IASB
Columbus Building
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Canary Wharf
London
UK

January 7, 2019

Ref: Discussion paper "Financial Instruments with Characteristics of Equity"

Dear Mr Hoogervorst,

We are pleased to have the opportunity to comment on the Discussion Paper – Financial Instruments with Characteristics of Equity (the DP).

The IASB has correctly identified the challenges presented by the current IAS 32, notably the accounting treatment for NCI puts and difficulties of putting into practice the fixed-for-fixed condition for equity instruments.

In addition to the challenges identified, an issue which is frequently cited by our members is one that is not directly related to IAS 32 but is a consequence of it. The issue is that of the scope of application of the FVOCI option on equity instruments held (an option governed by the conditions in paragraph 5.7.5 of IFRS 9 for equity instruments, but which is not permitted for instruments eligible for presentation in equity by dint of the "puttable instruments exception" in IAS 32 paragraphs 16A-16D).

Concerning the proposed solutions to the identified challenges, we share EFRAG's tentative view (quoted below) about the risks and uncertainties which could be mechanically induced by the introduction of new notions and definitions without their superiority being clearly identified.

"More generally, EFRAG notes that the approach in the DP introduces completely new terminology. EFRAG acknowledges that a better articulation of IAS 32's underlying principles could be an effective way to improve the consistency, clarity and completeness of the requirements and would require new terminology. However, new terminology would also require preparers and auditors to reconsider a wide range of past classification decisions. Accordingly, this approach, while addressing various interpretive

issues, will also cause some disruption, create additional costs for preparers and risks the emergence of new issues and uncertainties."

We agree that IAS 32 is in need of some improvements and clarifications but think that this could be achieved within the existing framework of the criteria for distinguishing between financial liabilities and equity. We think that clarification of the effect of certain current requirements could be developed within the current standard without changing the underlying principles. Such areas include the requirements for anti-dilution provisions, the conditionality of settlement outcomes, instruments denominated in foreign currencies, the effect of non-contractual elements, , etc. Similarly, it seems to us that the treatment of NCI puts can be settled without fundamental changes having to be made to the standard.

We are therefore in favour of the maintaining of the principles of the current standard and complementing the guidance in certain areas as described above.

Our comments on the individual questions posed in the DP are laid out in the Appendix.

If you require any further information on the content of this letter, please do not hesitate to contact us.

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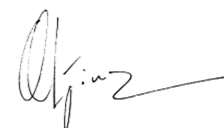
Patrice MARTEAU Chairman	François SOULMAGNON Director General	Agnès LEPINAY Director of economic and financial affairs
		

Section 1 - Objective, scope and challenges

Question 1 Paragraphs 1.23–1.37 describe the challenges identified and provide an explanation of their causes.

a. Do you agree with this description of the problems and their causes? Why or why not? Do you think there are other factors contributing to the challenges?

We agree with the list of applicational challenges included in the DP and we agree that the IASB must find ways to resolve them. However, we are convinced that a number of issues can be resolved within the current framework of IAS 32 without any reworking of the underlying principles.

As far as the conceptual challenges are concerned, we do not think that they are a hindrance to the understanding of financial statements, particularly if the IASB envisages the development of new forms and content for the disclosures in the notes, with the aim of providing more transparency about the different characteristics of equity instruments and the equity components of debt instruments, and about the criteria used and judgement applied in their classification. Moreover, it seems to us that the modifications proposed in the DP do not provide perfect solutions to the conceptual challenges identified since exemptions, exceptions are created or maintained, such as, for example, the puttable instrument exception, IFRIC 2 Members' Shares in Cooperative Entities and Similar Instruments, the inconsistency with the definition of an obligation in the Conceptual Framework, the inconsistency with IFRS 2, etc.

We would also add to the list of conceptual challenges the effect of IAS 32 on the accounting options for holdings of financial instruments in IFRS 9. The FVOCI option of IFRS 9 is currently available only for instruments defined as equity instruments according to the criteria of IFRS 9.5.7.5. We would encourage the IASB to consider, as part of this project, the possibility of opening up this option to all instruments which are permitted to be presented in equity although they do not satisfy directly the definition of an equity instrument. This would include those instruments that are covered by the puttable exception of IAS 32.16A-16B and Members' Shares in Cooperative Entities and Similar Instruments (IFRIC 2).

b. Do you agree that the challenges identified are important to users of financial statements and are pervasive enough to require standard-setting activity? Why or why not?

