IFRS® Accounting

Staff paper

Agenda reference: 5C

IASB® meeting

Date	**February 2023**
Project	**Financial Instruments with Characteristics of Equity**
Topic	**Presentation of equity instruments**
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Purpose and structure

1. The purpose of this paper is to ask the International Accounting Standards Board (IASB) for tentative decisions on proposed clarifications related to the presentation of equity instruments in the scope of IAS 32 *Financial Instruments: Presentation*.

2. At its December 2022 meeting (Agenda Paper 5A), the IASB discussed stakeholder concerns that the information an entity provides in its financial statements about the equity instruments it has issued is too limited. The IASB also discussed the interaction between the FICE project and the IASB's project on Primary Financial Statements (PFS Project). The IASB did not make any decisions on this matter but asked the staff to further explore potential presentation requirements that meet the needs of users of financial statements.

3. At this meeting, the staff present further analysis taking into account feedback from IASB members and recommend proposed amendments to IAS 1 *Presentation of Financial Statements*. Our recommendation is also summarised in paragraph 6 of Agenda Paper 5 of this meeting.

4. This paper is structured as follows:

   (a) Staff analysis:

(i) Current requirements in IFRS Accounting Standards;
(ii) PFS project;
(iii) Information needs of users of financial statements;
(iv) IASB tentative decisions; and
(v) Potential additional solutions considered;

(b) Staff recommendation; and

(c) Question for the IASB.

Staff analysis

Current requirements in IFRS Accounting Standards

5. IAS 1 contains the following requirements related to the presentation of equity instruments, amongst others (**emphasis added**):

(a) the statement of financial position shall include **line items** that present non-controlling interests presented within equity and issued capital and reserves attributable to **owners** of the parent (paragraph 54(q)-(r));

(b) an entity shall present **additional line items** (including by disaggregating the line items listed in paragraph 54), headings and subtotals in the statement of financial position when such presentation is relevant to an understanding of the entity's financial position (paragraph 55);

(c) an entity shall disclose, either in the statement of financial position or in the notes, **further subclassifications** of the line items presented, classified in a manner appropriate to the entity's operations (paragraph 77);

(d) an entity shall present profit or loss and comprehensive income for the period attributable to non-controlling interests and **owners** of the parent in the statement of profit or loss and other comprehensive income (paragraph 81B);

(e) an entity shall present, either in the statement of changes in equity or in the notes, the amount of dividends recognised as distributions to **owners** during the period, and the related amount of dividends per share (paragraph 107); and

(f) the components of equity include, for example**, each class of contributed equity**, the accumulated balance of each class of other comprehensive income and retained earnings (paragraph 108).

6. IAS 33 *Earnings per Share* contains the following requirements related to equity instruments, amongst others:

   (a) For the purpose of calculating basic earnings per share, the amounts attributable to **ordinary equity holders** of the parent entity in respect of:

      (i) profit or loss from continuing operations attributable to the parent entity; and

      (ii) profit or loss attributable to the parent entity

   shall be the amounts in (a) and (b) adjusted for the after-tax amounts of preference dividends, differences arising on the settlement of preference shares, and other similar effects of preference shares classified as equity (paragraph 12).

   (b) An entity shall disclose the amounts used as the numerators in calculating basic and diluted earnings per share, and a reconciliation of those amounts to profit or loss attributable to the parent entity for the period. The reconciliation shall include the individual effect of **each class of instruments** that affects earnings per share (paragraph 70(a)).

PFS project

7. In its January 2023 meeting (Agenda Paper 21B), as part of the PFS project, the IASB discussed how it will balance the use of specific requirements with a reliance on the general requirements, to help it apply a consistent approach in future decisions across

projects. The IASB was not asked to make any decisions at the January 2023 meeting. Paragraphs 8-9 below are extracts from that paper.

8. The general requirements for disaggregation of amounts in the primary financial statements are established by:

   (a) the role of the primary financial statements, which is to provide a structured summary that is useful for:

      (i) obtaining an understandable overview of the entity's assets, liabilities, equity, income, expenses and cash flows;

      (ii) making comparisons between entities, and between reporting periods for the same entity; and

      (iii) identifying items or areas about which users of financial statements may wish to seek additional information in the notes; and

   (b) specifically for the statement(s) of financial performance and the statement of financial position, the requirement to present additional line items when necessary to give an understandable overview of income and expenses or assets, liabilities and equity.

9. The IASB also tentatively decided that it would set out the following benefits and costs of specifying any line items to consider in future projects:

   (a) the benefits of specifying line items are:

      (i) specific requirements result in increased comparability of primary financial statements across entities.

