EFRAG

European Financial Reporting Advisory Group

INVITATION TO COMMENT ON THE EFRAG'S ASSESSMENTS OF THE AMENDMENTS TO IAS 32 AND IAS 1 "PUTTABLE FINANCIAL INSTRUMENTS AND OBLIGATIONS ARISING ON LIQUIDATION"

Comments should be sent to commentletter@efrag.org by 28 April 2008

EFRAG has been assessing the Amendments to IAS 32 and IAS 1 "Puttable Financial Instruments and Obligations Arising on Liquidation" (the amendments) against the criteria for endorsement set out in Regulation (EC) No 1606/2002 and has also been assessing the costs and benefits that would arise from their implementation in the EU.

A brief summary of the amendments is set out in Appendix 1.

EFRAG would welcome your views on the issues set out below. Please note that all responses received will be placed on the public record unless the respondent requests confidentiality. In the interests of transparency EFRAG will wish to discuss the responses it receives in a public meeting, so we would prefer to be able to publish all the responses received.

1 Please provide the following details about yourself:

(a) Your name or, if you are responding on behalf of an organisation or company, its name:

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(b) Are you/Is your organisation or company a:

□ Preparer □ User □ Other (please specify)_____________

(c) Please provide a short description of your activity/ the general activity of your organisation or company:

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(d) Country where you/your organisation or company is located:

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(e) Contact details including e-mail address:

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2 EFRAG's initial assessment of the amendments is that they meet the technical criteria for endorsement. In other words, they are not contrary to the true and fair principle and they meet the criteria of understandability, relevance, reliability and comparability. EFRAG's reasoning is set out in Appendix 2.

(a) Do you agree with this assessment?

Yes No

□ □

If you do not, please explain why you do not agree and what you believe the implications of this should be for EFRAG's endorsement advice.

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(b) Are there any issues that are not mentioned in Appendix 2 that you believe EFRAG should take into account in its technical evaluation of the amendments? If there are, what are those issues and why do you believe they are relevant to the evaluation?

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3 EFRAG is also assessing the costs that will arise for preparers and for users to implement the amendments both in year one and in subsequent years. Some initial work has been carried out, and the responses to this Invitation to Comment will be used to complete the work. The results of the initial assessment are set out in Appendix 3. To summarise, the amendments will:

(a) involve preparers incurring some year one costs—in order to read, understand and implement the new requirements—but that those costs will not be significant (see Appendix 3 paragraphs 1-7) ;

(b) not involve preparers incurring significant incremental ongoing costs (see Appendix 3 paragraphs 1-7) ; and

(c) involve users incurring only insignificant incremental year one and no incremental ongoing costs. Indeed, the amendments might reduce the ongoing costs to some users by making it easier to understand and analyse the financial statements of entities issuing instruments of the type addressed in the amendments (see Appendix 3 paragraph 8).

Do you agree with this assessment?

Yes No

□ □

If you do not, please explain why you do not and (if possible) explain broadly what you believe the costs involved will be?

4 As EFRAG believes (as explained in Appendix 3) that the amendments will improve the quality of the financial information provided and its implementation will involve on an overall level additional costs that will not be significant, it has tentatively concluded that the benefits to be derived from applying the amendments will exceed the costs involved.

Do you agree with this assessment?

Yes No

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If you do not, please explain why you do not and what you think the implications should be for EFRAG's endorsement advice?

5 EFRAG is not aware of any other factors that should be taken into account in reaching a decision as to what endorsement advice it should give the European Commission on the amendments.

Do you agree that there are no other factors?

Yes No

☐ ☐

If you do not, please explain why you do not and what you think the implications should be for EFRAG's endorsement advice?

APPENDIX 1
A SUMMARY OF THE AMENDMENTS TO IAS 32 AND IAS 1

1 All companies need financing, and they obtain that financing from a range of sources, including capital instruments (shares, traded loans, etc.), bank loans and overdrafts, and trade creditors.