We think that some standard-setting activity is required but the proposals go beyond what is needed.

A first important and effective step would be to improve the quality of the information provided to users through further development and structuring of the disclosure in the notes. This would not require a revision of the current principles. For example, it seems to us that the potentially dilutive effects of certain instruments are either insufficiently or poorly explained under current requirements, and that the presentation of diluted EPS alone is not explicit enough.

Furthermore, in our view, many of the proposals of the DP could be put into effect without the need for a revision of the existing framework:

- Clarification of the application of the fixed-for-fixed criteria could be developed on the basis of the discussion of variables that are dependent on the entity's economic resources contained in the DP (paragraphs 4.47 and following). We think that the explanations of the time value of money, the effect of foreign currency, anti-dilution provisions, and contingencies could also provide

clarification about the fixed-for-fixed condition. Furthermore, we think that application of the new notion of a "variable (that) is independent of the entity's available resources" is also likely be as open to questions of interpretation and difficulties in application as the current approach.

- The taking into account or otherwise of conditional elements, non-contractual obligations and economic compulsion: Here too, we think that the clarification and positions of the DP could reinforce the notion of an obligation within the framework of IAS 32 without modifying the current criteria for distinguishing between debt and equity.

- The treatment of NCI Puts: The issue here is not so much whether an obligation (and hence a debt) exists but rather what the accounting model should be (that is, what is the opposite side of the initial creation of the debt and how to account for subsequent variations in that debt). We think that the IASB could have chosen to deal with this issue without making a fundamental change to IAS 32, since this standard already clearly identifies the debt. In addition, we regret the fact that the IASB has not taken its consideration of this issue any further, by, for example, pursuing the idea that this is a transaction between shareholders. See our response to Q6.

To conclude, we reiterate that we do not think that the challenges identified justify a fundamental modification of the standard, which of necessity imposes a complete re-examination of the classification of all instruments, including those that today pose no problem. This creates the risk that instruments that today are not considered to be problematic (such as, for example, irredeemable preference shares with discretionary but cumulative share payments) would also be impacted.

We therefore fully share EFRAG's tentative view as follows:

To address the issues that currently arise in practice, EFRAG considers that the IASB should, as in 2003, take the opportunity to clarify existing guidance, refine the underlying rationale of the distinction between liabilities and equity if necessary, reduce complexity, eliminate internal inconsistencies to the extent possible, improve presentation and disclosure requirements, use previous tentative decisions from the IFRS IC and incorporate elements of existing Interpretations. ***EFRAG considers that this is possible without fundamentally changing the existing classification outcomes of IAS 32.***

Section 2 - The IASB's preferred approach

Question 2 The IASB's preferred approach to classification would classify a claim as a liability if it contains: a. an unavoidable obligation to transfer economic resources at a specified time other than at liquidation; and/or b. an unavoidable obligation for an amount independent of the entity's available economic resources. This is because information about both of these features is relevant to assessments of the entity's financial position and financial performance, as summarised in paragraph 2.50 of the DP.

The IASB's preliminary view is that information about other features of claims should be provided through presentation and disclosure. Do you agree? Why, or why not?

We agree with the following aspects of the IASB's approach:

- Not to start with a clean sheet of paper;
- To retain the current approach in which equity is defined as a residual;
- To consider that the liquidity is a fundamental criterion underlying the debt/equity analysis; and
- To improve the disclosures relating to the other criteria used to distinguish between debt or equity.

In respect of the two criteria proposed, we are content with the first (the "timing feature") which specifies that an instrument which contains an unavoidable obligation to transfer economic resources at a specified time other than at liquidation is a debt. This seems to us to be the essential criterion for the distinction between debts and equity.

