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Direct dial: Tel.: (+31) 88 4960 391
Date: Hoofddorp, March 25th 2024
Re: DASB Comment on Draft comment letter Financial Instruments with Characteristics of Equity

Dear members of the EFRAG Technical Expert Group,

The Dutch Accounting Standards Board (DASB) appreciates the opportunity to provide a response to the EFRAG Draft Comment Letter on the Exposure Draft ED/2023/5 ‘Financial Instruments with Characteristics of Equity’, issued by the IASB in November 2023.

We generally support EFRAG’s comments.

Hereafter we set out our responses to the questions to constituents as included in EFRAG’s draft comment letter. We have included the numbers of the paragraphs in the draft comment letter containing the questions we are responding to.

Paragraph 16, 17 and 18– The effects of relevant laws or regulations transfer
Like EFRAG we acknowledge that a classification that is solely based on contractual terms may lead to outcomes that contradict the principle-based nature of IFRS accounting standards. We believe that the current proposal by the IASB of considering only those contractual rights and obligations that are in addition to those created by relevant laws and regulations could lead to inconsistencies in the classification of instruments in the practice. However taking into consideration rights and obligations created by relevant laws and regulations could result in significant classification changes for certain instruments and would represent a change in current requirements beyond the scope of the FICE project.

We believe the current standard and the interpretations thereof have generally led to an acceptable classification outcome in many jurisdictions. Therefore we think current practice may be continued and are not in favor of the proposed clarifications.

We also share the view of EFRAG that there may be practical challenges in applying the proposals. Specifically we want to note the complexity to assess whether the terms explicitly stated in the contract are actually in addition to what is established by law. We think the application of the proposals to Mandatory Tender Offers is an area that needs to be addressed by the IASB.

Notwithstanding the above we do not expect significant classification changes or unintended consequences in the Dutch market based on the IASB proposals, although we have not conducted an exhaustive investigation into which type of contracts may potentially be impacted.

Paragraph 40 – Settlement in an entity's own equity instruments
We generally concur with the view of EFRAG.

We think the IASB's proposals on passage-of-time adjustments may lead to classification changes for options that can be exercised at different pre-determined dates because it may be difficult to demonstrate the difference between the amount of consideration to be paid or received on each settlement date represents only compensation proportional to the passage of time.

Paragraph 52, 53, 59 and 60– Obligation to purchase an entity's own equity instruments
We concur with the view of EFRAG that the debit entry related to the recognition of a liability to repurchase own equity should be presented as part of non-controlling interests (view 'b' in paragraph 52 of your draft comment letter). The IASB proposes that the initial amount of the financial liability would be removed from a component of equity other than non-controlling interests (NCI) if the entity does not yet have access to the rights and returns associated with ownership of the equity instruments to which the obligation relates even though, when settled, it is the NCI component of equity that will be debited. We think such accounting treatment, in addition to changing the current practice for a number of entities, could provide information to users which does not reflect the substance of the contracts regarding the share of equity that does not belong to NCI. For example this would lead to an undue and punitive impact on banks prudential own funds where the obligation to purchase NCI would have a more detrimental impact on prudential own funds than the actual purchase of such NCI.

We also support the suggestion of EFRAG for the IASB to address more comprehensively the questions that arise in practice related to the measurement of liabilities under IAS 32. Although we generally welcome the IASB proposals to reduce the current diversity in practice and improve comparability. Assuming the gross presentation is retained we acknowledge there are arguments to consider the measurement of the liability as part of transactions with owners in their capacity as owners and presentation within equity would be consistent with this. Therefore we suggest to make the classification of any gains or losses on remeasurement of the financial liability dependent on whether the entity has access to the rights and returns associated with ownership of the equity instruments to which the obligation relates. If the entity has access to the rights and returns associated with ownership of the equity instruments and thus the NCI is derecognized, any gains or losses on remeasurement of the financial liability should be recognized in profit or loss. However if access to the rights and returns associated with ownership of the equity instruments remains with the NCI any gains or losses on remeasurement of the financial liability should be recognized in equity.

