Grupo Latinoamericano
de Emisores de Normas
de Información Financiera

Group of Latin American
Accounting Standard Setters

March 21, 2022

International Accounting Standards Board
Columbus Building
7 Westferry Circus
Canary Wharf
London E14 4HD
United Kingdom

RE: Exposure Draft ED/2021/9, Non-current Liabilities with Covenants: Proposed amendments to IAS 1.

Dear IASB Board Members,

The "Group of Latin American Accounting Standard Setters" – GLASS[1] welcomes the opportunity to comment on the Exposure Draft ED/2021/9, Non-current Liabilities with Covenants: Proposed amendments to IAS 1 (the "ED"). This response summarizes the points of view of the members of the different countries of GLASS, which has been prepared in accordance with the following due process.

Due process

The discussions regarding the ED were held within a specified Technical Working Group ("TWG") created in December 2021. All country-members had the opportunity to appoint at least one member to participate in this TWG. Each standard setter represented in the TWG has undertaken different tasks in their respective countries (e.g., surveys, internal working groups). All results were summarized, and this summary was the platform for the TWG discussion process.

The TWG discussed the different points of view included in the summary during conference calls. In those calls the TWG developed a final document based on the agreed-upon responses and the technical points of view of its members. Finally, the TWG document was submitted to and approved by the GLASS Board.

[1]The overall objective of the Group of Latin American Accounting Standard Setters (GLASS) is to present technical contributions with respect to all Exposure Drafts, Requests for Information and Discussion Papers issued by the IASB, and to generate proposals originated from the regional initiatives. Therefore, GLASS aims to have a unified regional opinion before the IASB. GLASS is constituted by: Argentina (Chairman), Bolivia, Brazil (Vice Chairman), Chile (Board), Colombia (Board), Costa Rica (Board), Dominican Republic, Ecuador, Guatemala, Honduras, Mexico (Board), Panama, Paraguay, Peru (Board), Uruguay (Board) and Venezuela (Board).

GLENIF GLASS

Grupo Latinoamericano
de Emisores de Normas
de Información Financiera

Group of Latin American
Accounting Standard Setters

Overall Comments

While GLASS agrees with the clarifications made in the ED to assert that the conditions with which an entity must comply within twelve months after the reporting period have no effect on whether an entity has, at the end of the reporting period, a right to defer settlement of a liability for at least twelve months after the reporting period, in general, we do not believe that the suggested separate presentation in the statement of financial position of the non-current liabilities for which covenants are required within 12 months is appropriate, especially given the existing guidelines and definitions of IAS 1, *Presentation of Financial Statements*.

Certain jurisdictions within GLASS have also pointed out a potential overlap between the additional disclosures required under the proposal and the existing risk disclosures (especially those relating to liquidity risk) that are already in essence part of IFRS 7, *Financial Instruments: Disclosures*.

Detailed information and observations from GLASS on the overall comments referred to above are included further below in the specific responses.

Specific Comments

Attached please find our specific responses to the questions presented in the ED.

Contact

If you have any questions about our comments, please contact glenif@glenif.org .

Sincerely yours

Jorge José Gil
President
Group of Latin American Accounting Standard Setters (GLASS)

Group of Latin American Accounting Standard Setters (GLASS)

GLASS Comment letter on the Exposure Draft ED/2021/9,
Non-current Liabilities with Covenants: Proposed amendments to IAS 1

Question 1 - Classification and disclosure (paragraphs 72B and 76ZA (b))

The Board proposes to require that, for the purposes of applying paragraph 69(d) of IAS 1, specified conditions with which an entity must comply within twelve months after the reporting period have no effect on whether an entity has, at the end of the reporting period, a right to defer settlement of a liability for at least twelve months after the reporting period. Such conditions would therefore have no effect on the classification of a liability as current or non-current. Instead, when an entity classifies a liability subject to such 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, including: *(a) the conditions (including, for example, their nature and the date on which the entity must comply with them);* *(b) whether the entity would have complied with the conditions based on its circumstances at the end of the reporting period; and* *(c) whether and how the entity expects to comply with the conditions after the end of the reporting period.* *Paragraphs BC15–BC17 and BC23–BC26 of the Basis for Conclusions explain the Board's rationale for this proposal.* *Do you agree with this proposal? Why or why not? If you disagree with the proposal, please explain what you suggest instead and why.*

