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LE PRÉSIDENT

JFL/MPC

N°455

PARIS, 5TH SEPTEMBER 2008

IASB

30 Cannon Street

London EC4M 6XH

UK

Re : Discussion Paper *Financial Instruments with Characteristics of Equity*

Dear Sir / Madam,

I am writing on behalf of the Conseil National de la Comptabilité (CNC) to express our views on the above-mentioned Discussion Paper.

The CNC understands the intent of the FASB to rationalise, within US GAAP, the accounting principles relative to the recognition of liabilities and equity for US entities. Nevertheless, the CNC thinks that any kind of transposition into IFRS of the approaches proposed by the FASB will not be suitable without fundamental discussions regarding their consistency with the IFRS Conceptual Framework. Furthermore, we have not found in the Discussion Paper any analysis regarding the attributes of equity instruments unlike the document issued by the PAAinE (Pro-Active Accounting group in Europe) which provides interesting basis for conclusions about the main characteristics of equity and debt instruments.

The CNC considers that the three approaches proposed by the FASB do not provide any particular improvements relative to the provisions of the currently applicable IAS 32. Moreover, they do not deal with the cases which are currently under the scope of IAS 32's interpretation IFRIC 2 *Members' Shares in Co-operative entities and Similar Instruments*, and any change on this topic should reflect the conclusions then reached as a result of considerable debates.

The CNC regards the “basic ownership approach” as very restrictive. The REO approach raises significant operational difficulties. At last, if the results obtained through application of the “ownership settlement approach” seem to be the closest to the ones obtained according to the current provisions of IAS 32, this approach is nevertheless inconsistent with the IASB’s Conceptual Framework and provides no noteworthy improvement relative to IAS 32 and its related interpretation.

As a consequence, the CNC is in favour of keeping the current IAS 32 and its related interpretation. And in order to resolve some difficulties currently existing under IFRS in the distinction between debt instruments and equity instruments, the CNC then advocates in favour of an improvement of the current IAS 32 which should focus on some fundamental issues like the introduction of the concept of an issuer’s economic repayment obligation (or “economic compulsion”) in order to qualify an issued instrument as a debt instrument, as replacement for the strictly contractual obligation currently applicable under IAS 32.

We hope you find these comments useful and would be pleased to provide any further information you might require.

Yours sincerely

Jean-François Lepetit

Discussion Paper de l'IASB

Financial Instruments with Characteristics of Equity

B1. Are the three approaches expressed in the FASB Preliminary Views document a suitable starting point for a project to improve and simplify IAS 32? If not, why?

(a) Do you believe that the three approaches would be feasible to implement? If not, what aspects do you believe could be difficult to apply, and why?

1. The CNC considers that the three approaches proposed by the FASB do not provide any improvements relative to the provisions of IAS 32.

The CNC considers that the three approaches proposed by the FASB regarding the definition and presentation of liabilities and equity which could be taken up by the IASB do not provide any particular improvements relative to the provisions of the currently applicable IAS 32.

The CNC understands the intent of the FASB to rationalize, within US GAAP, the accounting principles relative to the recognition of liabilities and equity for US GAAP entities. However, this rationalization need does not affect companies using IFRS in the same terms, insofar as the distinction between liabilities and equity is described therein by means of a single standard (IAS 32). As far as this project for improving the distinction between debt and equity is carried out following a joint approach, the CNC would have expected to find in the FASB Preliminary Views document some stronger links with the issues currently encountered by IFRS constituents when applying IFRS requirements on this classification topic.

In this context, the CNC wonders, on the one hand, about the timeliness of changing the current IFRS rules and, on the other hand, about the fact that the FASB has not considered the alternative of adopting the provisions of IAS 32 and of its interpretation.

2. The approaches proposed by the FASB cannot be transposed into IFRS without discussions on their consistency with the conceptual framework of IFRS .