We note that the liquidity criterion proposed in the DP leads to a definition different from that in IAS 32 inasmuch as an obligation is created only when settlement must occur before liquidation. We are in favour of this approach and think that it should not be restricted by specific provisions such as that stated in footnote 24 on page 32 of the DP, which states that a contractually-specified liquidation is not a liquidation for the purposes of the debt/equity analysis. We do not agree with this restriction since we think that without it certain instruments that are to be settled only on liquidation could be classified as equity without having recourse to the exceptions provided by paragraphs 16A-16D of IAS 32, which have been retained in the DP's proposals.

As far as the solvency criterion or "amount feature" ("an unavoidable obligation for an amount independent of the entity's available economic resources") is concerned, we think that this is indeed also relevant, but we are concerned that its application in the proposed model may pose a number of problems:

- Its application to non-derivative instruments leads to changes in the classification of instruments for which no problems had previously been identified (such as, for example, irredeemable preference shares with discretionary but cumulative share payments). In the absence of an obligation to transfer resources before liquidation an instrument should never qualify as debt.

- Its application seems to us to be just as complex and debatable as the application of the current fixed-for-fixed condition for derivatives.

- This criterion could be used solely for the purpose of presentation in order to distinguish between debts whose settlement amount is independent of the entity's resources from those whose amount depends on those resources.

- If the IASB decides against the idea of retaining the principles of IAS 32 unchanged and merely adding clarifications and complementary treatment for NCI puts, we would be in favour of an alternative approach which would be based only on the liquidation criterion for the classification between debt and equity and would use the solvency criterion only for the allocation of variations in debt between profit and loss and OCI.

Section 3 Classification of non-derivative financial instruments

Question 3 The IASB's preliminary view is that a non-derivative financial instrument should be classified as a financial liability if it contains:

a. an unavoidable contractual obligation to transfer cash or another financial asset at a specified time other than at liquidation; and/or b. an unavoidable contractual obligation for an amount independent of the entity's available economic resources. This will also be the case if the financial instrument has at least one settlement outcome that has the features of a non-derivative financial liability. Do you agree? Why, or why not?

We have not encountered any particular difficulties in the application of the debt/equity determination to non-derivative instruments under IAS 32.

As stated in our response to question 2, we are of the view that:

- It is not necessary to amend the current standard since this brings the following disadvantages:
    - The requirement for an onerous systematic review of all instruments to determine their classification under the new definition;
    - A change in the classification of certain instruments whose classification under the current definition did not pose a problem (such as, for example, irredeemable preference shares with discretionary but cumulative share payments)
    - An increase in complexity as a result of the additional criterion for non-derivative instruments (the present analysis looks only at the obligation to transfer resources).

- The proposals also still require exceptions to the principles (puttable instrument exception, IFRIC 2 Members' Shares in Cooperative Entities and Similar Instruments).

Question 4

The Board's preliminary view is that the puttable exception would be required under the Board's preferred approach. Do you agree? Why, or why not?

In our view:

- In the context of a definition of debt which is based on the obligation to settle before liquidation and in the absence of the specification about programmed liquidation in footnote 24, instruments currently covered by the exceptions provided by paragraphs 16A-16D of IAS 32 could be classified as equity without having recourse to such exemption

- The exception remains valid for the other instruments that it currently applies to and it should be retained.

- The FVOCI option provided by paragraph 5.7.5 of IFRS 9 should be opened up to include those instruments which do not qualify under as equity under the current definition, but which qualify for the exception provided by IAS 32.16A-16D on the issuer's side.

Given that the IASB has as its starting point that there should be a symmetry of classification between financial instruments issued and financial instruments held, this symmetry should be respected in its entirety. Even though IAS 32 requires a two-stage process for these puttables, the end result is nonetheless that they are classified as equity for the issuer, both in their presentation and accounting. It therefore does not seem logical to stop at the definition test on the holder's side.

It also seems necessary to us that the IASB deals specifically with the members' shares in co-operative entities and similar instruments. Indeed, cooperatives shares have specific features, which are consistent with the specific objective of cooperatives, that is, to meet the common economic or social needs of its members. This objective is achieved by the application of particular principles as for example, the "one man, one vote" rule. At the time of liquidation, member shares are the most subordinated claim and are paid back after all other claims.
These instruments are considered in international regulations as equity (as for example in European regulation for capital requirements for banks). That's why we think that in order to avoid different interpretations across jurisdictions, it is necessary to make it clear in the new text that cooperatives share that meet the IFRIC 2 conditions and represent the most subordinated claim are equity, under any criteria of classification.

