Project: **New items for initial consideration**

Topic: **IAS 1 *Presentation of Financial Statements* – current/non-current classification of debt**

Purpose of this paper

1. The purpose of this paper is to document the staff analysis and recommendations relating to a request received by the IFRS Interpretations Committee to clarify the meaning of 'unconditional right to defer settlement' in paragraph 69(d) of IAS 1 *Presentation of Financial Statements*.

2. This paper:

   (a) Provides background information on the issue;

   (b) Analyses the issue within the context of IFRSs;

   (c) Makes a staff recommendation on the tentative agenda decision; and

   (d) Asks the Interpretations Committee whether they agree with the staff recommendation.

Background information

3. The submission (to be found in Appendix B) requests clarification of one of the criteria for classification of liabilities in paragraph 69 of IAS 1, as read with paragraph 73. Specifically, the submission is asking for guidance on what an 'unconditional right to defer settlement' means. The submission expands this

This paper has been prepared by the technical staff of the IFRS Foundation for discussion at a public meeting of the IFRS Interpretations Committee.

The views expressed in this paper are those of the staff preparing the paper. They do not purport to represent the views of any individual members of the IFRS Interpretations Committee or the IASB. Comments made in relation to the application of an IFRS do not purport to be acceptable or unacceptable application of that IFRS—only the IFRS Interpretations Committee or the IASB can make such a determination.

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request, stating that interpreting 'unconditional right to defer settlement' involves the clarification of:

(a) the meaning of the words 'refinance' and 'roll over'. The submission introduces a related fact pattern involving the classification of commercial paper as current or non-current, which the staff analyse, and

(b) whether the assessment of a right as unconditional requires consideration of all possible future circumstances, or only those that exist at the reporting date.

4. Issue (a) is dealt with in this paper. Issue (b) is dealt with in Agenda paper 11A, a supplementary paper to this one..

Analysis of the issue

5. Paragraph 69 of IAS 1 states the following:

> 69 An entity shall classify a liability as current when:
> (a) it expects to settle the liability in its normal operating cycle;
> (b) it holds the liability primarily for the purpose of trading;
> (c) the liability is due to be settled within twelve months after the reporting period; or
> (d) it does not have an unconditional right 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.
>
> An entity shall classify all other liabilities as non-current.

6. Paragraph 73 states the following:

> 73 If an entity expects, and has the discretion, 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), the entity does not consider the potential to refinance the obligation and classifies the obligation as current.

'Roll-over' vs. 'refinance'

The issue

7. Consider the following fact pattern:

> **Scenario 1**
>
> Company A took out a loan with a 5 year term with SuperBank in June 2006. The loan is due to be settled via a balloon payment in June 2011. Company A's financial year end is 31 December.
>
> During December 2010, Company A and SuperBank agree a new facility that expires in 5 years, into which Company A is able to roll the outstanding balance of its existing loan. Company A intends to roll over the existing loan into the new facility when the loan matures in June 2011, and intends not to settle the new facility until it is due in June 2016.

8. The staff thinks that, according to paragraph 73, the Company A would classify the loan as non-current in its balance sheet at 31 December 2010, because Company A has the ability and intent to roll the obligation over into the new facility. The substance is that the debt does not require settlement until the new facility expires in 5 years' time.

9. However, if the fact pattern in scenario 1 is altered such that the new facility is negotiated with a different bank (call that **scenario 2**), would the classification of debt at 31 December 2010 be different? It is unclear whether paragraph 73 deliberately intended 'roll over' to mean the obligation is renegotiated with the *same* party, and 'refinance' to mean the obligation is negotiated with a *different* party.

10. Some think that although Company A had the ability and intention to refinance the loan at balance sheet date, the loan with SuperBank would still have to be settled in June 2011, albeit with funds provided from the facility with the new lender. The new loan is not an extension of the existing loan, so the existing loan should be classified as current at 31 December 2010.

11. However, others think that whether the loan is refinanced with the same bank or a different bank, paragraph 73 still applies. Some argue that paragraph 73 uses the two terms 'roll over' and 'refinance' because they mean different things: roll over being an extension of the loan with the existing lender and refinance being the transfer of the loan to a new lender with new terms.