Responses:

GLASS agrees with the clarifications made in the ED, including the assertion made that the conditions with which an entity must comply within twelve months after the reporting period <u>have no effect</u> on whether an entity has, at the end of the reporting period, a right to defer settlement of a liability for at least twelve months after the reporting period, which in our view are appropriate.

Supporting the abovementioned conclusion certain jurisdictions within GLASS noted that (i) this conclusion seems more consistent with the overall classification principle that liabilities are classified as current or non-current on the basis of the rights and obligations that exist at the end of the reporting period and is also consistent with the principles set forth by IAS 10, *Events after the Reporting Period*; and (ii) this direction suggested by the Board can also prevent the entity from improperly classifying a liability as non-current in situations where there is evidence or indicative that fulfilment of the conditions agreed within the following twelve months on the specified contractual date is expected to be achieved.

As it relates to the suggested additional disclosures, GLASS believes that while such disclosures provide relevant information for the users of the financial statements, those are in essence part of the general requirements of IFRS 7 (i.e., paragraphs 31 and 32 and the discussion on liquidity risk on paragraph B10A). As such, the more specific and granular requirements provided by the ED including (i) the conditions; (ii) whether the entity would have complied with those conditions based on its circumstances at the end of the reporting period; and (iii) whether and how the entity expects to comply with the conditions after the end of the reporting period would, in GLASS's view, be better presented as amendments to IFRS 7 rather than IAS 1.

We also refer to the example provided on the IFRS Practice Statement 2 - Making Materiality Judgments (paragraphs 81 through 83), which in our view is complementary to the IFRS 7 discussion, especially regarding the nature of the disclosures for covenants.

Question 2 - Presentation (paragraph 76ZA(a))

The Board proposes 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.

Paragraphs BC21–BC22 of the Basis for Conclusions explain the Board's rationale for this proposal.

Do you agree with this proposal? Why or why not? If you disagree with the proposal, do you agree with either alternative considered by the Board (see paragraph BC22)? Please explain what you suggest instead and why.

Responses:

In GLASS's opinion the separate presentation in the statement of financial position does not seem necessary and that addressing the additional circumstances and/or risks relating to such non-current liabilities subject to covenants within 12 months from the reporting date on extended disclosures in the footnotes to the financial statements would be more appropriate. As such, GLASS does not agree with the proposal 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.

In our view, separate presentation for such liabilities would create an inconsistency with other financial instruments, such as financial assets and other financial liabilities classified as current or non-current. GLASS also notes that there are existing guidance and requirements set forth by IAS 1 which are sufficient for assessing aggregation or disaggregation of items in the statement of financial position on the basis of their relevance and similarities (or lack thereof), especially as it relates to paragraphs 7, 29 through 31 and 57 through 59.

We also point out the IFRIC discussion on the matter of whether supply chain financing arrangements merit separate presentation (IFRIC tentative agenda decision on Supply Chain Financing Arrangements - Reverse Factoring), in which it was concluded that in assessing whether to present such liabilities separately (including whether to disaggregate trade and other payables), an entity considers the amounts, nature and timing of those liabilities as well as whether the terms of liabilities that are part of the arrangement are substantially different from the terms of the entity's trade payables that are not part of the arrangement.

