FRC Financial Reporting Council

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10 September, 2012

Dear Françoise,

Draft IFRIC Interpretation 'Put Options Written on Non-controlling Interests'

Thank you for providing the Financial Reporting Council (FRC) with the opportunity to comment on your draft comment letter (DCL) to the IFRS Interpretations Committee's draft IFRIC Interpretation 'Put Options Written on Non-controlling Interests (NCI)'.

Whilst we share EFRAG's view that this interpretation raises a number of broader issues, we believe that these need to be considered by the IASB as part of its Financial Instruments with Characteristics of Equity (FICE) project. Given the IASB's current agenda, we broadly support the draft Interpretation on the basis that it provides a pragmatic solution to the current diversity in practice.

Our responses to the questions in the DCL are included in the Appendix to this letter. We also attach our response to the IFRS Interpretations Committee for your information.

If you would like to discuss these comments, please contact Deepa Raval on 020 7492 2424.

Yours sincerely

Roger Marshall

Roger Marshall
Chair of the Accounting Council
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Appendix: responses to the questions set out in the DCL

Paragraph 16. Do you agree that the Interpretations Committee should develop a broader interpretation that is consistent with IFRS 3, IFRS 10/IAS 27, IAS 32 and IFRIC 17 (as recommended in paragraph 8 above)? Please explain why?

1. No. As noted in our covering letter, whilst we agree that this interpretation raises a number of broader issues, we do not believe that these matters that can be resolved through the issue of an Interpretation.

Paragraph 17. To what extent do you believe diversity in practice arises on initial recognition of NCI puts? If you are not aware of wider practice, please explain how your organisation accounts for the debit entry of an NCI put liability.

2. We are not aware that the issue of where debit entry is presented within equity is particularly problematic in practice. Therefore, we do not believe that an interpretation on this issue is needed at this stage.

   We believe that EFRAG is right to question whether the accounting at initial recognition is appropriate. However, we believe that there are other wider issues, other than accounting for the debit entry, which have not been raised in the DCL. For instance, some hold the view that NCI puts should be accounted for as derivatives at initial recognition. We believe that these wider issues would be better dealt with as part of the FICE project.

Paragraph 51. How do you believe NCI puts should be accounted for? Please explain why?

See our response to the IFRS Interpretations Committee. We support the accounting that is set out in the draft Interpretation as an interim solution.

Paragraph 52. Do you believe that the whether or not NCI has been derecognised should determine the accounting for NCI puts? Please explain why?

Paragraph 53. Do you believe that the exercise price of NCI puts (e.g. fixed, fair value or formula-based) should determine the accounting for NCI puts? Please explain why

Paragraphs 52 and 53 - No. We support view 1 as set out in the DCL.

We believe that principles for debt equity classification should drive the accounting at initial recognition and subsequent measurement. Having rules for re-measurement in equity in particular circumstances is complex.

Financial Reporting Council

Michael Stewart
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10 September, 2012

Dear Michael,

Draft IFRIC Interpretation 'Put Options Written on Non-controlling Interests'

This letter sets out the comments of the Financial Reporting Council (FRC) on the Draft IFRIC Interpretation 'Put Options Written on Non-controlling Interests (NCI)'.

The FRC broadly supports the draft interpretation on the basis that it provides clarification in practice. We agree that a put option written over NCI should be subsequently measured at fair value through profit and loss in accordance with IAS 39 *Financial Instruments: Recognition and Measurement.*

Our responses to the questions contained in the 'Invitation to Comment' section of the ED are included in the Appendix to this letter. However, the FRC has the following overarching comments, relating to the scope of the draft Interpretation, which we set out below.

a) *NCI forwards* – We believe that the scope of the interpretation should be extended to include NCI forwards. We do not believe that there is a clear basis for treating NCI puts and NCI forwards differently.

b) *Broader issues* - Whilst we agree that this interpretation provides a short term solution, we believe that this is part of a broader issue. There is a need to review the initial recognition of derivatives over own equity, holistically.

   IAS 32 *Financial Instruments: Presentation* contains a number of exceptions and consequently derivatives over own equity can be accounted for in different ways. We believe that there is a need to establish clear principles for debt equity classification. In our view, these are not issues that require urgent attention as IAS 32 is a standard that is reasonably well understood in practice. Therefore, we recommend that the IASB consider these issues in time as part of its Financial Instruments with Characteristics of Equity project.

If you would like to discuss these comments, please contact Deepa Raval on 020 7492 2424.

Yours sincerely

Roger Marshall
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Appendix: responses to questions set out in the draft Interpretation

Question 1 – Scope

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.

Do you agree with the proposed scope? If not what do you propose and why?

1. No. As noted in our covering letter, we believe that the scope of the interpretation should be extended to include NCI forwards. That said, for the purposes of this interpretation, we agree with excluding NCI puts that are accounted for as contingent consideration as IFRS 3 (2008) provides guidance in this area.

   In addition and as explained in our covering letter, the draft Interpretation has raised a number of broader issues which need to be resolved in the longer term.

   We note that IAS 32 now contains a number of exceptions - paragraph 23; the 'fixed for fixed' criteria; and the requirements arising from the recent puttables amendment. Consequently, NCI puts and other derivatives over own equity can potentially be accounted for in three different ways - as equity instruments; as financial liabilities, measured on a gross basis in accordance with IAS 32 ; or as derivatives, measured on a net basis in accordance with IAS 39.

   Specifically, paragraph 23 of IAS 32 requires NCI puts to be measured at the fair value of the redemption amount. This is inconsistent with the initial measurement of other derivatives which are accounted for on a net basis. We also note that where a parent has written a put over the shares in its subsidiary, the NCI put would be treated as a derivative in the separate financial statements of the parent entity as this would not be a derivative over 'own equity' of the parent.

Question 2 – Consensus

The consensus in the draft Interpretation (paragraphs 7 and 8) provides guidance on the accounting for the subsequent measurement of the financial liability that is recognised for an NCI put. Changes in the measurement of that financial liability would be required to be recognised in profit or loss in accordance with IAS 39 *Financial Instruments: Recognition and Measurement* and IFRS 9 *Financial Instruments.*

Do you agree with the consensus proposed in the draft Interpretation? If not, what alternative do you propose?

2. Yes. We support the consensus. At initial measurement, the NCI put is presented as a financial liability in accordance with IAS 32. Therefore, consistent with the accounting for most other financial liabilities, it follows that subsequent changes in the measurement of that financial liability should be measured at fair value through the profit and loss account in accordance with IAS 39 and IFRS 9.

Question 3 – Transition

Entities would be required to apply the draft Interpretation retrospectively in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors.*

Do you agree with the proposed transition requirements? If not, what do you propose and why?

3. Yes. We agree with the proposed transition requirements. However, we note that the draft interpretation does not propose an effective date. We suggest that the effective date should not be before 1 January 2013.