**30 Cannon Street, London EC4M 6XH, United Kingdom**
**Phone: +44 (0)20 7246 6410, Fax: +44 (0)20 7246 6411**
**Email: iasb@iasb.org   Website: http://www.iasb.org**

**International Accounting Standards Board**



# INFORMATION FOR OBSERVERS

**Board Meeting:** **26 April 2006, London**

**Project:** **Financial Instruments Puttable at Fair Value and Obligations Arising on Liquidation (Agenda Paper 6)**

---

## ANALYSIS OF BENEFITS AND COSTS

### Introduction

1. At its meeting in December 2005, the Board decided to amend IAS 32 *Financial Instrument: Presentation* to require equity classification for instruments puttable at the fair value of a pro rata share of the net assets of the entity ('financial instruments puttable at fair value') and instruments that entitle the holder to a pro rata share of the entity's net assets payable on liquidation (affecting partnerships and limited life entities) ('obligations arising on liquidation'), subject to these instruments meeting specified criteria.

2. This paper considers the costs and benefits of the proposed changes to IAS 32 and IAS 1 *Presentation of Financial Statements*.[1] [Not reproduced in the Observer Notes.]

[1] At its meeting in February 2005, the Board decided to require additional disclosures for the instruments affected by the amendments to IAS 32.

| Proposed changes to IAS 32 | New information required | Analysis of benefits and costs | Impact on transitional arrangements |
|---|---|---|---|
| 1. Change to the definition of financial liability to exclude financial instrument puttable at fair value when all instruments in the most subordinated class are financial instruments puttable at fair value.<br><br>The following are the conditions for a financial instrument puttable at fair value:<br><br>(a) the instrument entitles the holder to require the entity to repurchase or redeem the instrument for the fair value of a pro rata share of the net assets of the entity and would, but for this entitlement, have met the definition of an equity instrument;<br><br>(b) the instrument entitles the holder to a pro rata share of the net assets of the entity in the event of the entity's liquidation;<br><br>(c) the financial instrument's right to a pro rata share of the net assets of the entity is neither limited nor guaranteed, either before or at liquidation;<br><br>(d) the instrument is in the most subordinated class of instruments with a claim to the entity's net assets; and<br><br>(e) the instrument's issue price was the fair value of a pro rata share of the net assets of the entity at the time of issue.<br><br>In the group's consolidated financial statements, minority interests puttable at fair value are precluded from equity classification.<br><br>Change in the classification to equity of financial instruments puttable at fair value provided specified criteria | Potentially a new analysis of existing information to determine the classification of financial instruments puttable at fair value. The information required to conduct the analysis should be readily available.<br><br>If financial instruments puttable at fair value are classified as equity, information will be needed to reverse all previous remeasurements of these instruments to fair value at every reporting date in the past. Going forward these instruments will be measured at the net proceeds received on issue. | [Not reproduced in the Observer Notes.] | [Not reproduced in the Observer Notes.] |

| Proposed changes to IAS 32 | New information required | Analysis of benefits and costs | Impact on transitional arrangements |
|---|---|---|---|
| are met. | | | |
| 2. Change in the definition of a financial liability to exclude financial instruments with an obligation to a pro rata share of the net assets of the entity upon its liquidation, provided that all instruments (or components of financial instruments) imposes such an obligation.<br>The following are the conditions for an instrument with an obligation for a pro rata share of net assets arising on liquidation:<br>(a) the instrument entitles the holder to a pro rata share of the net assets of the entity in the event of the entity's liquidation;<br>(b) the financial instrument's right to a pro rata share of the net assets of the entity is neither limited nor guaranteed, either before or at liquidation; and<br>(c) the instrument is in the most subordinated class of instruments with a claim to the entity's net assets.<br>In the group's consolidated financial statements, minority interests with obligations arising on liquidation are precluded from equity classification.<br>Change in the classification to equity of instruments with an obligation for a pro rata share of net assets on liquidation provided specified criteria are met. | Potentially a new analysis of existing information about the classification of instruments (or components of instruments) with an obligation arising on liquidation.<br>The information required to conduct the analysis should be readily available. | [Not reproduced in the Observer Notes.] | [Not reproduced in the Observer Notes.] |

| Proposed changes to IAS 32 | New information required | Analysis of benefits and costs | Impact on transitional arrangements |
|---|---|---|---|
| 3. Proposed change to the definition of a financial liability so that a derivative that will be settled by the issuer exchanging a fixed amount of cash or another financial asset with a fixed number of its own equity instruments continues to be classified as a financial liability when the entity's own equity instruments are financial instruments puttable at fair value or instruments with obligations arising on liquidation. | No new analysis is needed as these instruments will continue to be classified as financial liabilities. | [Not reproduced in the Observer Notes.] | [Not reproduced in the Observer Notes.] |

| Proposed changes to IAS 1 | New information required | Analysis of benefits and costs | Impact on transitional arrangements |
|---|---|---|---|
| 1. New requirement to disclose information about the reclassification of instruments between equity and financial liabilities of the instruments affected by the amendments. | The information required by the disclosure requirement will be readily available. | [Not reproduced in the Observer Notes.] | [Not reproduced in the Observer Notes.] |
| 2. New requirement to disclose the fair values of financial instruments puttable at fair value classified as equity.<br><br>Change for entities without public accountability as these entities are permitted to use a formula to calculate the fair value of these instruments. | No new information required, as the information required by this disclosure would have been previously produced to revalue these instruments if the instruments continued to be classified as financial liabilities. This information is only required from entities with financial instruments puttable at fair value classified as equity. | [Not reproduced in the Observer Notes.] | [Not reproduced in the Observer Notes.] |
| 3. New requirement to disclose information about length of the life of a limited life entity. | New information is needed but the information should be readily available. | [Not reproduced in the Observer Notes.] | [Not reproduced in the Observer Notes.] |