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## Financial Instruments with Characteristics of Equity

### Cover Note

#### Introduction and objective

- 1 The objectives of the session are to:
  - (a) consider the feedback received in response to EFRAG’s draft comment letter on the Exposure Draft *Financial Instruments with Characteristics of Equity*, issued by the IASB in November 2023 (the ‘ED’); and
  - (b) discuss and recommend to the EFRAG FRB a final comment letter on the ED.

#### Overview of outreach activities

- 2 Refer to the overview of outreach activities in agenda paper 01-02 from paragraphs 4 to 30.

#### Overview of comment letters received

- 3 Refer to the executive summary of the comment letters received in agenda paper 01-02 from paragraphs 32 to 71. At the time of writing, 18 comment letters have been received.

#### Key changes to EFRAG’s Comment Letter

IASB questions	Significant changes made to EFRAG’s comment letter compared to EFRAG’s draft comment letter
Question 1 - The effects of relevant laws or regulations (paragraphs 15A and AG24A–AG24B of IAS 32)	<ul style="list-style-type: none"> <li>• General change of EFRAG’s initial position</li> <li>• Expressed significant concerns on the IASB proposals on their current status as it seems to solve limited issues but risks of raising many new others and unintended consequences</li> <li>• In particular, instruments for which some or all key parameters derive from law and regulation and some cooperative banks’ products</li> </ul>
Question 2 - Classification: Settlement in an entity’s own equity instruments (including fixed-for-fixed condition in IAS 32)	<ul style="list-style-type: none"> <li>• No significant changes to the initial position</li> <li>• Suggested that the IASB should provide additional examples and guidance on preservation adjustments and passage-of-time adjustments to help with implementation</li> </ul>

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IASB questions	Significant changes made to EFRAG’s comment letter compared to EFRAG’s draft comment letter
	<ul style="list-style-type: none"> <li>Propose additional guidance regarding which functional currency should the reference point be in determining whether a derivative is denominated in a foreign currency</li> </ul>
Question 3 – Obligation to purchase an entity’s own equity instruments	<ul style="list-style-type: none"> <li>Added a paragraph explaining that the issues are too broad and complex for the current narrow-scope project</li> <li>Added a further argument against the treatment at initial recognition proposed by the IASB (reference to paragraphs BC11, BC68 and AG29 of the existing IAS 32)</li> <li>Correction of the initial EFRAG position to explore the net presentation -deleted in the cover letter on the basis that no feedback supported it and considering emphasis that this change would be too fundamental for this narrow scope-project.</li> </ul>
Question 4 - Contingent settlement provisions	<ul style="list-style-type: none"> <li>Continued to maintain that there are mixed views on the measurement of financial instruments with contingent settlement provisions and it is difficult to address complex measurement issues within narrow scope amendments.</li> <li>Also indicated that if the IASB proceeds with the measurement proposals, it puts pressure on the definition of “present value of the redemption amount” and that the IASB would have to provide more guidance in this area, including interaction with IFRS 9 and IFRS 13</li> </ul>
Question 5 - Shareholder discretion	<ul style="list-style-type: none"> <li>Indicated support for the IASB’s proposals (previously EFRAG indicated that it was unsure of the factors and would conduct testing to gather evidence on the impact of the factors)</li> <li>Indicted that in order to help with the high level of subjectivity, the IASB should provide illustrative examples or specific principles relating to the application of the factors</li> </ul>
Question 6 - Reclassification of financial liabilities and equity instruments	<ul style="list-style-type: none"> <li>Whilst maintaining our disagreement with the IASB’s proposals, added a paragraph explaining that stakeholder feedback reflected that assessing at each reporting period for ‘passage-of-time changes’ is not an issue and is needed for the disclosures in any case.</li> </ul>
Question 7 - Disclosures	<ul style="list-style-type: none"> <li>Mentioned the support from users on the disclosure requirements.</li> <li>Agreed with the proposed disclosure requirements except for significant operational concerns relating to the disclosures on liquidation (the nature and priority of claims against the entity on liquidation; and terms and conditions related to priority on liquidation) and the terms and conditions of financial instruments that determine their classification as financial liabilities or equity instruments.</li> <li>Expanded the reasons for the significant operational concerns stated above.</li> </ul>

IASB questions	Significant changes made to EFRAG’s comment letter compared to EFRAG’s draft comment letter
Question 8 – Presentation	<ul style="list-style-type: none"> <li>Added a paragraph explaining that, given concerns from many stakeholders, the IASB should further clarify the benefits of its proposals for the users and should provide additional application guidance and illustrative examples.</li> </ul>
Question 9 – Transition	<ul style="list-style-type: none"> <li>No changes made.</li> </ul>
Question 10 - Disclosure requirements for eligible subsidiaries	<ul style="list-style-type: none"> <li>Mentioned that the significant operational issues relating to Question 7: Disclosures would also be relevant in this section.</li> </ul>

### Agenda papers

- 4 In addition to this cover note, the agenda papers for this session are:
- (a) Agenda paper 01-02 – Comment letter analysis and outreach feedback;
  - (b) Agenda paper 01-03 – Updated EFRAG comment letter (clean);
  - (c) Agenda paper 01-04 – Updated EFRAG comment letter (marked-up compared to EFRAG’s draft comment letter); and
  - (d) Agenda paper 01-05 – Summary of EFRAG’s survey results.
- 5 In addition, please find a link [here](#) to all the comment letters received that are on EFRAG’s website (section ‘Documents’).

#### Question for EFRAG FR TEG members

- 6 Does EFRAG FR TEG agree to recommend to the EFRAG FRB a final comment letter on the ED?