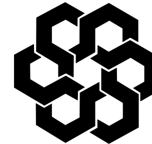

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International Accounting Standards Board

This document is provided as a convenience to observers at IASB meetings, to assist them in following the Board's discussion. It does not represent an official position of the IASB. Board positions are set out in Standards.

These notes are based on the staff papers prepared for the IASB. Paragraph numbers correspond to paragraph numbers used in the IASB papers. However, because these notes are less detailed, some paragraph numbers are not used.

INFORMATION FOR OBSERVERS

Board Meeting:	**November 2008, London**
Project:	**Ratification of IFRIC Interpretation**
Subject:	**Cover note - IFRIC 17 *Distributions of Non-cash Assets to Owners* (Agenda Paper 5)**

Purpose of this paper

1. This agenda item asks the Board to ratify an Interpretation on distributions of non-cash assets to owners. This paper provides an overview of the Interpretation to assist the Board in its review.

Agenda papers for this meeting

2. The following agenda papers are provided:
   - AP 5 — Cover note (this agenda paper)
   - AP 5A — Interpretation IFRIC 17 *Distributions of Non-cash Assets to Owners*

Project history

3. In early 2006, the IFRIC was asked to provide guidance on how to account for non-cash distributions to owners in the financial statements of the entity making such distributions. The submission focused on situations in which an entity distributes its ownership interest in a subsidiary to its shareholders and loses control over that subsidiary.

4. After deliberations by the IFRIC, Draft Interpretation D23 was published in January 2008 with a comment deadline of 25 April 2008. The IFRIC received 56 comment letters.

5. In general the comment letters supported the IFRIC's conclusions set out in D23. However, commentators asked the IFRIC to clarify the scope of the Interpretation, particularly when the shares of group entities are distributed and how the Interpretation interacts with IAS 27 (2008).

6. They also raised concerns about linking the measurement of a dividend liability to a specific standard (IAS 37 – as proposed by D23) because they thought that doing so could implicitly require fair value measurement of all other liabilities within the scope of IAS 37.

7. In response to commentators, the IFRIC clarified in the final Interpretation and the Illustrative Example that transactions in which the shares of group entities are distributed to shareholders outside the group do not meet the definition of common control transactions in IFRS 3 *Business Combinations* and therefore are within the scope of the Interpretation.

8. The IFRIC also clarified that this Interpretation does not apply when an entity distributes some of its ownership interests in a subsidiary but retains control of the subsidiary. The distribution that results in the entity recognising a non-controlling interest in the subsidiary should be accounted for in accordance with IAS 27 (as amended in 2008).

9. The IFRIC also decided to require dividend liabilities to be measured at the fair value of the assets to be distributed without linking its conclusion to a specific standard.

10. Respondents were also concerned about the potential ‘accounting mismatch’ in equity resulting from measuring the assets to be distributed at their carrying amount and measuring the dividend payable at the fair value of the assets to be distributed. Consequently, the IFRIC considered whether it should recommend that the Board amend IFRS 5 to require the assets to be distributed to be measured at fair value.

11. The IFRIC did not identify any IFRS literature that would support an upward remeasurement of the assets solely on the basis of a commitment to distribute them. The IFRIC noted that such a change would result in an inconsistency within IFRS 5 between assets held for sale and those held for distribution. The IFRIC also noted this ‘mismatch’ would arise only in the normally short period between when the dividend payable is recognised and when it is settled. Therefore, the IFRIC decided not to recommend that the Board amend IFRS 5 in this regard.

12. At its meeting in September 2008, the IFRIC voted and confirmed the consensus in the Interpretation.

Consensus

13. The IFRIC reached consensus on the following issues:

    (a) When should the entity recognise the dividend payable?
    **when declaration of the divided by management is approved by the shareholders, if the jurisdiction requires such approval*

    **when the dividend is declared by management, if the jurisdiction does not require shareholders’ approval*

    (b) How should an entity measure the dividend payable?
    ** at the fair value of the assets to be distributed*

(c) When an entity settles the dividend payable, how should it account for any difference between the carrying amount of the assets distributed and the carrying amount of the dividend payable?
** recognise the credit balance in profit or loss*

Implications

14. The staff would like to highlight several of the implications of the IFRIC's conclusions to assist the Board in reviewing the Interpretation.