Definitions

12. The Collins English Dictionary defines ‘roll over’ as ‘to allow (a loan, prize, etc) to continue in force for a further period’.

13. The Random House Dictionary defines ‘refinance’ as: ‘to satisfy (a debt) by making another loan on new terms; to increase or change the financing of.’ Merriam-Webster’s Dictionary of Law defines the term as ‘to revise the terms of (a debt obligation) esp. in regard to interest rate or payment schedule’.

Staff view

14. The staff thinks that there is a difference between the two terms. The staff think that **roll over** is generally understood to mean renegotiating with the *same party* and on *similar terms* (for example, the roll over of a lease). The staff think that **refinance** could mean either or both of the following circumstances:

    (a) replace the existing finance arrangement with a new one, with *the same lender*, but with different terms, and/or

    (b) replace the existing finance arrangement with a new one, with a *new lender*, with similar or different terms. For example, where long-term finance nearing maturity is refinanced by a different lender that provides a new long-term loan: the staff thinks this is a refinance and qualifies for non-current classification.

Question 1 for the Committee
1(a) Does the Committee think there is a difference between the terms ‘roll over’ and ‘refinance’? 1(b) Does the Committee agree with the staff’s distinction between roll-over and refinance? 1(c) Considering a case such as Scenario 2 above, does the Committee think that the loan qualifies as non-current if the entity agrees a new finance arrangement with a different lender?

The commercial paper issue

The issue

15. The submission states that 'a specific example of a situation in which the refinancing would not be from the same lender as the initial debt is commercial paper'. Commercial paper is a short-term debt instrument that is sold publicly and held widely, and which matures in 90 or 180 days. It may be secured by specific assets, but if not (and this usually only applies to highly rated entities), the commercial paper is typically issued under a programme managed by a sponsoring bank, which acts as an agent for the entity. The bank usually provides the entity with an specific line of credit, which the bank will draw upon if the commercial paper issue is under-subscribed. Note that, despite the involvement of the bank, the obligation to the holders of the commercial paper remains with the entity.

16. Consider the following fact pattern:

Scenario 3

Company B is an AA rated entity and it undertakes to issue commercial paper into the market. The issue is managed by BigBank. BigBank issues the first tranche of 180 day commercial paper into the market on behalf of Company B, and remits the funds received to Company B. After 180 days, BigBank settles the commercial paper with the holders, and issues a second tranche. This process will continue according to the agreement between Company B and BigBank – assume for longer than 12 months. The bank receives a service fee for managing the issue.

In the event that the market does not buy up all the commercial paper, the bank draws on a line of credit backing the issue (available for the extent of the agreement, that is, longer than one year).

Company B reflects a commercial paper liability in its accounts, and discloses the line of credit backing up the issue.

17. The first question that arises is whether the commercial paper liability is classified as current or non-current. Consider the case where an entity issues (typically asset-backed) commercial paper into the market without involvement from a bank. The commercial paper is issued to the public. Since it matures within 12 months, the liability would be classified as current according to IAS 1.

18. In scenario 3, the commercial paper is also issued to the public. However, in the event the commercial paper does not sell, Company B can draw on a facility from *another lender* – BigBank. Drawing on the facility is effectively to ensure

that the commercial paper keeps rolling, so Company B does not need to repay the notes from its own cash resources.

19. Company B can be said to be ‘rolling over’ or ‘refinancing’ the commercial paper in this case, according to paragraph 73, with a long-term loan facility.

Support for current classification

20. Some think that the commercial paper in scenario 3 should be classified as current. Further, the commercial paper is being redeemed at the end of each 180 day cycle by Company B – although the mechanics of this are managed by BigBank. Following the redemption, the paper is reissued, to the same or new lenders. This leads to continual redemption and reissue, but for which there is little or no liquidity risk for Company B, because BigBank provides the back-up finance. The fact that the commercial paper is redeemed is an indicator of a current classification, even though it may be immediately reissued.

