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24 April 2015

The Chairman  
The International Accounting Standards Board  
30 Cannon Street  
LONDON EC4M 6XH  
UK

The Chairwoman  
Australian Accounting Standards Board  
PO Box 204, Collins Street West  
MELBOURNE VIC 8007

*By email*

Dear Sir and Madam

**Re: Classification of Liabilities – Proposed amendments to AASB 101**

Westworth Kemp Consultants ([www.westworthkemp.com.au](http://www.westworthkemp.com.au)) value the opportunity to provide feedback into the amendment of AASB 101 (IAS 1). We are a boutique consultancy, based in Sydney, Australia, specialising in financial reporting, assurance and compliance issues, particularly in the context of litigation and dispute resolution and we also provide advice to clients on the application of financial reporting standards.

We are particularly interested in the disclosure of liabilities as current or non-current as we are aware of a number of cases involving failed entities where liabilities had been wrongly classified. Non-accountants find a failure to distinguish between current and non-current hard to understand as it is such a fundamental part of the balance sheet. Consequently, if errors are being made in this basic area, it should be looked at and we support the IASB's proposals as, in our view, they articulate the requirements more clearly than the current version of the standard, while not actually changing the requirements.

Our answers to the detailed questions posed by the IASB and the AASB are below:

## IASB 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 support the proposed amendments and reordering of this section of IAS 1/AASB 101 as in our view the revised wording makes the circumstances in which a liability has to be presented as current clearer than in the present version of the standard.

The focus on rights at the period end makes it clear that preparers and auditors must only look at the documented rights that the entity has within its borrowing agreements at period end and not consider any arrangements that may have been customary hitherto, but are not actually supported by rights.

### 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 support the inclusion of the new sentence at the end of paragraph 69 clarifying what constitutes settlement of a liability and the fact that settlement requires an outflow of resources or the issue of new equity to replace the liability. Some practitioners seem to have been confused between settlement and roll over.

### 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?

Because in our view the new wording does not change the requirements of the standard, but merely clarifies them, we support retrospective application.

## AASB Questions

### AASB Specific Matters for Comment

The AASB would particularly value comments on the following:

1. whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, particularly any issues relating to:
  - (a) not-for-profit entities; and
  - (b) public sector entities, including GAAP/GFS implications;
2. whether, overall, the proposals would result in financial statements that would be useful to users;
3. whether the proposals are in the best interests of the Australian economy; and
4. unless already provided in response to specific matters for comment 1 – 3 above, the costs and benefits of the proposals relative to the current requirements, whether quantitative (financial or non-financial) or qualitative. In relation to quantitative financial costs, the AASB is particularly seeking to know the nature(s) and estimated amount(s) of any expected incremental costs, or cost savings, of the proposals relative to the existing requirements.

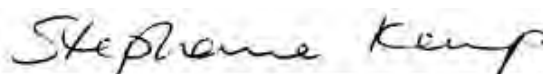
In our view the proposed changes merely clarify the existing requirements and therefore pose no issues for not-for-profits or public sector entities and have no cost/benefit implications. Keeping our standards consistent with those of the IASB is in the best interests of the Australian economy.

If you wish to discuss any of these matters further, please contact me at [chris@westworthkemp.com.au](mailto:chris@westworthkemp.com.au).

Yours faithfully



Chris Westworth, LLB, FCA, FAICD



Stephanie Kemp MA, FCA



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The Chair  
Australian Accounting Standards Board  
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Dear Ms Peach

### ED 259 Classification of Liabilities

Our comments and recommendations regarding ED 259 are provided in this submission. Responses to specific questions as requested by the AASB and IASB are provided in the attachment on pages 3-5.

Saward Dawson operates in Melbourne, Australia. Our clients come from a range of industries and include large private businesses, small to medium enterprises, and a significant number of not-for-profit entities. We are focused on enhancing the relevance, reliability and understand ability of financial reporting for users.

In summary we hold the following views in relation to the attachment:

1. **The removal of the term 'unconditional right' and replacement with 'a right' or 'the right' is** likely to result in additional confusion and divergence of liability classification as the proposal appears to not to address the fact that most loan agreements (or any other contract) contain various rights and obligations on each party to the contract and not an explicit right.

