STAFF PAPER

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IFRS Interpretations Committee Meeting

Project	IAS 32 *Financial Instruments: Presentation*		
Paper topic	IFRIC Interpretation X *Put Options Written on Non-controlling Interests*		
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Introduction

1. In May 2012 the IFRS Interpretations Committee (the Interpretations Committee) published a draft Interpretation on the accounting for put options written by a parent on the shares of its subsidiary that are held by non-controlling-interest shareholders.
2. The comment period ended on 1 October 2012. We received 68 comment letters.
3. The purpose of this paper is to:
   (a) present a summary of the comments received on the draft Interpretation; and
   (b) provide a recommendation for next steps.

Summary of the comments received on the draft Interpretation

4. The draft Interpretation asked three questions—one each on the proposed scope, consensus and transition. The responses to those questions, as well as other feedback provided in the comment letters, are summarised below.

Question 1: scope

5. The draft Interpretation would apply, in the parent's consolidated financial statements, to put options that oblige the parent to purchase shares of its subsidiary that are held by a non-controlling-interest shareholder for cash or another financial asset (NCI puts). However, the draft Interpretation would not apply to NCI puts that were accounted for as contingent consideration in accordance with IFRS 3 *Business Combinations* (2004) because IFRS 3 (2008) provides the relevant measurement requirements for those contracts.
6. Some respondents agreed with the proposed scope and noted that it appropriately reflects the narrow, well-defined and urgent issue that was submitted to the Interpretations Committee.
7. However, the majority of respondents expressed the view that the scope is too narrow and also should include:
    (a) **forward contracts** that oblige the parent to purchase shares of its subsidiary that are held by a non-controlling-interest shareholder for cash or another financial asset (NCI forwards); and
    (b) puts (and forwards) that oblige **any entity in the consolidated group** to purchase shares of a subsidiary that are held by a non-controlling-interest shareholder for cash or another financial asset (eg one subsidiary in the consolidated group writes a put option that obliges it to purchase shares of a fellow subsidiary that are held by a non-controlling-interest shareholder).
8. Respondents said that the accounting for those contracts should be the same as the accounting for NCI puts— and expressed concern that excluding them from the scope could suggest that the Interpretations Committee thinks the accounting should be different.
9. A few respondents raised other concerns or questions related to the scope of the draft Interpretation:
    (a) The Interpretations Committee should address situations where a parent (or another entity in the consolidated group) issues an NCI put and, at

the same time, purchases a 'mirror-image' call option (ie whether those instruments should be linked and accounted for as an NCI forward).

(b) The Interpretations Committee should consider situations where the parent is obliged to purchase shares of its subsidiary that are held by a non-controlling-interest shareholder by delivering its own shares or a non-financial asset. These respondents stated that it is unclear whether paragraph 23 of IAS 32 *Financial Instruments: Presentation*[1] applies to such contracts because that paragraph discusses only circumstances in which the parent is obliged to deliver cash or another financial asset.

(c) It is unclear whether the draft Interpretation would apply to both (i) situations in which the parent writes the NCI put at its own discretion and (ii) situations in which the parent writes the NCI put (or is otherwise obliged to purchase the shares of its subsidiary that are held by non-controlling-interest shareholders) as the result of particular legal requirements in its jurisdiction.

(d) The Interpretations Committee should clarify why the draft Interpretation would not apply to the parent's **separate** financial statements.

(e) It is unclear whether the requirements in paragraph 23 of IAS 32 —and thus the draft Interpretation —would (or should) apply to all NCI puts or only to those that meet the 'fixed for fixed' condition in paragraph 16(b)(ii) of IAS 32.[2]

(f) It would be more logical to confirm the accounting for **all** put options and forward contracts written on an entity's own equity instruments before focusing on puts and forwards written on a particular component of an entity's equity (eg non-controlling interests).

[1] Paragraph 23 of IAS 32 requires particular derivatives written on an entity's own equity instruments to be initially measured at the present value of the redemption amount (ie the contracts are 'grossed up')

[2] Paragraph 16(b)(ii) of IAS 32 describes which derivatives written on an entity's own equity instruments meet the definition of an equity instrument.

