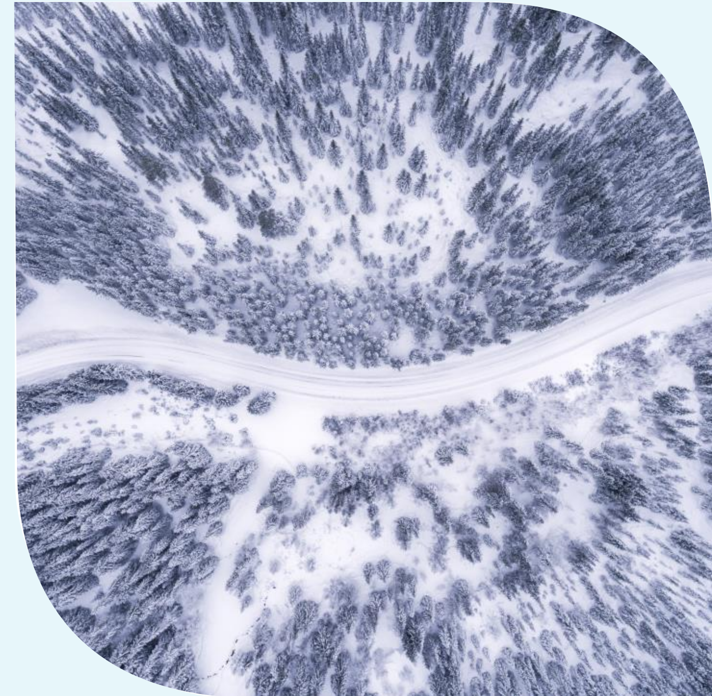
OVERVIEW ON FICE

FINANCIAL INSTRUMENTS WITH CHARACTERISTICS OF EQUITY

As of 24 August 2023

FICE team

Paper 05-03



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OVERVIEW

BACKGROUND

PROJECT OVERVIEW

PRACTICAL ISSUES ADDRESSED

APPENDIX 1: DETAILED UPDATE

- CLASSIFICATION
- PRESENTATION
- DISCLOSURES
- SUBSIDIARIES WITHOUT PUBLIC ACCOUNTABILITY —DISCLOSURES
- TRANSITION

APPENDIX 2: EXAMPLES OF DISCLOSURE REQUIREMENTS

BACKGROUND AND PROJECT OVERVIEW

BACKGROUND

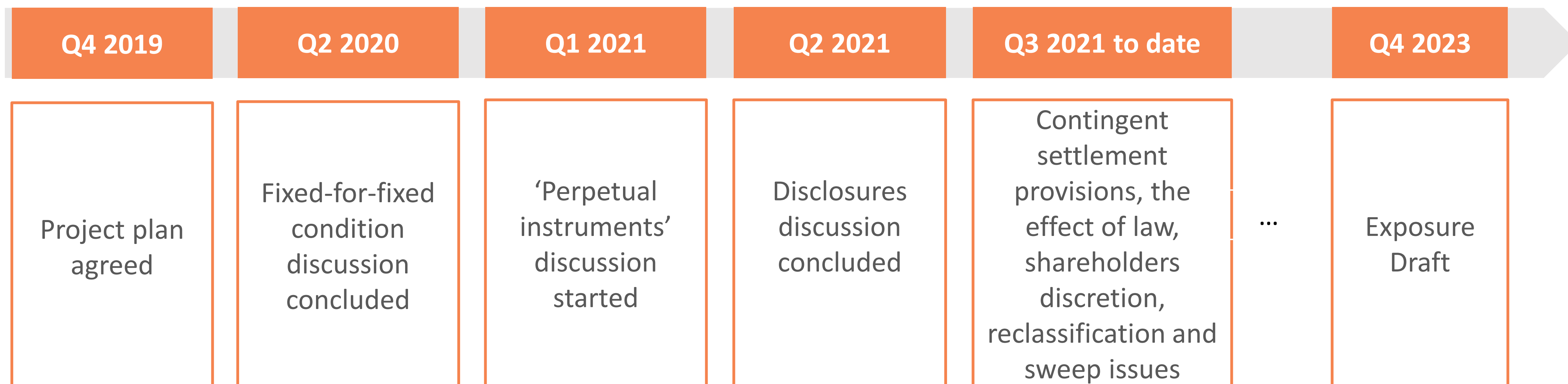
2018 IASB DISCUSSION PAPER AND EFRAG COMMENT LETTER

