Staff paper

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IASB® meeting

Date	**September 2025**
Project	**Financial Instruments with Characteristics of Equity (FICE)**
Topic	**Detailed feedback—shareholder discretion**
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Introduction

1. In this paper the staff summarises the feedback from comment letters and outreach on the proposals about shareholder discretion in the Exposure Draft *Financial Instruments with Characteristics of Equity* (the ED) issued in November 2023.

2. Agenda Paper 5C for this meeting contains the staff's analysis and recommendations on this topic. That paper also asks whether the IASB agrees with the staff recommendations.

Overview

3. This paper is structured as follows:

   (a) background and questions in the ED;

   (b) summary of feedback; and

   (c) Appendix A—proposed amendments to IAS 32 in the ED related to shareholder discretion.

Background and questions in the ED

4. In applying paragraph 19 of IAS 32 *Financial Instruments: Presentation* to classify a financial instrument as a financial liability or an equity instrument, an entity considers whether it has an unconditional right to avoid delivering cash or another financial asset to settle a contractual obligation. In some cases, the settlement is at the discretion of the entity's shareholders. For example, an entity might issue preference shares that require the entity to pay coupons, which are subject to ordinary shareholders' approval.

5. Stakeholders have said that in practice, questions arise about whether, or when, to consider a decision of shareholders as a decision by the entity. These questions specifically relate to how shareholder decision-making rights affect whether a financial instrument is classified as equity or a financial liability, ie whether the entity has an unconditional right to avoid delivering cash or another financial asset (or to settle the instrument in such a way that it would be a financial liability).

6. The ED proposed factors an entity would be required to consider in assessing whether shareholder decisions are treated as entity decisions. The proposed factors would be relevant for the purposes of IAS 32 only and could not be applied by analogy when an entity applies the requirements in other IFRS Accounting Standards.

7. The IASB asked these questions:

Question 5—Shareholder discretion (paragraphs AG28A–AG28C of IAS 32)
The IASB proposes: (a) to clarify that whether an entity has an unconditional right to avoid delivering cash or another financial asset (or otherwise to settle a financial instrument in such a way that it would be a financial liability) depends on the facts and circumstances in which shareholder discretion arises. Judgement is required to assess whether shareholder decisions are treated as entity decisions (paragraph AG28A). (b) to describe the factors an entity is required to consider in making that assessment, namely whether:

Question 5—Shareholder discretion (paragraphs AG28A–AG28C of IAS 32)
(i) a shareholder decision would be routine in nature—made in the ordinary course of the entity's business activities; (ii) a shareholder decision relates to an action that would be proposed or a transaction that would be initiated by the entity's management; (iii) different classes of shareholders would benefit differently from a shareholder decision; and (iv) the exercise of a shareholder decision-making right would enable a shareholder to require the entity to redeem (or pay a return on) its shares in cash or another financial asset (or otherwise to settle it in such a way that it would be a financial liability) (paragraph AG28A(a)–(d)). (c) to provide guidance on applying those factors (paragraph AG28B). Paragraphs BC116–BC125 of the Basis for Conclusions explain the IASB's rationale for these proposals. Do you agree with these proposals? Why or why not? If you disagree with any of the proposals, please explain what you suggest instead and why.

Summary of feedback

Overall feedback

8. Most respondents that submitted comment letters on the ED included comments on the proposals about shareholder discretion.[1] Of these respondents, most (mainly standard-setters, preparers and accountancy bodies) agreed with the proposals, saying that IAS 32 currently contains no such guidance, which causes significant differences in the classification of similar instruments in practice. They agreed that:

   (a) judgement is required for the assessment of whether shareholder decisions are treated as entity decisions based on the legal and regulatory requirements they are subject to.

[1] Please refer to Agenda Paper 5 for this meeting for explanations of the terms used to broadly indicate the portion of respondents that reported a particular view. The feedback analysis on specific matters is based on the comments specifically made on that matter. Therefore, the terms that are used to indicate the portion of respondents that expressed a view are based on the population of respondents who specifically commented on that matter.