Such decision conveys a view in a similar discussion that separate presentation would assume terms and conditions that are "substantially different" from the line item that includes the remaining transactions presented. As the term "substantially different" is not defined under IFRS, we consider similar guidance in accounting literature that provides a basis for our conclusion. Consistent with the IASB staff (views provided on the October 2019 staff meeting for the IBOR Reform and its Effects on Financial Reporting project, where a topic "how to determine whether a modification is substantial" had been included in the agenda), determining whether the terms of a financial liability are substantially different from a qualitative perspective depends on the specific facts and circumstances that apply to each case and may vary from jurisdiction, product types and agreements, among others. Also, according to the IASB staff, a modification deemed substantial would be one that results in "a significant value transfer and/or a new underwriting/pricing assessment of the financial instrument, including the following examples: (a) modifications to the currency in which the financial instrument is denominated; (b) a significant extension of the maturity date; (c) modifications to a floating-rate financial instrument so that if becomes a fixed-rate financial instrument; and (d) modifications to contractual cash flows that would cause a financial asset that previously passed the solely payments of principle and interest (SPPI) assessment to fail that assessment because of the modifications".

The abovementioned examples of "substantially different" terms and conditions of financial liabilities are more significant than those that are under discussion in this ED. It could also raise the question on whether other terms and conditions that typically apply to such financing liabilities could be deemed equally or more significant to users of financial statements to the point of also deeming separate presentation (bearing in mind that the entities may have different profile of primary users with different concerns that may value one aspect or another relating to debt, such as different interest rates, currency in which the financial liability is denominated, guarantees, among others) and, in light of the guidance provided by the ED, would be obscured by the emphasis included in the presentation in the statement of financial position to other terms and conditions empirically determined to be separate by the standard (the non-current liabilities subject to covenants required for within 12 months after the reporting period).

As such, it was pointed out that to prescribe separate presentation would be to establish a rule and not a principle in IFRS, which goes against the philosophy of basing IFRS standards on principles. The proposed amendments should state that, if the loan is significant and there is a possibility of defaulting in the future, the guidance in IAS 1 should be followed to determine whether the loan has substantially different terms and conditions that warrant separate presentation in the statement of financial position. In other words, the modifications should refer to the principles in IAS 1 and not establish a rule.

Question 3 - Other aspects of the proposals

The Board proposes to:

(a) 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 for the purposes of applying paragraph 69(d) of IAS 1 (paragraph 72C);

(b) require an entity to apply the amendments retrospectively in accordance with IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors, with earlier application permitted (paragraph 139V); and

(c) defer the effective date of the amendments to IAS 1, Classification of Liabilities as Current or Non-current, to annual reporting periods beginning on or after a date to be decided after exposure, but no earlier than 1 January 2024 (paragraph 139U).

Paragraphs BC18–BC20 and BC30–BC32 of the Basis for Conclusions explain the Board's rationale for these proposals.

Do you agree with these proposals? Why or why not? If you disagree with any of the proposals, please explain what you suggest instead and why.

Responses:

While we draw attention to the responses provided in the previous questions, we agree with the proposed clarification specified in 3(a) above. We also agree with the proposal in 3(b) above since this allows a more consistent and uniform presentation in the periods reported. However, in our opinion there may be circumstances associated with such liabilities in prior years that may lead the entities to the conclusion that retroactive application may be impracticable (such as those discussed on paragraph 5 of IAS 8). Finally, we agree with the proposal in 3(c) above as this would allow preparers more time to ensure all necessary adjustments in processes and controls are properly made.

Other matters: Application of paragraphs 74 through 76 of IAS 1:

While we are aware that this is a narrow scope project and the abovementioned paragraphs are not part of the consultation, we would like to use the opportunity to refer to a disagreement that certain jurisdictions within GLASS have with the guidelines for the presentation of a liability as current when the entity breaches a covenant, but the lender has agreed after the reporting period and before the authorisation of the financial statements for issue, not to demand payment as a consequence of the breach. This is defined in paragraphs 74 through 76 of IAS 1.

In GLASS's view, as the project discusses aspects relating to financial liabilities subject to covenants, this would be a good opportunity to initiate a project to redeliberate whether the application of the aforementioned paragraphs as currently stated in the standard provides a true and fair presentation of the economic substance to the transactions reported, especially since given the jurisdictions observation that in practice, the reclassification of a liability to current in circumstances when a waiver has been obtained after the reporting date but prior to the issuance of the financial statements creates a gap between the information that is reported and the information that is used by Management in its activities and decision-making process.