In relation to your question about accounting for written put options on NCI in the separate financial statements we are of the view that accounting for such contracts as a derivate under IFRS 9 would provide the most useful information to the users of the financial statements (when the contract meets the definition of a derivative under the standard).

Paragraph 75, 76 and 77 – Contingent settlement provisions
We do not have specific concerns that the initial and subsequent measurement of the financial liability (or liability component of a compound financial instrument) arising from a contingent settlement provision would ignore probability. We think the proposed measurement is consistent with existing principles in IAS 32 and would appropriately reflect the potential outflow. However we would request the IASB to clarify the interaction between the principles in IAS 32 and IFRS 9.

We note some parties have concerns about the ability to continue to apply hedge accounting if certain payments to holders compound instruments would be classified as equity as a result of the proposals. We would welcome the IASB providing clarification on the impact on hedge accounting for different examples of hedges (cash flow hedges and fair value hedges) or to consider the potential impact in their final amendments.

We are of the view that term ‘non-genuine’ has been sufficiently clarified in the proposal. On the meaning of liquidation we concur with the view of EFRAG that IASB should clearly explain the meaning of the process for permanently ceasing operations and how it interacts with resolution and administration processes and insolvency. We believe that the definition that liquidation is the process that begins *after* an entity has permanently ceased its operations may be too narrow. It may for example be the case that instruments are repaid when the entity has not fully ceased its operations whilst at the same time liquidation, and thus the ultimate ceasing of its operations, is inevitable. We think in such a scenario, when it is certain that all shareholders will be repaid, the timing of such payments before or after the entity formally ceases operations should not impact an instrument’s classification.

Paragraph 86 and 87 – Shareholder discretion
We are currently unsure whether the proposals will cause changes in classification. To reduce diversity in practice we suggest that the IASB provides examples of how the proposals are applied to common fact patterns. We also believe that in the Dutch legal and regulatory context any decisions made in the ordinary General Meeting of Shareholders should be considered a decision made by the entity.

Paragraph 139, 140 and 141 – Disclosures
While acknowledging the interest of users of financial statement to understand the complex instruments issued we do not believe the proposal strikes the right balance between the benefit of disclosures to the users and the cost of preparers. Also we have concerns about potential disclosure overload. We believe the proposed scope is too broad and catches all types of issued instruments and potentially also deposits (i.e. almost the entire liability side in a financial institution). We believe the scope should be more narrow focusing on the more complex instruments. It should also be noted that for some entities that issue a large number of bespoke instruments (e.g. financial institutions), listing all terms and conditions for all instruments would be a very extensive exercise and such disclosure would potentially be of limited use for users of financial statements.

We generally agree with the guidance provided on debt-like characteristics and equity-like characteristics.

Paragraph 156 - presentation of amounts attributable to ordinary shareholders
We agree with EFRAG’s view on the term ‘ordinary shareholders’, as there could be different specific classes of shares, which makes it difficult to assess which type of shareholder is considered to be ordinary. Although we recognize the inherent limitation in the current binary debt-equity split, additional application guidance and illustrative examples would be needed to be able to perform the split.

Paragraph 174 -Transition
We agree with the retrospective application of the proposed amendments and also recognize the concerns indicated by EFRAG on the cost-benefit analysis and the accounting mismatches that could arise for entities applying hedge accounting. We do not have concerns in addition to the ones indicated by the EFRAG.

Paragraph 189 - Disclosure requirements for eligible subsidiaries
We welcome the reduced disclosure requirements for eligible subsidiaries in the scope of the forthcoming draft Accounting Standard. We believe that the proposed reduced disclosure requirements for subsidiaries without public accountability, in particular disclosures on the nature and priority of claims in liquidation, strikes a balance between costs for preparers and benefits for the users of financial statements.

If you have any questions please do not hesitate to contact me.

Yours sincerely,

drs. G.M. van Santen RA
Chairman Dutch Accounting Standards Board