With regard to the approaches proposed by the FASB, the CNC considers that it is currently difficult to envisage any kind of transposition of these approaches into IFRS without fundamental discussions regarding their consistency with the conceptual framework. In a context in which the IASB is continuing its reflections on the conceptual framework and an IASB Discussion Paper on the "Reporting Entity" has just been issued, the IASB cannot continue these efforts regarding liabilities and equity without establishing a link with the reflections simultaneously under way on this conceptual framework.

The questions to be debated revolve around the following central matters:

- what are the arguments that would allow a preference for a positive definition of equity, instead of the definition of financial liabilities currently available in IFRS ?

- how does the current definition of liabilities in the IFRS conceptual framework link up with that of debts that would result from the positive definition of equity if one of the FASB's approaches were to be adopted, bearing in mind that according to the approach preferred by the FASB ("basic ownership approach"), the equity category is extremely restrictive ?

- why does the FASB prefer the proprietary view as opposed to the entity view, even though these substantive questions have not been debated ?

- in what way do the three proposed approaches reduce the complexity of the currently applicable IAS 32 ? The CNC considers that re-examining the classification of instruments or of their components at the time of each accounting closing is a source of complexity, both for users of the financial statements and for preparers, given that reclassifications can be more frequent under these approaches. The consequences resulting from such reclassifications with regard to the recognition of the outcome (interests or dividends) of the issued instruments are also a source of additional complexity.

The CNC is far from being convinced by the basis for the FASB Preliminary Views in favour of the Basic Ownership Approach. Simplicity is presented as the main criterion for justifying the preference for this approach without considering other one. All extensions of the scope of equity, such as including perpetual instruments, are simply described as generating complexity. But all these assertions are not supported by convincing arguments.

The CNC wishes to underline that the alternative Discussion Paper issued by the PAAinE (Pro-Active Accounting group in Europe) advantageously discusses all fundamental issues regarding the main characteristics of equity and debt instruments. An interesting discussion has been developed about the characteristics of equity instruments such as voting rights, subordination ranking, maturity and permanence of funding resources, all issues that can not be ignored in such a debate.

As far as the IASB is currently working on the revision of the Framework, the CNC encourages it to include in its project specific reflections about the necessity to distinguish equity and liabilities. Unlike FASB in its Preliminary Views document, the PAAinE has presented such a useful study in its own discussion paper.

3. The CNC considers that technical questions must still be resolved with regard to the FASB's three approaches.

Over and above these substantive questions, this CNC thinks that the FASB's proposed approaches elicit the following comments:

- The remuneration of the instruments and consequences of the mandatory nature of this outcome has not been considered. Hence, questions arise as to the classification of certain instruments, and notably perpetual instruments (for example, perpetual instruments with mandatory minimum coupon), and regarding the recognition of this remuneration (indefinitely reportable cumulative dividends of perpetual instruments, recognition of the mandatory remuneration of "basic ownership instruments"). As a result, there are remaining uncertainties with regard to the application of the "split accounting" principle.

- Only the most subordinate share class meets the definition of “basic ownership instruments”. This principle results in comparability difficulties between companies and over time, since as soon as a new and more subordinate instrument is issued, the other instruments initially presented as equity must then be reclassified as liabilities.

- Though essential for an instrument’s analysis, the notions of “linkage” and of “substance” are insufficiently explained in the DP.

4. CNC position regarding each of the three approaches.

More precisely, the CNC’s comments on each of the three approaches are the followings :

- The CNC regards the “basic ownership approach” as very restrictive, since only “basic ownership instruments” are eligible for the equity category under this approach.

- While the results obtained through application of the “ownership settlement approach” seem to be the closest to the ones obtained according to the current provisions of IAS 32, this approach is not consistent with the IASB’s conceptual framework and provides no noteworthy improvement relative to IAS 32. Moreover, this approach does not deal with the cases which are currently under the scope of IAS 32 ‘s interpretation IFRIC 2 *Members’ Shares in Co-operative entities and Similar Instruments*. Additional reflections would be needed in order to reconcile the IAS 32 standard and the “ownership settlement approach”, and to conceptually justify it. In this context, the improvement relative to the current IFRS, as brought by this approach, is still questionable.