(b) the proposed factors in draft paragraph AG28A of IAS 32 are reasonable and useful in determining whether a shareholder decision is treated as an entity decision.

(c) the proposed factors are sufficiently 'principles-based' so as not to be overly prescriptive or rules-based. Applying a principles-based approach would help to resolve some practice questions, reduce diversity in practice and improve consistency which would be helpful for users of financial statements.

9. However, some (mainly standard-setters and accountancy bodies) provided mixed views. They welcomed the IASB's attempt to provide additional guidance and acknowledged that judgment is required to assess whether shareholder decisions are treated as entity decisions. Despite the overall support for the IASB's efforts, they either:

(a) said that further application guidance, illustrative examples or the establishment of more specific principles for the proposed factors-based approach was critical (eg what are other relevant factors, how to determine the weighting of the factors and examples of cases where shareholders' decisions are treated as entity's decisions). They believed that without providing further guidance, there will be significant uncertainty and subjectivity as to how judgement should be applied, which will not significantly reduce the existing diversity in practice or improve comparability. In addition, it could result in unintended consequences eg if shareholder decisions over dividends (see paragraph 18 of this paper) are not considered entity decisions, instruments currently classified as equity would be classified as financial liabilities.

(b) did not agree that the IASB should provide a list of factors that an entity would be required to consider when assessing whether shareholder decisions are treated as entity decisions. They believed the proposed factors may be seen as having more prominence than other factors that may be more relevant to the analysis. They questioned whether the factors to consider are suitable for resolving existing interpretation issues but they did not specify other relevant factors that could be considered.

10. Some others (mainly preparers) disagreed with and questioned the usefulness of the proposals because:

    (a) they see no need for clarification given that there is existing industry practice.

    (b) they do not think the factors proposed in draft paragraph AG28A of IAS 32 provide a sufficient basis to make an informed judgement or reach a conclusion on whether the entity has an unconditional right to avoid payment of cash. They think requiring an overall assessment of various factors weighed up against each other might also be impractical (see paragraph 21 of this paper).

    (c) the cost of implementing these proposals may outweigh the benefits and may not significantly reduce diversity in practice as intended. For example, they said the factors to consider may lead to frequent re-assessments of whether the decision of shareholders is within the control of the entity. In their view, this could result in the reclassification of financial instruments from equity to financial liabilities or vice-versa.

11. Of the small number of users of financial statements that commented on classification topics in the ED, one respondent commented that the proposed application guidance should be more specific to eliminate uncertainty and subjectivity in classification and requested examples of cases in which the shareholder decision is treated as the entity's decision.[2]

12. Instead of a factor-based approach as proposed in the ED, a few respondents expressed differing views on what an appropriate approach to shareholder discretion could be, such as:

[2] Agenda Paper 5A for the July 2024 IASB meeting includes a summary of the feedback from users of financial statements on the proposals in the ED.

(a) a rebuttable presumption that shareholders will always vote for their own benefit and therefore any decisions subject to shareholder approval would not be seen as entity decisions. They said such an assessment should consider, as a primary factor, the objective of financial reporting, which is focused on providing information to investors and other users of the financial statements. Based on that objective, investors should generally not be considered part of the entity. However, they acknowledged that the assessment may still require judgment, particularly when investors are members of management or the board of directors.

(b) starting from the presumption that shareholder decisions should generally be considered as entity decisions. They said the assessment of whether to treat a shareholder decision as an entity decision should be determined by considering whether the shareholder decision is made as part of the decision-making process under the entity's corporate governance. They did not think the assessment should be dependent on the party that proposed the action. Even if a shareholder exercises its redemption right, they believe the shareholder decision should be treated as an entity decision if the entity approves the redemption as part of its decision-making process.

(c) first the entity must evaluate if the contract gives an individual shareholder a unilateral decision-making right to require the entity to redeem shares or other instruments for cash or another financial asset, and if so, they believe there is no need for further assessment as this would be a financial liability at inception.

