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Topic **Cover page**

Purpose of this paper

1. At the May 2010 meeting, the Interpretations Committee decided to add to its agenda a request for guidance on how an entity should account for changes in the carrying amount of a financial liability for a put option, written over shares held by a non-controlling interest shareholder, in the consolidated financial statements of a parent entity (NCI puts).

2. The issue arises because of a potential conflict between the financial instruments guidance in IAS 32 *Financial Instruments: Presentation* and IAS 39 *Financial Instruments: Recognition and Measurement* and the guidance in IAS 27 *Consolidated and Separate Financial Statements*.

3. At its July 2010 meeting the Interpretations Committee discussed which components of the accounting for put options written over non-controlling interests should be included within the scope of the draft Interpretation.

4. The purpose of the September 2010 agenda papers is to address additional requests made by the Interpretations Committee at the July 2010 meeting.

Background information

5. At the July 2010 meeting, the Interpretations Committee tentatively decided to include guidance for the:

   (a) initial recognition of NCI puts proposing that a financial liability should be recognised and initially measured at fair value (the present value of the redemption amount) of the NCI put; and

   (b) subsequent measurement of NCI puts, proposing that changes in the carrying amount of a financial liability for a NCI put should be recognised in profit or loss in accordance with the guidance in IAS 39.

6. The Interpretations Committee also requested that the staff develop papers for discussion at the next meeting that provide additional analysis of the approach to initial recognition of NCI puts, specifically the debit entry to be recognised.

Overview of September 2010 agenda papers

7. As a result of the requests made by the Interpretations Committee at the July 2010 meeting, the staff have prepared agenda papers for the September Interpretations Committee meeting analysing:

   (a) whether the financial liability recognised for the NCI put represents a reclassification of NCI; (**agenda paper 4B**)

   (b) the interaction between changes in the carrying amount of the financial liability and changes in the amount, if any, that is recognised for NCI; (**agenda paper 4B**)

   This includes consideration of how to resolve any perceived 'double counting' within equity or profit or loss that is associated with the subsequent accounting for a NCI put.

   (c) the implications of the NCI put being written as part of a business combination; (**agenda paper 4C**) and

(d) consideration of the alternatives to interpreting guidance for the initial recognition of an NCI put, including whether amendments should be made to the current requirements in IFRSs. (**agenda paper 4D**)

Staff recommendations for the scope and approach to be included within the proposed Interpretation

8. Appendix A to this agenda paper includes a summary, based on the Interpretations Committee tentative agenda decisions to date, of the components of the accounting for put options written over NCI that would **be within the scope of the proposed** Interpretation. It also includes a summary of other components of the accounting for put options written over NCI that the Interpretations Committee could decide to include in the scope of the proposed Interpretation.

9. Appendix B includes an overview, based on the Interpretations Committee tentative agenda decisions to date, of the proposed Interpretation.

Proposals for the next steps in the project

10. The staff propose that the next steps in the project should be presented at the November Interpretations Committee meeting in the form of agenda papers analysing:

    (a) other components of the accounting for put options written over NCI that are affected by the initial recognition approach.

    For example, how should NCI be recognised and measured if it was previously derecognised when the NCI put was written?

    (b) the transition provision for the proposed Interpretation.

For example, should application be limited to NCI puts written after the effective date of the proposed Interpretation, or should guidance be provided for NCI puts written in previous periods? Furthermore, should a distinction be made between NCI puts that have been settled or have expired at the effective date and those that have not?

11. In addition, the staff will continue to provide relevant updates from the *Financial Instruments with Characteristics of Equity* (FICE) project, and specifically the discussion expected to be held by in the September IASB meeting to determine the next steps, if any, to be taken.

Appendix A – Summary of scope of proposed Interpretation

A1. Based on the Interpretations Committee **tentative agenda decisions to date** relating to the project, the summary of the scope of the proposed Interpretation would include:

(a) initial recognition of the credit entity for a put option written by the parent over non-controlling interests separately from a business combination; and

(b) subsequent recognition and measurement of the financial liability, recognised on initial recognition, for a put option written by the parent over non-controlling interests separately from a business combination;

A2. In addition, other matters that could be within the scope of the proposed Interpretation, depending on the **decisions made by the Interpretations Committee at the September 2010** meeting, include:

(a) initial recognition of the debit entity for a put option written by the parent over non-controlling interests separately from a business combination;

(b) initial recognition for a put option written by the parent over non-controlling interests as part of a business combination; and

(c) subsequent recognition and measurement of the financial liability, recognised on initial recognition, for a put option written by the parent over non-controlling interests as part of a business combination.

