

International Financial Reporting Interpretations Committee  
1st Floor  
30 Cannon Street  
London  
EC4M 6XH

25 April 2008

Dear Sir or Madam

## **IFRIC Draft Interpretation D23, Distributions of Non-Cash Assets to Owners**

We are responding to your invitation to comment on the above draft interpretation, published in January 2008, on behalf of PricewaterhouseCoopers. Following consultation with members of the PricewaterhouseCoopers network of firms, this response summarises the views of member firms who commented on the draft interpretation. 'PricewaterhouseCoopers' refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

### **Overall comments**

We welcome the opportunity to respond to this draft interpretation. We recognise the need for guidance in the area of non-reciprocal transactions. However, we note that the issue addressed by this draft interpretation is part of a more fundamental question of how to account for any transactions with shareholders. In our view, the existing IFRS literature contains little guidance from which to build an interpretation.

We were previously asked to advise the IASB when we believe standards or interpretation to be issued are inconsistent with high quality principles-based standards as discussed in the January 2008 Global Public Policy Symposium. We believe this is the case here. The underlying issue as to how to account for transactions with shareholders is broad but the scope of interpretation is narrow. And the foundation needed to develop an accounting treatment for transactions with owners, including non-cash distributions has not been developed. Therefore, we recommend that the issue be removed from the IFRIC agenda and the broader issue be addressed by the IASB in a more comprehensive process.

We further observe that the IASB has recently included common control transactions on its agenda and that this project will consider the accounting for demergers, such as a spin-off of a subsidiary or business. Based on our experience, spin-offs are the most common example of non-cash distributions to owners found in practice. As the IASB is expected to address this matter as part of its common control transactions project, any conclusion reached should be consistent with the conclusions reached in the more comprehensive project referred to above.

Further arguments supporting the removal of the proposed interpretation from the IFRIC's agenda include:

- The proposed scope of D23 is very narrow (in particular if demergers are removed and included in the IASB's project as suggested above) and based on our experience transactions within the suggested scope are rare. More common examples of non-cash

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distributions we have seen in practice include distributions within the same group, exchanges of assets with shareholders on a non–arm’s length basis and distributions where the owners are not treated equally. These examples are excluded from the current scope of the proposed interpretation. Therefore the interpretation would be relevant to a very small number of transactions. At the same time there is a risk that it may be applied by analogy to other situations and it may unintentionally establish a broader principle of fair value accounting for non-reciprocal transactions.

- We are also concerned that the interpretation may restrict companies’ ability to pay non-cash dividends. In a number of jurisdictions (e.g. in China and a number of EU countries) the amount of dividends declared cannot exceed retained earnings at the time the dividend is declared. As the proposed interpretation requires that dividends payable be measured at fair value while the related asset shall remain at book value until distributed, the interpretation could preclude companies from paying non-cash dividends where the fair value of the distribution exceeds retained earnings as of the date of declaration.

Lastly, we observe that the interpretation, if issued consistent with its proposed form, would create a difference compared to US GAAP for the accounting of spin-offs.

In summary, for the reasons listed above, we believe that IFRIC should not proceed with this interpretation and the issue should be passed to the IASB so it can undertake a more detailed examination of the underlying conceptual issues.

We have set out our more detailed comments in Appendix A, including some issues that the IFRIC in our view should consider if it decides to continue with this interpretation.

If you have any questions in relation to this letter please do not hesitate to contact Richard Keys (020 7212 4555) or Mary Dolson (020 7804 2930) .

Yours faithfully

PricewaterhouseCoopers LLP

## Appendix A

### Detailed comments on the IFRIC Draft Interpretation D23, Distributions of Non-Cash Assets to Owners

#### Question 1 – Specifying how an entity should measure a liability for a dividend payable

#### Question 2 – Specifying how any difference between the carrying amount of the assets distributed and the carrying amount of the dividend payable should be accounted for when an entity settles the dividend payable

The draft interpretation proposes that an entity should measure a liability to distribute non-cash assets to its owners in accordance with IAS 37 and any difference between the carrying amount of the assets distributed and the carrying amount of dividend payable (measured with reference to the fair value of assets distributed) should be recognised in profit or loss. We do not believe that sound support for mandating such treatment exists in the current IFRS literature.

As indicated in the framework and IAS 1.97-98, transactions between the entity and its owners acting in their capacity as owners are fundamentally different from ordinary exchange transactions. Therefore, in our view it is not appropriate to mandate an accounting treatment based on IAS 37 or other existing IFRS standards developed for exchange transactions. Non-reciprocal transactions represent transactions with owners acting in their capacity as such, and in accordance with IAS 1.97-98 they should be fully recorded within equity.

We regard the distribution of non-cash assets to owners as representing a non-reciprocal transaction. Accordingly, we consider it is inappropriate to split this into an asset disposal component and a dividend distribution component, and to recognise a gain on the first component.

