JOINT OUTREACH EVENT FINANCIAL INSTRUMENTS WITH CHARACTERISTICS OF EQUITY

AMSTERDAM

20 NOVEMBER 2018

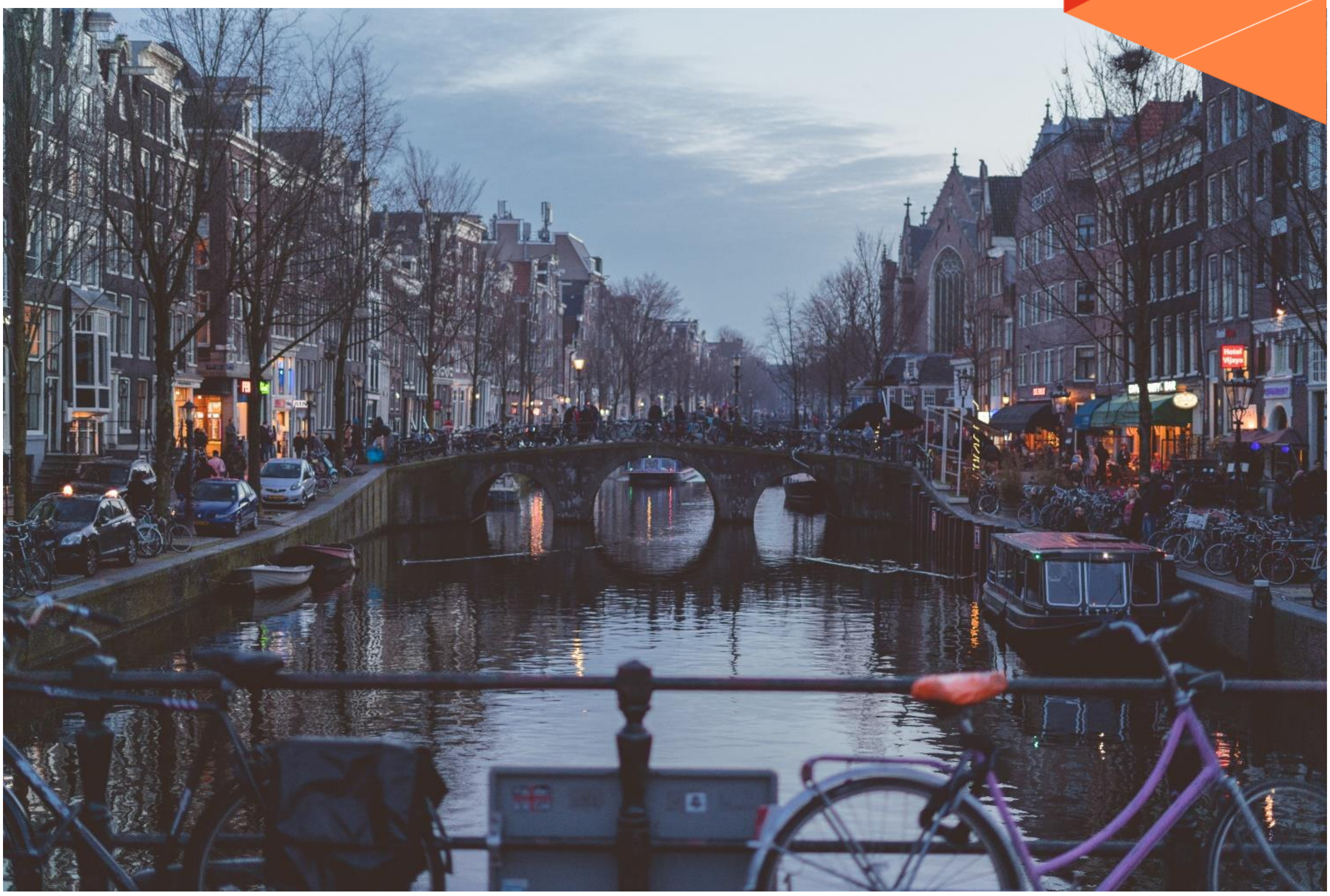

Photo by [Leif Niemczik]

This report has been prepared for the convenience of European constituents by the EFRAG Secretariat and has not been subject to review or discussion by neither the EFRAG Board nor the EFRAG Technical Expert Group. It has been reviewed by IASB® staff and has been jointly approved for publication by representatives of EFRAG, the Dutch Accounting Standards Board and Eumedion who attended the outreach event.