- Finally, the “REO approach” raises significant operational difficulties and is considered to be far too complex, for both users and preparers.

Despite the CNC’s reservations regarding these three approaches, if the choice had to be made, the CNC thinks that the reflection should focus on the “ownership settlement approach”, since this is the approach that most closely resembles the provisions of IAS 32, provided that these reflections are carried out in order to ensure the continuity with both the current IAS 32 and its interpretation IFRIC 2 *Members’ Shares in Co-operative entities and Similar Instruments*.

(b) Are there alternative approaches to improve and simplify IAS 32 that you would recommend? What are those approaches and what would be the benefit of those alternatives to users of financial statements?

The CNC considers that it remains certain difficulties to resolve with IAS 32.

In order to resolve certain difficulties currently existing under IFRS in the distinction between debt instruments and equity instruments, the CNC would prefer a solution involving a modification of the current IAS 32 relative to the following fundamental points, points that have also been identified by the IASB in its Discussion Paper.

- The CNC considers that it is necessary to introduce the concept of an issuer's economic repayment obligation (or "economic compulsion") in order to qualify an issued instrument as a debt instrument, as replacement for the strictly contractual obligation currently preferred in IAS 32. This concept of economic compulsion is to be appreciated through a linkage between the contractual conditions and the economic environment, both at inception and when contractual provisions are amended. Thus, for example, an instrument issued with a "step-up" clause could create an economic repayment obligation on the issuer if the contractual rates after application of the "step-up" clause (increase of the interest rate to be paid on the issued instrument) appear to be too high compared to the interest rates then currently observed on the market.

- The CNC suggests a reconsideration of the provisions that imply a classification as equity of some equity derivatives, the settlement of which can only take place through an exchange of a fixed number of treasury shares against a fixed amount of cash ("fixed / fixed" rule). Indeed, the provisions of IAS 32 are very "rule-based". With this complex topic, it would be best to focus on a principle, which could be based on the nature of the risk borne by the bearer, in particular if it could be compared to a shareholder's risk, in which case a classification as net assets could be suitable, or even on the fact that the share can be used as a settlement currency, in which case a liability classification would need to be applied.

Additionally to these two main points, other issues could be pointed out as being improvable (such as the classification and treatment of treasury shares purchased for the purpose of arbitrage and trading activities on stock indexes, for example, that should be consistently treated as trading financial instruments in the balance sheet, unlike required by the current IAS 32).

B2. Is the scope of the project as set out in paragraph 15 of the FASB Preliminary Views document appropriate? If not, why? What other scope would you recommend and why?

Paragraph 15 b, mentions the "other instruments that are ownership interests in legal form". The CNC wonders about the scope of this definition, which would only target financial instruments with ownership interests in legal form in the American environment, and wonders if the perpetual instruments defined in this approach might only target the perpetual instruments with ownership interests in legal form.

As IAS 32 makes no reference to ownership interests in legal form, the CNC consequently wishes to point out the fact that the provisions that will finally be adopted by the IASB must not refer to legal notions, which necessarily differ between countries.

Finally, the CNC considers that the scope of the project shall not differ from the current scope of IAS 32.

B3. Are the principles behind the basic ownership instrument inappropriate to any types of entities or in any jurisdictions? If so, to which types of entities or in which jurisdictions are they inappropriate, and why?

Regarding the presentation in the consolidated financial statements of financial instruments issued by subsidiaries, the CNC wonders about the relevance of keeping, in the consolidated statements, the classification used on the level of the individual financial statements for the equity instruments issued by special purpose entities.

The CNC asks for additional reflections in order to determine if such equity instruments issued by special purpose entities should be presented as such in consolidated financial statements.