Section 4—Classification of derivative financial instruments

Question 5

The Board's preliminary view for classifying derivatives on own equity—other than derivatives that include an obligation to extinguish an entity's own equity instruments—are as follows:

(a) a derivative on own equity would be classified in its entirety as an equity instrument, a financial asset or a financial liability; the individual legs of the exchange would not be separately classified; and

(b) a derivative on own equity is classified as a financial asset or a financial liability if:

(i) it is net-cash settled—the derivative requires the entity to deliver cash or another financial asset, and/or contains a right to receive cash for the net amount, at a specified time other than at liquidation; and/or

(ii) the net amount of the derivative is affected by a variable that is independent of the entity's available economic resources.

Do you agree? Why, or why not?

We agree with the proposal to classify the derivative in its entirety without separately classifying the two legs of the derivative.

We are also convinced that a derivative can satisfy the definition of a financial asset, a financial liability or an equity instrument. We therefore do not agree with EFRAG's suggestion that derivatives on own equity should be scoped out of IAS 32 and dealt with within the scope of IFRS 9.

However, we are not convinced that the introduction of the new criterion of the presence of a variable that is independent of the entity's available economic resources in place of the current fixed-for-fixed condition can pass the cost/benefit test. We think that complementary guidance about the application of the fixed-for-fixed condition would be sufficient. Indeed, as is the case for non-derivative instruments, we do not judge it necessary to modify fundamentally the current standard and thereby create increased complexity and impose a systematic and onerous review of all such instruments to validate their new classification.

In respect of derivatives on own equity denominated in a foreign currency, we think that the conditions laid out in paragraph 6.34 should be used to permit classification in equity and not solely to determine presentation in OCI of the variations in the debt that must be recognised. The proposed criteria provide assurance that there is no leverage effect present and thus such an instrument should not be classified as debt.

However, if these instruments were qualified as equity as we suggest, or if their revaluation was presented in non-recyclable OCI according to the proposal in the DP, we would be concerned that foreign currency exposure arising from such embedded foreign currency derivatives on own equity could not be eligible for hedge accounting since:

- Under IFRS 9, it is only possible to hedge "exposures arising from particular risks that could affect profit or loss (or other comprehensive income, in the case of investments in equity instruments for which an entity has elected to present changes in fair value in other comprehensive income in accordance with paragraph 5.7.5)" (IFRS 9 paragraph 6.1.1)

- Under IFRIC 16, it is only possible to hedge "the foreign exchange differences arising between the functional currency of the foreign operation and the parent entity's functional currency" (IFRIC 16 paragraph 10)

We consider that when an instrument would meet the criteria in paragraph 6.34(d) "the denomination in the foreign currency is imposed by an external factor", then it would be logical and normal for the issuer entity to decide to hedge its own exposure to foreign currency risk and such hedges should be eligible for hedge accounting.

Therefor we think that IFRS 9 should be amended in order to allow such hedge accounting, even if, in that particular case, foreign currency exposure would never affect profit or loss. That amendment could be made on the model of what has been introduced in paragraph 6.5.3 of IFRS 9 for fair value hedges of financial assets that are equity instruments for which an entity has elected to present changes in fair value in other comprehensive income in accordance with paragraph 5.7.5 of IFRS 9.

Section 5—Compound instruments and redemption obligation arrangements

Question 6

Do you agree with the Board's preliminary views set out in paragraphs 5.48(a)–(b)? Why, or why not? Applying these preliminary views to a derivative that could result in the extinguishment of an entity's own equity instruments, such as a written put option on own shares, would result in the accounting as described in paragraph 5.30 and as illustrated in paragraphs 5.33–5.34.

Our response is directed essentially at the issue of NCI puts, since these are instruments whose treatment concerns us the most and for which a number of questions have arisen.

