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DESMISTIFYING FICE

A CLEARER PICTURE ON CLASSIFICATION



This bulletin is issued by the European Financial Reporting Advisory Group (EFRAG). The publication of bulletins is part of EFRAG's strategy to stimulate debate within Europe and clarify the IASB discussions on the distinction between debt and equity. Any views expressed are tentative. EFRAG will develop its final views after considering the feedback received from its constituents.

Due to the nature of the bulletin, EFRAG has not included questions to constituents. However, constituents may provide their comments by 3 December 2018 through EFRAG's website [here](#) or by post to:

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All comments received will be placed on the public record unless confidentiality is requested.

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Executive Summary

- ES1 In June 2018, the IASB issued the Discussion Paper DP/2018/1 *Financial Instruments with Characteristics of Equity* ('the DP'). In the DP, the IASB describes its preferred approach for distinguishing financial liabilities from equity instruments.
- ES2 The IASB's preferred approach would not fundamentally change the existing classification outcomes. For the most common financial instruments (e.g. ordinary shares, non-cumulative preference shares and bonds), the classification would not change.
- ES3 For non-derivatives, the classification changes are mainly related to claims for a fix amount (amount feature) for which payment is only due on liquidation (e.g. financial instrument with cumulative features).
- ES4 For derivatives, the classification changes are mainly related to net-share settled derivatives and instruments that currently meet the foreign currency rights issue exception.
- ES5 EFRAG expects that the IASB's proposals would mainly affect entities that issue complex instruments, like financial institutions.

Chapter 1: Background

Purpose of this bulletin

- 1.1 The IASB's DP describes its preferred approach for distinguishing financial liabilities from equity. In order to help constituents to understand the IASB's preferred approach and help constituents participating in the debate around the DP, EFRAG has issued this bulletin which explains, in simple words, the proposed classification criteria included in the DP.

Why the IASB published a DP

- 1.2 The IASB has considered how to distinguish liabilities and equity as respondents to the IASB's 2015 Agenda Consultation said that the requirements in IAS 32 *Financial Instruments: Presentation*:
- a) Are, in some cases, complex, poorly understood and difficult to apply;
 - b) Lead to classification outcomes that do not reflect the economic substance of particular financial instruments common in some jurisdictions;
 - c) Have, over the years, been amended in a piecemeal fashion that has raised practical issues, introduced exceptions and resulted in diversity in practice; and
 - d) Are not robust enough to address the increasing complexity and sophistication of some financial instruments being issued.
- 1.3 In addition, submissions to the IFRS Interpretations Committee ('IFRS IC') have revealed challenges in distinguishing financial liabilities from equity instruments in IAS 32 for more complex financial instruments. Such challenges include:
- a) Application of the fixed-for-fixed condition to derivatives on own equity;
 - b) Application of the requirements in IAS 32 to recognise a 'gross' liability for derivatives that include an obligation for the entity to purchase its own ordinary shares, including the repurchase of non-controlling interest shares in a subsidiary (e.g. put options written on non-controlling interests); and
 - c) Bonds that pay interest at the discretion of the issuer and mandatorily convert to a variable number of the issuer's own shares if the issuer breaches a specified condition.
- 1.4 The DP states that while the objective of the project is to respond to challenges in distinguishing financial liabilities from equity instruments when applying IAS 32, any potential solution should limit unnecessary changes to classification outcomes that are already well understood.
- 1.5 The DP notes that the changes to the classification principles might not be sufficient to resolve all the challenges the IASB has identified. Enhancing presentation and disclosure requirements could, according to the DP, help address some of those challenges.
- 1.6 The DP is therefore also providing some views on presentation and disclosures. These requirements are explained in the EFRAG bulletin *Visualising FICE*. When assessing how useful the information resulting from the approach described in the DP would be, it would therefore also be relevant to take the information provided by the proposed presentation and disclosures into account.

Scope of the discussion paper

- 1.7 Similar to IAS 32, the classification principles presented in the DP (only):
- a) Apply to rights and obligations arising from contracts; and
 - b) Exclude rights and obligations to receive, transfer or exchange types of economic resources other than cash or other financial instruments.
- 1.8 Therefore, while the application of the IASB's preferred approach might change the classification of a financial instrument as a financial asset, financial liability or an equity instrument, the scope of IAS 32 would remain unchanged.