2 The accounting model that underpins IFRS requires financing to be split into two categories: equity and liabilities. Currently in general the principle is that this is done by asking, in the case of shares, derivatives and other financial instruments, whether the item is a financial liability as defined in IFRS. If it is not, it is equity. Thus, normal ordinary shares are equity. Some other types of share might be however treated as liabilities.

3 Normally the existence of secondary markets provides holders of capital instruments with a liquidity mechanism (i.e. the ability to sell their holdings). Even if a liquid market does not exist in a particular instrument, there remains the potential to liquidate the holding by finding a purchaser. However, sometimes privately held companies, such as for example partnerships or co-operatives, might be obliged (sometimes by the company law in the country of their incorporation) to redeem ordinary shares in the company if the holders of such instruments request the redemption. The purpose of the redemption could be to provide a liquidity mechanism for holders of such instruments.

4 Certain types of entities could be required to liquidate on the exit of any partner or in accordance with the law can have only a limited life (for example 100 years).

5 Under existing IFRS, the existence of an obligation to redeem ordinary shares at the request of their holders or on liquidation means that the shares are treated as financial liabilities. In other words, even though the shares might be identical to ordinary shares except that the holder has the right to require the issuer to redeem the shares ("a put") that has been provided in order to enable holders to dispose of their holding, the shares will be classified as financial liabilities because of the put.

6 It is the treatment of certain puttable shares that the amendments will change.

7 In particular, the amendments will change the classification of certain instruments that are similar to an ordinary share except for an obligation to redeem (referred to in the amendments as puttable instruments or instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation); they would be classified as equity if they meet certain criteria. The purpose of those criteria is to ensure that the instruments, as a class, represent a residual interest in the net assets of entity.

8 The amendments further require disclosure of certain qualitative and quantitative information regarding these instruments even though the existing standards usually do not require such disclosures for equity instruments. The purpose of the disclosures is to ensure that the users of financial statements understand the nature of such instruments and are able to assess their effect on the entity.

APPENDIX 2
EFRAG'S ASSESSMENT OF THE AMENDMENTS TO IAS 32 AND IAS 1 AGAINST THE ENDORSEMENT CRITERIA

This appendix sets out the basis for the conclusions reached, and for the recommendation made, by EFRAG on the Amendments to Financial Instruments: Presentation and IAS 1 Presentation of Financial Statement Puttable Financial Instruments and Obligations Arising on Liquidation.

In its comment letters to the IASB, EFRAG points out that such letters are submitted in EFRAG's capacity as a contributor to the IASB's due process. They do not necessarily indicate the conclusions that would be reached by EFRAG in its capacity as advisor to the European Commission on endorsement of the final IFRS or Interpretation on the issue.

In the latter capacity, EFRAG's role is to make a recommendation about endorsement based on its assessment of the final IFRS or Interpretation against the European endorsement criteria, as currently defined. These are explicit criteria which have been designed specifically for application in the endorsement process, and therefore the conclusions reached on endorsement may be different from those arrived at by EFRAG in developing its comments on proposed IFRSs or Interpretations. Another reason for a difference is that EFRAG's thinking may evolve.

1 When evaluating the amendments to IAS 32 and IAS 1 *Puttable Financial Instruments and Obligations Arising on Liquidation*—henceforth "the amendments"—in light of the endorsement criteria, EFRAG considered the following key questions:

   (a) Is there an issue that needs to be addressed?

   (b) Are the amendments consistent with the IASB's *Framework for the Preparation and Presentation of Financial Statements* (the Framework)?

   (c) Would the implementation of the amendments result in an improvement in accounting?

   (d) Does the accounting that results from the application of the amendments meet the criteria for EU endorsement?

Is there an issue that needs to be addressed?