Specific feedback on the factors-based approach

13. Although most respondents agreed with the factors proposed in draft paragraph AG28A of IAS 32 in the ED (as discussed in paragraph 8 of this paper), some respondents asked for the proposed factors to be further clarified with regard to:

(a) decisions that are 'routine in nature' and made in the ordinary course of the entity's business activities;

(b) decisions that relate to actions proposed by an entity's management for shareholder approval;

(c) decisions that could result in different classes of shareholders benefiting differently; and

(d) decisions that could result in requiring the entity to redeem—or pay a return on—its shares to shareholders.

Routine in nature

14. With regard to decisions that are routine in nature, respondents asked for clarification of the intended meaning of routine in nature and how this should be interpreted in different circumstances. They asked for example, whether the declaration of a dividend is considered to be routinely made in the ordinary course of business. Respondents noted that shareholder decisions that could be deemed routine in nature by one entity might not be routine in nature for another entity. Therefore, similar financial instruments could be classified differently depending on the particular facts and circumstances. A few respondents suggested including examples of 'routine' and 'non-routine' shareholder decisions from paragraph BC119 of the Basis for Conclusions on the ED into the main body of the Standard.

15. A few respondents also asked whether all decisions involving a higher level of approval (ie special resolution or 75% of the votes) should automatically be considered as not a decision of the entity. One respondent did not think this would always be the case. They said it is not uncommon for some company constitutions to require special majority for entering into a new significant customer contract or incurring expenses over a certain threshold amount. In addition, in their view, requiring 75% majority means more shareholders have to act in concert and therefore provides more evidence that it represents an entity decision.

Action proposed by the entity's management for shareholder approval

16. With regard to the factor in paragraph 13(b) of this paper, a few respondents were concerned that if this factor is considered in isolation, structuring opportunities could arise because entities could include contractual terms that require initiation of transactions by management to achieve equity classification. Other respondents asked for clarification of:

    (a) whether the board of directors are included in the meaning of 'management' and how it would apply if one shareholder (or a group of shareholders) controls the board of directors (for example when making decisions about preference shares and the majority of the directors are controlled by the preference shareholders);

    (b) how to identify the party initiating the transaction when it is not straightforward, especially where management may propose an action but equally shareholders may propose the same action; and

    (c) how to determine whether a decision made by shareholders that are also acting as management (eg private equity sector), is made in their fiduciary capacity or investor capacity.

Different classes of shareholders benefit differently

17. In analysing decisions that could result in different classes of shareholders benefiting differently (paragraph 13(c) of this paper), a few respondents asked for further guidance with regard to the kind of judgments that should be made in analysing the different benefits. They noted that each individual shareholder will be affected differently by all the entity's decisions and therefore the purpose and relevance of this factor should be clarified.

Exercise of a shareholder decision-making right enables a shareholder to require the entity to redeem—or pay a return on—its shares

18. With regard to the exercise of a shareholder decision-making right that enables a shareholder to require the entity to redeem—or pay a return on—its shares (paragraph 13(d) of this paper), respondents were concerned that this factor could:

    (a) be interpreted as requiring a shareholder decision over dividends or to redeem an instrument not to be considered as an entity's decision. This is because, 'a return on its shares' implies the declaration of dividends. In their view, such shareholder decisions could be considered decisions of the entity if they are decisions made in accordance with the entity's governance structure and generally benefits the shareholder group as a whole or where all shareholders participate in the decision and not only one class of shareholders.

    (b) could result in ordinary shares that may be repurchased following a decision agreed at a general shareholders' meeting being classified initially as a financial liability.

Other comments on the proposed factors

19. Although some respondents generally agreed that all of the proposed factors would need to be considered in making the assessment, a few respondents said that the current wording that 'factors an entity *is required to consider* in making that assessment…' is too prescriptive and needs to be softened. They believed the factors are intended to be illustrative guidance or an indication of factors that *could* be considered in making the assessment and not a conclusive list of factors.

20. A few respondents suggested removing the directional indicators (the use of 'unlikely' and 'likely' when explaining the outcome of the factors) or using language that is less determinative, to allow for judgement considering the specific facts and circumstances at hand. In contrast, others objected to the reference to likelihood for the opposite reason—that it leaves or opens room for too much interpretation or judgement.

