they are directly relevant to the disclosure objective.	The IASB has made a number of modifications to the specific disclosure requirements proposed in the original ED. The proposals we suggested be deleted have been removed. A specific requirement to disclose information about facts and circumstances that indicate the entity may have difficulty complying with covenants when it is required to do so has been added.

1 See the UKEB's Feedback Statement on the ED: Feedback Statement - Non-Current Liabilities with Covenants

IASB proposal	UKEB final position[2]	Final Amendment
To require an entity to present separately, in its statement of financial position, liabilities classified as non-current for which the entity's right to defer settlement for at least twelve months after the reporting period is subject to compliance with specified conditions within twelve months after the reporting period.	We did not support this proposal for a number of reasons, including concerns that few liabilities would not meet these conditions, and that such a requirement was not consistent with a principle-based approach to financial accounting.	The IASB has deleted this requirement. It is to be replaced with a requirement to disclose the carrying amount of non-current liabilities with covenants in the notes together with information on the nature of the covenants and when the entity is required to comply with them.
To clarify circumstances in which an entity does not have a right to defer settlement of a liability for at least twelve months after the reporting period.	We believed the proposals in paragraph 72C(b) were likely to lead to diversity in practice and have unintended consequences when it comes to classification. We recommended deletion of paragraph 72C.	The IASB has deleted paragraph 72C.
To require retrospective application of the amendments and defer the effective date of the 2020 Amendments to no earlier than 1 January 2024.	We agreed but noted that entities should not be able to early adopt the 2020 amendments without also adopting these amendments.	The IASB retained this proposal but has made it clear that entities cannot early adopt the 2020 Amendments without also adopting the 2022 Amendments.

[2] See the UKEB's Feedback Statement on the ED: Feedback Statement - Non-Current Liabilities with Covenants

Appendix C Key paragraphs from the 2022 Amendments

C1 Paragraph 72A:

An entity's right to defer settlement of a liability for at least twelve months after the reporting period must have substance and, as illustrated in paragraphs 72B–75 ~~73–75~~, must exist at the end of the reporting period. ~~If the right to defer settlement is subject to the entity complying with specified conditions, the right exists at the end of the reporting period only if the entity complies with those conditions at the end of the reporting period. The entity must comply with the conditions at the end of the reporting period even if the lender does not test compliance until a later date.~~

C2 Paragraph 72B:

An entity's right to defer settlement of a liability arising from a loan arrangement for at least twelve months after the reporting period may be subject to the entity complying with conditions specified in that loan arrangement (hereafter referred to as 'covenants'). For the purposes of applying paragraph 69(d), such covenants:

(a) affect whether that right exists at the end of the reporting period—as illustrated in paragraphs 74–75—if an entity is required to comply with the covenant on or before the end of the reporting period. Such a covenant affects whether the right exists at the end of the reporting period even if compliance with the covenant is assessed only after the reporting period (for example, a covenant based on the entity's financial position at the end of the reporting period but assessed for compliance only after the reporting period).

(b) do not affect whether that right exists at the end of the reporting period if an entity is required to comply with the covenant only after the reporting period (for example, a covenant based on the entity's financial position six months after the end of the reporting period).

C3 Paragraph 76ZA

In applying paragraphs 69–75, an entity might classify liabilities arising from loan arrangements as non-current when the entity's right to defer settlement of those liabilities is subject to the entity complying with covenants within twelve months after the reporting period (see paragraph 72B(b)). In such situations, the entity shall disclose information in the notes that enables users of financial statements to understand the risk that the liabilities could become repayable within twelve months after the reporting period, including:

(a) information about the covenants (including the nature of the covenants and when the entity is required to comply with them) and the carrying amount of related liabilities.

(b) facts and circumstances, if any, that indicate the entity may have difficulty complying with the covenants—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 if they were to be assessed for compliance based on the entity's circumstances at the end of the reporting period.

C4 Paragraph 139U

Classification of Liabilities as Current or Non-current, issued in January 2020 amended paragraphs 69, 73, 74 and 76 and added paragraphs 72A, 75A, 76A and 76B. An entity shall apply those amendments for annual reporting periods beginning on or after 1 January 2024 ~~1 January 2023~~ retrospectively in accordance with IAS 8. Earlier application is permitted. If an entity applies those amendments for an earlier period after the issue of *Non-current Liabilities with Covenants* (see paragraph 139W), it shall also apply *Non-current Liabilities with Covenants* for that period. If an entity applies *Classification of Liabilities as Current or Non-current* ~~those amendments~~ for an earlier period, it shall disclose that fact.

C5 Paragraph 139W

Non-current Liabilities with Covenants, issued in October 2022, amended paragraphs 60, 71, 72A, 74 and 139U and added paragraphs 72B and 76ZA. An entity shall apply:

(a) the amendment to paragraph 139U immediately on issue of *Non-current Liabilities with Covenants*.

(b) all other amendments for annual reporting periods beginning on or after 1 January 2024 retrospectively in accordance with IAS 8. Earlier application is permitted. If an entity applies these amendments for an earlier period, it shall also apply *Classification of Liabilities as Current or Non-current* for that period. If an entity applies *Non-current Liabilities with Covenants* for an earlier period, it shall disclose that fact.