The most common non-cash distributions to owners found in practice are demergers. In substance, demergers represent a restructuring of the reporting entity. We do not believe that any economic benefits are generated through the restructuring process that would meet the definition of income in accordance with F.70 and should be recognised in profit or loss.

We are also concerned that recognizing the liability at fair value of the related asset while maintaining the asset at its carrying value will not appropriately reflect the economic substance of the distribution, due to the creation of an accounting mismatch if the recognition and settlement of the liability fall into different accounting periods.

Furthermore, we note that even if the interpretation would be based on the guidance in the existing IFRS standards addressing exchange transactions, we are not convinced that all dividends payable should be measured in accordance with IAS 37. For example, if an entity declares a distribution in the form of financial assets other than cash, we consider it is more appropriate to account for such a dividend payable in accordance with IAS 39. We also note that according to IAS 32 AG13, “an issuer of non-puttable ordinary shares assumes a liability when it formally acts to make a distribution and becomes legally obligated to the shareholders to do so.” This clarifies that a liability for a dividend payable should be recognised when there is a legal obligation, indicating a tension with IAS 37 which would also take into account the existence of a constructive obligation.

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We believe that accounting for non-reciprocal transactions is a more fundamental issue that should be addressed by the IASB. Until such broader analysis is carried out by the IASB we do not believe that IFRIC should mandate a single approach for non-cash distributions to owners.

**Question 3 - Whether an entity should apply the requirements in IFRS 5 to non-current assets held for distribution to owners.**

We believe that IFRS 5 at present does not apply to assets held for distribution to owners as it only applies to assets held for sale.

We draw your attention to the fact that expanding the scope of IFRS 5 to cover non-cash distributions to owners would result in inconsistent treatment depending on whether such distributions involve assets within or outside the presentation and measurement provisions of IFRS 5 (e.g. financial assets versus non-financial assets; current assets versus non-current assets). Also, it is not clear if the proposed amendment to IFRS 5 is meant to only apply to those assets held for distribution that are within the scope of the proposed interpretation (i.e. excluding those referred to in D23.5) or any assets held for distribution.

We also note that the potential amendment to IFRS 5 would create a difference with US GAAP, under which (similarly to the current IFRS 5) distributions to owners in a spin-off are not classified as held for sale or as discontinued operations until the distribution is completed.

**Question 3 (a) - Should an entity apply IFRS 5 when it is committed to make a distribution or when it has an obligation to distribute the assets?**

We believe that IFRS 5, if amended, shall be applied on the commitment date rather than obligation date as this is consistent with the current IFRS 5 approach.

**Question 3 (b) - Do you think there is a difference between those dates?**

We believe that commitment date as defined by IFRS 5 and obligation date are different as a commitment date involves management's or owners' intention while an obligation is legally binding. We would expect that the commitment date will come earlier than the obligation date. Normally we would not expect a considerable time gap between these two dates.

**Question 3 (c) - If there is a difference between the dates and you think that an entity should apply IFRS 5 at the commitment date, what is the difference? What indicators should be included in IFRS 5 to help an entity to determine that date?**

We believe that IFRS 5, if amended, should list specific indicators for classifying assets as held for distribution. Such indicators may include the following:

- Assets are available for immediate distribution in their current condition (incl. there are no legal restrictions to make the distribution)
- Owners have committed to a plan to distribute the assets
- The distribution is expected to be completed within 1 year
- Changes to the plan to distribute the assets are unlikely

**Other comments**

The draft interpretation applies to distributions other than those within the same group. It is not clear why distributions within the same group are excluded from the scope of the proposed interpretation and why the scope exclusion specifically addresses a controlling parent entity rather than a controlling party. We do not see any reason why distributions to a controlling individual are within the proposed scope of D23 but distributions to a controlling corporate entity are excluded.

It is also unclear whether the scope exclusion covers any distribution to a controlling corporate entity. Considering the illustrative example in D23, we understand that if the reporting entity were owned by two corporations in the proportion 60:40 rather than 50:50 as currently illustrated in the example, then the distribution to the controlling owner would be scoped out. We do not see a valid reason for treating dividends differently depending on the ownership interest of the parties involved when the parties are treated equally based on their ownership interests.

The draft interpretation applies to 'distributions of non-cash assets'. This term should be defined in the interpretation because it is not a term currently defined in IFRS and it is not clear what items 'non-cash assets' encompass and in particular whether they would also include financial assets (e.g. receivables).

The draft interpretation applies to non-reciprocal transactions and specifically scopes out exchange transactions with shareholders. Neither of the two terms are defined or explained in the proposed interpretation or anywhere else in the IFRS literature. We therefore believe that D23 should specify what is meant by non-reciprocal and exchange transactions.

Finally, we do not see a need for presentation of a gain on distribution as a separate line item in profit or loss. Instead, we would generally suggest that it be disclosed separately in the notes.