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**International
Accounting Standards
Board**

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Amendments to IAS 32 (Financial Instruments: Presentation) and IAS 1 (Presentation of Financial Statements) in respect of Puttable Financial Instruments and Instruments with Obligations Arising on Liquidation

Project Updates are provided for the information and convenience of constituents who wish to follow the IASB's deliberations. All conclusions reported are tentative and may be changed at future IASB meetings. Decisions become final only after completion of a formal ballot to issue an International Financial Reporting Standard, Interpretation, or Exposure Draft.

Introduction

This project report is structured as follows:

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Objective

1. The objective of the project is to provide a short-term, limited scope amendment to improve the financial reporting of particular puttable financial instruments and particular instruments with obligations for a pro rata share of the net assets of the entity on its liquidation (obligations arising on liquidation). At present, these instruments are classified as financial liabilities under IAS 32 *Financial Instruments: Presentation*.

Next Steps

2. On 22 June 2006, the IASB published an Exposure Draft of Proposed Amendments to IAS 32 *Financial Instruments: Presentation* and IAS 1 *Presentation of Financial Statements: Financial Instruments Puttable at Fair Value and Obligations Arising on Liquidation*. The Exposure Draft is available from the IASB's website. The comment deadline on the Exposure Draft closed on 23 October 2006.
3. In November 2007 the Board held two public roundtables to discuss a staff draft of the proposed amendment. A near-final staff draft was also posted on the IASB website.
4. The Board expects to finalise the amendments in the first quarter of 2008.

Background

Reasons for amending IAS 32

5. Constituents raised the following concerns about the application of IAS 32 and IAS 39 *Financial Instruments: Recognition and Measurement* to puttable financial instruments:
 - (a) On an ongoing basis, the liability is recognised at not less than the amount payable on demand. This can result in the entire market capitalisation of the entity being recognised as a liability depending on the value at which the instrument is put.

- (b) The changes in the carrying value of the liability are recognised in profit or loss. When the entity performs well and the fair value of the liabilities increases, a loss is recognised. When the entity performs poorly and the fair value of the liability decreases, a gain is recognised.
- (c) It is possible that the entity will report negative net assets because of unrecognised intangible assets and goodwill, and because the measurement of recognised assets and liabilities may not be at fair value.
- (d) The issuing entity's balance sheet portrays the entity as wholly, or mostly, debt funded.
- (e) Distributions of profits to shareholders are recognised as expenses. Hence, it may appear that net income is a function of the distribution policy, not performance.

Furthermore, constituents considered that additional disclosures and adapting the format of the income statement and balance sheet did not resolve these concerns.

6. The Board noted

- that some puttable financial instruments do represent a residual interest in the entity;
- that some puttable financial instruments would meet the definition of equity instruments in accordance with IAS 32 but for the holder's right to put the instruments back to the issuer; and
- that additional disclosures and adapting the format of the entity's financial statements, supplementing the treatment of these instruments in accordance with IAS 32 and IAS 39, did not resolve the problem of the lack of relevance and understandability of that current accounting treatment.

The Board decided to consider whether IAS 32 should be amended, as a short-term solution, pending the outcome of the longer-term project on liabilities and equity.

7. Issues similar to those raised by constituents relating to the classification of puttable financial instruments also apply to the classification of financial instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity on liquidation (for example, ordinary shares (or equivalent instruments) in a limited life entity and some partnerships that are required to

liquidate upon exit of a partner). Hence, the Board decided to add such instruments to the scope of the project.

Tentative Decisions to Date

The Board's tentative decisions to date can be found in the staff draft of the proposed amendments, which is available on the project summary page.

Contact information

8. Staff contacts

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