      (ii) specific requirements are easier to apply and enforce compared to the application of a general principle.

      (iii) specific requirements can include guidance on how the requirement can be met, for example on how items covered by the requirement might be identified or presented. Such guidance could enhance comparability of amounts and help make the requirements more operational.

(iv) specific requirements can be accompanied by a specific cost relief, should the IASB decide such relief is appropriate.

(b) the cost of specifying line items is that a list of specified line items is more likely to promote a checklist compliance approach. Entities may simply present the specified line items and not consider whether:

(i) the line item results in the statement giving a less understandable overview of the assets/liabilities/equity or income/expenses; or

(ii) additional disaggregation would be useful.

Information needs of users of financial statements

10. The staff considered that most users of financial statements are investors or potential investors in an entity's ordinary shares. Users of financial statements have over the years (including through feedback on the 2018 Discussion Paper *Financial Instruments with Characteristics of Equity* (2018 DP)) told us that they require:

(a) information to be more accessible and less confusing so that they can navigate the financial statements;

(b) a clearer distinction of the distribution of profits amongst holders of different types of equity instruments so that they can understand the effect other classes of equity instruments have on the returns to ordinary shareholders;

(c) transparency as to whether an entity has issued other instruments classified as equity without having to go through multiple notes to the financial statements to try and piece together the information needed to calculate ratios; and

(d) information to understand the key features that lead to the classification as equity or financial liability so that they can perform their own analyses and valuations.

IASB tentative decisions

11. In February 2021 (Agenda Papers 5E and 5F), the IASB discussed the classification of perpetual instruments containing obligations that arise only on liquidation ('perpetual instruments'). Applying IAS 32, these instruments are classified as equity although they have many features usually associated with financial liabilities ('debt-like features'). Applying the classification approach in the 2018 DP these instruments would have been classified as financial liabilities, at least in part and many respondents were opposed to this change.

12. Considering the feedback from further outreach with equity investors in ordinary shares together with the costs and benefits of a classification change, the IASB tentatively decided not to change classification of these perpetual instruments but to develop presentation and disclosure requirements instead.

13. In April (Agenda Papers 5A, 5B and 5C) and May 2021 (Agenda Paper 5), the IASB discussed potential refinements to three new types of disclosures proposed in the 2018 DP.

14. In April 2021, the IASB tentatively decided that, for financial instruments with characteristics of both financial liabilities and equity instruments (except for stand-alone derivatives), an entity would be required to disclose in the notes information about:

    (a) 'debt-like features' in financial instruments that are classified as equity instruments;

    (b) 'equity-like features' in financial instruments that are classified as financial liabilities; and

    (c) debt-like and equity-like features that determine the classification of such financial instruments as financial liabilities, equity instruments or compound financial instruments.

15. In April 2021, the IASB also tentatively decided to require an entity to disclose information about the maximum dilution of ordinary shares in the notes, including:

    (a) the maximum number of additional ordinary shares that an entity could be required to deliver for each type of potential ordinary share outstanding at the reporting date. An entity would:

        (i) include the total number of share options outstanding (as required to be disclosed by IFRS 2 *Share-based Payment*) and the number of unvested shares, if known; and

        (ii) indicate the possibility for unknown dilution where the maximum number of additional ordinary shares that could be delivered is not yet known.

    (b) the minimum number of ordinary shares required to be repurchased.

    (c) sources of any significant changes in (a) and (b) from the prior reporting period and how these sources contributed to those changes.

    (d) terms and conditions relevant to understanding the likelihood of maximum dilution, including a cross-reference to disclosures required by IFRS 2 for a description of share-based payment arrangements.

    (e) a description of any share buy-back programmes or other arrangements that may reduce the number of shares outstanding.

16. In May 2021, the IASB tentatively decided to require:

    (a) an entity to disclose and categorise in the notes its claims that are financial instruments in a way that reflects differences in their nature and priority, and at a minimum, to distinguish between:

        (i) secured and unsecured financial instruments;

        (ii) contractually subordinated and unsubordinated financial instruments; and

(iii) those issued or owed by the parent and those issued or owed by subsidiaries; and

(b) the disclosures to be made for all financial liabilities and equity instruments that are within the scope of IAS 32.

17. Considering the types of equity instruments issued by entities, the staff are of the view that the disclosures tentatively decided by the IASB in the FICE project largely meet the information needs of users of financial statements (as described in paragraph 10 of this paper), including the need to understand the key features that lead to the classification and transparency about the existence of other equity instruments.

