

STAFF PAPER

12 – 13 March 2013

IFRS Interpretations Committee Meeting

Project	New issues
Paper topic	IFRS 5 <i>Non-current Assets Held for Sale and Discontinued Operations</i> —classification in conjunction with a planned IPO and change of disposal method
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This paper has been prepared by the staff of the IFRS Foundation for discussion at a public meeting of the IFRS Interpretations Committee. Comments made in relation to the application of an IFRS do not purport to be acceptable or unacceptable application of that IFRS—only the IFRS Interpretations Committee or the IASB can make such a determination. Decisions made by the IFRS Interpretations Committee are reported in *IFRIC Update*. The approval of a final Interpretation by the Board is reported in *IASB Update*.

Introduction

1. In February 2013, the IFRS Interpretations Committee (‘the Interpretations Committee’) received a request from the European Securities and Markets Authority (ESMA) to clarify the application of the guidance in IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* regarding the classification of a non-current asset (or disposal group) as held for sale, in the case of:
 - (a) a disposal plan that is intended to be achieved by means of an initial public offering (IPO) but where the prospectus has not been approved by the securities regulator; and
 - (b) a change in a disposal plan from a plan that previously qualified as held for sale into a plan to spin off the disposal group and distribute a dividend in kind to its shareholders.
2. We performed outreach with national accounting standard-setters (ie the International Forum of Accounting Standard Setters (IFASS)) and a securities regulator (IOSCO) on this topic in order to find out whether the issue raised by

the submitter is widespread and whether significant diversity in practice exists. We will report these results orally at the March 2013 Interpretations Committee meeting, because the deadline to receive comments will not close until a day before this meeting.

3. The submission is reproduced in full in **Appendix C** to this paper.

Purpose of the paper

4. The purpose of this paper is to:
 - (a) provide an analysis of the issues raised in the submission;
 - (b) present an assessment of the issue against the Interpretations Committee's agenda criteria;
 - (c) make a recommendation that the Interpretations Committee should not take these issues onto its agenda (we have set out our proposed wording for the proposed two tentative agenda decisions in **Appendix A** and **Appendix B** of this paper, respectively); and
 - (d) ask the Interpretations Committee whether it agrees with the staff recommendation.

Description of the fact pattern submitted

5. The submitter refers the case of Entity A's plan to dispose of a profitable Division B by way of an initial public offering (IPO). This plan is approved by Entity A's Board of Directors on June 30, 20X1. The IPO is intended to be completed within 12 months of its original classification.
6. In preparation for the sale of Division B, Entity A's management has performed the following activities:
 - (a) initiated internal IPO preparations (it has prepared regulatory and sales documents and engaged external advisors);

- (b) has regularly communicated its plans to the public and third-party analysts;
- (c) has separated the business activities of Division B into a distinct legal corporation. It has:
 - (i) classified Division B as a discontinued operation in its interim financial statements; and
 - (ii) classified the disposal group's net assets of Division B as held for sale.

7. Entity A:

- (a) has not filed any offering documents (a 'prospectus') with its securities regulators;
- (b) has not publicly announced an offering price; and
- (c) has not contacted prospective buyers (because by law it is unable to do so before it gets the approval from the securities regulator) but may contact institutional buyers.

8. During the second half of 20X1 market conditions decline. As of December 31, 20X1 Entity A re-evaluates the criteria in IFRS 5 and continues to classify Division B as a discontinued operation, based on the fact that Entity A:

- (a) is still committed to the disposal of Division B through an IPO during the first half of 20X2; and
- (b) believes that market conditions will improve and enable Entity A to sell Division B by way of an IPO.

9. On June 30 20X2, Entity A reassesses the market and confirms its intention to dispose of Division B. However, management decides that a disposal through an IPO is no longer feasible. Consequently, management decides to:

- (a) spin off Division B by distributing Division B's shares to Entity A's shareholders by means of a dividend-in-kind; and
- (b) list the shares of Division B on the stock exchange by means of an IPO.

10. Entity A determines that the new plan to spin off Division B constitutes a change to a plan of sale, on the basis of the guidance in paragraph 26 of IFRS 5.
11. Entity A decides to maintain the classification of the disposal group as “held for distribution to owners”, because there is a plan to make the distribution and to list the shares of Division B by means of an IPO and this plan is expected to be completed within the next 12 months.