2 Under current IAS 32 shares that are identical to ordinary shares except that the holder has the right to require the issuer to redeem the shares meet the definition of a financial liability because they embody a contractual obligation to deliver cash or another financial asset. However, classification of such instruments as liabilities raised the following concerns in practice:

   (a) As liabilities, the instruments would be required under existing IFRS to be measured on an ongoing basis at not less than the amount payable on demand. This would have the following implications:

      (i) the entire market capitalisation of the entity may be recognised as a liability;

(ii) when the entity performs well and as a result the value of the instruments increases, a loss will be recognised. Similarly, when the entity performs poorly and the value of the instruments decreases, a gain is recognised; and

(iii) the entity is likely to have negative net assets, because of unrecognised intangible assets and goodwill, and because the measurement of recognised assets and liabilities is not at fair value.

(b) An entity's balance sheet might appear to be wholly, or mostly, debt funded.

(c) Distributions of profits to shareholders are recognised as expenses. As a result, net income is a function of the distribution policy, not performance.

3 Existing IFRS suggested alternative income statement and balance sheet formats that could be used by entities that did not have equity as defined in IAS 32. However, those alternative presentation possibilities do not address some of the above concerns and have not fully resolved those they do address.

4 EFRAG agrees that, when the entity has issued instruments that are identical to ordinary shares except for a put obligation, the issues highlighted in paragraph 2 result in anomalies and those anomalies need to be addressed.

5 EFRAG has noted that the IASB is currently addressing the issue of the definition of equity and liabilities in a broader context at two levels: at the conceptual level as part of its project on the Framework, and at the standards level through a research project that is considering ways to improve and simplify the equity versus financial liabilities classification approach in IAS 32. One way of addressing the anomalies mentioned above would be to wait for new IFRSs resulting from these projects to be finalised. However, that is likely to take some years and, in the mean time, the anomalies would remain. The IASB therefore decided to amend IAS 32 to provide a limited exception to the existing requirements as a short-term solution pending the outcome of its longer-term projects. EFRAG believes that such an approach is reasonable in the circumstances.

Are the amendments consistent with the Framework?

6 In EFRAG's view, the aspects of the Framework that are most relevant for this purpose are the qualitative characteristics of relevance, reliability, comparability and understandability and the material dealing with the elements of financial statements (in particular the definitions of liabilities and equity). As the amendments will be judged against the qualitative characteristics later in this appendix, the focus in this section is on the extent to which the amendments are consistent with what the Framework says about liabilities and equity.

7 According to paragraph 49 of the Framework, a liability is "a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits". Equity is "the residual interest in the assets of the entity after deducting all its liabilities."

8 The contractual provisions attached to puttable instruments that the amendments would require to be classified as equity give the holders the right to put the instruments to the entity and demand cash or other resources. Thus, there is a present obligation of the entity arising from a past event, the settlement of which is expected to result in

an outflow of resources of the entity. In other words, the puttable instruments that the amendments would require to be classified as equity meet the definition of a liability.

9 However, things are not as simple as that. Although the Framework's approach to distinguishing between liabilities and equity has been implemented in IFRS for liabilities that are *not* financial instruments, existing IFRS apply a different approach in the case of financial instruments. In particular, as the IASB's recently issued Discussion Paper *Financial Instruments with Characteristics of Equity* explains:

> 30 The definitions of a financial asset and financial liability in IAS 32 are inconsistent with the definitions of an asset and liability in the IASB's *Framework for the Preparation and Presentation of Financial Statements*. As a result, some derivative financial instruments that are settled with the issuer's own equity instruments would be classified in accordance with the *Framework*'s guidance differently from their classification in accordance with IAS 32.
>
> 31 For example, some financial instruments that are settled with the issuer's own equity instruments meet the definition of a financial liability in IAS 32 (paragraphs 19 and 20 above). However, such instruments do not always meet the definition of a liability in the *Framework*. That is because the instrument may not result in the sacrifice of an asset (eg cash); rather it involves the delivery of the entity's own equity instruments. For example, a written call option for a variable number of the issuer's ordinary shares would meet the definition of a financial liability in IAS 32 but would not meet the definition of a liability in the *Framework*.
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> 32 Another example of the differences between IAS 32 and the *Framework* is some purchased options that are settled with the issuer's own equity instruments. Such instruments meet the definition of an asset in the *Framework* because they have the potential to contribute to the entity's cash inflows. However, some of those instruments do not meet the definition of a financial asset in IAS 32 (and are classified as equity) because they meet the 'fixed for fixed' principle.