Contingent consideration

10. Respondents generally agreed with the proposed scope exclusion for NCI puts that were accounted for as contingent consideration in accordance with IFRS 3 (2004). They agreed that IFRS 3 (2008) provides the relevant measurement requirements for those contracts. However a few respondents noted that an explicit reference to the relevant paragraphs in IFRS 3 (2008) would be helpful.

11. A few respondents asked the Interpretations Committee to clarify the accounting for NCI puts that were accounted for as contingent consideration after the application of IFRS 3 (2008). For example, the European Financial Reporting Advisory Group (EFRAG) noted that the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* (published in May 2012) contains a proposed amendment to IFRS 3 (2008) to clarify that contingent consideration that is not classified as an equity instrument is subsequently measured at fair value. That exposure draft also proposes a consequential amendment to IFRS 9 *Financial Instruments* that would require a contingent consideration liability to be subsequently measured as if it were designated under the fair value option at initial recognition. Those proposed annual improvements appear inconsistent with paragraph 7 of the draft Interpretation, which indicates that an NCI put could be measured at either amortised cost or fair value in accordance with IAS 39 *Financial Instruments: Recognition and Measurement* or IFRS 9. Therefore, if both the proposed annual improvements and draft Interpretation are finalised, EFRAG asked that the Interpretations Committee clarify whether all NCI puts that were accounted for as contingent consideration after the adoption of IFRS 3 (2008) must be subsequently measured at fair value.

Question 2: consensus

12. The draft consensus clarifies that in accordance with IAS 32, an NCI put gives rise to a financial liability that is initially measured at the present value of the redemption amount in the parent's consolidated financial statements (ie the NCI put is 'grossed-up'). Subsequently, the financial liability is measured in accordance with IAS 39 or IFRS 9. Paragraphs 55 and 56 in IAS 39 and

paragraphs 5.7.1 and 5.7.2 in IFRS 9 require that changes in the measurement of that financial liability are recognised in profit or loss (P&L).

13. Responses to the consensus were mixed. Respondents expressed four primary views:

    (a) The draft consensus provides the appropriate interpretation of existing IFRS.

    (b) The draft consensus reflects existing IFRS requirements; however, those requirements do not result in useful information.

    (c) There is a conflict in IFRS and the draft consensus sets out only one possible interpretation. Another interpretation is that IFRS requires that subsequent changes in the measurement of an NCI put are recognised in equity.

    (d) The correct interpretation of IFRS depends on the facts and circumstances of the NCI put.

View (a): The draft consensus provides the appropriate interpretation of existing IFRS

14. Some respondents agreed with the draft consensus and the rationale described in the Basis for Conclusions. These respondents agreed that an NCI put gives rise to a financial liability representing the issuer's obligation to deliver cash (or another financial asset) upon the holder's request—and therefore agreed that IAS 39 or IFRS 9 must be applied when that financial liability is subsequently measured.

15. Many of these respondents acknowledged that IAS 27 *Consolidated and Separate Financial Statements* and IFRS 10 *Consolidated Financial Statements* require that changes in the parent's ownership interest in the subsidiary that do not result in the parent losing control are equity transactions. However they agreed with the view set out in the Basis for Conclusions that those requirements are not relevant because the remeasurement of an NCI put does not result from a change in the parent's or non-controlling-interest shareholder's relative ownership interest in the subsidiary.

16. Others acknowledged that IAS 1 *Presentation of Financial Statements* states that transactions with owners in their capacity as owners do not affect total

comprehensive income. However these respondents pointed out that 'owners' are defined by IAS 1 as 'holders of instruments classified as equity' — therefore, a party in its capacity as a holder of an NCI put is not an 'owner' because the NCI put is a financial liability.

17. These respondents also pointed out that the IASB's *Conceptual Framework for Financial Reporting* states that changes in a liability's balance are recognised as income or expense.