Questions asked by the submitter

12. The submitter asks the Interpretations Committee to clarify the accounting requirements in IFRSs in respect of the following questions:
 - (a) Would Division B qualify as held for sale as of December 31, 20X1 when there is a disposal plan that is intended to be achieved by means of an initial public offering, but where the prospectus has not been approved by the securities regulator, assuming all the other criteria in IFRS 5 have been fulfilled?
 - (b) Irrespective of the response to point (a) above, does a change in a disposal method from a plan that previously qualified as held for sale to a plan to spin off Division B, and issue a dividend in kind to the shareholders, qualify as a change to a plan of sale?
13. We will analyse these questions in separate sections of this paper.

Section 1—Is an approved prospectus needed to qualify as held for sale?

Background information

14. We understand that according to the Directive 2010/73/EU¹ a prospectus is a formal legal document that is required by and filed with a securities regulator “when securities are offered to the public or admitted to trading”. Although this

¹ <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2010:327:0001:0012:EN:PDF>

directive is an EU directive, it provides some useful background that we think will be of general use.

15. A prospectus also enables investors make informed investment decisions as stated in the following extract of paragraph 15 of Directive 2010/73/EU (emphasis added):

The summary of the prospectus should be a key source of information for retail investors. It should be a self-contained part of the prospectus and should be short, simple, clear and easy for targeted investors to understand. **It should focus on key information that investors need in order to be able to decide which offers and admissions of securities to consider further. Such key information should convey the essential characteristics of, and risks associated with, the issuer, any guarantor, and the securities offered or admitted to trading on a regulated market.** It should also provide the general terms of the offer, including estimated expenses charged to the investor by the issuer or the offeror, and indicate the total estimated expenses, since these could be substantial. **It should also inform the investor of any rights attaching to the securities and of the risks associated with an investment in the relevant security.**

16. Paragraph 20 of Directive 2010/73/EU refers to the conditions that give a prospectus official validity before the competent authority, as follows:

In order to improve legal certainty, the validity of a prospectus should commence at its approval, a point in time which is easily verified by the competent authority. Furthermore, in order to enhance flexibility, issuers should also be able to update the registration document in accordance with the procedure for supplementing prospectuses.

17. Paragraph 22 of the same Directive further states that prospectus information should be made public for investors. An extract of this paragraph is shown below (emphasis added):

Internet ensures easy access to information. **In order to ensure better accessibility for investors, the prospectus should always be published in an electronic form on the relevant website.** Where a person other than the issuer is responsible for drawing up the prospectus, it should be sufficient for that person to publish the prospectus on the website of that person.

Question asked by the submitter

18. The submitter asks the following question:
- **Would Division B qualify as held for sale as of December 31, 20X1 when there is a disposal plan that is intended to be achieved by means of an initial public offering, but where the prospectus has not been approved by the securities regulator, assuming all the other criteria in IFRS 5 have been fulfilled?**

Views identified

19. The submitter identified two views in addressing this question:
- (a) **View 1:** the approval of the prospectus by the competent securities regulator is a condition that **is** required for the disposal plan to qualify as held for sale under the requirements in IFRS 5.
 - (b) **View 2:** the approval of the prospectus by the competent securities regulator is a condition that **is not** required for the disposal plan to qualify as held for sale under the requirements in IFRS 5.

*View 1—the approval of the prospectus by the securities regulator is a condition that **is** required to qualify as held for sale*

20. Supporters of View 1 believe that the approval of the prospectus by the securities regulator is a condition that is required to meet the criteria in paragraph 8 of IFRS 5, so that the sale of the disposal group can be considered *highly probable*.
21. They observe that without an approved prospectus from the securities regulator the sale cannot be considered *highly probable* because:
 - (a) the disposal group cannot be actively marketed for sale at a price that is reasonable in relation to its current fair value; and
 - (b) Entity A cannot initiate an active programme to locate a buyer.
22. Consequently, because some of the criteria in paragraph 8 of IFRS 5 for the classification of a disposal group as held for sale are not met, Division B would not qualify as held for sale as of December 31, 20X1.

*View 2—the approval of the prospectus by the securities regulator is a condition that **is not** required to qualify as held for sale*

23. Supporters of View 2 believe that the approval of the prospectus by the securities regulator is not needed to classify the disposal group as held for sale. This is because they can see that Entity A has been actively involved in the preparation of the prospectus and in ensuring that the prospectus' approval by the securities regulator will be *highly probable*.
24. For instance, they observe that Entity A has invested significant time and resources in the preparation of regulatory and sales documents for the securities regulators (ie meeting weekly with its outside advisors, and monitoring market conditions) and has contacted prospective institutional buyers before it receives regulatory approval. Entity A has also regularly communicated its plans to the public and is keeping its plans updated.

Staff analysis*Current guidance in IFRS 5*

25. We observe that paragraph 7 of IFRS 5 sets the following two requirements for the classification of a non-current asset (or disposal group) as held for sale (emphasis added):
- (a) the asset (or disposal group) must be **available for immediate sale** in its present condition subject only to terms that are usual and customary for sales of such assets (or disposal groups); and
 - (b) its sale must be **highly probable**. Appendix A of IFRS defines:
 - (i) *highly probable* as: “significantly more likely than probable”; and
 - (ii) *probable* as: “more likely than not”.
26. Paragraph 8 of IFRS 5 provides the following specific criteria that should be met for the sale to be *highly probable*:
- (a) the appropriate level of management must be committed to a plan to sell the asset (or disposal group);
 - (b) an active programme to locate a buyer and complete the plan must have been initiated;
 - (c) the asset (or disposal group) must be actively marketed for sale at a price that is reasonable in relation to its current fair value;
 - (d) the sale should be expected to qualify for recognition as a completed sale within one year from the date of classification, except as permitted by paragraph 9;
 - (e) actions required to complete the plan should indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn; and

- (f) the probability of shareholders’ approval (if required in the jurisdiction) should be considered as part of the assessment of whether the sale is highly probable.

Our view

27. We agree with supporters of **View 1**. On the basis of our assessment of the criteria described in paragraph 8 of IFRS 5 against the facts and circumstances described in the submitter’s fact pattern, we think that the sale of Division B by means of an IPO **cannot** be considered *highly probable*.
28. We note that a relevant action required to consider the disposal plan as *highly probable* is locating a buyer for the disposal group after marketing the disposal group actively at a sales price that is reasonable. In this respect we observe that Entity A has not been able to perform these actions because it has not obtained approval of the prospectus from the securities regulator.
29. For example, in the case of the EU prospectus directive, we note that the validity of a prospectus commences at its approval, when it is verified by the competent authority. We also think that the prospectus approval is important to ensure that the plan will not be affected by significant changes or by a risk that the plan will be withdrawn.
30. Our full assessment of the criteria in paragraph 8 of IFRS 5 is shown below:

Assessment of the criteria in paragraph 8 of IFRS 5 for a sale to be considered highly probable

Criteria in paragraph 8 of IFRS 5 for a sale to be <i>highly probable</i>:	Has the criterion been met?
The appropriate level of management must be committed to a plan to sell the asset (or disposal group.	YES. We note that there is a commitment to a plan to dispose of Division B by an IPO. Management has communicated its plans to the public.
An active programme to locate a buyer and complete the plan must have been initiated.	NO. We observe that Entity A has initiated internal preparations for a public offering including the preparation of regulatory and sales documents and has engaged with external advisors. However, Entity A is prevented by law from contacting prospective buyers until it receives regulatory approval. The latter factor has also prevented Entity A

Criteria in paragraph 8 of IFRS 5 for a sale to be <i>highly probable</i> :	Has the criterion been met?
The asset (or disposal group) must be actively marketed for sale at a price that is reasonable in relation to its current fair value.	from announcing an offering price publicly. NO. The entity has not: (a) publicly announced an offering price or (b) contacted prospective buyers. In our view these facts indicate that the disposal group has not been actively marketed at a price that is reasonable in relation to its current fair value.
The sale should be expected to qualify for recognition as a completed sale within one year from the date of classification, except as permitted by paragraph 9,	NO. Entity A is aware that there has been a decline in the market in which it planned to list its initial public offering and appears to be waiting for market conditions to change. Because the market conditions continue to decline, Entity A decides to defer the IPO. We think that this decision is an indication that the sale is not expected to qualify for recognition as a completed sale within one year from the date of classification.
Actions required to complete the plan should indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.	NO. We think that a relevant action required to complete the plan is to receive regulatory approval for the planned public offering, so that the entity can locate a buyer. In our view this is one of the actions that is missing to complete the plan so that the entity can make sure that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.
The probability of shareholders' approval (if required in the jurisdiction) should be considered as part of the assessment of whether the sale is highly probable.	YES. On June 30, 20X1 Entity A's Board of Directors approved a plan to dispose of Division B by way of an initial public offering, which is planned to occur by the end of the January 20X2.

31. On the basis of our assessment we think that the disposal plan (as described in the fact pattern, above) does not meet all the criteria in paragraph 8 (among those criteria is the lack of approval of the prospectus by the securities regulator). Consequently, we think that Division B would not qualify for classification as held for sale as of December 31, 20X1.
32. We also think that the requirements in IFRS 5 for the classification of an asset (or disposal group) as held for sale are clear and sufficient and no further guidance in IFRS 5 is needed.

Does a planned IPO meet the held for sale criteria (without the prospectus being issued and approved)?

33. We do not think that a planned public offering (without the prospectus being issued and approved) meets the condition established in paragraph 8 of IFRS 5 because it does not constitute an active programme that will allow the issuer to locate a buyer (ie it is just a plan). Also we think that there is a high level of uncertainty on whether the planned IPO would be or not completed.
34. Consequently, we think that a planned IPO by itself, cannot meet the ‘highly probable’ criteria in paragraph 8 of IFRS 5. In our view a prospectus needs to be in place and approved by a competent authority.

Section 2—Does a change in a disposal method qualify as a change to a plan of sale?

Question asked by the submitter

35. The submitter asks the following question:
- **Does a change in a disposal method from a plan that previously qualified as held for sale to a plan to spin off Division B and issue a dividend in kind to the shareholders qualify as a change to a plan of sale?**

Views identified

36. The submitter identified two views in addressing this question:
- (a) **View 1:** the change in the disposal method qualifies as a change to a plan of sale because a disposal and a distribution are different transactions and have different classification requirements.
- (b) **View 2:** the change in the disposal method does not qualify as a change to a plan of sale because a disposal and a distribution are both means to achieve the intended disposal.

View 1—the change in the disposal method qualifies as a change to a plan of sale because a disposal and a distribution are different transactions

37. Supporters of View 1 think that the requirements to classify a disposal group as held for sale (in accordance with paragraphs 7–9 of IFRS 5) are different from the requirements to classify a disposal group classified as held for distribution in accordance with paragraph 12A of IFRS 5. This is because supporters of this view think that these transactions are different in the following aspects:
- (a) a dividend-in-kind does not generate a cash flow for Entity A whereas an IPO does; and
 - (b) management can approve an IPO whereas a spin-off must be approved by the shareholders.
38. Consequently, supporters of View 1 think that changing the disposal plan (from a plan that involves an IPO to a plan that involves a distribution of dividends) constitutes a significant change in plan and the guidance in paragraph 26–29 of IFRS 5 should be followed.

View 2—the change in the disposal method does not qualify as a change to a plan of sale because a disposal and a distribution are both means to achieve the intended disposal

39. Supporters of View 2 observe that the classification, presentation and measurement requirements in IFRS 5, which apply to a disposal group that is classified as held for sale, also apply to a disposal group that is classified as held for distribution to owners (as stated in paragraph 5A of IFRS 5).
40. They also observe that the focus in IFRS 5 is whether an entity has a disposal plan irrespective of the method of disposal (ie whether the disposal group is sold through an IPO or through a spin-off and distribution to shareholders).

Staff analysis

Current guidance in IFRS 5

41. In accordance with paragraph 26 of IFRS 5, a change of plan of sale occurs when the criteria in paragraphs 7–9 are no longer met and the entity consequently, shall cease to classify the asset (or disposal group) as held for sale. In this respect, paragraph 26 of IFRS 5 states the following (emphasis added):

If an entity has classified an asset (or disposal group) as held for sale, but the criteria in paragraphs 7-9 are no longer met, the entity shall cease to classify the asset (or disposal group) as held for sale.

42. In addition, in accordance with paragraph 27 of IFRS 5, a non-current asset that ceases to be classified as held for sale (or ceases to be included in a disposal group classified as held for sale) at the lower of:

(a) its carrying amount before the asset (or disposal group) was classified as held for sale, adjusted for any depreciation, amortisation or revaluations that would have been recognised had the asset (or disposal group) not been classified as held for sale, and

(b) its recoverable amount at the date of the subsequent decision not to sell.

Our view

43. We do not think that the focus of analysis should be about whether a disposal group ‘held for distribution’ qualifies or not as a ‘held for sale transaction’ (as discussed in View 1 above) or on whether both methods of disposal are similar or not (as discussed in View 2 above). In this respect, we note that IFRS 5 does not distinguish among forms of disposal, as reflected in the definition of disposal group in Appendix A of IFRS 5. This definition states that (emphasis added):

A group of assets to be disposed of, by sale or otherwise, together as a group in a single transaction, and liabilities directly associated with those assets that will be

transferred in the transaction. The group includes goodwill acquired in a business combination if the group is a cash-generating unit to which goodwill has been allocated in accordance with the requirements of paragraphs 80–87 of IAS 36 Impairment of Assets (as revised in 2004) or if it is an operation within such a cash-generating unit.

44. Rather, we think that the focus of this analysis should be about whether the held for sale criteria in paragraph 8 of IFRS 5 will continue to be met despite of a change in the method of disposal.
45. We observe that, on the basis of the guidance in paragraph 26 of IFRS 5, what triggers a change in the classification (and measurement) of an asset (or disposal group) as held for sale is when the sale (or distribution) ceases to be highly probable. A sale (or distribution) ceases to be highly probable when the criteria in paragraphs 7–9 are no longer met. Said differently, a disposal group will continue to be classified as held for sale as long as the criteria in paragraphs 7–9 of IFRS 5 are still met.
46. Consequently, it is our view that a change in the disposal method from an IPO to a dividend-in-kind does not automatically cause an entity to fail to meet the criteria in paragraphs 7–9 of IFRS 5. In fact, we think that the application of paragraph 26 of IFRS 5 implies continuous monitoring of the criteria in paragraphs 7–9 of IFRS 5. Consequently, the conclusion as to whether the disposal group continues to be held for sale is dependent on the continuous assessment of those criteria.
47. We also note that IFRS 5 provides some specific requirements to be met for a disposal group to be classified as either ‘held for sale’ (paragraphs 6-12) or as ‘held for distribution’ (paragraphs 5A and 12A of IFRS 5).
48. In this respect we observe that the conditions required by paragraph 8 of IFRS 5 for a sale to be highly probable are very similar, if not identical, to the conditions required by paragraph 12A of IFRS 5. We, consequently, think that an entity should monitor the compliance with any of these conditions depending on how the disposal group has been classified.

49. Overall, we think that the requirements in IFRS 5 for the classification of an asset (or disposal group) are clear and sufficient with respect to:
- (a) the classification of an asset (or disposal group) as held for sale and as held for distribution to owners in; and
 - (b) the circumstances where an entity should cease to classify the asset (or disposal group) as held for sale (ie when the criteria in paragraphs 7–9 are no longer met).
50. Consequently, we do not think that any further guidance should be provided in IFRS 5 regarding the change of a disposal method.

Agenda criteria assessment

51. In February 2013, the Trustees of the IFRS Foundation, responsible for the governance and oversight of the International Accounting Standards Board (IASB), published an updated version of the IFRS Foundation *Due Process Handbook* ('the Handbook').
52. The Handbook contains new agenda-setting criteria for any implementation or maintenance issues, in paragraphs 5.14 –5.22. The staff's assessment of the new agenda criteria is as follows:

New agenda criteria

<p>Issues could include the identification of divergent practices that have emerged for accounting for particular transactions, cases of doubt about the appropriate accounting treatment for a particular circumstance or concerns expressed by investors about poorly specified disclosure requirements (5.14).</p> <p>The following indicates the reasons why the Interpretations Committee should address an issue (5.16):</p>	
<p>This is an issue that has widespread effect and has, or is expected to have, a material effect on those affected;</p>	<p>To be confirmed. We have not received outreach results from standard-setters and regulators yet, so this aspect still needs to be tested.</p>
<p>This is an issue where financial reporting would be improved</p>	<p>No. We do not think that financial reporting would be improved if the guidance in IFRS 5</p>

through the elimination, or reduction, of diverse reporting methods; and	were to be modified to: (a) address the classification of an asset (or disposal group) by means of an IPO; or (b) provide guidance on the change of a disposal method.
This is an issue that can be resolved efficiently within the confines of existing IFRSs and the <i>Conceptual Framework for Financial Reporting</i> .	Yes. The requirements in IFRS 5 for the classification of an asset (or disposal group) are clear and sufficient with respect to: (a) the classification of an asset (or disposal group) as held for sale (paragraphs 6-12) and as held for distribution to owners in paragraphs 5A and 12A; and (b) the classification of an asset (or disposal group) as held for sale in circumstances where the criteria in paragraphs 7-9 are no longer met, in paragraph 26 of IFRS 5.
This an issue that can be addressed in an efficient manner (5.17)	Yes. The requirements in IFRS 5 the classification of an asset (or disposal group) as held for sale and as held for distribution to owners are clear and sufficient.

Staff recommendation

53. On the basis of our assessment of the Interpretations Committee's agenda criteria, and also on our analysis in this paper, we recommend that the Interpretations Committee should not take either of the two issues analysed onto its agenda.
54. Unless the results of the outreach causes us to change our view, we propose issuing two separate tentative agenda decisions for the two issues analysed. We have set out proposed wording for these two tentative agenda decisions in **Appendix A** and in **Appendix B**, respectively.

Question for the Interpretations Committee

Question for the Interpretations Committee
Does the Interpretations Committee agree with the wording for the tentative agenda decisions shown in Appendix A and in Appendix B?

Appendix A—Tentative agenda decision (issue #1)

A1. We propose the following wording for the agenda decision:

IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*—classification in conjunction with a planned IPO but where the prospectus has not been approved by the securities regulator

The Interpretations Committee received a request to clarify the application of the guidance in IFRS 5 regarding the classification of a non-current asset (or disposal group) as held for sale, in the case of a disposal plan that is intended to be achieved by means of an initial public offering (IPO), but where the prospectus (ie legal document with an initial offer) has not been approved by the securities regulator:

The submitter requests the Interpretations Committee to clarify whether the disposal group would qualify as held for sale before the prospectus is approved by the securities regulator, assuming all the other criteria in IFRS 5 have been fulfilled.

The Interpretations Committee noted that the approval of the prospectus by the securities regulator is a condition that is necessary to meet the criteria in paragraph 8 of IFRS 5, so that the sale of the disposal group can be considered highly probable.

The Interpretations Committee observed that this requirement is necessary for the sale to be highly probable, on the basis of the guidance in paragraph 8 of IFRS 5: (a) the disposal group can be actively marketed for sale at a price that is reasonable in relation to its current fair value; and (b) the entity selling the disposal group can initiate an active programme to locate a buyer.

On the basis of the analysis above, the Interpretations Committee determined that, in the light of the existing IFRS requirements, neither an interpretation nor an amendment to IFRSs was necessary and consequently [decided] not to add this issue to its agenda.

Appendix B—Tentative agenda decision (Question #2)

B1. We propose the following wording for the agenda decision:

IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations*—change in a disposal method from a plan that previously qualified as held for sale to a plan to spin off a division and issue a dividend in kind to the shareholders

The Interpretations Committee received a request to clarify the application of the guidance in IFRS 5 regarding the classification of a non-current asset (or disposal group) as held for sale, in the case of a change in a disposal plan from a plan that previously qualified as held for sale to a plan to spin off a division and issue a dividend in kind to the shareholders.

The submitter requests the Interpretations Committee to clarify whether such a change in a disposal method would qualify as a change to a plan of sale.

The Interpretations Committee noted that in accordance with paragraph 26 of IFRS 5 an asset (or disposal group) continues to be classified as held for sale as long as the criteria in paragraphs 7–9 of IFRS 5 are still met.

The Interpretations Committee observed that a decision to change the form of disposal does not automatically cause an entity to fail to meet these criteria. In this respect, it observed that the application of paragraph 26 of IFRS 5 implies continuous monitoring of the criteria in paragraphs 7–9 of IFRS 5. Consequently, the conclusion as to whether the disposal group continues to be held for sale is dependent on the continuous assessment of those criteria.

The Interpretations Committee further noted that similar to paragraph 8 (which establishes a set of criteria for a sale to be highly probable), paragraph 12A in IFRS 5 also requires a set of conditions to be met for a distribution to be highly probable. The Interpretations Committee further observed that an entity should monitor the compliance with these conditions depending on how the disposal group has been classified (ie as either ‘held for sale’ or as ‘held for distribution’).

On the basis of the analysis above, the Interpretations Committee determined that, in the light of the existing IFRS requirements, neither an interpretation nor an amendment to IFRSs was necessary and consequently [decided] not to add this issue to its agenda.

Appendix C—Submission

C1 We received the following request. All information has been copied without modification.

Agenda item request: Discontinued operations - Change in disposal method

20 February 2013

Dear Mr Upton,

The European Securities and Markets Authority (ESMA) is an independent EU Authority that contributes to enhancing the protection of investors and promoting stable and well-functioning financial markets in the European Union (EU). ESMA achieves this aim by building a single rule book for EU financial markets and ensuring its consistent application across the EU. ESMA contributes to the regulation of financial services firms with a pan-European reach, either through direct supervision or through the active co-ordination of national supervisory activity.

As a result of the review of the financial statements carried out by national competent authorities and ESMA's co-ordination activities, we have identified an issue related to the application of IFRS 5 – Non-current Assets Held for Sale and Discontinued Operations, which we would like to bring to the attention of the IFRS Interpretations Committee for further consideration.

A detailed description of the case is set out in the appendix to this letter.

We would be happy to further discuss this issue with you.

Yours sincerely,

Steven Maijor

Chair ESMA

Julie Galbo

Chair ESMA's Corporate Reporting Standing Committee

APPENDIX – DETAILED DESCRIPTION OF THE ISSUE

1. Enforcers have identified divergent practices regarding the impact of a change in disposal method on the classification of assets held for sale in accordance with IFRS 5, as illustrated in the example below.

Description of the issue

2. Entity A has a December fiscal yearend and prepares its annual consolidated financial statements in accordance with IFRS.
3. On 30 June 20X1 Entity A's Board of Directors approved a plan to dispose of its profitable Division B by way of an initial public offering (IPO) planned to be completed by the end of the January 20X2. Entity A initiated internal IPO preparations for the sale of Division B including the preparation of regulatory and sales documents and engaging external advisors. In preparing for the IPO the business activities of Division B were separated into a distinct legal entity. Entity A did not file documents with its regulators, yet management communicated regularly its plans to the public. It believed that approval of the prospectus was highly probable. It determined internal price ranges but has not publicly announced an offering price. Various third-party analysts commented on their estimated market value of Division B. Entity A classified Division B as a discontinued operation in its interim financial statements as of 30 June 20X1 with consequential changes to the presentation of the statement of comprehensive income. Entity A classified the disposal group's net assets as held for sale and discontinued depreciating Division B's non-current assets.
4. During the second half of 20X1 market conditions declined. As of 31 December, 20X1 Entity A de-termined that the disposal of Division B by way of an IPO was no longer feasible as initially sched-uled. The IPO was still intended to be completed within 12 months of the original classification as discontinued operations. As of 31 December 20X1 Entity A re-evaluated the criteria in IFRS 5 and continued to classify Division B as a discontinued operation. It asserted that it was still committed to the disposal of Division B through an IPO during the first half of 20X2. Entity A also asserted that it believed that market conditions would improve and enable Entity A to sell Division B by way of an IPO. Entity A continued to update its documents to be filed with its securities regulator, meet weekly with its outside advisors, and monitored market conditions. It has not filed any offering documents with its securities regulator. Although Entity A was not permitted by law to contact prospective non-institutional buyers until after it receives regulatory approval, it may contact institutional buyers. It has re-evaluated internal price ranges and has still not announced an offering price publicly.
5. On June 30 20X2, one year after the original designation of Division B as held for sale, Entity A again reassesses the market and confirms its intention to dispose of Division B; however, manage-ment has now decided that an IPO was less likely. Instead, Division B

will be spun off and distributed to its shareholders by means of a dividend-in-kind. The Division B shares would then be listed separately on the stock exchange. Thus, both alternatives will be pursued.

6. Since a spin-off to shareholders is now also being considered, Entity A treats the classification of discontinued operations as a change to the plan of sale (IFRS 5, paragraph 26) and in the second half of 20X2 recognizes any depreciation, amortisation or revaluations that would have been recognised had the disposal group not been classified as held for sale. Nevertheless, the classification of the disposal group as discontinued operations (or “held for distribution to owners”) remains since the spin off (or IPO) is expected to be complete within the next 12 months (IFRS 5 paragraph 12).

Discussion

7. This issue is divided into two parts corresponding to the two year-end balance sheets dates, 31 December 20X1 and 20X2 for which annual financial statements were prepared.

Analysis as of 31 December 20X1

8. One criterion in IFRS 5 paragraph 8 requires that the disposal group be actively marketed in order for it to be classified as held for sale. Would Division B qualify as held for sale in the annual financial statements as of 31 December 20X1 before the prospectus is approved assuming all the other criteria in IFRS 5 have been fulfilled?

View 1

9. Proponents of View 1 believe that Division B would not qualify as held for sale as of 31 December 20X1 since, without an approved prospectus, the disposal group is not being actively marketed. In addition, without a predefined price it cannot be ascertained whether the sales price is reasonable compared with its current fair value.

View 2

10. Supporters of View 2 believe that an approval for a prospectus is not a mandatory condition in order to classify a disposal group that will be sold by means of an IPO as held for sale. Entity A initiated internal IPO preparations for the sale of Division B investing significant time and resources into the preparation of regulatory and sales documents and engaging external advisors. It has not filed documents with its regulators but it assesses the prospectus’ approval to be highly probable. Management has regularly communicated its plans to the public. It is permitted by law to contact prospective institutional buyers before it receives regulatory approval, which the entity also did. Entity A continues to update its documents to be filed with its regulator, meet weekly with its outside advisors, and monitor market conditions.

11. Likewise, as with a direct sale of an asset, the final price is usually the result of a negotiation process (or in connection with an IPO, the book-building process) and not necessarily presented by the seller to the buyer at the beginning of the negotiations. Thus, having a final price included in a prospectus is not mandatory in order to classify a disposal group which is to be sold via IPO to qualify as held for sale. Entity A has determined and continues to evaluate internal price ranges and various third-party analysts have commented on their estimated market value of Division B.

Analysis as of 31 December 20X2

12. Due to unfavourable market conditions (finance crisis etc.), the IPO was less likely. If the IPO is not feasible, management has decided to spin off Division B and issue a dividend-in-kind to the shareholders. The Division B shares would then be listed on the stock exchange. Does the change in disposal method to a plan that previously qualified as held for sale under IFRS 5 constitute a change in plan as outlined in IFRS 5 paragraph 26?

View 1

13. IFRS 5 paragraphs 7 to 9 address the sale of a disposal group while paragraph 12A relates to the disposal through a dividend in kind. Paragraphs 7 to 9 are similar but not identical to paragraph 12A and thus, differentiating between the types of disposal is critical. Both types of transactions are inherently different since a dividend-in-kind does not generate a cash flow for Entity A whereas an IPO does. In addition, the management board can approve an IPO whereas a spin-off must be approved by the shareholders. Proponents of View 1 believe that a classification as discontinued operations can either be based on a sales scenario or on a dividend-in-kind scenario, but alternating between the two qualifies as a significant change in plan (IFRS 5 paragraph 8) and thus, the guidance in IFRS 5 paragraph 26 must be followed.

View 2

14. IFRS 5 does not define the required level of detail necessary in a disposal plan. Additionally, it does not define whether the plan relates specifically to the method used to dispose of the group or, for example, to the composition of the disposal group. In both the sale and the dividend-in-kind scenarios management's intention to dispose of the disposal group remains unchanged. Only the method of disposal has changed. IFRS 5 paragraph 5A also clarifies that the classification, presentation and measurement requirement in IFRS 5 applicable to a disposal group that is classified as held for sale also apply to a disposal group that is classified as held for distribution to owners. Regardless to whether the disposal group is sold through an IPO or spun off to shareholders, the disposal group will be removed from Entity A. The entity will not principally recover the book value of the disposal group through continuing use (IFRS 5 paragraph 6).

15. Treating the alternative disposal method as a change of plan effectively leads to a reversal of the initial held for sale classification of Division B followed by an immediate re-classification of the same disposal group again as held for sale.
16. Had management defined both alternatives at the onset of the disposal deliberations, no change in the disposal plan would have occurred. As stated in IFRS 5 paragraph 5A, the requirements in IFRS 5 apply to both a sale and a distribution to owners. Thus, expanding the disposal plan to include a dividend-in-kind would not represent a significant change in plan, assuming the criteria in IFRS 5 are otherwise fulfilled.
17. If a disposal does not occur within 12 months of the original designation as held for sale, the entity is required to take actions necessary to respond to the circumstances that were previously considered unlikely and that led to the postponement of the original 12-month disposal target (IFRS 5, Appendix B (c)). Adding the possibility of a spin-off of the division as an alternative mean of disposal of Division B qualifies as an action taken in response to those circumstances. Thus, by adding a different disposal method, the entity is complying with IFRS 5 Appendix B(c) and the designation as held-for-sale should not have been suspended.

Request

18. Is the approval of prospectus necessary to qualify Division B as held for sale in the annual financial statements as at 31 December 20X1 in light of the various legal restrictions?
19. Assuming all the criteria of IFRS 5 has previously been fulfilled (independent from the response to the first question), should a change in the disposal method from an IPO to a dividend-in-kind qualify as a change in disposal plan as discussed in IFRS 5 paragraph 26.