- The 2018 **IASB DP *Financial Instruments with Characteristics of Equity*** focused on potential improvements to the classification, presentation (3 alternative approaches) and disclosure requirements of financial instruments within the scope of IAS 32 *Financial Instruments: Presentation*
- **EFRAG final comment letter** issued in February 2019 where EFRAG did not support the IASB's preferred approach to classification
- EFRAG acknowledged that some constituents called for a more conceptual approach to distinguish debt from equity, however EFRAG did not identify any consensus on how to achieve such an approach
- **EFRAG suggested that the IASB focus on targeted improvements to current requirements in IAS 32** and other standards, including supporting guidance in IAS 32
- EFRAG also suggested that the **IASB pursue improvements to disclosures**
- For more details, please see EFRAG Website and EFRAG Feedback statement

OBJECTIVE AND TIMELINE

NEW OBJECTIVE OF THE PROJECT

- address known practice issues applying IAS 32 without fundamentally rewriting IAS 32
- improve information provided in financial statements about financial instruments issued, including improved disclosures under IFRS 7 on financial assets, financial liabilities and equity



PRACTICAL ISSUES ADDRESSED

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PRACTICAL ISSUES ADDRESSED - OVERVIEW

ISSUES IN PRACTICE	IASB POTENTIAL CLARIFICATIONS
Financial instruments settled in own equity instruments, including 'fixed-for-fixed' condition: diversity in practice and requests for guidance on the meaning and application of the fixed-for-fixed condition (e.g., foreign currency instruments)	The IASB developed two principles to meet the 'fixed-for-fixed' condition: a foundation principle and adjustment principle that would apply to the classification of derivatives on own equity
Obligations that arise only on liquidation: many consider that the current requirements lead to financial reporting that is counter-intuitive for a number of instruments such as perpetual instruments	The IASB will not change how such instruments should be classified. Instead, the IASB focused on developing presentation and disclosure requirements to meet the information needs of investors in ordinary shares
Financial instruments with contingent settlement provisions: there have been questions on how IAS 32 applies to features that are contingent on events beyond the control of the entity and the counterparty (e.g. bail-in instruments)	The IASB tentatively decided to clarify initial recognition and measurement of financial instruments with contingent settlement provisions and clarify the terms "liquidation" and "not genuine"

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PRACTICAL ISSUES ADDRESSED - OVERVIEW

ISSUES IN PRACTICE	IASB POTENTIAL CLARIFICATIONS
The effects of applicable laws on the contractual terms of financial instruments: there have been questions on whether the effects of law should be considered for classification purposes (e.g., bail in instruments)	The IASB decided to provide a principle to determine whether the rights and obligations arising from a legal requirement are taken into account in classifying the financial instrument as a financial liability or equity and in determining the 'substance of the contractual arrangement'.
Payments at the ultimate discretion of the issuer's shareholders: diversity in assessing whether an entity has an unconditional right to avoid delivering cash if the contractual obligation is at the ultimate discretion of the issuer's shareholders	The IASB tentatively decided to explore a factors-based approach to help an entity apply its judgement when classifying a financial instrument where payments are at the discretion of the issuer's shareholders
Reclassification between financial liabilities and equity instruments: there is currently lack of guidance on reclassification of financial instruments	The IASB developed general requirements and clarify reclassification requirements in IAS 32, particularly when the substance of the contractual terms changes because of changes in circumstances outside the contract. This without affecting reclassifications already required in IAS 32

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PRACTICAL ISSUES ADDRESSED - OVERVIEW

ISSUES IN PRACTICE	IASB POTENTIAL CLARIFICATIONS
Obligations to redeem own equity instruments: Diversity in practice and questions on how to initially recognise and measure obligations to redeem own equity instruments (e.g. NCI Puts)	The IASB tentatively decided to clarify recognition and measurement of obligations to redeem own equity instruments, including the accounting on initial recognition and on expiry, their presentation (gross basis), and their initial and subsequent measurement
Financial liabilities containing contractual obligations to pay amounts based on an entity's performance or changes in its net assets: Many have considered that the current requirements lead to financial reporting that is counter-intuitive for a number of instruments such as Financial liabilities containing contractual obligations to pay amounts based on an entity's performance or changes in its net assets	The IASB tentatively decided to require an entity with financial liabilities containing contractual obligations to pay amounts based on an entity's performance or changes in its net assets and measured at fair value through profit or loss to disclose in each reporting period the total gains or losses that arise from remeasuring such financial liabilities
Lack of information about financial instruments classified as equity: IFRS Standards have more comprehensive disclosure requirements for financial liabilities than for equity instruments.	IASB tentatively decided to amend the requirements in IAS 1 to ensure amounts attributable to ordinary shareholders are clearly visible on an entity's primary financial statements and improve disclosures on equity instrument within IFRS 7

APPENDIX 1
DETAILED UPDATE

CLASSIFICATION

CLARIFYING THE FIXED FOR FIXED CONDITION

- Questions arise in practice on the meaning of 'fixed-for-fixed' and whether there are types of variability that do not violate the fixed-for-fixed condition (e.g., anti-dilutive features or passage of time cash adjustments)
- The IASB proposes two principles to meet 'fixed-for-fixed' condition in paragraph 16(b)(ii) of IAS 32.