18. Some respondents noted that the accounting for an NCI put should be the same as the accounting for all other put options and forward contracts written on an entity's own equity instruments. They said that there is no compelling reason to treat NCI puts differently. Some also stated that the accounting for an NCI put should be the same as the accounting for a puttable share because the instruments are economically the same—and if the subsidiary had issued puttable shares, those instruments would be classified as financial liabilities in the consolidated financial statements and subsequent changes in their measurement would be recognised in P&L.[3]

19. While agreeing that the draft consensus is the appropriate interpretation of existing IFRS, at least one respondent suggested that the relevant IFRS should be amended to clarify existing IFRS and unequivocally address any potential conflict.

20. Finally, at least one respondent asked the Interpretations Committee to clarify whether an entity could elect to designate the financial liability that is recognised for an NCI put under the fair value option. If so, IFRS 9 requires that changes in fair value that are attributable to changes in the credit risk of that liability must be presented in other comprehensive income.

[3] In accordance with IAS 32 (paragraphs 16A and 16B) particular puttable shares are classified as equity in an entity's **standalone** financial statements. However, in accordance with paragraph AG29A, all puttable shares held by non-controlling-interest shareholders are classified as financial liabilities in the **consolidated** financial statements.

View (b): The draft consensus reflects existing IFRS requirements; however, those requirements do not result in useful information.

21. Respondents who expressed this view acknowledged that an NCI put is a financial liability and IFRS requires changes in the measurement of that financial liability to be recognised in P&L. However, these respondents believe that such treatment does not result in decision-useful information and questioned whether the quality of financial information will be improved by the draft consensus.

22. Almost all of the respondents with this view said that it is counterintuitive to recognise volatility in P&L if an NCI put is exercisable at the fair value of the underlying shares (a fair value NCI put) or at a formula that is intended to achieve a similar outcome. They said that such volatility is misleading because the fair value of the NCI put is always close to zero, ie if the put is exercised and the issuer is required to deliver cash, it will receive shares with an equal value in exchange.

23. Some respondents also pointed out that if an NCI put's strike price is based on the subsidiary's performance, the liability that is recognised for that NCI put will increase and thus a loss will be recognised when the subsidiary performs well (and vice versa). These respondents believe that such results are counter-intuitive and do not result in useful information—and many noted that their concerns are similar to concerns related to the effects of 'own credit' when financial liabilities are measured at fair value.[4]

24. Finally, a few respondents pointed out that if an NCI put expires, the liability will be derecognised with an offsetting entry to equity—and thus will not offset (or reverse) the volatility recognised in P&L over the life of the contract. These respondents questioned whether that volatility provides useful information to users since the NCI put ultimately expires.

Suggested path forward

25. Respondents who acknowledged that the draft Interpretation was technically correct but stated that existing IFRS requirements do not provide useful

[4] Many have told the IASB that it is counter-intuitive to recognise a gain in P&L when the credit quality of a financial liability measured at fair value deteriorates (and likewise it is counter-intuitive to recognise a loss in P&L when the credit quality of the liability improves).

information generally urged the IASB to amend IFRS. However, there were two views on what those amendments should be:

(a) Some urged the IASB to re-consider changing the measurement basis of NCI puts to that used for other derivatives (ie a net basis at fair value with all changes recognised in P&L). Some of these respondents expressed agreement with the dissenting opinion of Jim Leisenring from the issue of IAS 32 in December 2003. In his dissenting opinion, Mr Leisenring said that it is inappropriate to recognise put options as though the future transaction has already occurred and that such treatment is inconsistent with the accounting for other put options (and with the IASB's *Framework*).

(b) Others supported the existing (grossed-up) measurement basis for NCI puts but urged the Board to amend IFRS to require that subsequent changes in that measurement are recognised in equity.

26. However, while they acknowledged the counterintuitive results described in paragraphs 22 and 23, some respondents expressed the view that introducing a rules-based exception to IAS 32 in order to address NCI puts would add complexity to IFRS. For example, Grant Thornton noted that it would be hard to apply such an exception in practice due to the difficulty of defining the boundaries that would determine which contracts would (and would not) be eligible. These respondents generally preferred that the Interpretations Committee urgently confirm the draft Interpretation and, the IASB address the broader issue of accounting for derivatives written on an entity's own equity instruments as part of its long-term project on financial instruments with characteristics of equity (the FICE project).