18. Any equity instrument that is not an ordinary share will likely either have a debt-like feature (for example, non-redeemable preference shares with a fixed cumulative coupon) or expose ordinary shareholders to potential dilution (for example written call options on own shares) and will thus be included in the scope of those disclosure proposals. In addition, the different types of equity instruments would need to be described as part of the proposed disclosure of the nature and priority of claims against the entity. For example, perpetual instruments, non-redeemable preference shares, non-controlling interest and ordinary share capital could be disclosed separately as unsecured and subordinated claims.

Potential additional solutions considered

19. The staff analysed whether it is necessary to develop specific presentation requirements as part of the FICE project to address the information needs of investors in ordinary shares (see paragraph 10 of this paper). Any specific presentation requirements would be in addition to the existing general presentation requirements in IAS 1 and the proposed disclosures tentatively agreed to by the IASB (see paragraphs 14-16 of this paper). The staff also considered relevant tentative decisions made on the PFS project including the tentative decision described in paragraph 9 of this paper.

Transparency as to whether an entity has issued other instruments classified as equity

20. The staff considered whether specifying further sub-classes of equity instruments in the statement of financial position would be a feasible solution to provide transparency about an entity's issued equity instruments.

21. The staff highlight that there are already existing requirements in IAS 1:

    (a) paragraph 54(r) of IAS 1 requires the statement of financial position to include line items that present the issued capital and reserves attributable to **owners of the parent.** Owners are defined in paragraph 7 of IAS 1 as holders of instruments classified as equity.

    (b) paragraph 108 of IAS 1 explains that the components of equity in the statement of changes in equity include, for example**, each class** of contributed equity.

    (c) paragraph 77 of IAS 1 requires further subclassifications of the line items presented, either in the statement of financial position or in the notes classified in a manner appropriate to the entity's operations. Paragraph 78(e) of IAS 1 gives an example of subclassification of equity capital and reserves into **various classes**, such as paid-in capital, share premium and reserves.

22. The staff think requiring specified line items for particular types of equity instruments is not the best approach for the following reasons:

    (a) different entities issue different types of equity instruments (for example, non-redeemable preference shares, perpetual instruments, derivative equity instruments and equity components of compound instruments) in addition to ordinary shares depending on their financing or regulatory requirements.

    (b) if the IASB were to require specified line items for equity instruments in the statement of financial position, questions may arise whether those same equity instruments would need to be presented in separate columns in the statement of changes in equity and in separate lines as part of the attribution section of

the statement of comprehensive income. In addition, questions may arise whether the carrying amounts of these other equity instruments should be updated to include the amount of total comprehensive income attributable to the holders of these instruments, for example cumulative coupons for the period.

(c) based on the 2018 DP feedback there was not a clear request from users of financial statements for further line items in the statement of financial position and not all users of financial statements generally support additional line items on the face of the financial statements. For example, although in the context of separate presentation of financial liabilities with equity-like returns, some users of financial statements explained that separate presentation would complicate their understanding of the statement of comprehensive income and the statement of financial position.

(d) the proposed disclosures on key terms and conditions, potential dilution, and the nature and priority of claims already provide transparency about whether an entity has issued other equity instruments. The proposed disclosures would identify items or areas about which users of financial statements may seek additional information.

23. Even if the IASB does not require specified line items for particular types of equity instruments, entities are not precluded from presenting additional line items in the statement of financial position. Entities have to apply judgement and decide themselves whether they need to present additional line items or disaggregate existing line items for the different types of issued equity instruments in compliance with paragraphs 55 and 77 of IAS 1. Entities will also be subject to any future requirements coming out of the PFS project relating to the role of the primary financial statements, required line items, additional line items and the principles for aggregation and disaggregation.

Clearer distinction of the distribution of profits amongst holders of different types of equity instruments

24. Users of financial statements want a clearer distinction of the distribution of profits amongst holders of equity instruments so that they can understand how the entity distributes its returns to ordinary shareholders. The staff considered whether a stronger link could be made between the statement of comprehensive income and the disclosures (for example, earnings per share disclosures) to meet this need. In particular, we considered the attribution section presented at the end of the profit or loss section applying paragraph 81B of IAS 1 and how the amount of profit attributable to *ordinary shareholders* could be made more visible on the face of the statement of comprehensive income.

25. Paragraph 81B of IAS 1 requires an entity to present profit or loss and comprehensive income for the period attributable to non-controlling interests and **owners** of the parent (ie holders of instruments classified as equity). The staff note that before paragraph 81B of IAS 1 was introduced, entities would present profit attributable to *non-controlling interests* as a line-item deduction from net profit for the year. The net result of profit attributable to *owners of the parent* would then be presented on the face of the statement of comprehensive income. The staff considered but rejected a proposal to present dividends attributable to *preference and other equity holders* as a further deduction but from profit attributable to *owners of the parent* to arrive at *profit attributable to ordinary shareholders* on the face of the statement of comprehensive income.