Foundation principle - fixed-for-fixed condition for derivatives on own equity

The number of functional currency units to be exchanged with each share is fixed. This the condition is met if the entity knows how many functional currency units it will exchange per type of own share if the option is exercised.

Adjustment principle – these adjustments would not preclude equity classification

Preservation adjustments preserve relative economic interests of future shareholders to an equal or a lesser extent than those of existing shareholders

Passage-of-time adjustments:

- are pre-determined
- vary only with passage of time
- fix the amount per share in terms of present value

Discussions at EFRAG

What about the foreign currency rights issue' exception?

Support for the new principles that capture current practice, even if it may lead to some changes

The wording for the passage-of-time adjustments is key

OBLIGATIONS THAT ARISE ONLY ON LIQUIDATION

- Some financial instruments have no redemption date and contain terms that give an entity the contractual right to defer cash payment until liquidation (‘perpetual instruments’).
- These instruments may contain incentives for the issuer to routinely make cash payments such as coupon payments at specified date(s) or have other debt-like features (e.g. corporate hybrids, additional Tier 1 and restricted Tier 1).

Financial instruments with obligations that arise only on liquidation of the entity

- The IASB discussed the challenges in accounting for financial instruments with obligations that arise only on liquidation of an entity (e.g. financial liability classification might better represent the substance and economics of how these types of financial instruments are expected to behave, however concerns on classification changes that may cause market disruption).
- The IASB also discussed potential classification, presentation and disclosure requirements to address those challenges.
- The IASB tentatively decided not to change how such instruments should be classified; but instead to develop presentation (e.g. attribution to ordinary shareholders of the parent and other owners) and disclosure requirements in relation to them (e.g. debt-like features’ of the financial instruments that are classified as equity instruments).

Discussions at EFRAG

No specific concerns in retaining current classification

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CONTINGENT SETTLEMENT PROVISIONS

- After the 2008 global financial crisis, there has been an increase in the number of instruments issued by financial institutions that have loss absorption features using a contingent conversion mechanism (e.g., bail-in instruments, which are instruments mandatorily convertible into shares upon a contingent 'non-viability' event)

Clarifications to be included in IAS 32 for instruments with contingent settlement provisions

- Financial instruments with contingent settlement provisions may be compound instruments
- The liability component of a compound financial instrument with contingent settlement provisions, which could require immediate settlement if a contingent event occurs, is measured at the full amount of the conditional obligation.
- Payments at the discretion of the issuer are recognised in equity, even if all the proceeds are initially allocated to the liability component of a compound financial instrument.
- Clarify that an entity is required to use the same approach for initial and subsequent measurement of financial liabilities within the scope of paragraph 25 of IAS 32—that is, the entity would ignore the probability and estimated timing of the contingent event in initial and subsequent measurement.

Discussions at EFRAG

On the zero-value equity component, disclosures may be needed for users to understand why payments are recognised as dividends

Equity classification restrict hedging on interest payments in foreign currency

- Such guidance would clarify, for example, the accounting for some instruments discussed by the IFRS Interpretations Committee. For example, financial instruments that are mandatorily convertible into a variable number of shares upon a contingent 'non-viability (bail-in instruments) would be a **compound instrument** with a liability component (full amount) and an equity component. All interest payments recognised in equity.

CONTINGENT SETTLEMENT PROVISIONS

CLARIFYING WORDING IN IAS 32

- Questions arise in practice on how to interpret the **meaning of 'liquidation'** in paragraph 25(b) of IAS 32 in the context of processes that are similar to liquidation (e.g. resolution or restructuring)
- Questions also arise in practice on how to interpret the **meaning of 'non-genuine'** in paragraph 25(a) of IAS 32 (whether 'non-genuine' is a wider notion that considers the purpose for including such features in the terms of the instrument even if that contingent event is extremely rare, highly abnormal or very unlikely to occur)

Clarifications to be included in IAS 32

- Specify that the term 'liquidation' in paragraph 25(b) of IAS 32 refers to when an entity is in the process of permanently ceasing operations; and
- specify that an assessment of whether a contract term is 'not genuine' under paragraph 25(a) of IAS 32 is not made by considering only the probability of the contingent event occurring.