This is particularly evident in Australia where the majority of loan contracts with Australian banks **contain an 'Annual Review' clause. Under such agreements a borrower may have a facility that** does not require repayment for a number of years however this right to defer payment is subject to annual review by the financier. Currently such facilities are classified as current as the right to defer settlement is not unconditional even though the likelihood of repayment being required by the financier based on the annual review clause is often remote.

We strongly hold the view that the IASB should include a specific example with these facts to provide clear guidance to preparers and auditors of financial reports on the appropriate classification of such liabilities. Should the IASB fail to provide such guidance the AASB should address the issue.

2. We believe that the classification of a liability being based entirely on the legal right to defer settlement that exists at balance date in certain circumstances distorts the financial statements and results in them being less useful for users.

In particular where the lender agrees to extend grace for a breach, or rollover a facility post year end but prior to the signing of the financial report, extensive disclosures are often included to explain why the classification of the liability as current is misleading and that settlement is now not required to occur within the next 12 months.

Similarly where a breach of agreement occurs post balance date a liability is classified as non-current but extensive disclosures occur in relation the post balance date event and potentially going concern implications as required.

Accordingly we believe that the IASB should reconsider its view the liabilities are classified based on an as at balance date legal right. Where events occur post balance date we believe such events should impact classification as this would represent the commercial reality of the future requirement to settle a liability and would provide more useful information to users of financial statements.

Please do not hesitate to contact us should you wish to discuss further any matters arising from this submission.

Yours Sincerely

A handwritten signature in blue ink, appearing to read 'Peter J. Miller'.

P Shield  
Partner

A handwritten signature in blue ink, appearing to read 'Jeffrey Tulk'.

J Tulk  
Senior Manager - Technical

## **AASB Specific Matters for Comment**

*1. Whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, particularly any issues relating to:*

*(a) not-for-profit entities; and*

*(b) public sector entities, including GAAP/GFS implications;*

**As most current banking agreements in Australia contain an 'Annual Review' clause that result in them currently being classified as current liabilities by borrowers as the rights under a facility do not provide the borrower with an unconditional right to defer. The proposed removal of 'unconditional' is likely to result in further diversity of practice as a borrower will have a right to defer while a lender has a right to review and alter the agreement. This specific fact pattern should be addressed by the IASB or AASB to avoid uncertainty and diversity of practice should the proposed changes occur.**

*2. Whether, overall, the proposals would result in financial statements that would be useful to users;*

We consider the proposal **to remove 'unconditional' will be useful if the clarification detailed in 1 above is provided.**

A Statement of Financial position that accurately reflects a commercial reality of current and non-current liabilities taking into account rights that are established or removed post balance date will be more useful to users as this would reflect the commercial likelihood of the timing of the settlement of a liability rather than solely the legal right at balance date.

We believe that any legal right to review where the likelihood of altering the arrangement is in isolation remote could be more appropriately acknowledged through additional disclosure.

*3. Whether the proposals are in the best interests of the Australian economy; and*

We support revisions that improve the relevance, reliability and user understanding of financial reports.

*4. Unless already provided in response to specific matters for comment 1 – 3 above, the costs and benefits of the proposals relative to the current requirements, whether quantitative (financial or non-financial) or qualitative. In relation to quantitative financial costs, the AASB is particularly seeking to know the nature(s) and estimated amount(s) of any expected incremental costs, or cost savings, of the proposals relative to the existing requirements.*

In our experience significant time and cost is involved in justifying current classification requirements that are based on legal rights however remote the likelihood of them being exercised. Without specific clarification of the treatment of common facility agreements in Australia this cost is likely to continue to occur.



## IASB Specific Matters for Comment

### *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?*

Part (a) – we agree with the proposed amendments and the reasons stated in BC3

Part (b) – although we agree that the proposal achieves the aim of making an explicit requirement to classify liabilities based on the legal rights at the reporting date, we do not believe that this provides useful information for users and should be reconsidered by the IASB.

