Re: Exposure Draft ED 2015/1 Classification of Liabilities (Proposed amendments to IAS 1)

Dear Sir or Madam,

Mazars welcomes the opportunity to comment on the International Accounting Standards Board’s Exposure Draft Classification of Liabilities.

Mazars supports the objective of the IASB to improve the consistency of IAS 1 and its understandability.

We fully agree with the proposed amendments to clarify that only rights in place at the reporting date should affect this classification of a liability.

We support the Board decision not to take into account the management intention when analyzing the current/non-current classification to improve the overall coherence of this standard. However we would like to emphasize that deleting the word “expects” in paragraph 73 is a real change and not just a clarification in our view. We are also concerned that it may result in apparent inconsistency with IAS 39 which brings management intent into the calculation of the amortized cost of a financial liability.

We concur with the Board’s view that the classification of a liability as current or non-current should be based on the analysis of the outflow of resources from the entity. But we do not think that a clarification is needed on this point.
Furthermore, we suggest defining more precisely in which cases the transfer of equity instruments to settle a liability should impact the classification as either current or non-current liabilities (please refer to our answer to question 2).

Our answers to the questions raised in the Exposure Draft are shown in the appendix to this letter which summarises our concerns and opinion.

Please do not hesitate to contact us should you want to discuss any aspect of our comment letter.

Yours sincerely,

Michel Barbet-Massin
*Head of Financial Reporting Technical Support*
Appendix: Detailed answers to questions raised in the Exposure Draft 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’.

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

(a) We believe that the board proposal to replace «discretion» with «right» in paragraph 73 will improve the coherence and the readability of the text.

However we would like to emphasize that deleting the word “expects” in paragraph 73 is a real change and not just a clarification.

For instance, if a company has the right to roll over a 3-month debt but has no intention to do so (for example, if it was drawn on a 5-year revolving credit facility), we understand that this 3-month debt should be classified:

- As current according to the current version of paragraph 73
- As non-current according to the amended version of paragraphs 69 and 72R

We believe that deleting the notion of intention will better reflect the contractual maturity dates of the company and therefore its liquidity risk. However, it might increase inconsistency with IAS 39 which brings management intent into the amortized cost of a financial liability. Paragraph 9 of IAS 39 requires an entity to compute effective interest rate by estimating future cash flows through the expected life of the financial instrument, taking into account, for example, prepayment option. This divergence between IAS 39 and IAS 1 could lead to an accelerated amortization of borrowing costs according to IAS 39 AG 8 on a debt that remains recorded as a non-current liability according to IAS 1 § 69 if, for instance, an entity intends to prepay within a year a debt with a remaining contractual maturity of at least twelve months.
(b) We agree with the changes introduced to paragraphs 69(d) and 73 to make it explicit that only rights in place at the reporting date should affect this classification of a liability.

(c) Lastly, we agree with the Board’s proposal to delete “unconditional” from paragraph 69 (d) since liabilities are often subject to covenants and therefore, the right to defer their settlement is not unconditional.

**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 agree with the Board view that the classification of a liability as current or non-current should be based on the analysis of the outflow of resources from the entity.

However, since IAS 39 already provides a definition of an extinguishment of a liability, we do not believe that a new definition of a “settlement of a liability” is necessary to add clarity to the requirements of this standard.

Furthermore, the wording should be improved to avoid misleading interpretation or inconsistency.

In particular, we suggest defining more specifically the notion of equity instruments (own equity instruments or those of another company, new or existing shares...) in the sentence “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” to avoid inconsistency with the last sentence of paragraph 69 d) 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.

Based on our understanding, this amendment clarifies that the current or non-current classification should first provide information about the timing of outflow of resources from the entity. We concur with the idea that issuing new equity instruments does not directly impact the company liquidity position.

However, delivering own existing shares may lead to an outflow of resources if the entity does not hold enough of its own shares and therefore need to first buy them back to deliver them.

Therefore, we believe that the board could also clarify whether the derogation provided by the last sentence of paragraph 69 d) also covers instruments settled by the delivery of existing shares.
We also note that the Board decided not to include an explicit requirement that rolled-over lending must be with the same lender (BC11). We agree with this choice.

**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.

Yes, we agree with the retrospective application for comparability and consistency in financial statements.