Discussions at EFRAG

Clearly explain the meaning of 'process of permanently ceasing operations

Ensure consistency how these concepts are used in other IFRS Standards

- This guidance is likely to address some of the concerns that arise in practice, particularly with bail-in instruments (e.g. how non-genuine and liquidation interact with the bank recovery and resolution legislation)

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THE EFFECTS OF LAWS ON CONTRACTUAL TERMS

WHAT IS THE MEANING OF 'CONTRACTUAL'?

- The question is whether, and if so to what extent, a legal requirement is part of the contractual terms and must therefore be considered in classifying a financial instrument as a financial liability or an equity instrument
- This is particularly relevant for instruments such as bail-in instruments, ordinary shares with statutory minimum dividends and mandatory tender offers (e.g. whether the laws in a particular jurisdiction that affect the rights and obligations established in a contract should be considered part of or even reproduced in the contractual terms)

Clarifications to be included in IAS 32

An entity would be required to classify financial instruments as financial liabilities or equity by considering enforceable contractual terms that give rise to rights and obligations in addition to, or more specific than, those established by applicable law.

Discussions at EFRAG

Test the approach against well-know financial instruments (e.g. bail-in instruments and MTO)

Difficult to assess whether the terms stated in the contract are in addition to what is in the law

- This guidance is likely to address some of the concerns that arise in practice, particularly with bail-in legislation. However, this is not likely to address the issue of Mandatory Tender Offers.

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SHAREHOLDERS DISCRETION

- Questions arise in practice on whether an entity has an unconditional right to avoid delivering cash if the contractual obligation is at the ultimate discretion of the issuer's shareholders (e.g. preference shares that include a contractual obligation to deliver cash when the payment is at the discretion of the shareholders)
- More specifically, whether the shareholder decisions are part of the entity's operating and corporate governance processes (thus the entity has unconditional right to avoid payment of cash) or acting in their individual capacity (thus the entity does not have the unconditional right to avoid payment of cash)

Clarifications to be included in IAS 32

- Explore a factors-based approach to help an entity apply its judgement when classifying a financial instrument with a contractual obligation to deliver cash (or to settle it in such a way that it would be a financial liability) at the discretion of the issuer's shareholders. Such an approach would provide examples of potential factors for an entity to consider when assessing whether a decision of shareholders is treated as a decision of the entity.
- This assessment is needed to determine whether an entity has an unconditional right to avoid delivering cash (or settling a financial instrument in such a way that it would be a financial liability).

- There are mixed views on this issue and notes the difficulty and subjectivity of developing guidance on how to determine when the shareholders are acting in their individual capacity. If the IASB decides to proceed, it should be cautious at it may have a high impact on current requirements and practice (lead to less equity).

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RECLASSIFICATION BETWEEN FINANCIAL LIABILITIES AND EQUITY

- Currently, IAS 32 has no general requirements on reclassification between financial liabilities and equity instruments. Questions arise in practice on whether IAS 32 permits or requires reclassification after initial recognition where there has been no modification to the contract.
- IASB Staff indicated that practice has developed over time with some diversity as some firms permit reclassification.

Clarifications to be included in IAS 32

- Prohibit reclassification other than for changes in the substance of the contractual terms arising from changes in circumstances outside the contract. This does not affect reclassifications already required by IAS 32.
- Clarify that when the substance of the contractual terms changes due to changes in circumstances outside the contract, a financial liability reclassified from equity would be measured at fair value at the date of reclassification. Any difference between the carrying amount and the fair value would be recognised in equity.
- In addition, an equity instrument reclassified from a financial liability would be measured at the carrying value of the financial liability at the date of reclassification. No gain or loss would be recognised.
- Replace ‘reclassified’ and ‘reclassification’ with alternative wording in paragraph 23 of IAS 32.
- Finally, make a reclassification at the date of the change in circumstances that necessitated the reclassification.

OBLIGATIONS TO REDEEM OWN EQUITY INSTRUMENTS

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- Questions arise in practice on where to place the obligations to redeem own equity instruments (e.g. options, Forward/Future) in the balance sheet and where to put the final pay-off of these obligations.
- Another important matter is whether they need to be remeasured, and if yes, where do the gains and losses need to be presented.