21. The commercial paper instrument is and always was a short term instrument. Circumstances in practice may vary but in the submission we received, the back-up finance provided by the bank is not an upfront loan. It is a credit facility that is available to be drawn upon as the entity requires (and it is available for longer than a year). The staff understand that it would be paid off as and when the proceeds come in from successful issue of the commercial paper. The staff think it is reasonable to conclude therefore that sometimes the credit facility may not be made use of at all - or it may have a negligible balance. Therefore, if at a point in time the credit facility had a zero balance (and therefore was not being used to ‘refinance’ the commercial paper at that time), the staff think it may be misleading to classify the commercial paper as non-current, purely because it the entity *has the option* of drawing down on the long term facility.

Support for non-current classification

22. Others think that the commercial paper in scenario 3 should be classified as non-current, because it is backed up by a long-term facility from BigBank. The effect of this facility is that, in substance, the short-term commercial paper obligation is transformed into long-term finance. They do not dispute that BigBank is a different lender from the public, but they say that paragraph 73 is not clear that

the 'roll over' or 'refinance' has to be with the same party. They interpret 'roll over' to mean 'with the same party' and 'refinance' to mean 'with a different party'. Therefore, reading paragraph 73 this way, the commercial paper, backed by the long-term facility, can be viewed as 'refinanced' and therefore classified as non-current.

Staff view

23. The staff think that the existence of a long-term facility to back up short-term commercial paper is not equivalent to a refinance or a roll over of debt. The primary debt instrument remains a short-term obligation, which has always been short-term. Further, the long-term back-up facility is an option. Exercise of the option will be triggered in the event the short-term instrument (the commercial paper) is not re-sold. Whether the commercial paper is re-sold depends on the actions of others. Given this, the back-up facility does not appear to meet the criterion that the entity 'expects and has the discretion' to refinance the loan, as anticipated in paragraph 73. Consequently, the staff think that the commercial paper should be classified as current.

Question 2 for the Committee
Does the Committee agree with the staff view in paragraph 23, above?

Staff recommendation

24. The staff do not think that paragraph 73 of IAS 1 is clear as to whether 'roll over' and 'refinance' should be with the same party, or whether it can be with a different party. The application of paragraph 73 to various practical scenarios – of which commercial paper is one – means that there could be inconsistency in practice depending on how constituents interpret the paragraph.

25. The staff think that the guidance in paragraph 73 should be made clearer in terms of the meaning of 'roll over' and 'refinance'. The staff also think that the wording can be amended to provide a principle that can be applied to scenarios such as the submission describes. The staff think this is best achieved through an amendment rather than through developing an Interpretation.

26. Therefore, the staff recommends that paragraph 73 be reworded as follows:

73 If an entity expects, and has the discretion, to refinance or roll over an obligation for at least twelve months after the reporting period, whether the roll over or refinance is with the same lender or a new lender, and with similar or different terms, 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, or the refinancing is dependent on circumstances outside of the entity's control), the entity does not consider the potential to refinance the obligation and classifies the obligation as current.

Question 3 for the Committee
3(a) Does the Committee think that paragraph 73 should be clarified? 3(b) If so, does the Committee agree with the staff's suggested amended wording for paragraph 73? If not, what wording would the Committee suggest?

Agenda criteria assessment for the Committee

27. The submission is asking for guidance on what an 'unconditional right to defer settlement' means, involving the clarification of (1) the meaning of the words 'refinance' and 'roll over' (discussed in this paper), and (2) whether the assessment of a right as unconditional requires consideration of all possible future circumstances, or only those that exist at the reporting date (discussed in paper 11A).

28. The staff's assessment of the agenda criteria is as follows:

    (a) *The issue is widespread and has practical relevance.*

    The submission states that this issue is prevalent among 'Canadian companies that have issued commercial paper or have other short-term financing supported by longer-term credit facilities.' The submission states, and the staff are not aware, based on some limited outreach done, of the issue being widespread among UK IFRS users. However, the staff understand that entities applying US GAAP may have a similar issue with short-term financing that is backed up by long term credit facilities.