10 In other words, existing IFRS already introduces some exceptions to the Framework definitions of equity and liabilities in order to try to keep up with the increasing sophistication of the financing instruments available to companies. And, although EFRAG believes it is preferable for standards to be consistent with the Framework, those exceptions to the Framework did not stop EFRAG from concluding that existing IFRS met the criteria for endorsement. Bearing all this in mind, EFRAG has concluded that the fact that these amendments are not consistent with the Framework tells us nothing about their quality.

Would the implementation of the amendments result in an improvement in accounting?

Understandability

11 As already explained, the current approach to the classification of financial instruments between equity and liability is resulting in anomalies when the reporting entity has issued financial instruments that are largely equivalent to ordinary shares except for an obligation to redeem at the request of their holders or on liquidation that is outside the control of the entity (henceforth for simplicity 'puttable ordinary shares'). Those anomalies are affecting the understandability of the information provided by financial statements.

12 The amendments require puttable ordinary shares to be classified as equity if they meet criteria designed primarily to ensure that the class of financial instruments involved represent a residual interest in the entity.

13 EFRAG's view is that classifying puttable ordinary shares that meet the criteria set out in the amendments will resolve the anomalous reporting for such instruments. This will therefore result in an improvement in accounting as long as it does not at the same time result in other, new anomalies.

14 EFRAG notes that puttable ordinary shares that meet the criteria set out in the amendments are not the only instruments in respect of which the anomalies mentioned earlier arise. There are other instruments that will continue to be classified as liabilities and therefore in respect of which anomalies will continue to arise. This suggests that the amendments might give rise to comparability issues that could represent new anomalies. EFRAG has evaluated these concerns, and that evaluation is discussed in the next section.

15 The fact that puttable ordinary shares have a put option attached to them is significant to users, particularly when they are considering future cash outflows, liquidity etc. If classifying some puttable ordinary shares as equity rather than liabilities obscures the effect that such shares can have on the entity, the amendments will create new problems. EFRAG has therefore evaluated the additional disclosures that the amendments require with this in mind. This is discussed later in this appendix.

Comparability

16 Some commentators argue that the existing classification approach gives rise to comparability concerns because instruments that they see as economically very similar (ordinary shares and at least certain types of puttable ordinary shares) are classified very differently. In their eyes, classifying them in the same way would enhance the comparability of the information provided.

17 This argument is of course based on the view that ordinary shares and certain types of puttable ordinary shares are economically very similar. There is no doubt that the existence of the put option is economically significant for a number of reasons, but the issue that needs to be considered in order to decide whether they are economically similar for accounting purposes is which attribute of the instruments is the most relevant one to present in the financial statements, and which attributes are less relevant. The view taken in the amendments is that more relevant information would be provided by the financial statements were they to focus on residual nature of the instrument holders' interest in the assets and other liabilities of the entity, rather than on the obligation that the put option represents. Judged this perspective, the puttable ordinary shares that meet the criteria set out in the amendments are economically similar to ordinary shares and comparability is improved by classifying them in the same way.

18 On the other hand, it could be argued that there will be entities who have issued instruments that will continue to be classified as financial liabilities even though in substance they might be very similar to ordinary shares and/or to puttable ordinary shares that meet the criteria asset out in the amendments. For example, two entities might classify an identical type of puttable ordinary shares differently because it is a residual instrument of one entity but not the other. More generally, puttable ordinary shares that meet the criteria set out in the amendment will be classified differently from puttable ordinary shares that do not meet the criteria, even though those shares are economically similar.