Clarifications to be included in IAS 32

- Clarify that paragraph 23 also applies to an obligation to redeem an entity's own equity instruments that is required to be settled in a variable number of a different type of the entity's own equity instruments.
- The accounting on initial recognition of the obligation to redeem an entity's own equity instruments, if the entity does not already have access to the returns associated with an ownership interest. If the obligation involves non-controlling interests, the debit entry is recognised against a component of equity other than non-controlling interests. In the case of an entity's other obligations to purchase its own shares, the debit entry is recognised against a component of equity other than issued share capital.
- When remeasuring the financial liability, an entity is required to recognise gains or losses in profit or loss.
- The entity is required to use the same approach for initial and subsequent measurement of financial liabilities within the scope of paragraph 23 of IAS 32—that is, the entity would ignore the probability and estimated timing of the holder exercising the written put option in initial and subsequent measurement.
- Remove from paragraph 23 of IAS 32 the reference to IFRS 9 about subsequent measurement.

Discussions at EFRAG

Mainly it is important to have clear requirements in this area to improve comparability and eliminate diversity in practice

Include a question in the ED on subsequent measurement changes to the redemption amounts

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OBLIGATIONS TO REDEEM OWN EQUITY INSTRUMENTS

Clarifications to be included in IAS 32

- Clarify that on expiry of a written put option on an entity's own equity instruments:
  - the financial liability is reclassified to the same component of equity as that from which it was reclassified on initial recognition of the put option
  - the cumulative amount in retained earnings related to remeasuring the financial liability could be reclassified to another component of equity but is not reversed in profit or loss.
- Written put options and forward purchase contracts on an entity's own equity instruments are required to be presented gross, instead of net (to align the accounting for these instruments with the accounting for other obligations that are conditional on events or choices that are beyond the entity's control and to assist users of financial statements in assessing the entity's exposure to liquidity risk).

Discussions at EFRAG

It is important to have clear requirements on measurement when instruments are subject to a cap

Clarify the accounting for NCI puts in separate financial statements

PRESENTATION

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EQUITY INSTRUMENTS

Clarifications to be included in IAS 32

The IASB tentatively decided to amend IAS 1 to ensure amounts attributable to ordinary shareholders are clearly visible on an entity's statement of financial position, statement(s) of financial performance and statement of changes in equity by requiring an entity to:

- Present line items on issued capital and reserves attributable to ordinary shareholders of the parent separately from issued capital and reserves attributable to other owners of the parent in the statement of financial position.
- Present each class of ordinary share capital separately from each class of other contributed equity in the statement of changes in equity.
- Present profit or loss and comprehensive income for the period attributable to ordinary shareholders of the parent separately from the respective amounts attributable to other owners of the parent in the statement(s) of financial performance.
- Present the amount of dividends recognised as distributions to ordinary shareholders separately from dividends recognised as distributions to other owners during the period and present the related amount of dividends per share, either in the statement of changes in equity or in the notes.

Discussions at EFRAG

It would be useful to have illustrative examples to better understand the IASB tentative decisions

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FINANCIAL LIABILITIES BASED ON AN ENTITY PERFORMANCE

- Questions arise on whether it is appropriate for an entity to recognise changes in the carrying amount of the financial liability in profit or loss when the financial liability contains a contractual obligation to pay the holder an amount based on the entity's performance or changes in the entity's net assets.
- It results in counter-intuitive accounting in profit or loss because gains are recognised when an entity performs poorly, and losses are recognised when an entity performs well.

Clarifications to be included in IAS 32

- The IASB tentatively decided that for financial liabilities containing contractual obligations to pay amounts based on an entity's performance or changes in its net assets and measured at fair value through profit or loss an entity is required to disclose in each reporting period the total gains or losses that arise from remeasuring such financial liabilities.
- These disclosures, together with the proposed disclosures of terms and conditions will help to meet the information needs of users of financial statements.
- Finally, the IASB tentatively decided to delete the second sentence of paragraph 41 of IAS 32.

Discussions at EFRAG

Questions arise on which instruments would be captured by such disclosure requirements (questions on the scope and prevalence of such instruments)

DISCLOSURES

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DISCLOSURES: TERMS AND CONDITIONS

Scope

- Financial instruments with characteristics of both debt and equity including compound instruments
- Excludes standalone derivatives

Disclosure requirements

An entity is required to disclose:

- ‘debt-like features’ of the financial instruments that are classified as equity instruments
- ‘equity-like features’ of the financial instruments that are classified as financial liabilities
- debt-like and equity-like features that determine the classification of such financial instruments as financial liabilities, equity instruments or compound financial instruments

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DISCLOSURES: POTENTIAL DILUTION

Scope

- All instruments and transactions settled by delivering ordinary shares
- Includes IFRS 2 instruments and transactions (entities can leverage existing IFRS 2 disclosures)