View (c): There is a conflict in IFRS and the draft consensus sets out only one possible interpretation.

27. Respondents who expressed this view generally thought that the Interpretations Committee applied an oversimplified process to address this issue and, as a result, focused on particular requirements in IFRS (IAS 39 and IFRS 9) while seemingly disregarding or ignoring other requirements (IAS 1, IAS 27 and IFRS 10). Most

of these respondents said that the draft consensus does not reflect the true nature and economics of an NCI put—and thus causes inappropriate volatility in P&L.

28. These respondents stated that subsequent changes in the measurement of an NCI put should be recognised in equity. The following rationale was expressed:

(a) Paragraph 30 of IAS 27 and paragraph 23 of IFRS 10 state that changes in a parent's ownership interest in a subsidiary that do not result in the parent losing control are equity transactions (ie transactions with owners in their capacity as owners). In the view of these respondents, for accounting purposes, the requirements in paragraph 23 of IAS 32 to gross up the NCI put portrays the transaction as if the put has been exercised, which is an equity transaction. Any re-measurements are simply part of that equity transaction.

(b) The meaning of the phrase 'change in ownership' in IFRS is unclear. Moreover, some transactions are recognised in equity even though there is not a change in ownership. For example, IFRIC 17 *Distributions of Non-cash Assets to Owners* requires that an entity adjust the carrying amount of a non-cash dividend payable and recognise any changes directly in equity as adjustments to the amount of the distribution. The accounting for NCI puts should be consistent with IFRIC 17.

(c) IAS 1 states that transactions with owners in their capacity as owners do not affect total comprehensive income. Changes in the value of the liability that is recognised for an NCI put simply reflect the fact that the ultimate settlement price for a transaction between the controlling shareholder and the non-controlling-interest shareholder (in their capacity as owners) depends on what happens between the date that the NCI put is written and the date it is exercised—and therefore such changes should be recognised in equity.

(d) The liability that is recognised for an NCI put is not a 'normal' financial liability:

(i) The grossed-up liability is based on fiction because it assumes that the put option has been exercised. In other words, the liability recognised for an NCI put is an 'as-if' liability. Recording such a liability is inconsistent with the IASB's *Framework*.

(ii) The initial recognition of the grossed-up liability, as well as the accounting for its expiration (ie if the put is not exercised), affect equity.

Since the liability that is recognised for the NCI put is not a normal liability, the accounting for subsequent changes in its measurement should not simply follow the requirements for a normal liability. Rather, since the initial recognition and expiry of the NCI put affect equity, it is logical that all changes in-between those two events are also recognised in equity. That is, there is no reason to treat subsequent measurement differently from initial recognition or expiry—and to do so may create structuring opportunities because the amount initially recognised could be difficult to measure.

(e) Paragraph 23 in IAS 32 states that the liability recognised for an NCI put should be subsequently **measured** —not **accounted for**—in accordance with IAS 39 or IFRS 9. In other words, while it is clear that the liability must be subsequently measured at fair value or amortised cost, it is not clear where in the financial statements any changes in that measurement should be recognised.

(f) If the controlling shareholder purchased the non-controlling interest directly—ie without issuing an NCI put— there would be no effect on P&L. Acquiring those interests via an NCI put should have the same result in P&L.

(g) Changes in the measurement of the financial liability that is recognised for an NCI put should be recognised in equity as a 'correction' of the entry made upon initial recognition. That would appropriately present the amount initially recognised for the NCI put as a temporary amount—ie because the NCI put may or may not be exercised.

29. Some respondents disagreed with the IASB's view set out in paragraph BC11 of the draft Interpretation that NCI puts should be treated the same as other

derivatives written on an entity's own equity instruments. They said that NCI puts are indeed different because they often are used in different circumstances and for different purposes— and the writers often have different motivations. These respondents did not provide further details on why such differences should give rise to different accounting. However a few did question whether the IASB thoroughly considered the effects of subsequent measurement when it decided to 'gross up' some derivatives written on an entity's own equity instruments—particularly how these requirements would apply to derivatives on non-controlling interests.

