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## **EFRAG Equity Instruments – Research on Measurement**

### **Cover Note**

#### **Objective**

- 1 The objective of this session is to obtain comments from EFRAG TEG on a first draft of a discussion paper on alternative measurement options for equity instruments ('the DP').

#### **Background**

- 2 As set out in the joint Board and TEG paper of 19 December 2018, the DP is in response to the request for technical advice from the European Commission received in June 2018. The request was to consider alternatives to fair value as the measurement basis for equity long-term investment portfolios of equity and equity-like instruments.
- 3 At the September 2018 EFRAG TEG meeting, 3 initial criteria to define the long-term investing was discussed, however, the majority of EFRAG TEG members were not in favour of developing a definition of long-term investing.
- 4 In November 2018, EFRAG TEG discussed possible alternative measurement models for equity instruments and members noted the limitations of the various alternative measurements. Some members suggested that certain of the alternatives, such as the linked approach, would only work only in limited circumstances.

#### **Outline of the Discussion Paper**

- 5 In order to meet the tight deadline of the request by the European Commission, a first draft of the DP is brought to this meeting in order to obtain preliminary views from EFRAG TEG. The format of the DP is envisaged as follows.

##### *Objective of the DP*

- 6 In the first part, the DP provides the context of the consultation including the background in the request from the European Commission and the prior EFRAG Research project on Equity Instruments – Recycling and Impairment.
- 7 The objective of the consultation will be to gather input from European constituents on the advantages and disadvantages of alternative measurement bases for equity instruments, with the purpose of depicting their returns in the context of a long-term investment management.

*Scope of application*

- 8 This part will be brought to EFRAG TEG in the January meeting. But here, the DP will specify what financial instruments the proposals would be applied to, and in particular refer to the current definition of equity instruments in IAS 32 *Financial Instruments: Presentation*, and the potential changes brought by the approach explored in the IASB's DP *Financial Instruments with Characteristics of Equity*.
- 9 Based on the outcome of the discussion at the January EFRAG TEG meeting, the DP will illustrate how EFRAG proposes to apply the notion of equity-like instruments.

*Alternative measurement bases and their significance*

- 10 The DP discusses alternative views of how returns from equity instruments could be depicted with a specific focus on the profit or loss. The alternatives under consideration include a view that gives prominence to:
  - (a) cash realisation;
  - (b) reflection of value changes in the reporting period; and
  - (c) apportionment of returns over the holding period.
- 11 These are then illustrated with an example. The DP also describes how these methods compare to technical endorsement criteria and what operational challenges they could present.

*Other aspects*

- 12 Although the Discussion Paper is not expected to include a proposed definition of 'long-term investment', it may include suggestions on metrics entities may use to communicate about their investment strategy and performance. This part will also be brought to EFRAG TEG in the January meeting.
- 13 The executive summary and questions to constituents will also be brought to EFRAG TEG at a future meeting.

**EFRAG Secretariat proposed responses/recommendation**

- 14 Considering the input received from constituents, the EFRAG Secretariat [provide a description of how you propose to address respondents' comments].

**Questions for EFRAG TEG**

- 15 Does EFRAG TEG have comments on the draft DP?
- 16 Are there additional topics or aspects that should be addressed in the consultation?

**Agenda Papers**

- 17 In addition to this cover note, agenda paper 03-02 – *Equity instruments – Alternative measurement approaches, EFRAG Discussion Paper* – has been provided for the session.