Disclosure requirements

An entity is required to disclose information about the maximum dilution of ordinary shares in the notes, including

- the maximum number of additional ordinary shares that an entity could be required to deliver for each type of potential ordinary share outstanding at the reporting date
- the minimum number of ordinary shares required to be repurchased
- sources of any significant changes in above from the prior reporting period and how these sources contributed to those changes
- terms and conditions relevant to understanding the likelihood of maximum dilution, including a cross-reference to disclosures required by IFRS 2 for a description of share-based payment arrangements
- a description of any share buy-back programs or other arrangements that may reduce the number of shares outstanding

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DISCLOSURES: PRIORITY ON LIQUIDATION

NATURE AND CLAIMS AGAINST THE ENTITY

Scope

- All financial liabilities and equity instruments within the scope of IAS 32

Disclosure requirements

An entity to disclose and categorise in the notes its claims that are financial instruments in a way that reflects differences in their nature and priority, and at a minimum, to distinguish between financial instruments that are:

- secured and unsecured
- contractually subordinated and unsubordinated
- issued/owed by parent and issued/owed by subsidiaries

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DISCLOSURES: PRIORITY ON LIQUIDATION

TERMS AND CONDITIONS ABOUT PRIORITY ON LIQUIDATION

Scope

- Financial instruments with characteristics of both debt and equity including compound instruments
- Excludes standalone derivatives

Disclosure requirements

An entity to disclose:

- terms and conditions that indicate priority on liquidation
- terms and conditions that could lead to changes in priority on liquidation
- that a particular type of financial instrument has more than one level of contractual subordination, if applicable
- narrative information when an entity is aware of significant uncertainty about the application of relevant laws or regulations that could affect how priority will be determined on liquidation
- details of intra-group arrangements such as guarantees that may affect their priority on liquidation

SCOPE OF IFRS 7 FINANCIAL INSTRUMENTS: DISCLOSURES AND ADDITIONAL DISCLOSURES

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SCOPE OF IFRS 7

- Both users and preparers acknowledged that information on specific disclosure requirements in IFRS 7 in regard to an entity's issued equity instruments or equity components of compound instruments are lacking
- With the scope expansion in IFRS 7 stated below, the scope exclusion in paragraph 3(a) of IFRS 7 is no longer needed

Disclosure requirements

The IASB tentatively decided:

- to expand the objective of IFRS 7 to enable users of financial statements to understand how an entity is financed and what its current and potential ownership structures are
- to delete the reference to derivatives that meet the definition of an equity instrument in IAS 32 from paragraph 3(a) of IFRS 7, which excludes such derivatives from the scope of the latter Standard

SCOPE OF IFRS 7 FINANCIAL INSTRUMENTS: DISCLOSURES AND ADDITIONAL DISCLOSURES

TERMS AND CONDITIONS: REFINEMENTS AND ADDITIONAL DISCLOSURES

Disclosure requirements

The IASB tentatively decided:

- to include explanations and examples of 'debt-like' and 'equity-like' features in the sections of the forthcoming exposure draft containing application guidance and illustrative examples
- to clarify that the disclosures of 'debt-like' and 'equity-like' features would include both quantitative and qualitative information
- to require an entity to disclose the amounts allocated initially to the financial liability and equity components of compound financial instruments
- to require an entity to disclose the significant judgements it made in classifying the financial instrument, or its component parts, as a financial liability or as equity
- to require an entity to disclose, if applicable, information about terms and conditions that become, or stop being, effective with the passage of time before the end of the contractual term of the instrument

SCOPE OF IFRS 7 FINANCIAL INSTRUMENTS: DISCLOSURES AND ADDITIONAL DISCLOSURES

FURTHER DISCLOSURE REQUIREMENTS

Disclosure requirements

The IASB tentatively decided:

- to relocate the disclosure requirement in paragraph 80A of IAS 1 to IFRS 7 and expand it to cover reclassifications when changes in the substance of the contractual terms arise from changes in circumstances outside the contract. An entity would be required to disclose the amounts reclassified into and out of financial liabilities or equity, and the timing and reason for that reclassification
- to require an entity to disclose, for instruments containing obligations to redeem its own equity instruments:
  - the amount removed from equity and included in financial liabilities when the obligation was initially recognised and the component of equity from which it was removed
  - the amount of remeasurement gain or loss recognised in profit or loss during the reporting period
  - the amount of gain or loss, if any, that was recognised on settlement if the obligation is settled during the reporting period
  - the amount removed from financial liabilities and included in equity if the written put option has expired unexercised
  - the cumulative amount transferred within equity and the component of equity to which it was transferred, if any cumulative amount in retained earnings was transferred
- to amend paragraph 20(a)(i) of IFRS 7 to require the separate disclosure of the total gains or losses in each reporting period that arise from remeasuring financial liabilities containing contractual obligations to pay amounts based on an entity's performance or changes in the entity's net assets