Shares in Co-operative entities and similar instruments which are the most subordinated instruments issued by these entities are currently classified as equity following the provisions of IFRIC 2 *Members' Shares in Co-operative entities and Similar Instruments*. Under the "basic ownership approach", such instruments would be classified as debt, ignoring the considerable debates that have taken place before the issuance of IFRIC 2.

B4. Are the other principles set out in the FASB Preliminary Views document inappropriate to any types of entities or in any jurisdictions? (Those principles include separation, linkage and substance.) If so, to which types of entities or in which jurisdictions are they inappropriate, and why?

The CNC notes that FASB proposals are not consistent with IFRIC 2. According to the CNC, IFRIC 2 provisions shall be kept that allows shares issued by cooperative companies to be presented as equity.

The importance and the relevance of the equity classification of shares issued by such entities have been recognized positively during the elaboration of IFRIC 2 and should then not be ignored in the present debate.

B5. Please provide comments on any other matters raised by the discussion paper.

Appendix A of the IASB document presents financial instruments without describing precisely their characteristics. The classification as debt or equity which is then proposed under each of the three approaches and under IAS 32 then raises many questions for some of these instruments. Due to a lack of description of all the characteristics of these instruments and to the lack of explanation about the proposed classifications and the criteria used to determine these classifications, the reading of examples included in appendix A lead to a potential misunderstanding of the provisions included in the Discussion Paper.

Moreover, the Discussion Paper is not precise enough to allow a comprehensive analysis of the potential consequences of each approach proposed in the FASB document and consequently it can not guarantee that all the proposed provisions would be adequate for properly presenting some instruments with particular features issued by European entities.

FASB Preliminary views

Financial Instruments with Characteristics of Equity

Questions on the Basic Ownership Approach

1. ***Do you believe that the basic ownership approach would represent an improvement in financial reporting? Are the underlying principles clear and appropriate? Do you agree that the approach would significantly simplify the accounting for instruments within the scope of this Preliminary Views and provide minimal structuring opportunities?***

The CNC considers that the "basic ownership approach" does not constitute an improvement relative to the provisions of the current IAS 32. Indeed, the CNC regards this approach as very restrictive, as only "basic ownership instruments" are eligible for the category of equity instruments.

Only the most subordinate share class meets the definition of "basic ownership instruments". This principle results in comparability difficulties between companies and over time (since as soon as a new and more subordinate instrument is issued, the other instruments initially included in the equity must then be presented as liabilities).

Moreover, the remuneration (interest or dividends) of the instruments and consequences of the mandatory nature of this remuneration have not been considered. Also, questions arise as to the recognition of the mandatory remuneration of the "basic ownership instruments". As a result, there are remaining uncertainties with regard to the application of the "split accounting" principle.

Finally, the principles underpinning this approach would require further development. Indeed, though essential for an instrument's analysis, the concepts of "linkage" and "substance" are insufficiently explained. At this stage, it is therefore difficult to comment on this approach's simplicity, until such time as these concepts have been clarified.

Perpetual Instruments

2. ***Under current practice, perpetual instruments are classified as equity. Under the basic ownership approach (and the REO approach, which is described in Appendix B) certain perpetual instruments, such as preferred shares, would be classified as liabilities. What potential operational concerns, if any, does this classification present?***

The CNC takes note that under this approach, perpetual instruments are not classified as equity. It considers that, as a result of this, the "basic ownership approach" is somewhat inconsistent insofar as, according to this approach, certain instruments repayable at their fair value, namely "basic ownership instruments", are classified in the "equity" category, whereas perpetual instruments are liabilities.

3. ***The Board has not yet concluded how liability instruments without settlement requirements should be measured. What potential operational concerns, if any, do the potential measurement requirements in paragraph 34 present? The Board is interested in additional suggestions about subsequent measurement requirements for perpetual instruments that are classified as liabilities.***

If perpetual instruments are classified as equity instruments, the question relative to their measurement no longer arises. If perpetual instruments are classified as debt instruments, the CNC is in favour of their measurement at amortised cost, consistently with the measurement of other liabilities under IAS 39.

