European Financial Reporting Advisory Group

DI/2012/2 *Put Options Written on Non-controlling Interests*

Feedback to constituents – EFRAG Technical Expert Group Final Comment Letter

November 2012

Summary of contents

Introduction

Objective of this feedback statement

EFRAG published its final comment letter on the Draft Interpretation *DI/2012/02 Put Options Written on Non-controlling Interests* ('the Draft Interpretation') on 11 October 2012. This feedback statement summarises the main comments received by EFRAG on its Draft Comment Letter and explains how those comments were considered by the EFRAG Technical Experts Group (EFRAG TEG) during its technical discussions.

Background to the Draft Interpretation

The Draft Interpretation addresses diversity in practice on the remeasurement of the financial liability recognised when a parent entity writes a put option over non-controlling interests ('NCI puts'). Specifically, it requires subsequent measurement of the NCI put liability to be recognised in profit or loss. Further details are available on the EFRAG website.

EFRAG draft comment letter

EFRAG published a draft comment letter on the proposals in July 2012. In the draft comment letter EFRAG agreed that diversity in practice exists in accounting for the subsequent measurement of the financial liability that is recognised for NCI puts. Therefore, EFRAG supported the Interpretations Committee's efforts to address the issue. However, EFRAG expressed a number of significant concerns regarding the proposals and the use of Interpretation to resolve the issue, without addressing wider diversity in practice on accounting for NCI puts and transactions with NCI.

EFRAG did not reach a tentative view on the consensus in the Draft Interpretation and presented the following three different views of EFRAG TEG members:

(a) That remeasurement in profit or loss was always appropriate (the approach taken in the Draft Interpretation);

(b) That remeasurement in profit or loss was not appropriate and that changes should be recognised in equity; and

(c) That remeasurement in profit or loss was appropriate in some circumstances.

Comments received from constituents

Sixteen comment letters were received from constituents by the comment letter deadline, and are available on the EFRAG website.

The comment letters received came from national standard-setters, business associations, professional organisations, listed companies and EU authorities.

Detailed analysis of issues, comments received and changes made to EFRAG final comment letter

EFRAG's tentative views expressed in the draft comment letter and respondents' comments

EFRAG's response to constituent comments

General comments and Cover Letter

EFRAG's tentative position

EFRAG supported the Interpretations Committee addressing the issue of subsequent measurement of NCI puts, but felt that Interpretations Committee should attempt to develop an Interpretation that addressed the complexity and broad range of issues arising from transactions involving non-controlling interests, including NCI puts, in a manner consistent with the principles underlying IFRS 3, IAS 27/IFRS 10, IAS 32 and IFRIC 17, as this would result in a more robust and principles-based solution.

Constituents' comments

The majority of respondents expressed concerns about the scope of the Draft Interpretation and agreed with EFRAG that accounting for NCI puts was part of a broader issue. Some constituents believed that broadening the scope the Interpretations Committee would be able to achieve more consistency in accounting for similar contracts. However, the majority of constituents believed that the Interpretations Committee was correct to take steps that addressed the most significant current diversity in practice.

A significant number of constituents felt that the broader issues could only be addressed by the IASB as part of a comprehensive project, such as on *Financial Instruments with Characteristics of Equity.* Some constituents also called for the IASB to amend IAS 32 such that NCI puts would be accounted for on a net basis, consistent with the Interpretations Committee's original recommendation.

EFRAG changed its tentative position which called for the Interpretations Committee to address all of the broad range of issues arising from transactions with NCI at the same time as addressing subsequent measurement. In its final comment letter EFRAG supported the Interpretations Committee's pragmatic, short-term solution to address the issue, but called for the IASB and the Interpretations Committee to address other diversity in practice without delay.

EFRAG also said that it was important there was a common understanding of why the Interpretations Committee considered that the guidance in IFRS 10 was not relevant when deciding that the correct interpretation of existing standards is the accounting set out in IAS 32 and IAS 39.

Constituents' calls for NCI puts to be accounted for as net derivatives was considered at the November 2012 meeting of EFRAG TEG. EFRAG TEG did not believe derivative accounting was an appropriate alternative given the implications on the relevance information to users, who have informed EFRAG that the amount of the gross liability is useful information for their analysis. Furthermore, the net derivative treatment would also give rise to a number of broader consistency issues within IAS 32 and result in the presentation in equity of amounts that could, in fact, be payable in the near future.

Consensus

The Draft Interpretation requires changes in the gross liability measured for an NCI put to be recognised in profit or loss.

EFRAG's tentative position.

EFRAG did not reach a tentative view on the consensus in the draft interpretation and but expressed the following three different views of EFRAG TEG members:

(a) View 1: That remeasurement in profit or loss is always appropriate (the approach taken in the Draft Interpretation

(b) View 2: That remeasurement in profit or loss is not appropriate and that changes should be recognised in equity; and

(c) View 3: That remeasurement in profit or loss is appropriate in some circumstances.

Constituents' Comments

Most respondents who explicitly expressed a view supported view 1, but a significant minority supported either view 2 or view 3.

In its final comment letter EFRAG accepted that recognition of changes in the measurement of a financial liability for an NCI put in profit and loss is consistent with the requirements of IAS 32 *Financial Instruments: Presentation* and IAS 39 *Financial Instruments: Recognition and Measurement*.

EFRAG also accepted that the proposed treatment was consistent with that for other contracts written on an entity's own equity within the context of the requirements in IAS 32 and IAS 39, which requires an NCI put to be initially measured as a financial liability, and remeasured in accordance with IAS 39. Furthermore, EFRAG acknowledged that the proposed treatment ensures that the shares issued with a separate NCI put were treated in the same way as puttable shares.

EFRAG highlighted that its due process had indicated that NCI puts and related contracts involving own equity instruments presented a complex and controversial subject. EFRAG noted that a single basis of measurement might not be appropriate in all cases, particularly when NCI puts had different features and accounting for them in the same way might not reflect their economic substance. EFRAG recommended the Interpretations Committee to articulate in its Basis for Conclusion why it believed that a single basis for subsequent measurement of NCI puts was appropriate in all cases.