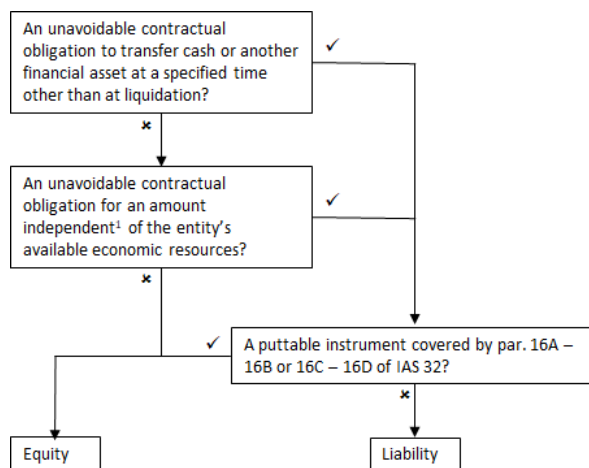
Chapter 2: Classification of non-derivative financial instruments

IASB's general approach for classification of financial instruments

- 2.1 The DP includes related but separate guidance on the classification of:
- a) Non-derivative financial instruments;
 - b) Compound instruments (e.g. bonds that can be converted to equity) and derivatives that include an obligation to extinguish an entity's own equity instruments; and
 - c) All other derivatives.
- 2.2 The overall classification principle of the IASB's preferred approach is, in simple words, that an instrument is classified as equity only if:
- a) The entity is not required to make any payments before liquidation; and
 - b) The amount to be paid on liquidation depends on the entity's own performance or performance of its share price.
- 2.3 This section describes the approach for non-derivative financial instruments described in section 3 of the DP. The approaches for the other instruments are described in the following section.

IASB's approach for classification of non-derivatives

- 2.4 The approach described in the DP for the classification of non-derivative financial instruments is illustrated below.



1: According to the DP an amount that potentially could exceed the entity's available economic resources should be considered to be independent of the entity's available economic resources.

An unavoidable obligation to transfer economic resources at a specified time other than at liquidation (timing feature)

- 2.5 According to the approach described in the DP, a claim is a liability if it contains an unavoidable obligation to transfer economic resources at a specified time other than at liquidation (i.e. the entity is required to pay before liquidation).
- 2.6 The DP states that information about obligations to transfer economic resources at a specified time is relevant to assess whether an entity will have sufficient economic resources to meet its obligations as and when they fall due (i.e. assessment of liquidity).
- 2.7 The DP explains that 'a specified time' could be a specified date (or dates) on which interests (e.g. coupon of a bond) or the principal should be paid. It can also be 'on demand' or when a specified event occurs.
- 2.8 If liquidation is at a specified time or at the option of the person or entity to which the entity is obligated to transfer economic resources, the criterion is met. In those cases, the obligation is accordingly a financial liability (unless it meets the exceptions in paragraphs 16A - 16B or 16C -16D of IAS 32).

An unavoidable obligation for an amount independent of the entity's available economic resources (amount feature)

- 2.9 A claim that contains an unavoidable obligation for an amount independent of the entity's available economic resources would be a liability according to the approach described in the DP.
- 2.10 The DP states that information about obligations for an amount independent of the entity's available economic resources is relevant to assess the risk that the amount of the obligation may exceed the entity's available economic resources (assessment of balance-sheet solvency).

