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RÉPUBLIQUE FRANÇAISE

AUTORITÉ DES NORMES COMPTABLES
5, PLACE DES VINS DE FRANCE
75573 PARIS CÉDEX 12
Phone 33 1 53 44 28 53
Internet http://www.autoritecomptable.fr/
Mel jerome.haas@anc.gouv.fr

Chairman

JH

n°108

Paris, the 17th September 2012

Mr Wayne UPTON
Chairman
IFRS Interpretations Committee
30 Cannon Street
LONDON EC4M 6XH

Re : Draft interpretation DI/2012/2 – Put options written on non-controlling interests

Dear Mr Upton,

I am writing on behalf of the Autorité des Normes Comptables (ANC) to express our views on the above-mentioned IFRS IC Draft Interpretation (DI).

The ANC considers that the accounting treatment of non controlling interest (NCI) put options is a complex issue to deal with to give a faithful representation of the economic phenomenon. This subject has raised lengthy and serious debates for several years both at IFRS IC and Board levels that demonstrate its complexity that a narrow and simple interpretation obviously fails to address properly.

The ANC strongly disagrees with the draft interpretation proposed by the Interpretations Committee for the main following reasons :

- The use of NCI puts raises several accounting issues that are not addressed by the DI (e.g. which component of equity should be debited at initial recognition? How to deal with the net result attributed or dividend distributed to NCI? How to deal with the inconsistency of treatment (equity vs P&L) upon the expiry of unexercised put options?). Having in mind all of these issues is helpful to have a full understanding of the economics of the operation which is a matter of transaction between majority shareholders and minority shareholders. The proposed DI does not address the broader questions related to NCI put options, as the IFRS IC is aware of (BC13).

- The recognition of a gross liability for puts written on NCI is not consistent with the economics of the transaction and will not provide useful information, as the IFRS IC acknowledged and agreed with in BC11.

- The argument that "*the remeasurement of that financial liability does not change the respective ownership interest of the parent or the NCI shareholder* (BC8)" is not convincing. A confusion is made between measurement matters and recognition or classification matters. Remeasurement rules follow the recognition or classification principles. The proper classification is driven by the nature and qualification of a transaction. Regarding NCI puts written by a parent entity, the purpose of the transaction is a change in the ownership of a subsidiary. Furthermore, we note that a change in the ownership is not defined under IFRS and that the IFRS IC did not reach a consensus on a similar question regarding the meaning of a "reduction in an entity's ownership interest in a foreign operation" under IAS 21 (see IFRIC Update September 2010).

- The proposed recognition of the change in P&L leads to counter-intuitive outcomes, i.e. when the controlled subsidiary's expected cash-flows improve, the parent company immediately recognises a loss due to the increase of the NCI debt. This counter-intuitive outcome is similar to the "own credit risk issue" for financial liabilities that the Board decided to exclude from profit or loss in the context of IFRS 9.

Therefore the ANC considers that the Committee should not proceed with the Draft Interpretation, in accordance with its original opinion, and asks the Board again to address the whole issue at a standard level in order to improve the current IFRS towards a more useful and economic outcome. This issue should be considered jointly with other critical issues related to the FICE project (e.g. fixed for fixed criterion).

Should the Committee or the Board decide to proceed with a short-term solution, the ANC would fully support the initial IFRS IC recommendation (described in BC11) to proceed with a narrow scope amendment of IAS 32 that would change the measurement basis of NCI puts in the parent's consolidated financial statements. As a result, the NCI puts would be measured on a net basis.

If this second solution were not retained, the ANC considers the recognition of the change in the measurement of the liability in equity to be the appropriate treatment. Such accounting treatment would be consistent with IAS 27R/IFRS3R and with IFRIC 17 *Distribution to non-cash assets to* owners which is based on the principle that transactions with owners in their capacity as owners should not be recognised in profit or loss (BC35-37). It would also be quite consistent with the Board's decision to exclude from P&L the fair value changes for financial liabilities due to own credit risk.

Our detailed comments on the DI are set out in the Appendix to this letter.

If you have any questions concerning our comments, we would be pleased to discuss them.

Yours sincerely,

Jérôme HAAS

Appendix

Detailed comments

Question 1 - Scope

The draft Interpretation would apply, in the parent's consolidated financial statements, to put options that oblige the parent to purchase shares of its subsidiary that are held by a non-controlling-interest shareholder for cash or another financial asset (NCI puts). However, the draft Interpretation would not apply to NCI puts that were accounted for as contingent consideration in accordance with IFRS 3 Business Combinations (2004) because IFRS 3 (2008) provides the relevant measurement requirements for those contracts.

Do you agree with the proposed scope? If not, what do you propose and why?

Nothwithstanding our strong disagreement with the DI, the ANC considers that the scope of the DI focuses on the relevant transactions (NCI puts written by a parent entity) that raise accounting difficulties under current standards.

We also note that the scope exception is consistent with IFRS 3 (2008) transition requirements.