(b) *The issue indicates that there are significantly divergent interpretations (either emerging or already existing in practice). The Committee will not add an item to its agenda if IFRSs are clear, with the result that divergent interpretations are not expected in practice.*

Yes, there is reportedly divergence in practice in Canada and it seems that the guidance in IAS 1 is not clear on this issue.

(c) *Financial reporting would be improved through elimination of the diverse reporting methods.*

Yes. If IAS 1 is not clear, there could be diversity in the classification of current and non-current liabilities.

(d) *The issue can be resolved efficiently within the confines of existing IFRSs and the Framework, and the demands of the interpretation process.*

No. If the Committee believe current IFRSs should be clarified, the staff thinks the most efficient way of resolving the issue would be to incorporate the extra guidance required in the standard itself.

(e) *It is probable that the Committee will be able to reach a consensus on the issue on a timely basis.*

Yes. The staff think that the Committee could reach consensus on this issue. However, the staff are aware that the issue of classification of liabilities as current or non-current is currently being discussed by the *Financial Statement Presentation* team (see below), so any consensus that the Committee may reach would have to be considered in light of any Board discussions that are to be held.

(f) *If the issue relates to a current or planned IASB project, there is a pressing need to provide guidance sooner than would be expected from the IASB's activities. The Committee will not add an item to its agenda if an IASB project is expected to resolve the issue in a shorter period than the Committee requires to complete its due process.*

Yes, this issue relates to the *Financial Statement Presentation (FSP)* project. The staff have discussed the issue with the FSP project team, and understand that they are currently considering the principles around the clarification of the current/non-current classification in IAS 1.

29. In the light of the above, on the issue of the meaning of the words 'refinance' and 'roll over', **the staff recommends** that the Committee does not take this issue onto the agenda, and that the Committee recommends that the Board consider clarifying the meaning of the concepts in paragraph 73 of IAS 1, per the staff's suggested wording in paragraph 26 of this paper. The Committee should recommend that the Board do this as part of the ongoing *Financial Statement Presentation* project.

30. In Agenda paper 11A (paragraph 10), **the staff recommends** that the Committee take no action in respect of whether an entity is required to assess the financial health of a finance provider beyond the provisions in IAS 1 paragraph 26 and IAS 10 paragraph 3.

31. The staff proposes wording for both of the above issues in the draft tentative agenda decision in Appendix A.

Question 4 for the Committee
4(a) Does the Committee agree with the staff's recommendation that the Interpretations Committee not add this issue to its agenda, but that it be referred to the Board? 4(b) Does the Committee have any comments on the proposed wording for the tentative agenda decision in Appendix A?

Appendix A – Proposed wording for tentative agenda decision

A1 The staff proposes the following wording for the tentative agenda decision:

IAS 1 *Presentation of Financial Statements* – current/non-current classification of debt

The Interpretations Committee received a request for guidance on the meaning of 'unconditional right to defer settlement' in paragraph 69(d) of IAS 1.To this end, the submission requested clarification of the meaning of the words 'refinance' and 'roll over', as stated in paragraph 73 of IAS 1. The Committee also considered a practical application of the issue, involving the classification of a short-term obligation (commercial paper) when it is backed by a long-term loan facility.

The Committee observed that the meanings of 'refinance' and 'roll over' are not clear. The Committee suggested that the wording of paragraph 73 be amended to state that, when the roll over or refinance of an obligation is at the discretion of the entity, this could be with the same lender or a new lender, and with similar or different terms.

Further, the Committee observed that IAS 1 and IAS 10 *Events after the Reporting Period* provide sufficient guidance on the extent to which an entity should look to the future when preparing financial statements.[1]

It also suggested amending the wording of paragraph 73 to provide a principle that can be applied to scenarios such as the submission describes.

The Committee noted that this request for guidance would be best addressed as part of the Board's *Financial Statement Presentation* project and therefore the Committee [decided] not to add this issue to its agenda..

[1] This wording relates to the supplementary issue discussed in Agenda paper 11A.