Interaction with common control transactions project

15. In December 2007, the Board decided to add to its active agenda a project on common control transactions. According to the technical plan provided in the June 2008 Board meeting, the scope of the project will be as follows:
“In December 2007, the Board decided to add to its active agenda a project on common control transactions. Business combinations involving entities or businesses under common control are excluded from the scope of IFRS 3 *Business Combinations*. As a consequence, practice diverges on the accounting for those transactions in the acquirer’s consolidated and separate financial statements. The project examines the definition of common control and the methods of accounting for a business combination between entities or businesses under common control in the *acquirer’s* consolidated and separate financial statements. *Similar issues arise with respect to the accounting for demergers, such as the spin-off of a subsidiary or business. Therefore, the Board decided to include demergers in the scope of the project.*” (*emphasis added*)

16. The scope of the Interpretation does not include the common control transactions defined in IFRS 3 and therefore is clearly different from the scope of the common control transactions project.

17. The common control transactions project will include the accounting for demergers, such as the spin-off of a subsidiary or business, in the financial statements of group entities. The Interpretation includes certain demerger/spin-off transactions in its scope. However, those transactions are limited to a pro-rata distribution to shareholders who are <u>outside the group</u> of the reporting entity. Therefore, the scope of the Interpretation is different from the Board project.

Consistency with US GAAP

18. The IFRIC's consensuses are mostly consistent with the requirements of US GAAP (APB Opinion No. 29, EITF Issue No. 01-2 and SFAS 153) for non-cash asset distributions to the owners. US GAAP basically requires a nonreciprocal transfer of nonmonetary assets to a shareholder to be recorded at the fair value of the asset transferred and gain or loss is recognised on the disposition of the assets.

19. US GAAP makes an exception to this requirement for a pro-rata distribution of shares of a subsidiary and when fair value is not determinable. In these cases, the transactions are recorded at the carrying amounts.

20. The Interpretation does not make exceptions for such cases. Recognition of profit and loss when shares of a subsidiary are distributed and control of the subsidiary is lost is consistent with the recent amendments to IAS 27 as a result of the Business Combinations project and the *Framework*.

21. The IFRIC also concluded that, when the management of an entity recommends a distribution of a non-cash asset to its owners, it would be expected to know the fair value of the asset.

Amendments to IFRS 5 and IAS 10

22. The IFRIC recommends that the Board approve amendments to IFRS 5 and IAS 10 as part of its approval of the Interpretation.

23. In considering the publication of D23, both the IFRIC and the Board concluded that the requirements of IFRS 5 should be applied to assets held for distribution to owners as well as to those held for sale. However, the Board noted that reclassification in accordance with IFRS 5 occurs on the commitment date, while the dividend payable is recognised when the entity has an obligation. Consequently, the Board asked the IFRIC to include a question in D23 asking

constituents if these dates would be different and, if so, at which date IFRS 5 should be applied. D23 did not include wording for the amendment to IFRS 5.

24. Constituents supported including distributions in the scope of IFRS 5 and reclassifying the assets to be distributed at the commitment date even though this date might precede the recognition of the dividend payable in some situations. The IFRIC concluded that IFRS 5 should be applied at the commitment date at which time the assets must be available for immediate distribution in their present condition and the distribution must be *highly probable.* For the distribution to be highly probable, it should meet essentially the same conditions required for assets held for sale.

25. Further, the IFRIC concluded that the probability of shareholders' approval (if required in the jurisdiction) should be considered as part of the assessment of whether the distribution is highly probable. The IFRIC noted that shareholder approval is also required for the sale of assets in some jurisdictions and concluded that similar consideration of the probability of such approval should be required for assets held for sale.

26. The IFRIC noted that IAS 10 *Events after the Reporting Period* paragraph 13 states that ‘If dividends are declared (ie the dividends are appropriately authorised and no longer at the discretion of the entity) after the reporting period but before the financial statements are authorised for issue, the dividends are not recognised as a liability at the end of the reporting period because no obligation exists at that time’.

27. Some commentators stated that in many jurisdictions a commonly held view is that the entity has discretion until the shareholders approve the dividend. Therefore, constituents holding this view believe a conflict exists between ‘declared’ and the explanatory phrase in the brackets in IAS 10 paragraph 13. This is especially true when the sentence is interpreted as ‘declared *by management but before the shareholders’ approval’*.

28. Therefore, as a consequence of this Interpretation the IFRIC decided to recommend that the Board amend IAS 10 to delete the explanatory phrase in the brackets to remove the perceived conflict in paragraph 13.

Effective date

29. The IFRIC decided that an entity should apply this Interpretation prospectively for annual periods beginning on or after 1 July 2009. The IFRIC considered whether the Interpretation could be effective earlier but concluded that the effective date had to be consistent with the effective date of IFRS 3 (as revised in 2008) and IAS 27 (as amended in 2008).

Question for the Board

30. Are you in favour of ratifying the Interpretation?