SUBSIDIARIES WITHOUT PUBLIC ACCOUNTABILITY — DISCLOSURES

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SUBSIDIARIES WITHOUT PUBLIC ACCOUNTABILITY —DISCLOSURES

- In its May 2023 meeting, the IASB considered each of the disclosures tentatively decided in the FICE ED and assessed them against the principles for disclosures in the ED SWPA

Consequential amendments to be made to the IFRS Accounting Standard *Subsidiaries without Public Accountability*

The IASB tentatively decided to included consequential amendments to the SWPA Standard to add disclosure requirements consistent with those proposed in the FICE ED in the following areas:

- **Nature and priority of claims against an entity**
- **Terms and conditions**, including debt-like and equity-like features, priority on liquidation and passage-of-time changes
- **Instruments containing obligations to redeem own equity instruments**, including the amount removed from equity and included in financial liabilities when the obligation was initially recognised and the component of equity from which it was removed
- **Financial liabilities with contractual obligations to pay amounts based on the entity's performance or net assets**
- **Significant judgements** it made in determining the classification of a financial instrument

Discussions at EFRAG

Acknowledged that the IASB's tentative decision would mean discussing potential amendments to a IFRS Standard that does not exist at the date of publication of the FICE ED

FRAG Secretariat will have to engage with subsidiaries without public accountability to collect input on the costs and benefits

TRANSITION

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TRANSITION

TRANSITION METHOD

- Retrospective application with restatement of comparatives:
  - would maximise consistency of financial information between periods and also facilitate analysis and understanding of comparative information
  - is consistent with the transition requirements of previous amendments to IAS 32
  - would result in benefits greater than costs as the resulting information would help users of financial statements identify and assess changes and trends in the entity’s liquidity and solvency; and most information should be readily available to preparers

Disclosure requirements

The IASB tentatively decided to require an entity to apply the proposed amendments retrospectively with the restatement of comparative information (i.e., a fully retrospective approach)

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TRANSITION

ENTITIES ALREADY APPLYING IFRS ACCOUNTING STANDARDS

Disclosure requirements

For an entity already applying IFRS Accounting Standards, the IASB tentatively decided:

- to require the entity to treat the fair value at the beginning of the earliest comparative period presented as the amortised cost of the financial liability at that date if it is impracticable (as defined in IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors) for the entity to apply the effective interest method retrospectively
- not to require the entity to separate the liability and equity components if the liability component of a compound financial instrument with a contingent settlement provision was no longer outstanding at the date of initial application
- to require the entity to disclose the nature and amount of any changes in classification resulting from initial application
- to provide transition relief from the quantitative disclosures in paragraph 28(f) of IAS 8
- not to provide any transition relief from the requirements in IAS 34 Interim Financial Reporting for interim financial statements issued within the annual period in which the entity first applies the amendments

ENTITIES ALREADY APPLYING IFRS ACCOUNTING STANDARDS

Disclosure requirements

For first-time adopters, the IASB tentatively decided not to require any additional transition relief.

APPENDIX 2
EXAMPLES OF DISCLOSURE REQUIREMENTS

APPENDIX – EXAMPLE ON TERMS AND CONDITIONS

Company X has perpetual subordinated notes that are classified as equity instruments

Note 16 Perpetual subordinated notes

At 31 December 2020, the total perpetual subordinated notes outstanding amounted to CU3,985 million (less net-of-tax transaction costs) and are included in the Company's equity. The table below includes the key terms of these financial instruments.

	Notional amount	Initial call date	Coupon reset after initial call date	2020 CU million	2019 CU million
5.5% Fixed Rate Subordinated Notes	USD 1,000m	Jan 2025	10.5%	690	714
4.5% Fixed Rate Subordinated Notes	EUR 750m	Mar 2028	market rate	647	658
4% Fixed Rate Subordinated Notes	EUR 2,000m	Oct 2032	market rate	1,724	-
3% Fixed Rate Subordinated Notes	GBP 1,000m	Jan 2027	market rate	925	910
				3,985	2,282

Coupon

These notes bear a fixed rate of coupon until their initial call dates. After the initial call dates, if they are not redeemed, the coupon on the notes reset. The coupon on the USD subordinated notes reset to 10.5%. The coupon on the other notes are fixed periodically in advance for five-year periods, based on prevailing market interest rates plus credit spreads of Company X, fixed at issuance.