21. Some respondents commented on the explanations in draft paragraph AG28B of IAS 32 that the proposed factors are not exhaustive and the weightings applied to each factor depend on the specific facts and circumstances. They noted that entities will need to apply careful judgement in deciding the weighting of the factors when different factors point in different directions. They also noted that different outcomes could be achieved if the factors are assessed individually compared to an overall assessment of the various factors that are weighed up against each other. They therefore suggested that:

    (a) more emphasis is needed that no factor is conclusive or determinative on its own.

    (b) further application guidance is provided on other relevant factors to consider, how to determine the weighting of the factors or assess any interdependencies between different decision-making rights. A suggestion was to incorporate the example in paragraph BC123 of the Basis for Conclusions on the ED into the main text of IAS 32.

22. Some respondents specifically commented on the prohibition to apply the proposed approach by analogy:

    (a) some were in favour of the prohibition because in their view, when applying the requirements in other IFRS Accounting Standards to transactions involving shareholders or management, those requirements may serve different purposes. They observed that analogies might create opportunities for 'accounting arbitrage' for example, in IFRS 3 *Business Combinations* when identifying whether an acquirer obtains control of one or more businesses.

    (b) some also said that instrument holders that apply IFRS 9 *Financial Instruments* should not be required to assess these factors by analogy. They noted that some entities, when determining whether they hold an investment in a debt or equity investment, might consider how the issuer would classify an instrument. However, in their view, instrument holders might not have access to information that would be necessary to assess whether a decision of the shareholder is a decision of the entity.

Feedback on other matters

23. A few respondents also requested more clarity on other matters related to the proposals. They suggested the IASB clarify:

(a) how to apply the factors for the purposes of individual subsidiary financial statements where the shareholder is the parent company. For example, they asked the IASB to clarify when a group shareholder decision might be perceived as a decision of the subsidiary. Similarly, a few respondents requested further guidance for situations where the holder of a financial instrument is also the controlling shareholder of the issuing entity.

(b) whether events such as illegal acts or breaches of contracts, and mergers or initial public offerings ('IPOs') could be viewed as decisions within the entity's discretion.

(c) the capacity in which shareholders make their decisions or the necessity to make such identification. They said that in considering the specific facts and circumstances of the entity's situation, the assessment should understand the relationship between the entity and its shareholders.

(d) whether continuous assessments are necessary and whether reclassification would be permitted or required. The change in assessment as facts and circumstances change could be regarded as a change in circumstances external to the contractual arrangement but in some cases, it may be regarded as arising from events specified in the contract that were previously considered in classifying the instrument on initial recognition.[3]

[3] Draft paragraph 32C of IAS 32 states: Changes in circumstances external to the contractual arrangement arise from events not specified in the contract that have not been considered in classifying the financial instrument on initial recognition. Such events are not specific to a particular instrument, but would affect an entity's business activities and operations, for example, a change in an entity's functional currency or a change in an entity's group structure.

(e) the interdependency between statutory legal rules which determine the distinction between equity and liability and the proposed factors that determine whether a shareholder decision is treated as an entity decision. They questioned whether it is still necessary to consider the proposed factors if statutory legal rules determine the distinction between equity and liability.

Requests for illustrative examples

24. Some respondents specifically asked the IASB to consider providing illustrative examples of how the proposed factors would be applied to common fact patterns and how competing factors should be analysed to reduce diversity in practice. They were concerned that even with the proposed requirements, the level of judgement required to perform such assessment would remain significantly high. Therefore, they said additional illustrative examples to explain the underlying principles and minimise the risk of diversity in application would be helpful for both preparers and users of financial statements.

25. While some respondents made a general request for the IASB to develop illustrative examples, other respondents suggested illustrating particular scenarios.