In particular, where a breach occurs post reporting date but prior to report signing, a liability may be classified as non-current where payment is in fact now due on demand. Similarly where a lender agrees to extend grace for a breach or rollover a facility after reporting date but prior to report signing, a liability is classified as current even though a settlement is no longer required within the next 12 months.

Part (c) – **although we agree with the proposal to delete 'unconditional'** we believe more explicit guidance is required where a borrower has rights in relation to a long term facility but where a lender also has rights to alter the agreement or an increase in uncertainty of classification and diversity of practice will result.

**In Australia such rights are often contained in an 'annual review' clause within borrowing agreements.** Although altering the agreement under an annual review clause is not common and the likelihood is often remote, certain lenders have utilised these clauses to demand settlement earlier than the term of the agreement.

### *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?*

No comment.

### *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 proposal as any change in classification should be applied to the comparative period to ensure consistency and comparability.

9 May 2015

Kris Peach CA  
Australian Accounting Standards Board  
Level 7, 600 Bourke Street  
Melbourne, VIC 3000

By email: [standard@aasb.gov.au](mailto:standard@aasb.gov.au)

Dear Ms Peach

**Submission on Exposure Draft ED 259: Classification of liabilities (ED)**

Thank you for the opportunity to comment on the proposed amendments to AASB 101 *Presentation of Financial Statements* relating to the classification of liabilities. CPA Australia and Chartered Accountants Australia and New Zealand (Chartered Accountants ANZ) have considered the Exposure Draft and our comments are set out below.

CPA Australia and Chartered Accountants ANZ represent over 250,000 professional accountants. Our members work in diverse roles across public practice, commerce, industry, government and academia in Australia and internationally.

We broadly support the amendments to AASB 101 to clarify when a liability should be classified as current or non-current, as we understand there are difficulties in applying the extant requirements in practice. The classification of liabilities provides important information to investors about when an entity may be required to settle a liability, and therefore its financial position. However, we are concerned that there will be inconsistent application of some of the proposed amendments, particularly in relation to the classification of loans as current or non-current liabilities, in accordance with proposed paragraphs 69(d) and 73.

**Representatives of the Australian Accounting Profession**



[cpaaustralia.com.au](http://cpaaustralia.com.au)



[charteredaccountantsanz.com](http://charteredaccountantsanz.com)



## Nature of the rights

The ED proposes to remove the word ‘unconditional’ from paragraph 69(d) so that the extant “unconditional right to defer settlement for at least 12 months” becomes a “right to defer settlement for at least 12 months”. This changes the meaning of paragraph 69(d), and consequently it may be difficult to establish whether a borrower has a ‘right’ to defer settlement.

This may be particularly relevant in the case of annual review clauses contained in bank loan agreements, which give the financial institution the potential to call in the loan. Many standard loan agreements in Australia include such clauses and have subsequently been classified as current on the basis that the borrower did not have an unconditional right to defer settlement. In such instances, the absence of the word ‘unconditional’ may cause loans to be classified as non-current.

We acknowledge the rationale outlined in the *Basis of Conclusions* (BC) for the proposed amendment to paragraph 69(d), and we agree that the wording should be consistent with paragraph 73, where the word ‘discretion’ (to refinance or roll over an obligation) has also been replaced with the word ‘right’. However, we encourage the provision of additional guidance to cover specific circumstances where annual review clauses exist.

## Conditions at the reporting date

We appreciate the intention of the proposed amendments to paragraphs 69(d) and 73 is to make it explicit that only rights that exist at the reporting date should affect the classification of a liability. We also note the concerns raised in paragraph BC16 that the classification of liabilities should not depend on management’s intentions and expectations. Furthermore, paragraph BC16 highlights the Board’s reluctance to propose amendments in relation to post-reporting date events, as this may result in ambiguity around the application of IAS 10 *Events after the Reporting Period*.

However, there may still 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 a 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. We believe that additional guidance is required in situations where it is evident that a breach has occurred but the timing of the breach is less apparent.