Suggested paths forward

30. Respondents who stated that the proposed consensus is not the appropriate interpretation of IFRS suggested two possible paths forward:

    (a) Most said that the Interpretations Committee should issue an Interpretation that clarifies that subsequent changes in the measurement of the liability that is recognised for an NCI put must be recognised in equity.

    (b) Some suggested that entities should be permitted to make an accounting policy decision to recognise such changes either in P&L or in equity. An entity would be required to disclose its decision and apply it consistently.

31. However, some respondents, including the European Securities and Markets Authority (ESMA) and the International Organization of Securities Commissions (IOSCO), noted the importance of addressing the current diversity in accounting for the subsequent measurement of NCI puts. Such diversity would not be addressed if entities were permitted to make a policy choice.

View (d): The correct interpretation of IFRS depends on the facts and circumstances of the NCI put

32. Some respondents expressed the view that there is not (or might not be) a single interpretation of IFRS for all NCI puts and indeed it may be inappropriate to impose uniform treatment. These respondents noted that NCI puts are written for

different reasons, have different contractual terms and the likelihood of their exercise varies.

33. For example, the following factors may be relevant to determining the appropriate accounting for NCI puts:

(a) Whether the controlling shareholder has, in substance, acquired a present ownership interest as a result of the NCI put;

(b) Why the NCI put was written and whether it was part of—or outside—a business combination;

(c) Whether the NCI put has been written on all of the shares held by the non-controlling-interest holders or only on some shares (or only to particular non-controlling-interest shareholders).

34. These respondents urged the Interpretations Committee to perform additional analysis of the substance of different types of NCI puts before finalising an Interpretation to ensure that the accounting correctly reflects the underlying economics of the transaction.

Question 3: transition

35. It was proposed that entities would be required to apply the draft Interpretation retrospectively in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*.

36. Almost all of the respondents agreed with the proposed transition requirements. Respondents agreed that entities would not face significant challenges or costs in applying the draft consensus, in particular because re-computations would not be necessary.

37. However a few respondents suggested that the Interpretations Committee require retrospective application only from the beginning of the earliest comparative period presented because application to earlier periods would result only in a reclassification within equity. Ernst &Young noted that such transition requirements would be consistent with those in IFRIC 19 *Extinguishing Financial Liabilities with Equity Instruments*.

Another issue: scope of the project on NCI puts

38. While expressing appreciation for the Interpretations Committee's efforts to reduce diversity in accounting for the subsequent measurement of NCI puts, many respondents said that either the Interpretations Committee or the IASB should address the accounting for NCI puts more comprehensively. They pointed out that other aspects of the accounting for NCI puts have resulted in diversity in practice, most notably: [5]

    (a) which component of equity should be debited when the grossed-up liability is initially recognised (ie whether the NCI balance should be derecognised);

    (b) how to account for the premium received for an NCI put;

    (c) whether a portion of the subsidiary's profit or loss should continue to be allocated to the non-controlling-interest shareholder after an NCI put is written;

    (d) whether any dividends paid to the non-controlling-interest shareholder after an NCI put is written are expenses or distributions; and

    (e) how to account for the expiration or settlement of the NCI put.

39. Some of these respondents said that it is difficult to analyse the subsequent measurement of NCI puts—and determine whether any conclusions reached by the Interpretations Committee are logical and appropriate— in isolation.

40. Some respondents pointed out that most of the issues set out in paragraph 38 — and the issue of whether changes in measurement should be recognised in P&L or equity—are not unique to NCI puts but rather are applicable to all put options and forward contracts written on an entity's own equity instruments. Accordingly, those respondents expressed the view that the accounting for all such derivatives should be comprehensively re-considered, including whether those contracts should be measured on a net basis at fair value with changes recognised in P&L (instead of on a gross basis at the present value of the redemption amount).

[5] This list sets out the topics that respondents raised most frequently. It is not exhaustive.