- 2.11 In the criterion ‘an amount’ refers to how the amount of an obligation is specified. ‘an amount’ can thus be specified as a fixed number of euros (or another currency) or it can be ‘an amount’ linked to an index or a proportionate share of the entity’s economic resources after deducting the economic resources required to meet all other claims. In the latter case, the ‘amount’ would not be independent of the entity’s available economic resources. The ‘amount’ is not the fair value of the financial instrument. The ‘amount’ of a financial instrument with a contractual obligation to transfer EUR 100 is thus EUR 100 regardless of whether the fair value is less as a result of the entity’s credit risk or the fact that the payment is not due for (say) 10 years. A financial instrument with a contractual obligation to transfer a fixed amount of euros would therefore always be independent of the entity’s available economic resources.
- 2.12 An entity’s available economic resources is defined as the total recognised and unrecognised assets of the entity that remain after deducting all other recognised and unrecognised claims against the entity (except for the financial instrument in question).
- 2.13 The DP specifies that ‘an amount’ that would be dependent of the entity’s available economic resources, cannot exceed the available economic resources of the entity. A claim that would require the entity to transfer 110% of its economic resources would therefore be a liability. The same would be the case if the amount to be transferred partly depends partly on the entity’s available economic resources and partly on other factors which could cause the amount to exceed the entity’s available economic resources.
- 2.14 Despite the guidance included in the DP on when an amount is independent of an entity’s available economic resources, EFRAG expresses concerns in its draft comment letter in response to the DP that the introduction of this new terminology might create confusion. Particularly, EFRAG notes that variables that are partly dependent on the entity’s economic resources could, against the intention of the DP, be considered not to be independent of the entity’s available economic resources.

Financial instruments with more than one obligation or settlement outcome


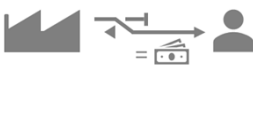
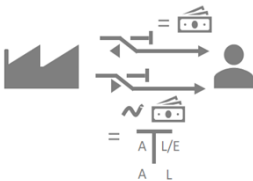
- 2.15 Financial instruments may include several obligations. For example, an instrument may require the entity to pay an amount each year and an amount at liquidation. Such an instrument has two obligations and the criteria above should be applied to each of those obligations (see classification details below).
- 2.16 A non-derivative financial instrument may also contain more than one possible settlement outcome (deliver cash or own shares) that might depend on future events, or on the holder or issuer exercising rights. If an entity does not have the unconditional contractual right to avoid a settlement outcome that would be classified as a financial liability according to the criteria above, the entity should first identify that unavoidable obligation (e.g. deliver cash). If another possible settlement outcome would not meet the criteria for being classified as a financial liability (e.g. deliver fixed number of shares), the entity should consider whether the financial instrument is a compound financial instrument and apply the requirements described in Chapter 3 for compound financial instruments.

A puttable instrument covered by paragraphs 16A – 16B or 16C – 16D of IAS 32



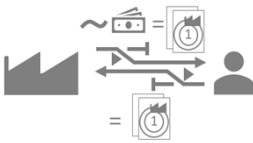
- 2.17 The DP proposes to continue to classify as equity instruments that meet the criteria in paragraphs 16A – 16B or 16C – 16D of IAS 32. The requirements are relevant for:
- obligations of the entity to buy back instruments that are subordinate to all other classes of instruments; and
 - obligations to deliver to another party a pro rata share of the net assets of the entity on liquidation when liquidation is at a specified time or at the option of the person or entity to which the entity is obligated to transfer economic resources.

Illustrative examples

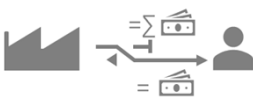
- 2.18 The table below includes three examples of claims that are classified as equity according to IAS 32 and will also be classified as equity under to the approach described in the DP.


	Description	Explanation for classification
	Ordinary shares with discretionary dividends.	The only unavoidable obligation the entity has is to pay an amount at liquidation which depends on the entity's available economic resources.
	An undated bond or irredeemable non-cumulative preference share with a stated coupon or dividend amount that is a specified rate of return or a specified amount of cash. Payment of the coupon or the dividend is at the option of the entity and the coupon or dividend amount is cancelled if the coupon or dividend is not paid by the entity. At liquidation, the entity is not obliged to pay anything.	The entity is neither required to transfer cash or another financial asset at a specified time nor obliged to transfer any amount at liquidation.
	A claim that gives the holder the right to receive a fixed amount if the entity chooses to pay a dividend. At any time, the holder can ask the entity to settle the claim by transferring a pro-rata share of net assets. The instrument entitles the holder to a pro rata share of the entity's net assets on liquidation and the claim is the most subordinate.	The entity has an unavoidable obligation to transfer cash at a specified time (when the holder of the claim would require the entity to do so). However, in the example, it is assumed that all the criteria in paragraphs 16A – 16B of IAS 32 are met.

- 2.19 The table below includes three examples of claims that are classified as liabilities according to IAS 32 and will also be classified as liabilities according to the approach described in the DP.