We note the concerns raised in paragraph BC16 on the classification of liabilities and their dependence on management’s intentions and expectations. However, it is not clear how management intentions or expectations are considered in the classification of liabilities in circumstances where a long-term liability is expected to be settled within the next 12 months. In such circumstances, the classification of the liability as current in accordance with paragraph 69(a) may be appropriate. We are of the opinion that clarification and further guidance is required on how management intention should affect the classification of liabilities in such circumstances.

## Right to roll over an obligation

Due to the difficulties in applying paragraph 73 in the context of lender consortia, we note that the ED did not include an explicit requirement for rolled over lending to be with the ‘same lender’. Without any amendment, practical difficulties remain when determining whether an entity still has a right to defer settlement of the liability by rolling over the borrowing under an existing loan facility. We encourage consideration of how changes in consortia members that may result in a change in loan facility be addressed in the amended standard, and the provision of guidance to assist with the application of the proposed amendments in such circumstances.

We also seek clarity and guidance on how to classify a liability in a situation where an agreement to refinance a loan is entered into before the reporting period end and involves the settlement of the liability with the old lender by a new lender after the reporting period end.

### **Transition and first-time adoption**

Paragraph BC19 indicates that the changes in classification are changes in estimate rather than changes in accounting policy. However, the proposals require retrospective application and paragraph BC20 provides the reasons for this approach. As changes in estimates normally require prospective application and to ensure consistent application of the requirements, we suggest reconsideration of the conclusion that the changes are to be considered as changes in estimates.

If you have any questions regarding this submission, please do not hesitate to contact either Dr Michael Fraser CA (Chartered Accountants ANZ) [michael.fraser@charteredaccountantsanz.com](mailto:michael.fraser@charteredaccountantsanz.com) or Ram Subramanian (CPA Australia) [ram.subramanian@cpaaustralia.com.au](mailto:ram.subramanian@cpaaustralia.com.au).

Yours sincerely



**Stuart Dignam**  
**General Manager – External Positioning**  
**CPA Australia**



**Rob Ward FCA**  
**Head of Leadership and Advocacy**  
**Chartered Accountants Australia and New Zealand**

Ms Kris Peach  
The Chair  
Australian Accounting Standards Board  
PO Box 204  
Collins Street West  
Victoria 8007

  
Dear Ms ~~Peach~~,

**Exposure Draft (ED) 259 *Classification of Liabilities* Proposed Amendments to AASB 101 and (IASB ED/2015/1)**

The Heads of Treasuries Accounting and Reporting Advisory Committee (HoTARAC) welcomes the opportunity to provide comments to the Australian Accounting Standards Board (AASB) on the ED: Classification of Liabilities (Proposed amendments to AASB101).

HoTARAC is generally supportive of the proposals and provides specific comments on questions from the ED in the Attachment below.

If you have any queries regarding HoTARAC's comments, please contact Peter Gibson from the Australian Department of Finance on 02 6215 3551.

Yours sincerely



David Nicol  
Chair  
Heads of Treasuries Accounting and Reporting Advisory Committee

 May 2015

## ATTACHMENT

### Questions for respondents:

#### **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 paragraph 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?

- (a) HoTARAC agrees with the proposed amendment to paragraph 73.,

HoTARAC supports using the same word in both paragraphs 73 and 69(d), as that would likely increase consistency when classifying liabilities under IAS 1.

The rights and conditions surrounding the liability to be classified are to be assessed by both preparers and auditors. If there is a currently exercisable right (without impediment) for the reporting entity to defer settlement, the classification is clearly non-current.

- (b) HoTARAC supports the proposed amendments to paragraphs 69(d) and 73, subject to the following comments.

HoTARAC agrees with the argument in paragraph BC2 that rights to defer settlement are often subject to specific conditions being met. It is questionable whether it is appropriate for an entity to take into account rights to defer settlement that exist at the end of the reporting period, before the entity has actually met the associated conditions.