Although we welcome the IASB's efforts in this area, we do not think that the Board has yet found a satisfactory solution. Our concerns relate to the following aspects:

1. The mechanism for derecognising the NCI seems complex:
    a) It would be simpler and more understandable to derecognise the shares at the amount of the expected debt [rather than to create a "conversion option within equity"].
    b) Clarification of the impact of this derecognition on, for example, the group share and the NCI share of both the result and equity, still requires to be developed.

2. In respect of the accounting for the variations in the debt:

    a) We are surprised not to see any discussion of the interactions between this issue and IFRS 3 which had been the source of some of the divergence in practice. These led to the solution which consists in recognising variations in equity and which has been largely adopted in France on the grounds that the application of IFRS 10 to transactions between shareholders was the most relevant approach and provided the most useful information.

b) The DP's proposal for the recognition of the variations in OCI applies only to puts at fair value. However, there are numerous instances where the puts are based on different values (such as, for example, EBITDA) which cannot always be deemed to be proxies for fair value in accordance with IFRS 13. For all these instruments the current contradictory and counter-intuitive situation of a deterioration in profit and loss caused by an improvement in the entity's performance will persist.

   We think that the IASB could have approached this question from the joint viewpoints of measurement and relevance of the information to the balance sheet and profit and loss, as was the case in the revision of the conceptual framework and for the issue of own credit risk for debts at fair value under IFRS 9. In the context of NCI puts we think that while fair value might be relevant for the measurement of the debt in the balance sheet, the variations in this amount should not have an impact on the profit or loss account as this is not relevant. In fact, just as in the case of own credit risk, all improvements in the entity's economic situation and performance lead to a corresponding degradation in the profit or loss account. This accounting treatment provides information which does not make sense. The use of OCI as a holding tank for these effects seems very appropriate, no matter which valuation method is used for the put – either fair value or another variable based on the entity's performance of the issuer.

c) We think that there is another approach, which may be worthy of consideration, as follows:
   - For puts at fair value- the treatment proposed in the DP would be applied;
   - For puts with other price-fixing mechanisms which at inception are considered to be a proxy for the fair value of the shares: at inception record a debt at fair value and a derivative which will capture the difference between fair value and the change in the fair value proxy. The variations in fair value are held in OCI and those in the derivative allocated to profit or loss.

For financial instruments with alternative settlement outcomes that do not contain an unavoidable contractual obligation that has the feature(s) of a financial liability as described in paragraph 5.48(c), the Board considered possible ways to provide information about the alternative settlement outcomes as described in paragraphs 5.43–5.47.

(a) Do you think the Board should seek to address the issue? Why, or why not?

(b) If so what approach do you think would be most effective in providing the information, and why?

We think it is most helpful if the IASB groups together all the provisions relating to compound instruments and alternative settlement outcomes in one section of the DP separately from the provisions relating to share repurchase obligations. It would also be logical in our view to deal at the same time with the consideration of the impact of any reglementary or legal provisions relating to instruments and the notion of economic compulsion in order to develop a comprehensive approach to all such factors and if and how they should be taken into account.

We think that the following scenarios could be presented in detail:

- An instrument which comprises two different types of obligation to be settled without alternative modes of settlement (for example, principal plus interest): the settlement methods should be analysed to ascertain whether either or both satisfy the definition of a debt
    - If both elements satisfy the definition of debt the whole of the instrument is classified in debt at its nominal value.
    - If only one component satisfies the debt definition, then this is measured first and the second, equity element is measured by difference.
    - If both components are equity instruments, then the whole instrument is classified in equity at nominal value.

- An instrument with an alternative mode of settlement
    - If the alternative is not contractual but rather imposed by reglementary or legal provisions it is not taken into account, Only the contractual obligation is assessed for the purpose of classification of the instrument (or the component).

    - If the alternative is at the choice of the holder one identifies in the first instance the obligation for a cash settlement which gives rise to a debt for the issuer. The option given to the holder for a conversion to shares is identified as an equity component measured by difference. In measuring the debt, one does not take into account the probability of the holder opting for a cash settlement. This probability is taken up solely in the measurement of the equity element.

    - If the issuer controls the settlement alternative and one of the alternatives is settlement in shares, the whole instrument (or component) is classified in equity.
        - The embedded derivative linked to a cash settlement is not identified.
        - Any economic compulsion to prefer one settlement method to another is not taken into account.