As a general consideration, the CNC notes that measurement rules for financial instruments not classified as equity already exist in IFRS in the form of IAS 39 and then considers that there is no need to introduce additional measurement provisions in a separate standard since it could easily generate inconsistency and complexity.

Redeemable Basic Ownership Instruments

4. ***Basic ownership instruments with redemption requirements may be classified as equity if they meet the criteria in paragraph 20. Are the criteria in paragraph 20 operational? For example, can compliance with criterion (a) be determined?***

The CNC considers that the criteria described in sub-paragraphs a and b of paragraph 20 are too theoretical and complex.

The criteria of paragraph 20 b, seems to be systematically met, as far as an instrument's repayment thereby systematically impair the claim of the other creditors.

With regard to the drafting of this sub-paragraph 20 b, does the word "term" refer to legal and contractual provisions? Do the words "redemption would impair" refer to a decrease in value of the instrument in question or to a cash decrease after repayment of the said instrument?

Separation

5. ***A basic ownership instrument with a required dividend payment would be separated into liability and equity components. That classification is based on the Board's understanding of two facts. First, the dividend is an obligation that the entity has little or no discretion to avoid. Second, the dividend right does not transfer with the stock after a specified ex-dividend date, so it is not necessarily a transaction with a current owner. Has the Board properly interpreted the facts? Especially, is the dividend an obligation that the entity has little or no discretion to avoid? Does separating the instrument provide useful information?***

The CNC is in favour of a "split accounting" if this fixed remuneration is of a mandatory nature, though it regrets that this aspect was not further developed in the Discussion Paper. As a result, there are uncertainties with regard to the application of the "split accounting" principle.

Moreover, the CNC is also in favour of the principle of the economic compulsion for repayment by an issuer, as an underlying principle to be used for determining the instrument's presentation. The CNC thinks that this principle of economic compulsion must be appreciated through a linkage between the contractual conditions and the economic environment, both at inception and when contractual provisions are amended. As such, as an illustration, an instrument issued with a “step-up” clause could create an economic compulsion for repayment for the issuer if the contractual interest rates appears to be too high when compared to the interest rates currently observable on the market.

Consequently, and in response to the question asked, the CNC considers that the distribution of dividends by a company that has historically always distributed them cannot be considered as an economic compulsion if the entity is not contractually obliged to make a distribution to its shareholders, even in the event that profits are generated. On the other hand, if the distribution of dividends or interest is contractually required, the issuer certainly has an obligation. In this regard, the “discretion” notion would need to be clarified, though it is very closely linked with the issuer’s legal environment.

Substance

6. ***Paragraph 44 would require an issuer to classify an instrument based on its substance. To do so, an issuer must consider factors that are stated in the contract and other factors that are not stated terms of the instrument. That proposed requirement is important under the ownership-settlement approach, which is described in Appendix A. However, the Board is unaware of any unstated factors that could affect an instrument’s classification under the basic ownership approach. Is the substance principle necessary under the basic ownership approach? Are there factors or circumstances other than the stated terms of the instrument that could change an instrument’s classification or measurement under the basic ownership approach? Additionally, do you believe that the basic ownership approach generally results in classification that is consistent with the economic substance of the instrument?***

The CNC regards the “substance” principle as essential, even in the “basic ownership approach”, and that it should be considered in greater depth. In this regard, the CNC encourages the FASB to continue the reflections on this matter, notably by analysing to what degree this substance principle would tally with the “economic compulsion” principle mentioned above.

The CNC nevertheless recognises that in the “basic ownership approach”, this principle is of lesser importance insofar as the “equity” category is very restrictive, and that its definition has less need for a substance analysis of the instruments.