HoTARAC notes that paragraph BC4 of the amending standard makes it clear that when a right is subject to a condition, it is whether the entity complies with that condition at the end of the reporting period that determines whether the right should affect the classification. However, HoTARAC is of the view that this intent is not clear in the proposed amendments to the existing standard. To avoid confusion and misinterpretation, HoTARAC recommends that the IASB clarify this in the final classification criteria and include further application guidance to reinforce this point.

(c) HoTARAC agrees with the proposed amendment to paragraph 69(d), subject to the following comments.

As discussed above, given the exercise of rights to defer settlement is usually based on the fulfilment of specific conditions, it seems appropriate to replace the term ‘an unconditional right’ with ‘a right’.

HoTARAC notes that the term ‘right’ is used differently in other IFRSs/IASs, for example IAS 18 *Revenue* uses ‘enforceable rights’ and ‘unconditional rights’.

Therefore HoTARAC would prefer consistency between these amendments and the usage of the word ‘right’ in other standards (e.g. perhaps ‘enforceable right’ better conveys the intent of these amendments, consistent with paragraph BC4).

**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?

HoTARAC generally agrees with the proposal subject to further clarification from the IASB. HoTARAC suggests the IASB clarify the scope of the proposed new paragraph for ‘settlement of a liability’ in paragraph 69, as to whether it encompasses circumstances where certain liabilities can be extinguished without the transfer of cash, equity instruments, other assets or services to the counterparty within twelve months after balance date.

In the public sector, certain arrangements allow for loans or part thereof to be forgiven. For example, a government department lends money to another public sector entity. Under the loan agreement, 100 per cent of the loan is repayable by a certain timeframe, but 30 per cent of the total amount may be waived by the government department if the borrowing entity meets certain terms and conditions. There is no assurance that the borrowing entity would meet those specific terms and conditions. Conceptually, the full amount of the loan should be initially recognised by the borrowing entity as a liability (i.e. at the inception of the agreement, the borrowing entity has a present obligation to repay the full amount of the loan). The 30 per cent of the loan would only be extinguished in subsequent periods upon the fulfilment of those terms and conditions.

Such an extinguishment (of the 30 per cent) does not involve the transfer of cash, equity instruments, other assets or services from the borrowing entity to the government department, and the borrowing entity is likely to be in control of whether and when it will fulfil those waiver terms and conditions. In such circumstances, it is unclear whether that constitutes a ‘right to defer settlement’. HoTARAC therefore seeks clarification whether liabilities extinguished through mechanisms other than those specified in paragraph 69 would also represent a ‘right to defer settlement’.

**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?

HoTARAC accepts the IASB's justification that, in principle, retrospective application is more appropriate. However, HoTARAC recommends that - prior to finalising these amendments - the IASB undertake outreach work to assess the extent and nature of practical issues with identifying 'rights' in existence at a point of time in the past.

**AASB Specific Matters for Comment**

**1. whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, particularly any issues relating to:**

**(a) not-for-profit entities; and**

**(b) public sector entities, including GAAP/GFS implications;**

HoTARAC is not aware of any regulatory implications for public sector entities. HoTARAC cannot comment on implications for other not-for-profit entities. HoTARAC does not believe there will be GAAP/GFS implications.

**2. whether, overall, the proposals would result in financial statements that would be useful to users;**

HoTARAC believes the clarification (for preparers to classify liabilities as either current or non-current based on rights in existence at the end of the reporting period) would result in financial statements that are more useful to users.

**3. whether the proposals are in the best interests of the Australian economy; and**

An appropriate classification of liabilities is critical to the assessments of a reporting entity's financial characteristics (e.g. solvency, going concern assumptions and ability to manage debt). This may assist in reducing misleading presentation of liabilities that ultimately may lead to "surprise" entity collapses.

**4. unless already provided in response to specific matters for comment 1 – 3 above, the costs and benefits of the proposals relative to the current requirements, whether quantitative (financial or non-financial) or qualitative.** In relation to quantitative financial costs, the AASB is particularly seeking to know the nature(s) and estimated amount(s) of any expected incremental costs, or cost savings, of the proposals relative to the existing requirements.

HoTARAC is unable to identify any additional quantitative or qualitative costs and benefits of the proposed amendments.