Section 6—Presentation

Question 7

Do you agree with the Board's preliminary views stated in paragraphs 6.53–6.54? Why, or why not?

The Board also considered whether or not it should require separation of embedded derivatives from the host contract for the purposes of the presentation requirements as discussed in paragraphs 6.37–6.41. Which alternative in paragraph 6.38 do you think strikes the right balance between the benefits of providing useful information and the costs of application, and why?

We reiterate that we are in favour of retaining the current provisions of IAS 32. However, if the IASB proceeds with its model:

- If the changes in NCI debt value cannot be recognized in equity, we are in favour of the use of OCI for these.
- We are in favour of the presenting in OCI of the variations in the value of those instruments which have qualified as debt instruments but whose value is directly linked to the economic resources of the entity.

In relation to the presentation in OCI of the exchange differences on instruments which would otherwise be qualified to pass in equity, we refer back to the remarks we made in our response to question 5 about the impact that might have on hedging relationships and the modification which would have to be made to IFRS 9.

As far as the separation of embedded derivatives is concerned, we think that the fair value option provided in IFRS 9 for a derivative embedded in a financial liability is intended to deal with the case of derivatives whose separation from the underlying is too complex to contemplate realistically.

We think that the (re)introduction of a mandatory separation of derivatives as proposed by the DP (alternative B) is not advisable or desirable, notably because of the unwonted complexity it would induce.

We would therefore be opposed to alternative B and we are not in favour of alternative A, which would require separation in some limited cases. Indeed, separating embedded derivatives is always complex and adding a new requirement to separate embedded derivatives that are currently not separated under IFRS 9 or IAS 32 would not be suitable as already discussed by the Board when issuing IAS 39 (fair value option discussions) or IFRS 9 (financial assets discussions).

Question 8

The Board's preliminary view is that it would be useful to users of financial statements assessing the distribution of returns among equity instruments to expand the attribution of income and expenses to some equity instruments other than ordinary shares. Do you agree? Why, or why not?

The Board's preliminary view is that the attribution for non-derivative equity instruments should be based on the existing requirements of IAS 33. Do you agree? Why, or why not?

The Board did not form a preliminary view in relation to the attribution approach for derivative equity instruments. However, the Board considered various approaches, including:

(a) a full fair value approach (paragraphs 6.74–6.78);

(b) the average-of-period approach (paragraphs 6.79–6.82);

(c) the end-of-period approach (paragraphs 6.83–6.86); and

(d) not requiring attribution, but using disclosure as introduced in paragraphs 6.87–6.90 and developed in paragraphs 7.13–7.25.

Which approach do you think would best balance the costs and benefits of improving information provided to users of financial statements?

We are opposed to all of these "attribution" proposals, which we think are complex and onerous to produce and complex for a user to understand. A more relevant and helpful approach would be to provide qualitative information about the dilutive characteristics of these instruments and to improve IAS 33.

Section 7—Disclosure

Question 9

The Board's preliminary view is that providing the following information in the notes to the financial statements would be useful to users of financial instruments:

(a) information about the priority of financial liabilities and equity instruments on liquidation (see paragraphs 7.7–7.8). Entities could choose to present financial liabilities and equity instruments in order of priority, either on the statement of financial position, or in the notes (see paragraphs 6.8–6.9).

(b) information about potential dilution of ordinary shares. These disclosures would include potential dilution for all potential issuance of ordinary shares (see paragraphs 7.21–7.22).

(c) information about terms and conditions should be provided for both financial liabilities and equity instruments in the notes to the financial statements (see paragraphs 7.26–7.29).

Do you agree with the Board's preliminary view? Why, or why not?

How would you improve the Board's suggestions in order to provide useful information to users of financial statements that will overcome the challenges identified in paragraphs 7.10 and 7.29?

Are there other challenges that you think the Board should consider when developing its preliminary views on disclosures?

As we state in our covering letter, we think that the information required by current standards should be improved to enhance the user's understanding of the different classifications of instruments and their impact on the financial statements. We think, nevertheless, that the effort would be better directed towards equity instruments or those that are classified as financial liabilities with variations taken through OCI, as proposed in the DP. The current requirements seem to us to be appropriate, with the possible exception of information about the seniority of instruments.