Linkage

7. ***Under what circumstances, if any, would the linkage principle in paragraph 41 not result in classification that reflects the economics of the transaction?***

The CNC agrees with the “linkage” principles listed in paragraphs 41 to 43. It nevertheless notes that the subsequent example proposed in the Discussion Paper does not correctly illustrate the principles described in sub-paragraphs a, and b, notably because the described operations are not contractually linked, as the shares were pre-existing.

Measurement

8. ***Under current accounting, many derivatives are measured at fair value with changes in value reported in net income. The basic ownership approach would increase the population of instruments subject to those requirements. Do you agree with that result? If not, why should the change in value of certain derivatives be excluded from current-period income?***

The CNC has certainly taken note that there would be fewer instruments eligible for the equity category, and that derivatives will be systematically excluded from this category, in particular derivatives on treasury shares.

The CNC nevertheless considers that certain derivatives on treasury shares should be included in the "equity" category, without subsequent revaluation, notably dilutive derivative instruments that are settled by physical delivery of equity instruments, including the "net-share settled" ones.

Presentation Issues

9. ***Statement of financial position. Basic ownership instruments with redemption requirements would be reported separately from perpetual basic ownership instruments. The purpose of the separate display is to provide users with information about the liquidity requirements of the reporting entity. Are additional separate display requirements necessary for the liability section of the statement of financial position in order to provide more information about an entity's potential cash requirements? For example, should liabilities required to be settled with equity instruments be reported separately from those required to be settled with cash?***

The CNC regards information on the repayment of the issued instruments as useful for the reader of financial statements. However, so as not to encumber the reading of the balance sheet, the CNC considers that these information elements must be disclosed in the appendix notes.

10. ***Income statement. The Board has not reached tentative conclusions about how to display the effects on net income that are related to the change in the instrument's fair value. Should the amount be disaggregated and separately displayed? If so, the Board would be interested in suggestions about how to disaggregate and display the amount. For example, some constituents have suggested that interest expense should be displayed separately from the unrealized gains and losses.***

The CNC considers that this question relative to the presentation of the fair value of re-valued instruments is premature and cannot be considered until the incidences of the proposed approaches on the scope of the financial instruments that will be re-valued after-the-fact have been discussed and assessed.

In particular, the CNC regards as important to have an analysis of the instruments that will be considered as liability instruments according to each approach, as these elements will require subsequent re-valuation according to the FASB proposals, even though the re-valuation of liability instruments is not included in the current IAS 39 in these terms. In this regard, the CNC stipulates that it is not in favour of the re-valuation of liabilities other than "trading" ones, and would like for these liabilities to be recognised at their amortised cost, as previously mentioned.

Moreover, the linkage of the proposed approaches with the current provisions of IAS 32, IAS 39 and IFRS 7 must also be analysed so as to assess the incidence of the proposed approaches, for both presentation and measurement of the instruments compared to the existing practices.

Earnings per Share (EPS)

11. ***The Board has not discussed the implications of the basic ownership approach for the EPS calculation in detail; however, it acknowledges that the approach will have a significant effect on the computation. How should equity instruments with redemption requirements be treated for EPS purposes? What EPS implications related to this approach, if any, should the Board be aware of or consider?***

The CNC thinks that questions relating to the earnings per share could only be considered once the consequences of the proposed approaches in terms of presentation and measurement have been discussed and examined in greater depth.

At this stage, however, the CNC sees no immediate advantage of distinguishing repayable financial instruments from any others when calculating the earnings per share. It also notes that the "basic ownership approach" calls into question the notion of the basic earnings per share, as the dilutive and accretive effects are already taken into account in the earnings, notably by the re-valuation of all derivative instruments.

Questions on the Ownership-Settlement Approach

1. ***Do you believe the ownership-settlement approach would represent an improvement in financial reporting? Do you prefer this approach over the basic ownership approach? If so, please explain why you believe the benefits of the approach justify its complexity.***

The CNC considers that the results obtained in terms of presentation in the "equity" and "liabilities" categories through this method's application would appear to be more satisfactory than the ones obtained from the other two approaches, notably because more instruments would be classified as equity according to the "ownership settlement approach" than it would be the case of the "basic ownership approach".

