RE: Comments on Draft IFRIC Interpretation DI/2012/2 Put options written on non-controlling interests

Dear Sir / Madam,

Mazars welcomes the opportunity to comment on the Draft IFRIC Interpretation on put options written on non-controlling interests

We strongly disagree with the proposed accounting treatment for puts written on non-controlling interests and the consensus reached by the Committee.

We believe that the Committee failed to consider both the specificities of the financial liabilities resulting from put options written on non-controlling interests and the diversity of the situations that exist in practice. This failure leads the Committee to propose a consensus that is built consistently with IAS 32 and IFRS 9 / IAS 39 but provides irrelevant and counter-intuitive outcomes.

As an example of these counter-intuitive outcomes:

- Where the exercise price of a put option is fair value, any increase in the fair value of the subsidiary would lead to the recognition of an expense in profit or loss, being the remeasurement of the liability. Thus, in that specific case, the group would show a loss while, in reality, it has become richer because of its existing stake. And the accounting treatment does not reflect the fact that, economically, buying the NCI at fair value would not enrich or impoverish the group.
On the contrary, a fixed exercise price may, in the case of a decrease in the fair value of the subsidiary, oblige the group to make an exchange under conditions that are unfavourable. In that case, the consensus proposed by the Committee would lead to no impact in profit or loss since there is no change in the measurement of the financial liability.

We believe that the situation is similar to that of IFRIC 3, where the Interpretation, although consistent with the applicable standards, led to an irrelevant outcome. At that time the Board decided to withdraw the Interpretation.
Regarding put options written on non-controlling interests, we encourage the Committee or the Board to consider the irrelevance of the outcome of the proposal and not to issue this Interpretation.
As a consequence the issue should be transferred to the Board, as there is a need for an in-depth review of this issue (as opposed to a narrow scope interpretation, which fails to satisfactorily portray the underlying economic reality) which should lead to adapting the standards to reflect in a proper way the economic outcomes of such a transaction.

We would be pleased to discuss our comments with you and are at your disposal should you require further clarification or additional information.

Yours sincerely

Michel Barbet-Massin

Head of Financial Reporting Technical Support
Appendix 1: detailed answers to the questions raised in the Draft IFRIC Interpretation.

**Question 1 Scope**

*The draft Interpretation would apply, in the parent's consolidated financial statements, to put options that oblige the parent to purchase shares of its subsidiary that are held by a non-controlling-interest shareholder for cash or another financial asset (NCI puts).*

*However, the draft Interpretation would not apply to NCI puts that were accounted for as contingent consideration in accordance with IFRS 3 Business Combinations (2004) because IFRS 3 (2008) provides the relevant measurement requirements for those contracts.*

*Do you agree with the proposed scope? If not, what do you propose and why?*

We do not understand why the scope only includes puts written by the parent company itself. The rationale behind the accounting for puts is to portray what disbursements the group could be forced to make. As a consequence, the scope should include puts written by both the parent company and its subsidiaries.

We agree that NCI puts accounted for as contingent consideration in accordance with IFRS 3 (2004) should be excluded from the scope of the interpretation. However we believe that the Committee should make it clear that this scope exclusion encompasses all NCI puts accounted for as contingent consideration in accordance with IFRS 3 (2004), irrespective of whether they have been issued as part of a business combination or not. Since puts issued after a business combination are very similar to those issued as part of a business combination, we would see no rationale to restate retrospectively the ones and not the others, provided that both were accounted for as contingent consideration.

We therefore suggest that the exemption applies to all puts accounted for as contingent consideration in accordance with IFRS 3 (2004), whether or not the puts have been issued as part of a business combination.
**Question 2 Consensus**

The consensus in the draft Interpretation (paragraphs 7 and 8) provides guidance on the accounting for the subsequent measurement of the financial liability that is recognised for an NCI put. Changes in the measurement of that financial liability would be required to be recognised in profit or loss in accordance with IAS 39 Financial Instruments: Recognition and Measurement and IFRS 9 Financial Instruments.