41. A few respondents expressed the view that the distinction between financial liabilities and equity instruments is highly complex in many instances and raises various accounting issues in addition to the issues related to grossing up particular derivatives written on an entity's own equity instruments. These respondents urged the IASB to address the broader, fundamental issues in IAS 32. They noted that there is a need to establish clear principles for classifying financial instruments as equity or non-equity and said that IAS 32 currently contains several complex exceptions. However, respondents had different views on the timeframe for this work—some urged the Board to urgently re-start the FICE project while others thought it was less urgent (but still important) and noted that the Interpretations Committee could urgently address narrow issues in the interim.[6]

Staff analysis and recommendations

42. Our analysis of the comments received is discussed in detail below. Our recommendations are:

(a) The Interpretation should apply to NCI puts **and** NCI forwards that are written by **any entity** in the consolidated group.

(b) The Interpretation should confirm the draft consensus and thus clarify that changes in the measurement of the financial liability that is recognised for an NCI put (or an NCI forward, consistent with the our recommendation to widen the scope) must be recognised in P&L in accordance with IAS 39 and IFRS 9.

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[6] In July 2011, the IASB published a request for views *Agenda Consultation 2011*. In January 2012 the Board discussed the comments received. Of the 54 letters that discussed the Board's FICE project, 25 said that it was a high priority, 12 said it was a medium priority and 17 said it was a low priority. The most frequently expressed comment on the FICE project related to the overlap between that project and the Board's project on the *Framework*. Respondents also raised concerns about particular requirements in IAS 32, including the application of the fixed-for-fixed condition, economic compulsion, classification of redeemable instruments and accounting for convertible debt. Feedback received from users on the request for views indicated that they think the currently distinction between equity and non-equity is too complex — and the FICE project is a medium priority (compared to the other projects discussed in the request for views).

(c) The Interpretation should require retrospective application in accordance with IAS 8.

(d) The Interpretations Committee should ask the IASB to re-consider in the near-term the requirements in paragraph 23 of IAS 32.

The scope of the Interpretation should be widened

46. We think the Interpretation should apply to both put options **and forward contracts** that oblige **any entity** in the consolidated group to purchase shares of a subsidiary that are held by a non-controlling-interest shareholder for cash or another financial asset. We think the accounting for those contracts is the same under existing IFRS.

47. We acknowledge that the Interpretations Committee specifically discussed widening the scope of the draft Interpretation on several occasions and decided to focus on the narrow issue that was submitted. Furthermore, the Interpretations Committee included paragraph BC10 in the draft Interpretation to reflect its view that all put options and forward contracts that oblige an entity to purchase its own equity instruments for cash or other financial assets are accounted for in the same way.

48. However, as discussed earlier in this paper, many respondents expressed concern that constituents could interpret the narrow scope of the draft Interpretation as an indication that the Interpretations Committee thinks that NCI forwards — or put options and forward contracts written by another entity in the consolidated group—should be treated differently than NCI puts. Therefore, to avoid such confusion or misinterpretation, we recommend that the Interpretations Committee widen the scope of the Interpretation.

49. As noted in paragraph 9 of this paper, a few constituents had other concerns or questions related to the scope of the draft Interpretation. We think that the Interpretation should address only the instruments described above in paragraph 46 for the following reasons:

(a) Some of the items set out in paragraph 9 are clear from existing IFRS—for example, an NCI put is accounted for on a net basis as a derivative in the parent's **separate** financial statements because it is not a contract written on the entity's own equity instruments and paragraph 23 of IAS 32 applies to all NCI puts (not only those that meet the 'fixed for fixed' condition).

(b) Other items in paragraph 9 are significantly outside the scope of the narrow issue that was submitted to the Interpretations Committee —for example, confirming the accounting for all puts and forwards written on an entity's own equity instruments, linkage (although we think the issue described in paragraph 9(a) becomes less troublesome if NCI forwards are within the scope of the Interpretation), whether contracts settled by delivering non-financial assets or the parent's own shares are within the scope of paragraph 23 of IAS 32 and whether particular legal obligations are within the scope of IAS 32.