Introduction

EFRAG together with the Dutch Accounting Standards Board, Eumedion and the IASB® organised an event covering the IASB's Discussion Paper *Financial Instruments with Characteristics of Equity* ('DP'). This report has been prepared for the convenience of European constituents to summarise the outreach event held in Amsterdam on 20 November 2018.

Peter Sampers (Chairman Dutch Accounting Standards Board) opened the outreach event and welcomed EFRAG, the IASB, Eumedion and the participants.

At the conference, Kumar Dasgupta (IASB Technical Director) introduced the DP.

Subsequently, Patricia McBride (EFRAG Technical Director) introduced EFRAG's tentative view in its Draft Comment Letter to the IASB.

The two presentations were followed by a general discussion.

Summary of observations

Objective, Scope and Challenges

Participants highlighted the fact that introducing new concepts maybe helpful in resolving existing issues, but it could introduce unintended consequences and financial engineering which will in turn create new questions.

When asked '*Should we be fine-tuning IAS 32* Financial Instruments: Presentation *or pushing the reset button?*' there were mixed views. Some participants regarded the proposals in the DP as creating too much change from IAS 32. Other participants noted that the existing issues could have been solved with additional disclosure without the introduction of the new terminology.

Participants highlighted the differences between the Conceptual Framework and the DP and expected more conceptual reasons for the split between debt and equity.

The IASB's Preferred Approach

Participants questioned the importance of liquidation and identified the need for information on what time period should be considered from a valuation perspective. They further highlighted that liquidation can take many forms. It was noted that investors find information on liquidation important and that jurisdictional differences should be considered.

Participants unanimously voted that liquidation is irrelevant to classifying financial instruments when the entity is a going concern. Participants questioned why the amount feature is needed and acknowledged that it would be a fundamental change from IAS 32.

Classification

Participants noted that one of the hot topics is the fact that certain perpetual debt instruments with a cumulative deferral feature will be classified as a liability under the proposals in the DP. They asked whether it is sufficient to look at market expectations when classifying instruments as liabilities. It was acknowledged that the amount feature causes cumulative perpetual debt instruments to be classified as liabilities. Therefore, the payment of the cumulative return upon liquidation causes the change in classification and neither market expectations nor economic incentives of the issuer are taken into account for classification purposes under the proposals in the DP.

Presentation

With regards to the proposed fair value attribution approach, participants highlighted the practical challenges that might arise from:

- calculating the fair value in cases where cash flow projections had to be used; and
- disclosing information on how the value has been calculated.

They also noted that applying the fair value attribution approach would be costly and onerous.

When asked whether attribution of total comprehensive income provides useful information, participants questioned the meaning of '*useful information*' and noted that information disclosed should be transparent and relevant. They highlighted that attribution of total comprehensive income is an area that can be useful but noted that disclosing the fair value of equity would not.

Participants discussed the use of other comprehensive income introduced by the proposals under the DP and questioned if the IASB considered the distinction between items presented directly in total comprehensive income and those that are purely equity.

Disclosure

Participants indicated that they are not clear on the disclosure proposals in the DP. Participants acknowledged that disclosures for the priority of claims are important, but the priority depends on the jurisdiction in which an entity operates. They also noted that the disclosure requirements under the proposals of the DP around derivatives are more extensive than before.

Participants questioned the scope of the disclosure requirements in the DP and the interaction with IFRS 7 *Financial Instruments: Disclosure*. They highlighted that IFRS® Standards should govern the disclosures of group structures and intercompany financial guarantees currently given in an entity's prospectus but noted that such disclosures might be outside the scope of the FICE project. They noted that the disclosure of terms and conditions are part of the proposals under the DP and acknowledged that the level of aggregation at which this disclosure should be provided could be challenging.

Closing remarks

Peter Sampers thanked participants and closed the event.