*Do you agree with the consensus proposed in the draft Interpretation? If not, why and what alternative do you propose?*

We totally disagree with the consensus proposed in the draft Interpretation.

From a technical standpoint, the Committee’s analysis is understandable insofar as it is true that changes in a financial liability normally impact profit or loss.

However, under different circumstances the Committee has decided that changes in a specific financial liability should be accounted through equity. According to IFRIC 17, any changes made to the dividend payable are to be recorded in a manner consistent with the original entry, i.e. in equity. The scope of IFRIC 17 includes distribution of non-cash assets, i.e. not only items of PPE but also financial assets. In other words, IFRIC 17 did envision instances where the dividend payable would be a financial liability.

We believe that regarding put options written on non-controlling interests, the Committee should have taken into account the features that make them different from other “normal” financial liabilities.

As the Committee did not consider the specificities of put options written on non-controlling interests, we do not believe that the proposed accounting treatment results in decision-useful information.

1. **The scope of the draft Interpretation is too narrow**, and many aspects of these contracts are not dealt with. Past discussions on this subject have proved how complex the issue is. Therefore, proposing an interpretation dealing with a very limited scope is unlikely to result in a significant improvement in financial reporting.

   There are many kinds of puts, issued for a variety of reasons. As a consequence, a unique accounting treatment will not be able to represent faithfully the economic reality.
2. **The proposed accounting treatment implicitly assumes that this is a “normal” liability**, whereas the particular nature of puts on non-controlling interests means that they straddle IAS 32 and IAS 27.

The fact that there are specific provisions in IAS 32 which require the recognition of a liability (a “gross” liability approach) makes it all the more appropriate to question the validity of the approach in this particular case.

3. **The outcome of the proposed accounting treatment is often counter-intuitive**, especially in the many cases where the exercise price is based on the fair value of the shares at the exercise date (which is frequent).

The proposed approach means that increases in the liability are accounted for as expenses, although it is the sound management of the entity by the controlling shareholder that created an (unrecognised) increase in the fair value of the subsidiary. Moreover the exercise price of the put option in that case is a “normal” price, and the purchasing entity has no obligation to make an exchange (cash as consideration for additional interests in the subsidiary) under conditions that are unfavourable.

In other words, a purchase, at a normal price, offering a simple and fair way out for a non-controlling shareholder, will have an impact on the group’s profit or loss where the group has entered into a commitment (i.e. has a granted a put), whereas a simple purchase, at the same price but without a prior commitment, will be accounted for through equity (i.e. with no impact on profit or loss).

Where the exercise price is based on the fair value of the shares, no P&L impact would be recognized if the put were accounted for as a derivative, whereas the proposed “gross” liability accounting would result in P&L impacts.

4. **From the standpoint of the user of the financial statements, these changes recorded in P&L would most likely not be deemed decision-useful information.**

Some puts have been outstanding for a long time, and are not likely to be exercised (e.g. put at fair value with a 20% discount). Therefore, systematically accounting for these changes in P&L only reflects a mechanical application of rules, as opposed to determining the appropriate accounting treatment (as one would expect from a principle based set of standards).
This draft Interpretation recalls the IFRIC 3 Interpretation on emission rights. When that interpretation was withdrawn, the Board concluded that it was a good technical interpretation, but that it could under some circumstances lead to unsatisfactory accounting consequences.

It seems that even the members of the Committee have reservations about the proposed accounting treatment, as evidenced by the fact that the Basis for Conclusion recall the Committee’s original proposal (rejected by the IASB) to amend IAS 32 to account for puts on non-controlling interests as derivatives.

For the above reasons, we believe that the Committee should transfer the subject to the Board, as there is a need for an in-depth review of this issue (as opposed to a narrow scope interpretation, which fails to satisfactorily portray the underlying economic reality).

### Question 3 Transition

*Entities would be required to apply the draft Interpretation retrospectively in accordance with IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors. Do you agree with the proposed transition requirements? If not, what do you propose and why?*

Subject to the comments above regarding the scope and the proposed accounting treatment, we have no comments on the proposed retrospective application.