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Mr Robert Garnett
Chair of the
International Financial Reporting Interpretations Committee
30 Cannon Street

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Dear Bob

Comment Letter on IFRIC Interpretation D23 *Distributions of Non-cash Assets to Owners*

We appreciate the opportunity to comment on the draft Interpretation IFRIC D23. We fully endorse the IFRIC's aim to support the IASB in establishing and improving International Financial Reporting Standards.

While we generally do not agree that a separate IFRIC interpretation should focus on such a narrow accounting area as defined in the scope of D23.3-7, we understand the need for such guidance due to the significance of future business transactions to which this interpretation will apply (i.e. in Germany demergers in the public utility sector would be expected to fall under this interpretation upon divestiture of the network's operating investments).

One of our main concerns in respect to the Draft Interpretation is the inconsistency in the proposed accounting treatment for the carrying amount of the assets to be distributed compared with the treatment for the settlement of the dividend payable.

In the following we will first address the three specific questions as posed in the "Invitation to Comment"-section of D23 before we will also comment on certain other issues.



Question 1 - Specifying how an entity should measure a liability for a dividend payable (dividend payable)

Paragraph 9 of the draft Interpretation proposes that an entity should measure a liability to distribute non-cash assets to its owners in accordance with IAS 37 *Provisions, Contingent Liabilities and Contingent Assets*. The IFRIC concluded that all dividends payable, regardless of the types of assets to be distributed, should be addressed by a single standard.

Do you agree with this proposal? If not, do you agree that dividends payable should be addressed by a single standard? Why? What alternative do you propose?

We agree that an entity should measure the liability for the dividend payable in accordance with one single standard and that IAS 37 is the most appropriate standard to apply. The measurement should be based on the guidance as given in IAS 37, regardless of the types of assets to be distributed.

Regarding the best estimate at which to measure the present obligation of a dividend payable the third sentence of paragraph D23.10 is worded as follows: "Consequently, to apply the requirements in IAS 37 to measure a dividend payable, an entity shall consider the fair value of the asset to be distributed." However, to measure a liability at the best estimate of the expenditure incurred to settle the obligation (IAS 37.36) is not necessarily the same in all instances as the fair value of the asset to be distributed. In some circumstances the best estimate of the expenditure incurred to settle the obligation and the fair value of the asset to be distributed may need to be measured differently. We suggest that the IFRIC clarify the above in the Interpretation.

In D23.BC13-BC16 it is discussed, which IFRS is the most relevant to the measurement of a dividend payable. In this context we consider it necessary that the conclusion not to consider IAS 39 as the appropriate standard should be justified more thoroughly in the BC.

Further, while developing D23 the IFRIC appears to have focused on how to measure the liability. The measurement of the assets to be distributed has not been addressed by D23. Thus, while the liability will in most instances be measured at an amount based on the fair value of the asset, the asset itself will often continue to be measured at its (different) carrying amount. Thus, there will be an accounting mismatch (lack of symmetry) on the balance sheet that is of significant concern. This mismatch on the balance sheet will be followed by a reporting mismatch, since some gains and losses are recognised in equity (re-measuring the dividend payable as proposed in D23.11) - others are recognised in profit and loss (e.g.: amortisation, depreciation and impairment losses in accordance with the relevant standards).

Although we understand that this accounting mismatch can not be solved by the draft Interpretation (the IFRIC's proposal in D23 appears to be consistent with existing IFRS), we, on the other hand, have concerns that the IFRIC focuses solely on the measurement of the liability.



In order to address the “accounting mismatch” issue, the IFRIC might wish to consider asking the IASB to amend IFRS 5 to permit an entity to remeasure the assets to be distributed so that it equals the amount of the corresponding liability. Alternatively, the IASB may be asked to amend IAS 37 in a way to allow the measurement of the liability for a dividend payable be based on the carrying value of the asset to be distributed. We believe that either such an amendment might indeed be helpful since it would solve some of the key concerns with the proposals as made in D23.

Remeasuring the liability

D23.11 requires an entity to remeasure the liability at the end of each subsequent reporting period and at the date when the liability is settled, with changes in the amount of the liability to be recognised in equity. We fully concur that the requirement to remeasure the liability is a correct interpretation of IAS 37. We also agree that the remeasurement, if any, should be accounted for as an adjustment to the distribution and be recognised in equity, consistent with the initial recognition of the liability. However, we are concerned with the implications that remeasuring the liability might have on the accounting mismatch we have described above.

Reference to the comment letter filed by the GASB and the IDW in May 2007 – