

STAFF PAPER

November 2014

IFRS Interpretations Committee Meeting

Project	IAS 39— <i>Financial instruments: Recognition and Measurement</i>		
Paper topic	Holder's accounting for exchange of equity instruments		
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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. The IFRS Interpretations Committee ('the Interpretations Committee') received a submission from Organismo Italiano di Contabilità, the Italian national standard-setter, about the accounting by the holder of equity instruments when the issuer exchanges its original equity instruments for new equity instruments in the same organisation but with different terms. Specifically, this transaction involved equity instruments issued by a central bank. The exchange of the instruments was imposed on the holders as a consequence of a change in legislation.
2. The accounting question asked is whether the holders of the equity instruments should account for this exchange under IAS 39 *Financial Instruments: Recognition and Measurement* as a derecognition of the original equity instruments and the recognition of new instruments.
3. The Interpretations Committee discussed this issue in July 2014.¹ At that meeting the Interpretations Committee tentatively decided not to add the issue to its agenda because:
 - (a) the issue is not widespread, due to the unique nature of the transaction;and

¹ See [Agenda Paper 15 for the IFRS Interpretations Committee meeting in July 2014](#).

(b) the submitter had not identified significant diversity in accounting for this transaction among the holders of the equity instruments in question.

4. This paper contains:

- (a) a summary of the comments received on the tentative agenda decision;
- (b) the staff analysis of those comments; and
- (c) the staff recommendation to finalise the agenda decision without modification.

Comments received on the tentative agenda decision

5. We received three comment letters on the tentative agenda decision that was published in July 2014. These are included in Appendix B.
6. Two respondents (Deloitte and the Comitê de Pronunciamentos Contábeis (the Brazilian Accounting Pronouncements Committee)) both agree with the decision not to add the issue to the Interpretations Committee's agenda for the reasons set out in the tentative agenda decision.
7. The other respondent (ESMA) expresses concern over the lack of guidance in IFRS on the broader issue of derecognition of financial assets that have been exchanged or modified, including exchanges of equity instruments. They believe that this has led to diversity in practice in respect of this broader issue.
8. Consequently ESMA urges the Interpretation Committee to reconsider its decision and refer the broader issue to the IASB to be addressed comprehensively. They give the following reasons:
- (a) although these types of transactions are not widespread, they can have a significant impact on a number of entities (eg accounting for Greek Sovereign debt that was discussed by the Interpretations Committee in 2012 and accounting for increases of share capital from reserves);
 - (b) in the current economic environment, it is expected that other significant transactions that include modification of financial assets will

occur in the near future, thus increasing the risk that divergent practices will become entrenched; and

- (c) addressing the wider issue would promote transparency, achieve consistent application of IFRS and improve enforceability of the Standards.

Staff analysis

9. Financial asset restructurings were part of the IASB's comprehensive Derecognition project. However, after publishing an Exposure Draft in 2009, the IASB decided to remove the project from its agenda. This was because of the largely negative responses to the proposed approach in the Exposure Draft. Guidance from National Standards-Setters, and some responses to the Exposure Draft, indicated that the existing IFRS derecognition requirements had worked well during the financial crisis. Instead, the IASB focused on enhancing the disclosure requirements for transferred financial assets in IFRS 7 *Financial Instruments: Disclosures*. As a consequence, IAS 39's derecognition requirements were incorporated unchanged into IFRS 9 *Financial Instruments*.
10. Responses to the Exposure Draft highlighted the complexities associated with the proposals. This experience highlights that modifications and exchanges of financial assets is a difficult and controversial issue that cannot be addressed in isolation from the more general derecognition model for both financial assets and financial liabilities.
11. Whether to tackle the wider issue about lack of derecognition guidance for exchanges and modifications of financial assets in general was also touched upon during discussions at the Interpretations Committee meeting in July 2014 within the context of this issue. It was also discussed by the Interpretations Committee in September 2012 within the context of the Greek Government Bond issue.²
12. In both cases, the Interpretations Committee noted that this wider issue was too broad for the Interpretations Committee to deal with.

² See [Agenda Paper 3 of the IFRS Interpretations Committee meeting in September 2012](#).

Staff recommendation

13. Consequently, the staff recommend that the Interpretations Committee should finalise the agenda decision, without modification, as proposed in Appendix A.

Questions for the Interpretations Committee

Questions

1. Does the Interpretations Committee agree with the staff's recommendation that the Interpretations Committee should finalise its decision not to add this issue to its agenda?
2. If the answer to Question 1 is 'Yes', does the Interpretations Committee agree with the wording of the final agenda decision in Appendix A of this Agenda Paper?

Appendix A—Proposed wording for the final agenda decision**IAS 39 *Financial Instruments: Recognition and Measurement*—Holder’s accounting for exchange of equity instruments**

The Interpretations Committee received a request about the accounting by the holder of equity instruments in the circumstance in which the issuer exchanges its original equity instruments for new equity instruments in the same entity but with different terms. Specifically, this transaction involved equity instruments issued by a central bank, and the exchange of instruments was imposed on the holders as a consequence of a change in legislation.

The submitter asked whether the holders of the equity instruments should account for this exchange under IAS 39 as a derecognition of the original equity instruments and the recognition of new instruments.

The Interpretations Committee observed that:

- (a) because of the unique nature of the transaction, the issue is not widespread; and
- (b) the submitter had not identified significant diversity in accounting for this transaction among the holders of the equity instruments in question.

For these reasons, the Interpretations Committee decided not to add this issue to its agenda.

Appendix B—Comment letters on the tentative agenda decision

Please refer to separate pdf document for the comment letters.