Other suggestions

26. A few respondents made some suggestions the IASB could consider in their view, to enhance the usefulness of the requirements such as:

(a) clarifying that obligations that will or may be settled by delivering a variable number of the entity's own equity instruments are in the scope of the proposals even though paragraph 19 of IAS 32 requires an entity to assess whether it has an unconditional right to avoid delivering cash or another financial asset.[4]

[4] Paragraph 19 of IAS 32 states: "If an entity does not have an unconditional right to avoid delivering cash or another financial asset to settle a contractual obligation, the obligation meets the definition of a financial liability, except for those instruments classified as equity instruments in accordance with paragraphs 16A and 16B or paragraphs 16C and 16D…"

(b) noting any deviation from the IASB's previously held views, especially where those views informed the development of the *Conceptual framework for financial reporting* and explaining why it would be suitable to come to a different conclusion. In their view, the approach taken appears to be inconsistent with the views expressed by the IASB on the entity perspective—the concept of separation between the entity and its shareholders due to the fact that the vast majority of business entities have a substance distinct from that of their capital providers.

(c) clarifying the application of the disclosure requirements concerning shareholders discretion eg requiring more targeted disclosure requirements relating to the judgements applied in classifying a financial instrument.

(d) permitting the use of hindsight for the retrospective application of the requirements on shareholder discretion or introduce an exception to retrospective application if it can only be done with hindsight. For example, determining whether a particular shareholder decision was routine or non-routine at the time a contract was entered into may be onerous. Therefore, they suggested transitional relief could be provided whereby an entity may be permitted to assess whether a shareholder decision is routine or non-routine based on facts and circumstances at the date of transition.

Appendix A—proposed amendments to IAS 32 in the ED related to shareholder discretion

A1. The IASB proposed adding the following paragraphs to IAS 32 related to shareholder discretion:

Paragraph AG28A:

In determining whether an obligation meets the definition of a financial liability, paragraph 19 requires an entity to assess whether it has an unconditional right to avoid delivering cash or another financial asset. For some financial instruments, settlement of an obligation is at the discretion of the entity's shareholders. Whether the entity has an unconditional right to avoid delivering cash or another financial asset (or otherwise to settle it in such a way that it would be a financial liability) depends, therefore, on the facts and circumstances relating to that shareholder discretion. Judgement is required to assess whether such shareholder decisions are treated as entity decisions that result in it having an unconditional right to avoid delivering cash or another financial asset (or otherwise to settle it in such a way that it would be a financial liability). Factors an entity is required to consider in making that assessment include whether:

(a) a shareholder decision is routine in nature—made in the ordinary course of the entity's business activities. Routine decisions that are part of the entity's ordinary course of business are more likely to be treated as entity decisions.

(b) a shareholder decision relates to an action proposed or a transaction initiated by the entity's management for shareholder approval. If the entity's management can avoid an outflow of cash from the entity by not proposing an action requiring shareholder approval, shareholder discretion would have no bearing on the classification of the instrument because the shareholders would not have to make a decision. In contrast, if a shareholder decision relates to an action proposed or a transaction initiated by a third party, the shareholder decision is unlikely to be treated as an entity decision.

(c) different classes of shareholders benefit differently from a shareholder decision. If so, each class of shareholder is likely to make an independent decision as investors in a particular class of shares, and the shareholder decision is unlikely to be treated as an entity decision.

(d) exercise of a shareholder decision-making right enables a shareholder to require the entity to redeem—or pay a return on—its shares in cash or another financial asset (or otherwise to settle it in such a way that it would be a financial liability). Such decision-making rights indicate that the shareholders would make their individual decisions as investors in the shares, and the shareholder decision is unlikely to be treated as an entity decision

Paragraph AG28B:

An entity shall consider relevant factors in assessing whether a particular shareholder decision is treated as an entity decision. The factors set out in paragraph AG28A(a)–(d) are not exhaustive; other factors might be relevant in assessing whether a shareholder decision is treated as an entity decision. The weightings applied to each factor in making that assessment depend on the specific facts and circumstances. Different factors might provide more persuasive evidence in different circumstances. An entity shall also consider whether any interdependencies between shareholder decision-making rights affect whether, overall, it has an unconditional right to avoid delivering cash or another financial asset (or otherwise to settle a financial instrument in such a way that it would be a financial liability).

Paragraph AG28C:

The requirements in paragraphs AG28A–AG28B apply for the purposes of this Standard only. An entity shall not apply these requirements by analogy in applying the requirements in other IFRS Accounting Standards.