Note that it is unclear to us whether put options written by a sister entity within a group or at a subconsolidation level are included in the scope of the DI. If a final Interpretation is issued, this should be clarified.

Question 2 - Consensus

The consensus in the draft Interpretation (paragraphs 7 and 8) provides guidance on the accounting for the subsequent measurement of the financial liability that is recognised for an NCI put. Changes in the measurement of that financial liability would be required to be recognised in profit or loss in accordance with IAS 39 Financial Instruments: Recognition and Measurement and IFRS 9 Financial Instruments.

Do you agree with the consensus proposed in the draft Interpretation? If not, why and what alternative do you propose?

The ANC considers that the accounting treatment of non controlling interest (NCI) put options is a complex issue to deal with to give a faithful representation of the economic phenomenon. This subject has raised lengthy and serious debates for several years both at IFRS IC and Board levels that demonstrate its complexity that a narrow and simple interpretation obviously fails to address properly.

The ANC strongly disagrees with the DI proposed by the Interpretations Committee for the main following reasons :

- The use of NCI puts raise several accounting issues that are not addressed by the DI (e.g. which component of equity should be debited at initial recognition? How to deal with the net result attributed and dividend distributed to NCI? How to deal with the inconsistency of treatment (equity vs P&L) upon the expiry of unexercised put options?). Having in mind all of these issues is helpful to have a full understanding of the economics of the operation which is a matter of transaction between majority shareholders and minority shareholders. The proposed DI does not address the broader questions related to NCI put options, as the IFRS IC is aware of (BC13).

- The recognition of a gross liability for puts written on NCI is not consistent with the economics of the transaction and will not provide useful information. We note that the IFRS IC agreed with this view as mentioned in BC11, "*the requirements in IAS 32, to measure particular derivatives written on an entity's own equity instruments on a gross basis at the present value of the redemption amount, does not result in useful information [...]. The Interpretations Committee agreed with that view [...].*"

- The argument that "*the remeasurement of that financial liability does not change the respective ownership interest of the parent or the NCI shareholder* (BC8)" is not convincing. A confusion is made between measurement matters and recognition or classification matters. Remeasurement rules follow the recognition or classification principles. The proper classification is driven by the nature and qualification of a transaction. Regarding NCI puts written by a parent entity, the purpose of the transaction is a change in the ownership of a subsidiary. Furthermore, we note that a change in the ownership is not defined under IFRS and that the IFRS IC did not reach a consensus on a similar question regarding the meaning of a "reduction in an entity's ownership interest in a foreign operation" under IAS 21 (see IFRIC Update September 2010).

- The proposed recognition of the change in P&L leads to counter-intuitive outcomes, i.e. when the controlled subsidiary's expected cash-flows improve, the parent company immediately recognises a loss due to the increase of the NCI debt. This counter-intuitive outcome is similar to the "own credit risk issue" for financial liabilities that the Board decided to exclude from profit or loss.

Therefore, the ANC asks the Committee not to proceed with the Draft Interpretation, in accordance with its original opinion, and asks the Board again to address the whole issue at a standard level in order to improve the current IFRS towards a more useful and economic outcome. This issue should be considered jointly with other critical issues related to the Financial Instruments with Characteristics of Equity (FICE) project (e.g. fixed for fixed criterion).

Should the Committee or the Board decide to proceed with a short-term solution, the ANC would otherwise fully support the initial IFRS IC recommendation (described in BC11) to proceed with a narrow scope amendment of IAS 32 that would change the measurement basis of NCI puts in the parent's consolidated financial statements. As a result, the NCI puts would be measured on a net basis. This solution would allow the improvement of the accounting for NCI put options on a timely basis without waiting for the comprehensive review expected in the context of the future research project on FICE. Contrary to the assertion made by the Board that "*the criticisms about the usefulness of the information provided by the gross measurement basis required by paragraph 23 in IAS 32 are equally applicable to all put options and forward purchase contracts written on an entity's own equity (and not only to NCI puts)*", the ANC considers that NCI put options raise specific questions that need specific solutions. The use of NCI puts is indeed not similar to other options written on own equity instruments (NCI puts are privately negotiated, not standardised contracts, involve a parent entity with the minority interest of a subsidiary, arise in the context of business combinations,...).

If the above solution were not retained, the ANC considers the recognition of the change in the measurement of the liability in equity to be the appropriate treatment. Such accounting treatment would be consistent with IAS 27R/IFRS 3R and with IFRIC 17 *Distribution to non-cash assets to* owners which is based on the principle that transactions with owners in their capacity as owners should not be recognised in profit or loss (BC35-37). It would also be quite consistent with the Board's decision to exclude from P&L the change in of fair value for financial liabilities due to own credit risk.

Question 3 - Transition
Entities would be required to apply the draft Interpretation retrospectively in accordance with IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors.
Do you agree with the proposed transition requirements? If not, what do you propose and why?

Nothwithstanding our strong disagreement with the DI, the ANC generally supports retrospective application which is usually relevant for new interpretations or standards unless it is impracticable to implement them.