50. Although we think the items described above in paragraph 49(b) are outside the scope of this Interpretation, we discuss later in this paper whether the Board should address those (and other) issues related to the accounting for derivatives written on an entity's own equity instruments.

Contingent consideration

51. We acknowledge that there is a link between the draft Interpretation and the amendments proposed to IFRS 3 (2008) and IFRS 9 as part of the 2010-2012 Annual Improvements cycle. We think the proposed annual improvements would clarify that all NCI puts that were accounted for as contingent consideration in accordance with IFRS 3 (2008) must be subsequently measured at fair value—as intended by the Board when it issued IFRS 3 (2008). We are aware that the Interpretations Committee is discussing that proposed annual improvement at its January 2013 meeting. If the Interpretations Committee agrees with our recommendation to finalise an Interpretation for NCI puts, we will need to ensure that it is drafted such that it does not create any conflicts.

Question 1 for the Interpretations Committee

Does the Interpretations Committee agree that the Interpretation should apply, in the group's consolidated financial statements, to put options and forward contracts that oblige an entity in the group to purchase shares of a subsidiary that are held by a non-controlling-interest shareholder for cash or another financial asset? If not, why and what does the Interpretations Committee want to do instead and why?

Subsequent changes in the measurement of an NCI put must be recognised in P&L

51. We think the Interpretations Committee should confirm the consensus in the draft Interpretation. Consistent with the Basis for Conclusions, we think the liability that is recognised for an NCI put (and an NCI forward, consistent with our recommendation above) reflects the obligation to pay the contract's exercise price, and that financial liability must be accounted for consistently with all other financial liabilities that are within the scope of IAS 39 and IFRS 9. That is, changes in the measurement of an NCI put or NCI forward must be recognised in P&L.

52. We think NCI puts and NCI forwards should be accounted for consistently with all other puts and forward contracts written on an entity's own equity. Paragraph 23 in IAS 32 provides guidance that is specific to these contracts and states that they are subsequently measured in accordance with IAS 39 or IFRS 9. We think it is clear from paragraphs BC11 and BC12 in the Basis for Conclusions on IAS 32 that the Board intended that the 'grossed-up' measurement basis for particular put options and forward contracts written on an entity's own equity instruments would result in those contracts being accounted for consistently with puttable and mandatorily redeemable shares. If the subsidiary had issued puttable or mandatorily redeemable shares, those shares would be classified as financial liabilities in the consolidated financial statements and any changes in their measurement would be recognised in P&L.[7]

[7] Please see paragraph 18(b) and paragraph AG29A in IAS 32.

53. Moreover, we think that paragraph 30 in IAS 27 and paragraph 23 in IFRS 10 simply re-articulate the principle in paragraph 33 of IAS 32 that no gain or loss shall be recognised in P&L on the purchase, sale, issue or cancellation of an entity's own equity instruments. Therefore, if there is a conflict between

(a) paragraph 30 in IAS 27 or paragraph 23 in IFRS 10; and

(b) paragraph 23 in IAS 32

then that would necessarily mean that there is an internal conflict in IAS 32 (ie between paragraphs 33 and 23 of that Standard). We do not think such a conflict exists because paragraph 33 of IAS 32—and hence paragraph 30 in IAS 27 and paragraph 23 in IFRS 10—are not relevant to the remeasurement of a financial liability (including the liability that is recognised for an NCI put).

54. We agree with the point made by some respondents that 'owners' are defined by IAS 1 as 'holders of instruments classified as equity' — and therefore, a party in its capacity as a holder of an NCI put is not an 'owner' because the NCI put is a financial liability (ie the reference to 'equity' in IAS 1 is a reference to the classification of the instrument for accounting purposes, which in this case is a liability). Therefore we do not think the requirements in IAS 1 (or IAS 27 or IFRS 10) related to 'transactions with owners in their capacity of owners' are relevant to the remeasurement of NCI puts.

Question 2 for the Interpretations Committee

Does the Interpretations Committee agree that the Interpretation should confirm that changes in the measurement of the financial liability that is recognised for an NCI put (or NCI forward, consistent with our recommendation in paragraph 46) must be recognised in P&L in accordance with IAS 39 and IFRS 9? If not, what does the Interpretations Committee want to do instead and why?