Appendix B – Request for the Interpretations Committee agenda

A1. The staff received the following Interpretations Committee request. All information has been copied without modification, except for details that would identify the submitter of the request and details that are subject to confidentiality.

Submission to the IFRS Interpretations Committee

IAS 1: Clarification of "unconditional right to defer settlement".

Issue – What does an "unconditional right to defer settlement" in IAS 1 *Presentation of Financial Statements* mean?

A2. IAS 1 provides guidance on the classification of liabilities within the statement of financial position. Paragraph 69 has four criteria, any one of which would require a liability to be classified as current including "when the entity does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting period." Paragraph 73 states that if the entity expects, and has the discretion, to refinance or roll over an obligation for at least twelve months after the reporting period under an existing loan facility, it can classify the obligation as non-current. Sometimes the loan facility that would refinance the existing debt is not with the current lender.

A3. A specific example of a situation in which the refinancing would not be from the same lender as the initial debt is commercial paper. Commercial paper that is not secured by specific assets is usually issued only by the most highly rated corporate entities. Commercial paper is sold publicly; it is widely held and typically matures in 90 or 180 days. It is usually issued under a program managed by a sponsoring bank that generally also provides a line of credit, often referred to as a backstop or liquidity facility. This facility allows the entity to draw on a bank line of credit if it is unable to sell sufficient commercial paper into the market to replace maturing commercial paper. The line of credit may be restricted so that it can be drawn on only when the entity is unable to sell commercial paper into the market, but not always. A backstop line of credit is often subject to clauses that require the issuer of the commercial paper to have had no material adverse changes in its financial condition. Each agreement is different, with different restrictions and different time lines. However, entities have an incentive to obtain 100% liquidity support in order to receive positive ratings on the commercial paper from rating agencies. For purposes of our discussion, we assume the liquidity agreement is a line of credit that can be drawn on only when the entity is unable to sell commercial paper into the market and it is available for longer than one year. This arrangement is clearly an "existing loan facility." The issue is whether it can be considered in classifying the commercial paper in accordance with paragraph 73 of IAS 1.

A4. **Current Practice —**

A5. There are three views on the classification of debt such as the commercial paper described. Some believe it should be classified as current, some believe it should be classified as non-current and others think either treatment can be selected as a matter of accounting policy.

A6. ***Support for classification as current***

A7. Those who support current classification for the commercial paper note that it matures every 90 days. They would derecognize the debt in accordance with paragraph 39 of IAS 39 *Financial Instruments: Recognition and Measurement* that requires the removal of a "financial liability (or part of a financial liability) from its statements of financial position when, and only when, it is extinguished ie when the obligation specified in the contract is discharged or cancelled or expires."

A8. In addition, supporters of this view do not believe that the existence of any liquidity agreement would have any bearing on the classification of the commercial paper. They believe that paragraph 73 of IAS 1 requires the entity's expectation or discretion to refinance or roll over the obligation for at least twelve months to be under an existing loan facility with the same lender. Because the commercial paper was issued to the public, but the line of credit is provided by the bank they do not think that the line of credit can be considered.

A9. Although paragraph 75 of the standard is in the context of a breach of covenants, supporters of the first view believe the words "an entity classifies the liability as non-current *if the lender* agreed (emphasis added)" imply that a refinancing under paragraph 73 is meant to be with the same lender.

A10. Proponents of this view also argue that when the entity's ability to refinance is with a party other than the lender, it does not have an *unconditional* right to defer settlement. They note that in all circumstances, the entity would be required to repay the holders of the commercial paper at maturity whether or not it also has a line of credit arrangement. If the party that is providing the line of credit becomes bankrupt, the entity has no ability to defer settlement by refinancing.

A11. Furthermore, proponents of this view argue that the ability to draw on the liquidity facility is typically subject to clauses such that the issuer of the commercial paper can have had no "material adverse changes" in its financial condition. If material adverse changes occur, the lender can refuse to honour the liquidity commitment and this means the right is not unconditional.