Company X has discretion to defer coupons on these notes. The deferred coupons accumulate and become payable at the call date if the notes are called, or when Company X is liquidated, if the notes are not called.

Company X is prevented from paying dividends or other distributions in respect of its ordinary shares, or from repurchasing its ordinary shares, until the cumulative coupons on the perpetual subordinated notes have been paid in full.

Redemption option

These notes are redeemable at the option of Company X at the initial call date or any fifth anniversary after this date. The amount redeemable will be the notional amount plus accumulated coupons.

Classification

These notes are classified as equity instruments because Company X has the unconditional contractual right to defer coupons and principal repayments until liquidation of Company X.

Priority on liquidation

[Information about priority of the notes on liquidation of Company X (see Agenda Paper 5B for this meeting.)]

Source: April 2021 IASB paper 5A

APPENDIX – EXAMPLE ON POTENTIAL DILUTION

Instruments	*Maximum number of additional ordinary shares to be disclosed*	*Key terms and conditions relating to the instrument/transaction*
Convertible bonds B	250	In the event of a change of control of Company X prior to the conversion date, the conversion ratio is adjusted downwards to a pre-determined strike price.
Convertible bonds D	350	Issuer holds an option to settle in shares or cash (equal to the value of the shares).
Convertible bonds (A and C)	600	Holder holds an option to convert the bond at a specified conversion date using a specified conversion ratio.
Contingently convertible bond E	50	Conversion contingent on the occurrence of non-viability event X. Redeemable at the option of the issuer for cash.
Share-settled bond F	50 Or unknown dilution (if unlisted shares)	Depending on the share price at settlement date a higher number of shares might need to be delivered.
Mandatorily convertible note G	100	Subject to a cap of 100 shares and a floor of 10 shares.
Number of share options in the scope of IFRS 2 outstanding at reporting date	100	Refer to note x (IFRS 2 disclosures on share options).
Number of known unvested shares from share awards in the scope of IFRS 2 at reporting date	100	Refer to note y (IFRS 2 disclosures on share awards).
Maximum number of additional ordinary shares	**1,600**	

Less: minimum reduction in the number of ordinary shares		
Share buy-back	(100)	Commitment to buy 100 –500 shares.
Net maximum number of additional ordinary shares	**1,500**	

Source: April 2021 IASB paper 5C

APPENDIX – EXAMPLE ON PRIORITY ON LIQUIDATION

Note 12 Nature and priority of claims arising from financial instruments

	As of 31 Dec 2020 (CU million)		
		Issued/owed by	
	Consolidated	parent	subsidiaries
Secured and unsubordinated			
Senior secured debt (a)	1,200	-	1,200
Lease liabilities (a)	920	780	140
Unsecured and unsubordinated			
Trade and other payables	1,450	320	1,130
Senior unsecured debt (a)	450	-	450
Unsecured and subordinated			
Subordinated liabilities (see note 15)	590	480	110
Classified as financial liabilities	*4,610*	*1,580*	*3,030*
Unsecured and subordinated			
Perpetual notes (see note 18)	200	200	-
Irredeemable preference shares (See note 19)	500	400	100
Non-controlling interest	1,250	-	1,250
Shareholders' equity	8,500	8,500	-
Classified as equity	*10,450*	*9,100*	*1,350*
Total	***15,060***	***10,680***	***4,380***

(a) They are included in the 'Borrowings' line item in the statement of financial position.

Source: May 2021 IASB paper 5

Note 15 Subordinated liabilities

	As of 31 Dec 2020 (CU million)	As of 31 Dec 2019 (CU million)
EUR100mil 7.125% subordinated notes due 2025	110	110
GBP250mil 6.75% senior subordinated notes due 2030	230	230
USD225mil 7.20% subordinated notes due 2033	165	-
Other subordinated liabilities each less than CU50 millio	85	85
Total subordinated liabilities	590	425

In the event of the respective issuer's liquidation, any amounts due in respect of the subordinated liabilities rank junior to all present and future unsubordinated claims of the respective issuer and rank senior to the respective issuer's ordinary shares, and if any, preference shares and perpetual notes. Subordinated liabilities listed in the table above do not rank pari passu with one another. Some subordinated liabilities are contractually subordinated to other subordinated liabilities.

[other key terms and conditions as discussed at the April 2021 Board meeting, for example, 'equity-like' features in these liabilities and the features that determine their financial liability classification]

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