	Description	Explanation for classification
	4-year zero-coupon bond with a face value on maturity of EUR 100.	The entity has an unavoidable contractual obligation to transfer cash at a specified time other than at liquidation. In addition, a fixed amount does not depend on the entity's available economic resources and the fixed amount may potentially exceed the entity's available economic resources.
	A share-settled bond which requires the entity to deliver a variable number of its own shares with a total value equal to EUR 100 in two years.	The entity is only required to transfer own shares and not economic resources. However, the amount of the obligation does not change in response to changes in the entity's available economic resources, introducing the risk that the entity may not be able to meet its obligation. The amount is therefore independent of the entity's available economic resources.
	Preference shares puttable at fair value.	Although it is a claim for an amount that is dependent on the entity's available economic resources, the entity has an unavoidable contractual obligation to transfer cash at a specified time other than at liquidation.

- 2.20 The table below includes two examples of claims that will be classified differently under the approach described in the DP compared with the categorisation under IAS 32.

	Description	Explanation for classification
	<p>An undated cumulative bond or irredeemable cumulative preference share with a stated coupon or dividend amount that is a specified rate of return or a specified amount of cash.</p> <p>The entity will have to pay the accumulated amount at liquidation, at the latest.</p>	<p>Under IAS 32 this instrument is classified as equity.</p> <p>Under the DP it will be classified as a liability. The entity can postpone the payment until liquidation and does therefore not have an unavoidable contractual obligation to transfer cash or another financial asset at a specified time other than at liquidation. However, at liquidation or earlier, the entity has to pay an amount that does not change in response to changes in</p>

	Description	Explanation for classification
	<p>A share with a dividend feature that does not accumulate but is reset periodically when not paid (e.g. callable preferred shares with a discretionary dividend). With this instrument, the entity has the option not to pay the dividend in a given year, but if the entity does not pay in a year, the percentage on which the dividend should be based is increased at a predetermined rate (with the effect that it is in fact cumulative). The entity will have to pay dividend at liquidation.</p>	<p>Under IAS 32 this instrument is classified as equity. Under the DP it will be classified as a liability. The entity can postpone payment until liquidation and does therefore not have an unavoidable contractual obligation to transfer cash or another financial asset at a specified time other than at liquidation. However, at liquidation or earlier, the entity has to pay an amount that is independent of its available economic resources. The fact that the dividend rate increases at a specified rate when it is not paid results in an amount that is independent of the entity's available economic resources.</p>

- 2.21 The examples shows that the classification outcomes would not change for the most common non-derivative financial instruments. The classification changes are mainly related to claims for a fixed amount (amount feature) which payment is only required on liquidation (e.g. financial instrument with cumulative features).

Chapter 3: Classification of derivatives on own equity and compound financial instruments

- 3.1 Derivatives on own equity such as financial options, futures and forwards allow the entity or the investor to buy or sell the entity's share at some future date at a guaranteed price. One simple example is an entity's obligation under a forward contract to purchase its ordinary shares for a fixed amount of cash at a future date. Such instruments can be settled differently, according to the entity and investor's needs: physically settled (cash for shares), net-cash settled (i.e. settled with cash for the net position) or net-share settled (i.e. settled with own shares for the net position).
- 3.2 The DP distinguishes between:
- Asset/equity exchanges:** contracts to sell own ordinary shares to investors in the future. (e.g. written call options, purchased put options and forward contracts to sell own shares to investors);
 - Liability/equity exchanges:** contracts to acquire own ordinary shares from investors in the future and contracts to convert debt into equity (e.g. written put options and forwards to buy one shares to investors and embedded options in convertible bonds).


- 3.3 Entities also issue compound instruments, such convertible as bonds, which give the holder the option to receive shares of the entity, instead of cash, on maturity.

Contracts to sell own shares to investors in the future (asset/equity exchanges)

- 3.4 According to the DP, a derivative on own equity should be classified in its entirety. This means that the individual legs of the exchange ('obligation to sell own shares' and 'right to receive cash') would not be separately classified. The classification principle described in paragraph 2.2 above are then applied to the derivatives considering together the rights and obligations of the instrument (i.e. to the net amount of the derivative). Accordingly, a derivative on own equity would be classified as a financial asset or a financial liability if:
- It is net-cash settled – the derivative may require the entity to deliver or receive cash or another financial asset at a specified time before liquidation; and/or
 - The 'net amount' of the derivative is affected by a variable that is independent of the entity's available economic resources.
- 3.5 The two criteria are described further in the sections below.