A second argument in favour of the results obtained using this approach is that these results seem to be relatively close, in terms of eligibility for the "equity" and "liabilities" categories, to the ones obtained using the current provisions of IAS 32.

Using this approach, an instrument is an equity instrument if it firstly includes a right to the net assets (notion of residual interest), or secondly, if it has a certain degree of permanency. Indeed, these two characteristics are fundamental and they must not be ignored when classifying a financial instrument among equity. Nevertheless, additional reflections would be required such as to reconcile them, and to conceptually justify this approach. In this context, the improvement relative to the current IFRS, as brought by this approach, is still questionable.

Finally, paragraph 15 b, mentions the "other instruments that are ownership interests in legal form". The CNC wonders about the scope of this definition, which would only target financial instruments with ownership interests in legal form in the US environment, and wonders if the perpetual instruments defined in this approach might only target the perpetual instruments with ownership interests in legal form. As IAS 32 makes no reference to ownership interests in legal form, the CNC consequently wishes to point out the fact that the provisions that will finally be adopted by the IASB must not refer to legal notions, which necessarily differ between countries.

Finally, the CNC is in favour of excluding, from this project's scope, instruments that are currently treated under specific standards, such as those instruments subject to IFRS 2 provisions or insurance contracts with a discretionary profit-sharing clause.

2. Are there ways to simplify the approach? Please explain.

The CNC regards this approach as somewhat complex, due to the definition of the "indirect ownership instruments" and to the eligibility conditions of certain derivatives on treasury equity in the "equity" category.

The CNC considers that greater precision in the principles underlying the recognition of these "indirect ownership instruments" would serve to attenuate the "rules-based" character and to reduce the complexity. In this regard, the CNC understands that a treasury share derivative is allocated to the equity category if its fair value fluctuates in the same direction as that of the underlying share, which leads one to suppose that the instrument is dilutive, provided it is not cash-settled. If true, this principle would need to be more clearly presented.

One of the identified sources of complexity results from the notion of direction ("slope" in paragraph A 8), which would also require additional explanations and even illustrative examples.

Substance

3. Paragraph A40 describes how the substance principle would be applied to indirect ownership instruments. Similar to the basic ownership approach, an issuer must consider factors that are stated in the contract and other factors that are not stated in the terms of the instrument. Is this principle sufficiently clear to be operational?

As mentioned above, with regard to the substance principle, the CNC encourages the FASB to continue the reflections on this matter, notably by analysing to what degree this substance principle would tally with the "economic compulsion" principle mentioned above. The CNC considers that it is necessary to take into consideration the concept of an issuer's economic repayment obligation (or "economic compulsion") in order to qualify an issued instruments as a debt instrument, as replacement for the strictly contractual obligation currently preferred in IAS 32. This concept of economic compulsion is to be appreciated through a linkage between the contractual conditions and the economic environment, both at inception and when contractual provisions are amended. But the CNC questions the necessity of a systematic reassessment when contractual provisions are not modified.

Relative to the provisions proposed for the "ownership settlement approach", the CNC would like to know if an analysis of the substance of instruments should result in the classification of certain perpetual instruments as debt in the event that this analysis of the substance of the perpetual instrument in question might call this perpetual character into question. The CNC considers that this question should be debated.

Presentation Issues

4. ***Statement of financial position. Equity instruments with redemption requirements would be reported separately from perpetual equity instruments. The purpose of the separate display is to provide users with information about the liquidity requirements of the reporting entity. What additional, separate display requirements, if any, are necessary for the liability section of the statement of financial position in order to provide more information about an entity's potential cash requirements? For example, should liabilities required to be settled with equity instruments be reported separately from those required to be settled with cash?***

The CNC regards that information on issued instruments as useful for the reader of financial statements, while notably distinguishing repayable instruments from perpetual instruments. However, so as not to encumber the reading of the balance sheet, the CNC considers that these information elements must be disclosed in the appendix notes.