A12. Support for classification as non-current

A13. Those who support the classification of the debt as non-current note that "refinance" and "rollover" in paragraph 73 are not defined. They argue that the standard would not include two terms if they were intended to have the same meaning. Consequently, they believe that "roll over" implies an agreement with the original lender; "refinance" implies an agreement with a different party. Therefore, even though the commercial paper debt is maturing every 90 days or so, the entity does have the ability, albeit with a different lender, to refinance on a longer term basis through a line of credit if necessary.

A14. Proponents of this view argue there is no mention in the standard as to whether paragraph 73 in IAS 1 applies only when the ability to refinance is with the same lender and in fact paragraph 69(d) refers the reader to paragraph 73 not paragraph 75.

A15. Proponents of this view also argue that the ability of the entity providing the refinancing to honour the agreement does not affect existence the entity's unconditional right to refinance, although that right could be affected by *its own* circumstances if the agreement includes conditions such a "material adverse change" clause. In such cases, proponents of this view believe that at each reporting date the entity would consider whether changes in circumstances affect either the existence of its right (e.g., whether material adverse changes have occurred) or its ability to exercise that right (e.g., the capacity of the lender has changed. Changes in circumstances would affect the classification of the commercial paper when they occurred.

A16. Proponents of this view believe that changes in circumstances need to be considered even when the refinancing agreement is with the same lender. Such agreements often contain the same conditions as agreements with different lenders. Adopting the logic set out in the first view implies that in assessing its "unconditional right" an entity would have to consider the future solvency of the entity providing the refinancing. This assessment of conditions outside the terms of the contracts could have far reaching implications for other issues.

A17. Support for either classification – select a policy and disclose

A18. As there is no clear guidance on how to interpret paragraphs 69 or 73 of IAS 1, some believe an entity should develop a policy of how to interpret those paragraphs. Supporters of this view think it would be acceptable for an entity to adopt a policy to classify the debt as current or long-term as long as the policy is clearly disclosed.

A19. Others believe this view is not supportable because IAS 1 requires the classification decision to be based on an assessment of existing circumstances and rights and obligations. Consequently, they believe it cannot be an issue that can be determined by an accounting policy choice.

A20. Reasons for IFRIC to Address the Issue

A21. *Is the issue widespread and practical?*
The issue appears to be widespread for Canadian companies that have issued commercial paper or have other short-term financing supported by longer-term credit facilities. We are not aware of the existence or treatment of the issue in other IFRS jurisdictions.

A22. *Does the issue involve significantly divergent interpretations (either emerging or already existing in practice)?*
Yes, it appears that in Canada divergence exists as to the interpretation of paragraphs 69 and 73 of IAS 1.

A23. *Would financial reporting be improved through elimination of the diversity?*

Yes. Consistent classification of liabilities as current or non-current among entities within the same industry and between industries would improve comparability. Working capital and current ratios are important metrics used by financial analysts.

A24. *Is the issue sufficiently narrow in scope to be capable of interpretation within the confines of IFRSs and the Framework for the Preparation and Presentation of Financial Statements, but not so narrow that it is inefficient to apply the interpretations process?*
Yes. Interpreting "unconditional right to defer settlement" involves clarifying:

(a) whether the terms "refinance" and "rollover" in paragraph 73 of IAS 1 both require the arrangement to be with the same lender, and
(b) whether the assessment of a right as unconditional requires consideration of all possible future circumstances or only those that exist at the reporting date.

A25. *If the issue relates to a current or planned IASB project, is there a pressing need for guidance sooner than would be expected from the IASB project? (The IFRIC will not add an item to its agenda if an IASB project is expected to resolve the issue in a shorter period than the IFRIC would require to complete its due process.)*

The IASB has an active project to re-consider principles associated with financial statement presentation. Based on the "staff draft" of the standard, the IASB proposes to rename "current liabilities" as "short-term" obligations.

However, the guidance in paragraph 73 has been carried forward with minimal modification. As the financial statement presentation project has been deferred and is still to be exposed for comment, the Interpretations Committee could resolve this important issue on a more timely basis.