The Interpretation should require retrospective application in accordance with IAS 8

55. We recommend that the Interpretations Committee confirm the proposed transition guidance and require entities to apply the Interpretation retrospectively

in accordance with IAS 8. Almost all respondents agreed with that proposal and agreed that it would not pose any significant challenges for entities.

Question 3 for the Interpretations Committee
Does the Interpretations Committee agree that the Interpretation should be applied retrospectively in accordance with IAS 8? If not, what does the Interpretations Committee want to do instead and why?

The Interpretations Committee should ask the IASB to re-consider in the near-term the requirements in paragraph 23 in IAS 32

56. As discussed earlier in this paper, many respondents requested that either the Interpretations Committee or the IASB address the accounting for NCI puts more comprehensively—or indeed address the accounting for **all** derivatives written on an entity's own equity instruments. They pointed out that many aspects of the accounting for those derivatives have resulted in diversity in practice.

57. Moreover, we understand that several Interpretations Committee members believe that the requirements, to measure particular derivatives written on an entity's own equity instruments on a gross basis at the present value of the redemption amount, do not result in useful information. Some members believe that some or all such derivatives should be measured on a net basis at fair value, consistently with derivatives that are within the scope of IAS 39 and IFRS 9. Some respondents to the draft Interpretation expressed support for this view, or expressed support for analysing it further.

58. Given that feedback, we think the Interpretations Committee should ask the Board to re-consider in the near-term the requirements in paragraph 23 of IAS 32. Specifically the Board could re-consider whether derivatives written on an entity's own equity instruments should be grossed up — or whether IAS 32 should be amended with the result that all such derivatives are measured on a net basis at fair value. If the Board confirms the gross measurement basis that is currently required by IAS 32, it could consider whether additional guidance is needed in

that Standard to address some of the related issues that are currently resulting in diversity in practice (eg accounting for 'the debit').[8]

59. We acknowledge that the Interpretations Committee previously recommended that the Board propose a narrow scope amendment to IAS 32. Under that recommendation, IAS 32 would not apply to NCI puts. Instead the requirements for derivatives in IAS 39 or IFRS 9 would apply and, as a result, NCI puts would be measured on a net basis at fair value. At the time, the Board decided not to proceed with the Interpretations Committee's recommendation. It questioned whether NCI puts should be treated differently from other derivatives written on an entity's own equity instruments.

60. Since the Board made that decision, the comment letters received on the draft Interpretation have provided additional evidence that many constituents believe that further guidance is needed. Therefore we think it is appropriate for the Board to re-consider this issue. However we agree with the Board's concern about treating NCI differently than other contracts written on an entity's own equity instruments and thus recommend that the Board re-consider paragraph 23 in IAS 32 comprehensively.

Timing

61. If the Interpretations Committee decides to recommend that the Board reconsider paragraph 23 of IAS 32, we still think the Interpretation should be finalised in the interim. That is, we do not think the Interpretation should be deferred pending work on the wider-reaching issues. We think it is important that the Interpretations Committee address the diversity in accounting related to the subsequent measurement of NCI puts as soon as possible. This is consistent with the message we have received from regulators, such as ESMA and IOSCO.

[8] We are not recommending that the Board re-activate the FICE project. We note that the Board has decided that any consideration of the distinction between financial liabilities and equity instruments needs to be undertaken in conjunction with the work on elements in the *Conceptual Framework*.

Question 4 for the Interpretations Committee
Does the Interpretations Committee want to recommend that the Board re-consider in the near-term the accounting requirements in paragraph 23 of IAS 32, with a view to discuss issues such as: (a) whether put options and forward contracts written on an entity's own equity instruments should be recognised 'gross' at the present value of the redemption amount or 'net' at fair value; and (b) if such derivatives continue to be recognised at a 'gross' amount, whether additional guidance should be provided on other aspects of that accounting (such as the debit entry at initial recognition)? If not, what does the Interpretations Committee want to do instead and why?