Separation

5. ***Are the proposed requirements for separation and measurement of separated instruments operational? Does the separation result in decision-useful information?***

As mentioned above, the CNC agrees with the principle of separating instruments between a debt component and an equity component. Nevertheless, it thinks that this principle is insufficiently explained in the three US approaches to be considered operational. The practical provisions of this principle must be elaborated in all three approaches, in particular for the debt component, which is also re-measured with each closing.

As such, questions arise as to the classification of certain instruments, and notably perpetual instruments (perpetual instruments with a mandatory remuneration), and regarding the recognition of this remuneration (indefinitely reportable cumulative dividends of perpetual instruments, recognition of the mandatory remuneration of "basic ownership instruments").

Moreover, in paragraph A32 of the FASB document, it is indicated that the priority for the issued instrument's value allocation will go to the debt component, and only residually to the equity component. Given that equity instruments are positively defined, this allocation order would seem to be inconsistent.

Earnings per Share

6. ***The Board has not discussed the implications of the ownership-settlement approach for the EPS calculation in detail. How should equity instruments with redemption requirements be treated for EPS purposes? What EPS implications related to this approach, if any, should the Board be aware of or consider?***

As with the response elements provided relative to the question on the earnings per share in the "basic ownership reports", the CNC thinks that questions relating to the earnings per share could be considered once the consequences of the proposed approaches in terms of presentation and measurement have been discussed and examined in greater depth.

Given the diversity of the instruments eligible for the equity category using this approach, the CNC nevertheless wonders as to the possibility of determining different earnings per share according to the nature of the rights granted by these various equity instruments.

Settlement, Conversion, Expiration, or Modification

7. ***Are the requirements described in paragraphs A35–A38 operational? Do they provide meaningful results for users of financial statements?***

The CNC has no particular comments. Cf. response to question 5.

Questions on the REO Approach

1. ***Do you believe that the REO approach would represent an improvement in financial reporting? What would be the conceptual basis for distinguishing between assets, liabilities, and equity? Would the costs incurred to implement this approach exceed the benefits? Please explain.***

The CNC agrees with the provisions of paragraph B 21, which explain why the FASB has not selected this approach. Indeed, the main reason is complexity, though the cost of such an implementation must also not be ignored.

Separation and Measurement

2. ***Do the separation and measurement requirements provide meaningful results for the users of financial statements?***

Cf. response to the above question.

Earnings per Share

3. ***The Board has not discussed the implications of the REO approach for the EPS calculation in detail; however, it acknowledges that the approach will have a significant effect on the calculation. How should equity instruments with redemption requirements be treated for EPS purposes? What EPS implications related to this approach, if any, should the Board be aware of or consider?***

Cf. response to the above question.

Other Alternatives

1. ***Some other approaches the Board has considered but rejected are described in Appendix E. Is there a variation of any of the approaches described in this Preliminary Views or an alternative approach that the Board should consider? How would the approach classify and measure instruments? Why would the variation or alternative approach be superior to any of the approaches the Board has already developed?***

The “loss absorption approach” is an alternative that must be considered, insofar as it is an original approach relative to the ones proposed by the FASB. This approach should consequently be analysed and discussed.

The PAAinE Discussion Paper that explains this approach also has the advantage of pointing out all of the substantive questions (characteristics of the equity securities, voting rights, subordination ranks, maturity, notion of accounting losses, etc.), while presenting an interesting reflection on the owner view / entity view that should be considered in view of the recent Discussion Paper on the Reporting Entity.

Other comments

Paragraph 29 covers the fact of keeping, in the consolidated financial statements, the classification used on the level of the individual financial statements.
While this approach would appear to be justified relative to “basic ownership instruments” that have a repayable character as “puttable instruments”, the CNC wonders about the relevance of such a provision for the equity instruments issued by special purpose entities, with the reason being to limit opportunistic decisions to increase the consolidated shareholders equity.