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AUTORITÉ DES NORMES COMPTABLES

IASB - Mr Andreas Barckow
IASB Chair
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London E14 4HD

N°3

Paris, 28 March 2024

Exposure Draft Financial Instruments with Characteristics of Equity - ANC Comment Letter

Dear Mr Barckow, Dear Andreas

The Autorité des Normes Comptables (ANC) welcomes the opportunity offered by the IASB to comment on its Exposure Draft published on 29 November 2023 on Financial Instruments with Characteristics of Equity.

Scope of the project as defined by the IASB

Consistent with the Comment Letter issued in January 2019 on the Discussion Paper, the ANC is supportive of the IASB's efforts to continually develop high-quality accounting standards and specifically solutions that are based upon the principles of IAS 32 as a starting point. However, the ANC believes that the IASB should not limit its scope to the clarification of these principles and should consider amending such principles when they do not result in relevant information for users of financial statements.

Addressing the two following issues would thus have been useful.

The apparent conflict between paragraphs 20 and 25 of IAS 32, may have contributed to the development of financial instruments with discretionary payments, for which the entity has little if any practical ability to avoid delivering such discretionary cash-flows, including redeeming such instruments. Classifying such instruments as equity while many interested parties are viewing these as financial liabilities is not aligned with the principles of the Conceptual Framework, and may not result in relevant information for users of financial statements.

The application of the fixed-for-fixed condition introduced in IAS 32 has opened a large number of interpretative questions and has led to diversity in the accounting treatments applied. Although welcoming the efforts made to clarify the guidance in that area, the ANC remains of the view expressed in its Comment Letter on the 2018 Discussion Paper, that financial instruments settled by the delivery of a variable number of the issuer's own equity instruments should be classified as equity, while in its current state, paragraph 16(b) of IAS 32 requires these to be classified as financial liabilities, even if the number of own equity instruments is subject to a cap. Similarly, derivatives settled by the delivery of the entity's own equity instruments against cash should be classified as equity, regardless of whether the amount of cash or the number of own equity instruments is fixed. Paragraph 15 of the present Comment Letter further details such proposals.

The effects of relevant laws or regulations

The ANC identifies several unintended consequences to the IASB's proposal on the effects of relevant laws and regulations and supports instead the "all-inclusive" approach described in paragraph BC14 of the Basis for Conclusions on the Exposure Draft, as only the latter results in instruments presenting similar cash flows, but arising from contractual or legal sources to be classified identically. Conscious though that such an approach may disrupt some current practices, the ANC encourages the IASB to consider providing limited exceptions to such a principle, especially for bail-in instruments as further outlined in paragraph 13. However, if the IASB were not endorsing the principles of the "all-inclusive" approach, the ANC would highly recommend to withdraw its current proposal, while requiring transparency on the approaches and judgements applied by an entity.

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Obligations to purchase an entity's own equity instruments

Regarding the obligations to purchase an entity's own equity instruments arising from put options granted to non-controlling interest holders, the ANC does not support the IASB's proposal, as it would result in the double recognition of the rights attributable to non-controlling interest holders:

(a) In the statement of financial position: on the one hand, as a share in equity measured in accordance with applicable accounting standards; on the other hand, as a financial liability measured at the present value of the redemption amount; and

(b) In the statement of profit or loss, where the share in net income attributable to the parent is impacted twice by the interests attributable to non-controlling interest holders: on the one hand, through the allocation of the net income between entity's shareholders; and on the other hand, through the remeasurement of the financial liability for the component corresponding to the share of net income attributable to non-controlling interest holders (referred to as "component A" in paragraph 25).

Besides, the share of net income attributable to equity holders of the parent would be distorted by a measurement mismatch between the net income attributable to non-controlling interest holders and the portion of the change in the carrying amount of the financial liability, based on the fair value of non-controlling interests' shares (referred to as "component B" in paragraph 25).

The ANC considers that granting put options to non-controlling interest holders fundamentally changes the nature of the corresponding equity instruments. The "ANC Preferred Approach" (paragraphs 46-49) recognises a gross financial liability against equity attributable to non-controlling interests. The entire net income of the period would be allocated to the equity holders of the parent, while "component A" would be recognised as a debit in the share of profit or loss attributable to the equity holders of the parent. "Component B", which is at the origin of the mismatch in the statement of profit or loss, would be recognised as a debit from the share of equity attributable to the equity holders of the parent. The ANC considers that this approach is compatible with the existing standard-setting framework and achieves a consistent and useful presentation for the users of financial statements. The ANC therefore invites the IASB to examine its merits. In any case, the ANC will support any solution that: (i) recognises a gross financial liability against equity attributable to non-controlling interests; (ii) avoids the double recognition issues described in paragraphs 26 to 29; and (iii) avoids the profit or loss mismatch described in paragraph 29.

The ANC also encourages the IASB to reconcile its own proposal with paragraphs BC11, BC68 and AG29 of IAS 32. The ANC observes that a large part of the difficulties related to the recognition of obligations to purchase an entity's own equity instruments arises from the apparent conflict between paragraphs B89 of IFRS 10 and BC11 of IAS 32 and suggests the IASB to clarify how these two paragraphs should be read.

Disclosure and presentation of amounts attributable to ordinary shareholders

The ANC agrees with the IASB that disclosures on financial instruments with characteristics of equity need to be improved. However, the ANC encourages the IASB to enhance the robustness of its proposals, both for presentation- (paragraphs 76 to 78) and disclosures- (paragraphs 73 to 75) related proposals, in order to provide relevant information for users of financial statements.

Contingent settlement provisions

Finally, the ANC is overall supportive of the IASB's proposal on contingent settlement provisions. The ANC has provided suggestions to improve the relevance of the proposal when the amount that could be required to be paid varies with timing or leads to an amount greater than that of the initial fair value of the instrument (paragraphs 51 to 54).

RG

The Appendix to this Comment Letter is structured as follows:
. Question 1 - The effects of relevant laws or regulations (paragraphs 1-14);
. Question 2 - Settlement in an entity's own equity instruments (paragraphs 15-22);
. Question 3 - Obligations to purchase an entity's own equity instruments (paragraphs 23-49);
. Question 4 - Contingent settlement provisions (paragraphs 50-57);
. Question 5 - Shareholder discretion (paragraphs 58-60);
. Question 6 - Reclassification of financial liabilities and equity instruments (paragraphs 61-72);
. Question 7 - Disclosure (paragraphs 73-75);
. Question 8 - Presentation of amounts attributable to ordinary shareholders (76-78);
. Question 9 - Transition (paragraph 79); and
. Question 10 - Disclosure requirements for eligible subsidiaries (paragraph 80).

Should you wish to discuss our comments further, please do not hesitate to contact us.

Yours sincerely,

Robert Ophèle
ANC Chair