19 EFRAG's view is that puttable ordinary shares that meet the criteria set out in the amendment are *not* economically similar to puttable ordinary shares that do not meet the criteria, so it is not a concern if such instruments are classified differently.

20 That is because EFRAG believes that at the heart of the criteria for determining which puttable instruments should be classified as equity and which should not there is a difference of substance. Although the detailed provisions of the amendments are rather rule-based, they *do* focus on identifying whether the puttable instruments, as a class, represent a residual interest; only those instruments that meet those criteria are classified as equity.

21 EFRAG has therefore concluded that the amendments do not give rise to any new comparability or consistency anomalies.

Puttable ordinary shares held by minority shareholders

22 Another issue that EFRAG has considered to determine whether it represents a "new anomaly" is how the amendments would apply to puttable ordinary shares held by minority shareholders.

23 Assume that an entity's equity comprises puttable ordinary shares that meet the criteria set out in the amendments, and the majority of those instruments are held by one entity (the parent) and a minority by a second entity (the minority shareholder). In the separate financial statements of the issuer those shares they meet all the criteria under the amendments and will therefore be classified in those financial statements as equity. However, since minority interests are not a residual interest in the consolidated financial statements of the parent, the instruments held by the minority shareholder would still be classified as financial liabilities in the parent's consolidated financial statements. Some see this as a contradiction of the consolidation principles under IAS 27 *Consolidated and Separate Financial Statements* in accordance to which minority interest is classified as equity.

24 The IASB's recently issued Discussion Paper *Financial Instruments with Characteristics of Equity* touches on this subject:

> IAS 32 provides some guidance on how to classify non-controlling interests and refers to the guidance in IAS 1 *Presentation of Financial Statements* and IAS 27 *Consolidated and Separate Financial Statements*. IAS 32 requires an entity to consider all the terms and conditions agreed between members of the group and the instrument holders in assessing whether the consolidated group has an obligation that would result in liability classification of the instrument. In effect, the instrument would retain equity classification unless something else within the group affects the substance of that instrument. However, as an exception, some puttable instruments and some instruments that impose an obligation only on liquidation of the entity meet the definition of a financial liability but are required to be classified as equity in the entity's separate financial statements. That exception does not extend to the consolidated financial statements of the group.

25 EFRAG understands that this is the area where the opportunities to structure instruments that are liabilities in substance in a way that would result in them being classified as equity are the largest. One such opportunity is illustrated in the following example.

> A subsidiary may be established for the sole purpose of buying a particular asset. The creation of the subsidiary may be funded entirely by the issue of ordinary shares, some of which are issued to a third party (for example, a 30% shareholding might be issued to a bank) so the subsidiary has a minority interest. The shares held by the minority are puttable to the parent. As part of the agreement, the parent grants the subsidiary an option to put the asset to the parent for a specified amount. In effect, the consolidated group has guaranteed the value of the minority shares, however it did so indirectly without changing the terms and conditions of the minority interest at the consolidated group level.

The requirement that the redeemable instruments as a class must represent the residual interest in the entity to be classified as equity disqualifies the minority interest in the above example which economically represents a liability of the group from being classified as equity.

26 EFRAG notes that the focus on the residual interest helps to minimise structuring opportunities and thus to avoid creating new anomalies. Furthermore, EFRAG does not view this as a contradiction of the consolidation principle in IAS 27. To be classified as equity in the group consolidated accounts, puttable ordinary shares need to be the residual class of instruments of the reporting entity and if that is not the case (as it is not in the above example in the consolidated financial statements), the instruments should be classified as liabilities.