In respect of the latter, while we agree that this criterion should not affect the classification of an instrument, we think that it remains an important element for users of financial statements and that relevant information should be provided in the notes on this topic. However, we would draw the Board's attention to the risk that such information can very quickly become complex to collect and present, particularly in the context of a group as a result of the interaction between the instruments issued by the parent and the subsidiaries, as well as the different jurisdictions in which the group's instruments are issued.

We are of the view that the analysis required by paragraphs 7.8 and 7.10 of the DP, in particular, is far too complex to carry out successfully. A better cost/benefit balance would be achieved by requiring only the classification of instruments by class relevant to each entity, in accordance with the principle of paragraph 6 of IFRS 7, and to indicate for each class the principal characteristics for the most significant issues of instruments. For information about the seniority of instruments, the information could be based on an instrument-by-instrument basis, independently of the presentation of financial liabilities or equity. This approach could be based on the classification required by regulation, such as banking (CRR-CRD4 at present and CRR2-CRD5 in the near future) and markets in Europe. Nevertheless, we encourage the IASB to define carefully the objective of the new disclosures and to ensure that similar (or identical) information is not already required elsewhere by regulators. It would be useful, moreover, to allow cross-references since similar information might already be required by, for example, banking regulators in other parts of the financial reports.

It should always be possible for those entities who wish to do so to enhance further the categorisation. In respect of dilutive effects, we think that Board should reopen IAS 33 in its entirety in order to improve the information required about dilutive effects.

Section 8—Contractual terms

Question 10

Do you agree with the Board's preliminary view that:

(a) economic incentives that might influence the issuer's decision to exercise its rights should not be considered when classifying a financial instrument as a financial liability or an equity instrument?

(b) the requirements in paragraph 20 of IAS 32 for indirect obligations should be retained?

Why, or why not?

We agree that economic compulsion should not be taken into account in the analysis. The principal reasons for this are as follows:

- It would be necessary to provide a definition of economic compulsion and to define its scope of application in order to limit its use to reasonable domain;
- The notion would rely heavily on the use of judgement and could be detrimental to the comparison of the accounting for identical instruments issued by different groups;
- Application of this notion would require even more disclosure about use of judgement and estimations in order to facilitate users' understanding about the extent to which this has influenced the classification of instruments;
- In a model based upon the principle of symmetry between instruments issued and instruments held, one would equally have to analyse economic compulsion as it affects the holder. This would further complicate the analysis;
- In order to make use of the FVOCI option of IFRS 9, the holder of an instrument would have also to resolve the question of economic compulsion on the part of the issuer in order to determine whether the instrument satisfies the definition of an equity instrument;
- Use of this notion would also require systematic re-evaluation of facts and circumstances to ascertain whether the economic compulsion existing at the outset is still relevant, leading possibly to reclassification and thus complicating understanding of the financial statements.

We recognise that this approach (that is, the ignoring of economic compulsion) is not really consistent with the definition of an obligation as laid out in the Conceptual Framework. However, we prefer to accept this divergence rather than to suffer the consequences of an analysis which is too subjective and could have an unpredictable and fluctuating impact on the classification of debts and equity.

Question 11

The Board's preliminary view is that an entity shall apply the Board's preferred approach to the contractual terms of a financial instrument consistently with the existing scope of IAS 32. Do you agree? Why, or why not?

We agree with the tentative decision of the DP that the classification should be based solely on the contractual obligations. Thus, legal and reglementary obligations must not impinge on the analysis to the extent they are not explicitly included in the contract between the issuer and the holder of the instrument.

In this, we are particularly sensitive to the arguments given in paragraph 8.31 and the risk of broadening the scope of the rights and obligations that are currently accounted for.

Moreover, in the European Union (the EU), for example, in the case of a legal obligation imposed by the EU, individual jurisdictions have the option of mandating its inclusion in all contracts or to set it in place in the legal framework "supra contract". We think that the IASB should consider further how these situations should be dealt with in order to enhance comparability between contracts of essentially the same substance but concluded in different jurisdictions.