Net-cash settlement

- 3.6 An entity and an investor may enter into a derivative contract which is net-cash settled. In such cases, there is no receipt or delivery of the entity's own shares upon settlement of the contract. Instead, the contract is settled with cash.
- 3.7 For net-cash settled derivatives, the criterion related to the timing of the transfer applies in a similar manner as for non-derivatives. However, when considering derivatives, it should be taken into account that the classification could be a derivative financial asset rather than a financial liability if a derivative could result in the entity receiving cash.
- 3.8 If a derivative on own equity is not net-cash settled but is either physically settled or net-share settled, the criterion would not be met. In those cases, the instrument could then be equity if the criterion related to the dependence of the 'net amount' on the entity's available economic resources would also not be met.
- 3.9 The criterion would result in the instrument listed below being classified as a financial liability or a financial asset (which would also be the case under IAS 32):

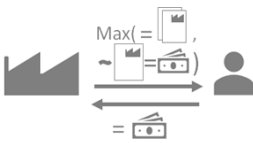
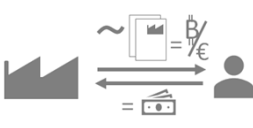
	Description	Explanation for classification
	A net-cash settled derivative promising the delivery of a cash amount equal to the fair value of 10 of its own ordinary shares in exchange for a fixed amount of EUR 100 on maturity date.	As the derivative is net-cash settled, the entity has an obligation to deliver (or receive) cash at a specified time other than at liquidation.

The 'net amount' of the derivative is affected by a variable that is independent of the entity's available economic resources



- 3.10 When assessing whether the net amount of the derivative is affected by a variable that is independent of the entity's available economic resources, the combined effect of both legs (i.e. rights and obligations) of the derivative should be considered. If the net amount is affected by just one variable that is independent of the entity's available economic resources, the instrument would be classified as a financial asset or a financial liability according to the approach described in the DP.
- 3.11 The DP notes that the following variables would affect the net amount of a derivative on own equity in a way that is independent of the entity's available economic resources, which would consequently preclude equity classification:
- a) *Currency (other than the entity's functional currency).* Accordingly, when the strike price of a physically written call option on own shares is set in a foreign currency, the option would be a financial asset or a financial liability. When an entity enters into a derivative contract on equity instruments of another entity within the same group, the functional currency of the entity whose equity instruments form the underlying of the derivative should be the reference point according to the DP.
 - b) *Fixed units of financial assets that are linked to an independent variable.* Accordingly, an instrument that would transfer 100 of an entity's own shares in exchange for an amount of cash calculated to equal the value of 100 ounces of gold would be a liability according to the DP.
 - c) *Variables that depend on the entity's economic resources before deducting all other claims against the entity.* Accordingly, a derivative that would transfer a variable number of an entity's own shares in exchange for an amount that would depend on the reported EBIT would be a financial asset or a financial liability according to the DP.
 - d) *Variables that represent a leveraged time value of money or a time value of money unrelated to the derivative instrument.* Accordingly, a derivative that would require the entity to transfer a fixed amount of own equity instruments in one year in return for EUR 100 plus the average interest on corporate bonds in the EU, would be a financial asset or a financial liability.
- 3.12 On the other hand, the DP notes that the following variables could not affect the net amount of a derivative on own equity in a way that is independent of the entity's available economic resources, which would not preclude equity classification:
- a) *Variables that reflect compensation for the time value of money that is relevant to the derivative.* Accordingly, a derivative that would transfer either tomorrow or in one year a fixed number of the entity's own shares for EUR 100 (tomorrow) or EUR 102 (in one year), would be an equity instrument if the increase from 100 EUR to 102 EUR is based solely on a relevant interest rate reflecting the time value of money.