Project **New items for initial consideration**

Topic **IAS 1 *Presentation of Financial Statements* – current/non-current classification of debt – supplementary issue**

Purpose of this paper

1. The purpose of this paper is to present for discussion a supplementary issue relating to a request received by the IFRS Interpretations Committee to clarify the meaning of 'unconditional right to defer settlement' in paragraph 69(d) of IAS 1 *Presentation of Financial Statements*. The analysis of this request was presented in Agenda paper 11 Current/non-current classification of debt, at this meeting.

2. This paper will discuss the issue and will ask the Interpretations Committee for their views.

Discussion and question for the Committee

The issue

3. The submission (to be found in Appendix B of Agenda paper 11) requests clarification of one of the criteria for classification of liabilities in paragraph 69 of IAS 1, as read with paragraph 73. Specifically, the submission is asking for guidance on what an 'unconditional right to defer settlement' means. The

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submission expands this request, stating that interpreting ‘unconditional right to defer settlement’ involves the clarification of:

(a) the meaning of the words ‘refinance’ and ‘roll over’. The submission introduces a related fact pattern involving the classification of commercial paper as current or non-current, which the staff analyse, and

(b) whether the assessment of a right as unconditional requires consideration of all possible future circumstances, or only those that exist at the reporting date.

4. Issue (a) was dealt with in Agenda paper 11. Issue (b) will be dealt with in this paper.

Analysis

5. It is the submitter’s view that an entity will, at balance sheet date, consider (using information publicly available) whether there is any reason to believe that the lender providing the long-term finance would not be able to honour the facility if called upon. Paragraph 72 of IAS 1 requires that an entity classify a liability based on the events *at the reporting date.*

6. However, some may think that the assessment of the financial stability of the lender needs to cover the entire period of the financing, and not only the circumstances existing at balance sheet date.

7. The following extracts from the submission further describe the issue:

‘Proponents of this view [support for classification of the commercial paper as current] also argue that when the entity’s ability to refinance is with a party other than the lender, it does not have an *unconditional* right to defer settlement. They note that in all circumstances, the entity would be required to repay the holders of the commercial paper at maturity whether or not it also has a line of credit arrangement. **If the party that is providing the line of credit becomes**

bankrupt, the entity has no ability to defer settlement by refinancing.' [emphasis added].

And

'Proponents of this view [support for the classification of the commercial paper as non-current] believe that changes in circumstances need to be considered even when the refinancing agreement is with the same lender. Such agreements often contain the same conditions as agreements with different lenders. **Adopting the logic set out in the first view implies that in assessing its "unconditional right" an entity would have to consider the future solvency of the entity providing the refinancing. This assessment of conditions outside the terms of the contracts could have far reaching implications for other issues.**' [emphasis added].

Staff view

8. The staff think that the financial health of the entity providing the re-financing is an important factor when considering whether a liability is current or non-current. Presenting a loan as non-current when there is evidence that the provider of the new loan is not financially stable at reporting date, may be misleading. This is especially relevant in circumstances where the liability is in the form of a long-term line of credit to be drawn upon as and when the borrowing entity requires funding.

9. IAS 10 *Events after the Reporting Period* states that an entity shall consider adjusting for particular events occurring between the end of the reporting period and the date when the financial statements are authorised for issue[1]. IAS 1 paragraph 26 explains that the assessment of the going concern of an entity requires looking forward at least 12 months from the end of the reporting period. The staff thinks that paragraph 69(d) does not require an entity to assess the financial health of the finance provider beyond this requirement.

[1] IAS 10 paragraph 3

10. The staff do not recommend that the Committee take any action in respect of this issue. The staff have included proposed wording in respect of this issue in the draft tentative agenda decision in Appendix A of Agenda paper 11.

Questions for the Committee
1. Does the Committee agree with the staff's view that paragraph 69(d) does not impose any further obligation on an entity to look to the future, than is already required by paragraph 26 of IAS 1 and paragraph 3 of IAS 10? 2. Does the Committee agree with the staff's recommendation that no action is required in respect of this issue?