26. The staff think such presentation would not comply with the requirements in IFRS Accounting Standards:

    (a) presenting dividends attributable to other equity holders as a deduction would require profit attributable to non-controlling interests to be presented as a *deduction* from net profit for the year (ie similar to an expense line item). However, paragraph 81B of IAS 1 explicitly requires an entity to present the

allocation of profit or loss and other comprehensive income for the period "*in addition to* the profit or loss and other comprehensive *sections*".

(b) dividends paid or payable by the entity on equity instruments cannot be included in the statement of comprehensive income:

   (i) paragraph 106(d)(iii) of IAS 1 requires distributions to owners to be presented in the statement of changes in equity. Distributions to holders of equity claims are not items of expense.

   (ii) paragraph 107 of IAS 1 requires the amount of dividends recognised as distributions to owners during the period, and the related amount of dividends per share to be presented either in the statement of changes in equity or in the notes.

   (iii) paragraph 13 of IAS 33 explains that dividends on preference shares classified as liabilities are included in the determination of profit or loss for the period attributable to ordinary equity holders of the parent entity.

27. The staff note that there is a disclosure requirement that would provide users of financial statements with the amount of net income attributable to ordinary shareholders. Paragraph 70(a) of IAS 33 requires disclosure of the numerator used in calculating basic earnings per share and a reconciliation of the numerator to profit or loss attributable to the parent which includes the individual effect of each class of instruments that affects earnings per share.

Staff recommendation

28. In considering the existing requirements in IAS 1 as highlighted in this paper, the staff note that they *could* be applied to meet the information needs of users of financial statements (as described in paragraph 10 of this paper). For example:

(a) paragraph 54(r) of IAS 1 *could* be interpreted as already requiring presentation of issued capital and reserves attributable to other equity holders in addition to ordinary shareholders;

(b) paragraph 108 of IAS 1 *could* be interpreted as already requiring the presentation of contributions from other equity holders in addition to ordinary shareholders;

(c) applying paragraph 81B of IAS 1, entities *could* present an allocation of profit or loss and other comprehensive income to ordinary shareholders separately from the allocation to other holders of instruments classified as equity; and

(d) applying paragraph 107 of IAS 1, entities *could* present or disclose dividends to ordinary shareholders separately from dividends to holders of other instruments classified as equity.

29. However, based on the staff's analysis and considering the particular needs of investors in ordinary shares for transparency and clearer distinction of returns to *ordinary shareholders*, the staff think the existing requirements in IAS 1 should be amended so that *amounts attributable to ordinary shareholders* are more visible on the statement of financial position, the statement of comprehensive income and the statement of changes in equity. The staff think these amendments are necessary so that the existing requirements explicitly *require* particular presentation of amounts attributable to ordinary shareholders instead of relying on entities to interpret existing requirements. The staff recommend the IASB propose amendments that would require:

(a) line items in the statement of financial position that present issued capital and reserves attributable to *ordinary shareholders of the parent* separately from issued capital and reserves attributable to other owners of the parent (paragraph 54(r) of IAS 1);

(b) the components of equity for the purposes of the statement of changes in equity to include *each class of ordinary share capital* separately from each class of other contributed equity (paragraph 108 of IAS 1);

(c) profit or loss and comprehensive income for the period attributable to *ordinary shareholders of the parent* to be presented separately from the respective amounts attributable to other owners of the parent (paragraph 81B of IAS 1); and

(d) presentation in the statement of changes in equity or disclosure in the notes of the amount of dividends to *ordinary shareholders* separately from dividends to other owners during the period, and the related amount of dividends per share (paragraph 107 of IAS 1).

30. The staff are of the view that these proposed presentation amendments, together with the proposed disclosures (see paragraphs 14-16 of this paper) would meet the information needs of users of financial statements described in paragraph 10 of this paper. In addition, considering the IASB's discussion in January 2023 as part of the PFS project, the staff think:

(a) the benefits to users of financial statements of requiring the presentation of amounts attributable to ordinary shareholders would outweigh the costs to preparers. The additional information related to ordinary shareholders would already be available to entities so would not result in additional costs for preparers.

(b) presenting separate line items (or columns or amounts) that relate to ordinary shareholders makes sense when considered in the context of the role of the primary financial statements rather than solely in the context of the specific Accounting Standard (IAS 32) to which they relate.

Question for the IASB

Questions for the IASB
1. Does the IASB agree with the staff's recommendations as set out in paragraph 29 of this paper?