- b) *Anti-dilution provisions to the extent they do not introduce another independent variable.* The DP states that it does not matter whether the provision only adjusts the number of shares to be delivered when there is an increase in the total number of shares or also in cases where there is a decrease in the total number of shares. Also, it does not matter whether the anti-dilution provision is triggered for all or only some dilution events. Accordingly, a derivative that would require the entity to transfer the higher of 100 shares or 4 % of all issued shares in return for a fixed amount of EUR 100 would be an equity instrument.



3.13 The criterion would result in the two instruments listed below being classified as a financial liability or a financial asset (which would also be the case under IAS 32):

	Description	Explanation for classification
	A derivative that requires the entity to deliver 100 of its own shares or, in the event of dilution, a variable number of own shares worth EUR 100 in return for EUR 101.	Although the guarantee that the shares delivered will at least have the value of EUR 100 could be seen as an anti-dilution provision, the obligation to deliver EUR 100 worth of own shares is independent of the entity's available economic resources (as the amount may exceed the entity's economic resources).
	A contract to deliver a variable number of shares linked to the price on Bitcoins and to receive a fixed amount of cash (in the functional currency of the entity)	The 'net amount' would be affected by a variable (the price on Bitcoins) which is independent of the entity's available economic resources.



3.14 Both the approach explained in the DP and the requirements in IAS 32 would result in the following two instruments being classified as equity:

	Description	Explanation for classification
	A derivative gives the entity the option to deliver a fixed amount of own equity instruments against a fixed amount of cash (in its functional currency).	No matter whether the entity will use the option or not, the settlement outcome does not have the feature(s) of a financial asset or a financial liability as the contract will neither be net-cash settled nor result in a 'net amount' that is affected by a variable that is independent of the entity's available economic resources.
	A derivative gives the counterparty the option to pay a fixed amount of cash (in the entity's functional currency) and receive a fixed number of shares in the company.	Same explanation as above.

- 3.15 Below are listed some instruments that would be classified differently under the approach in the DP and the requirements in IAS 32.

	Description	Explanation for classification
	<p>A gross-settled derivative which gives all existing shareholders a right to buy additional shares for cash in a currency that is not the functional currency of the entity. The contract offers the shares at a discount on a pro-rata basis of the shareholders' current share holdings.</p>	<p>Under IAS 32 the instrument is classified as equity. Under the approach in the DP, it would be a financial asset or liability. The 'net amount' is affected by the exchange rate of a foreign currency. Thus, the net amount is affected by a variable that is independent of the entity's available economic resources.</p>
	<p>A net-share settled derivative to deliver a fixed number of own shares in exchange for receiving a variable number of own shares with a total value equal to a fixed amount of the entity's functional currency.</p>	<p>Under IAS 32, the instrument is classified as a financial asset or a financial liability. Under the approach in the DP it would be equity. The derivative is not net-cash settled and does not result in a transfer of economic resources (as own shares are not considered to be an economic resource). The 'net amount' is also not affected by a variable that is independent of the entity's available economic resources.</p>

- 3.16 The approach in the DP would provide guidance on some instruments for which IAS 32 does not include guidance. This includes the following two instruments:

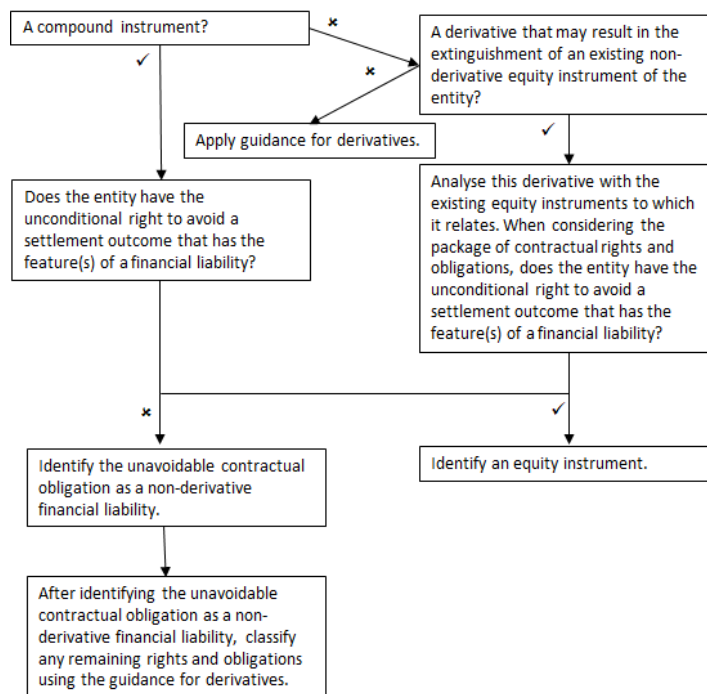
	Description	Explanation for classification
	<p>A contract to deliver a fixed number of shares in a subsidiary and receive a fixed amount in the (parent) entity's functional currency, which is different from the subsidiary's functional currency.</p>	<p>The 'net amount' would be affected by a variable (the parent's functional currency) which is independent of the subsidiary's available economic resources. Under the approach in the DP, this instrument would be classified as a financial liability.</p>
	<p>A derivative to deliver a fixed number of shares in a subsidiary and receive a fixed amount in the subsidiary's functional currency, which is different from the parent's functional currency.</p>	<p>In the consolidated financial statements this would be equity as the 'net amount' would only depend on the subsidiary's available economic resources. This applies even if the consolidated group financial statements are presented using another currency. Under the approach</p>

