Association pour la participation des entreprises françaises à l'harmonisation comptable internationale

The IFRS Interpretations Committee,

7 Westferry Circus,

Canary Wharf,

London E14 4HD,

United Kingdom

Dear Ms Lloyd,

Tentative Agenda Decision: Classification of Debt with Covenants as Current or Non-current (IAS 1)

We would like to express our concerns with both the due process and the outcome that will result from the above Tentative Agenda Decision (TAD) relating to the classification of debt with covenants.

Concerning the due process, we note that:

The paragraph IAS 1 72A, on which the IFRS Interpretations Committee (the Committee) has based its conclusion, was added after the publication of the exposure draft published in 2015 and was therefore excluded from the normal due process for exposure draft feedback.

There is no element in the basis for conclusion in the amended IAS 1 to explain why this paragraph was added (except to state its objective, that is, that it was added to clarify that an entity's right to defer settlement is subject to compliance with specified conditions but with no supporting explanation compared to the core standard).

The conclusion reached by the Committee is not obvious and clear-cut and other interpretations could be made; the Committee appears not even to have considered alternative views.

The outcome that will be obtained with the decision exposed in the TAD is not appropriate or useful; such a reading of the amendments indicates that these amendments themselves should be fully debated in a proper due process

The relevant amendment of IAS 1 will not be effective before 1 January 2023; in our view, this leaves enough time to undertake a standard-setting process.

C**oncerning the interpretation and the final expected outcome:**

We agree with the core principle that only rights and obligations existing at the reporting date should be considered in order to classify liabilities; intention and/or management expectation should not be used to decide on this classification.

Reading paragraph 72 A, we note that the right should exist at the end of the reporting period, which also means that the obligation to comply with the condition should also exist at this date. With no obligation to comply at the end of the reporting period, the right to defer cannot be questioned.

The same paragraph specifies that "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". We do not share the Committee's interpretation of this statement. Indeed, this requirement could also be considered to deal with the case where the terms (the conditions) of the covenant are based on figures as of 31.12.N but which, for practical reasons, cannot be effectively tested for compliance before March N+1 (because audited financial statements are required by the lender). In this case, we agree that the classification will depend on the assessment based on 31.12.N figures, even if the lender will test compliance at a later date.

However, we do not believe that this paragraph should be viewed as also dealing with other circumstances in which both parties have agreed that the covenant will be tested at a date other than the end of the annual reporting period. In cases 2 and 3 of the TAD, we believe that the right to defer settlement is not subject to a condition as at the reporting date because in Case 2 the condition is not based on the ratio at the end of the annual reporting period and in Case 3 the second part of the condition does not exist until a future date. There is no obligation based on 31.12.N figures. With no obligation on this date, no one could argue that the liabilities should be settled within less than 12 months. The right to defer settlement could never be breached as at the end of the annual reporting period–it could be breached only at an interim date because the condition only exists at a specified future date (31 March or 30 June). The test of a condition is not the same thing as the condition: the test confirms that the condition has been met, it is not a condition in itself.

Naturally, if the entity expects that the future covenant will be breached, appropriate disclosure will be needed.

We therefore believe that the TAD contradicts the terms of the contractual agreement and does not faithfully depict the arrangement and the economic situation. We believe that the classification proposed may go far beyond the intention and legal reality of contracts. We believe that covenants are negotiated with full consideration of the specific operating environment of the entity and the specific purpose of the contract. For example, entities that operate in a seasonal or cyclical activity or which have predictable periodical high cash inflows, will take care to ensure that the dates at which the compliance with covenants has to be confirmed take into account this cyclical environment.

Take the following example: an entity with a year-end date of 31 December borrows for 5 years; each year the bank examines the entity's debt-to-equity ratio and may demand early repayment if the ratio is greater than x%. Given the seasonal activity of the entity, the lender and the borrower have agreed that the ratio is to be considered and reported as of 1 March, since, because of this seasonal activity, the

covenant would always be breached if it were computed with figures as of 31 December (the reporting date). The intention of the two parties is clearly not to cause the covenant to be breached in the normal course of events. We believe that it is neither relevant, nor faithful, to present the liability as a current debt because the covenant is not effectively breached at the reporting date. If significant, information should be disclosed in notes.

If you require any further information on this subject, please do not hesitate to contact us.

Yours sincerely,

ACTEO	AFEP	MEDEF
Lise CHORQUES	Lé Quang TRAN VAN	Karine MERLE