A3. The Interpretations Committee may also decide to discuss **after the September 2010 Interpretations Committee** meeting whether the proposed Interpretation should include guidance on:

(a) subsequent recognition of dividends paid on the subsidiary shares subject to a put option written over non-controlling interests;

(b) accounting for the settlement (exercise) of a put option written over non-controlling interests; and

(c) accounting for the expiration of an unexercised put option written over non-controlling interests, including the carrying amount of NCI to be recognised at expiration.

Appendix B – Overview of the proposed Interpretation, based on Interpretations Committee tentative agenda decisions to date

Draft Consensus

Initial recognition

Initial recognition of a put option written by the parent over non-controlling interests separately from a business combination

A4. A financial liability shall be recognised for a put option written by a parent over non-controlling interest separately from a business combination in accordance with paragraph 23 of IAS 32.

A5. The financial liability initially recognised for a put option written by a parent over non-controlling interest separately from a business combination shall be measured at fair value (the present value of the redemption amount), in accordance with paragraph 43 of IAS 39.

A6. The initial recognition of a put option written by a parent over non-controlling interest separately from a business combination is accounted for as an equity transaction in accordance with paragraph 30 of IAS 27. Consequently, consistent with paragraph 23 of IAS 32, the financial liability initially recognised for the put option written by a parent over non-controlling interest separately from a business combination is reclassified from equity. No profit or loss would be recognised when the financial liabilities is initially recognised for the put option written by a parent over non-controlling interest separately from a business combination.

Subsequent recognition

Subsequent recognition and measurement of the financial liability recognised on initial recognition, for a put option written by the parent over non-controlling interests separately from a business combination

A7. The financial liability recognised for the put option written by the parent over non-controlling interests separately from a business combination is, in accordance with paragraph 23 of IAS 32 and paragraph 23 of IAS 39 subsequently measured at amortised cost using the effective interest method, or at fair value through profit or loss.

A8. Changes in the fair value of a financial liability recognised for the put option written by the parent over non-controlling interests separately from a business combination measured at fair value through profit or loss that is not part of a hedging relationship shall be recognised in profit or loss in accordance with paragraph 55 of IAS 39.

A9. If the financial liability recognised for the put option written by the parent over non-controlling interests is measured at amortised cost, and is not a hedged item, subsequent changes in the carrying amount of the financial liability are recognised in profit or loss in accordance with paragraph 56 of IAS 39.

Draft basis for conclusions

Initial recognition

Initial recognition of a put option written by the parent over non-controlling interests separately from a business combination

BC1. The initial recognition of a put option written by a parent over non-controlling interest separately from a business combination is accounted for as a transaction with owners in their capacity as owners in accordance with paragraph 30 of IAS 27 *Consolidated and Separate Financial Statements*. Consequently, it is reflected in the consolidated financial statements of the parent entity as an equity transaction.

BC2. In accordance with paragraph 23 of IAS 32 *Financial Instruments: Presentation*, the put option written by a parent over non-controlling interest separately from a business combination is an obligation that the parent has to purchase its own equity instruments (shares of a subsidiary) for cash or another financial asset and is presented as a financial liability. This financial liability, in accordance with paragraph 43 of IAS 39 *Financial Instruments: Recognition and Measurement*, is measured at fair value (the present value of the redemption amount).

BC3. In accordance with paragraph 23 of IAS 32, and consistent with the accounting for the initial recognition as a transaction with owners in their capacity as owners, the financial liability initially recognised for the put option written by a parent over non-controlling interest separately from a business combination is reclassified from equity.

Subsequent recognition

Subsequent recognition and measurement of the financial liability recognised on initial recognition, for a put option written by the parent over non-controlling interests separately from a business combination

BC4. In accordance with paragraph 23 of IAS 32 *Financial Instruments: Presentation*, the financial liability recognised for the put option written by the parent over non-controlling interests separately from a business combination is subsequently measured in accordance with IAS 39 at amortised cost using the effective interest method, or at fair value through profit or loss. Subsequent measurement of the financial liability is not an equity transaction, and consequently is not accounted for in accordance with IAS 27.

BC5. Changes in the fair value of a financial liability recognised for the put option written by the parent over non-controlling interests separately from a business combination measured at fair value through profit or loss that is not part of a hedging relationship shall be recognised in profit or loss in accordance with paragraph 55 of IAS 39.

BC6. If the financial liability recognised for the put option written by the parent over non-controlling interests separately from a business combination is measured at amortised cost, and is not a hedged item, paragraph 56 of IAS 39 requires that amortisation, and any gain or loss on derecognition of the financial liability, is recognised in profit or loss.