Description	Explanation for classification
	in the DP, this instrument would be classified as equity.

- 3.17 When derivatives have settlement options (e.g. the entity has the option to deliver own shares or cash), the derivative can only be classified as equity if the entity has an unconditional right to avoid a settlement outcome that has the feature(s) of a financial asset or a financial liability. In other cases, the derivative in its entirety is classified as a financial asset or a financial liability. It follows from the DP that the entity does not have an unconditional right to avoid a settlement outcome that has the features(s) of a financial asset or a financial liability if such a right is conditional on the entity's future revenues, profit or loss, financial position ratios or own share price.
- 3.18 In its draft comment letter, EFRAG questioned the relevance of having financial instruments that currently meet the foreign currency rights issue exception in IAS 32 being classified as financial liabilities and net-share settled derivatives being classified as equity. EFRAG was also concerned that the proposed guidance for derivatives on own equity differs significantly from current guidance, particularly in terms of terminology.

Compound instruments, contracts to acquire own shares and contracts to convert debt into equity (liability/equity transactions)

- 3.19 The DP includes specific guidance for compound instruments (e.g. convertible bonds) and derivatives that may result in the extinguishment of non-derivative equity instruments (e.g. a derivative that converts shares to bonds). The process described in the DP is illustrated below.



3.20 The process described in the DP when classifying compound instruments (e.g. bonds that can be converted to equity) and derivatives that may result in an extinguishment of an existing non-derivative equity instrument of the entity (e.g. a derivative that converts shares to bonds) is illustrated below.

3.21 The process is further clarified in the example below.

3.22 A derivative obliges an entity to exchange 100 of its own ordinary shares on which no dividend is paid for 100 bonds in 3 months at the request of the current shareholder. The bonds will each be settled for EUR 1.1 after another 9 months. This is not a compound instrument, but a derivative that results in the extinguishment of existing shares (a non-derivative equity instrument). The entity will therefore have to analyse the derivative together with the 100 shares and consider the package of rights and obligations. In this case, the entity does not have the unconditional right to avoid a settlement outcome that has the features of a financial liability as it has to pay EUR 100 at a specified date (in one year) if the holder of the derivative wants to convert shares into bonds in 3 months. The entity accordingly identifies the obligation to pay EUR 110 in one year as a non-derivative financial liability. The option of the holder of the derivative to decide whether or not to convert is a remaining obligation of the entity. In reality, the shareholder is holding shares and has the option to change these to bonds. However, because the approach would identify a non-derivative financial liability (the bonds), the additional instrument that would be identified is an option for the holder to exchange bonds into shares. As the 'net amount' of this additional derivative is only affected by a variable that is dependent of the entity's available economic resources, the derivative would be classified as equity.

- 3.23 The case described above would be reflected in the financial statements similar to the case in which the entity had issued a bond which could be converted into shares at the option of the holder of the bond. This is the intention of the approach included in the DP. However, in its draft comment letter, EFRAG was not convinced that the accounting for a written put option on own shares that is issued together with ordinary shares should be the same as the accounting for a convertible bond.



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