Disclosures

27 As mentioned above, the difference between ordinary shares and puttable ordinary shares is in the put obligation. Although the view has been taken in the amendments that, if certain criteria are met, the put feature should not affect the way in which the instrument is classified on the balance sheet, the existence of the put obligation could inflict a strain on liquidity and financial viability of the entity that will not be the case for ordinary shares without the put feature. For that reason, it is important that the existence and potential impact of the put feature is not obscured by classifying certain puttable ordinary shares as equity; disclosures are required that provide sufficient information for users of financial statements to understand the nature of the instruments and enables them to evaluate the potential effects of the instruments on the entity. EFRAG has considered the disclosure requirements set out in the amendments against this benchmark.

28 Under existing IFRS, these puttable instruments are shown as liabilities and the disclosures required by IFRS 7 *Financial Instruments: Disclosures* are provided. One of the disclosures required is a maturity analysis by reference to contractual maturity dates of financial liabilities. Under the amendments, the puttable instruments would not be included in the maturity analysis; instead the existence and amount of the puttable instruments within equity would be disclosed, along with an estimate of expected cash outflow arising from redemptions. In addition, entities would be required to provide summary quantitative data about the amount of puttable instruments classified as equity; and the entity's objectives, policies and process of managing the obligation to repurchase. EFRAG has considered whether the new disclosures are sufficient to support the amended classification system and whether there is any loss of information.

(a) Expected future redemptions can be difficult to estimate reliably because redemption rates and the price at which the redemptions take place are subject to inherent uncertainties. EFRAG thought nevertheless that the disclosure would shed further light on the put feature's implications in normal circumstances for the entity.

(b) Some commentators argue that a requirement to disclose quantitative information about cash outflows arising from redemptions, without a similar requirement to disclose cash inflows from the re-issue of the shares show users an incomplete picture of the financial position. EFRAG noted however that under existing IFRS there is also no requirement to disclose information about cash inflows from re-issues.

29 Overall EFRAG's assessment is that the disclosures required are sufficient for their purpose and in some respects require the disclosure of useful additional information not provided under existing IFRS.

Conclusion

30 To summarise the foregoing discussion, the current approach to the classification of equity and liability causes:

(a) anomalies that the amendments address. They thus improve the understandability of the financial information provided.

(b) a lack of consistency in the treatment of instruments that are economically very similar. The amendments improve that consistency, and hence the comparability of the information provided.

31 For those reasons, EFRAG has concluded that the amendments are likely to result in an improvement in accounting.

Does the accounting that results from the application of the revised standard meet the criteria for EU endorsement?

32 EFRAG has considered whether it believes that the amendments meet the requirements of the European Parliament and of the Council on the application of international accounting standards, in other words that the Interpretation:

(a) is not contrary to the 'true and fair principle' set out in Article 16(3) of Council Directive 83/349/EEC and Article 2(3) of Council Directive 78/660/EEC; and

(b) meets the criteria of understandability, relevance, reliability and comparability required of the financial information needed for making economic decisions and assessing the stewardship of management.

EFRAG has also considered whether it is in the European interest to adopt the interpretation.

33 As already mentioned, EFRAG has concluded that the amendments improve the understandability and comparability of the financial information provided, compared to that provided under IAS 32, a standard that EFRAG has previously concluded meets the criteria set out above.

34 EFRAG has also considered whether the relevance criteria is met. Earlier it was explained that a key issue in evaluating the accounting treatment required by the amendments was which attribute of the instruments under consideration is the most relevant one to present in the financial statements. It was noted that the IASB has taken the view in the amendments that more relevant information would be provided by the financial statements were they to focus on residual nature of the instrument holders' interest in the assets and other liabilities of the entity, rather than on the obligation that the put option represents. EFRAG agrees that is a relevant attribute for accounting purposes.

35 Finally, EFRAG has considered the reliability of the information that will result from the application of the amendments. In EFRAG's view, the key issues here are whether the revised accounting treatment enables a faithful representation to be given of the transactions involved, and whether it has enabled those transactions to be accounted

for in accordance with their substance and not merely their legal form. For the reasons set out earlier, EFRAG believes that it does.

36 EFRAG has also concluded that there was no reason to believe that the information resulting from the application of the amendments would be contrary to the true and fair view principle.

Conclusion

37 For the reasons set out above, EFRAG has concluded that the amendments satisfy the criteria for EU endorsement and that EFRAG should recommend their endorsement.

APPENDIX 3
EFRAG'S EVALUATION OF THE COSTS AND BENEFITS OF THE AMENDMENTS TO IAS 32 AND IAS 1

Costs for preparers

1 EFRAG has considered whether applying the accounting treatment required by the amendments would involve significant incremental costs for preparers. The amendments require certain classes of shares that were previously classified as liabilities to be shown henceforth as equities. At the same time, those financial instruments that are equity at the moment will stay in equity.

2 Implementing the amendments will involve some year-one work and some ongoing work.

(a) The year-one work will involve:

(i) Evaluating financial instruments against the specified criteria;

(ii) Reclassifying financial instruments as equity if they meet all the required criteria;

(iii) Developing systems and procedures to collect and evaluate information to meet the disclosure requirements; and

(iv) Restating the earliest prior periods presented in the financial statements as the amendments are to be applied retrospectively. :

(b) The ongoing work will involve:

(i) Monitoring the effect of any new issues of financial instruments on the classification of any puttable instruments as equity (because one of the criteria would no longer be satisfied) and monitoring the effect of any withdrawals of existing financial instruments on the classification of any puttable instruments as liabilities (because criteria that were not previously satisfied might now be satisfied); and

(ii) Collecting and evaluating information to meet the disclosure requirements.

3 It is our understanding that generally an amendment may prove quite costly to implement if the implementation requires significant system changes. However, we do not think that any of the above mentioned work would require significant system changes.

4 There could be some costs associated with estimating expected cash outflows on redemption to meet one of the disclosure requirements especially if an entity does not have in-house valuation expertise to make these kinds of estimations. However, EFRAG notes that it is not an incremental cost resulting from the introduction of the amendments because under existing IAS 32 entities would already be required to value these instruments.

5 The amendments would need to be applied retrospectively. EFRAG has not identified any significant difficulties that would mean that application of the amendments retrospectively would involve significant costs.

6 For the above reasons, EFRAG's initial assessment is that those companies that have instruments that fall within the scope of the amendments will not need to incur significant year one or ongoing incremental costs to apply the standard.

7 EFRAG understands the amendments concerns a limited number of entities (namely some partnerships, co-operatives and limited life entities) and that most entities do not have any instruments of the type falling within the scope of the amendments. The only costs that such companies will incur will be the costs necessary to read and understand the amendments. Such costs will be insignificant.

Costs to users

8 Users will incur some year one costs in understanding the new requirements and perhaps also in adapting their models to make use of the different note disclosures. EFRAG's initial assessment however is that these costs will be insignificant. On the other hand, the amendments might reduce the costs to some users by making it easier to understand and analyse the financial statements of entities issuing instruments of the type addressed in the amendments. This is because these users generally consider equity classification of puttable instruments in the scope of the amendments more appropriate than liability classification under the existing IFRS provided that sufficient information is disclosed to understand the nature of these instruments and their potential effect on the entity.

Benefits for preparers and users

9 EFRAG has concluded, for the reasons explained in Appendix 2 the amendments improve the understandability of the financial information provided, because they resolve the anomalies caused by the current approach in IAS 32. Furthermore, the amendments improve consistency in the treatment of instruments that are economically very similar; and hence the comparability of the information provided.

Conclusion

10 To summarise, EFRAG's tentative assessment is that the amendments will involve only insignificant costs for users. Companies with instruments of the type addressed in the amendments will incur year one and ongoing incremental costs, but they will not be significant; other companies will incur insignificant additional costs. On the other hand, the amendments will improve understandability and comparability of financial reporting for the puttable instruments, which will be of benefit to all concerned stakeholders. As a result, EFRAG's initial assessment is that the benefits of implementing the amendments will exceed the costs.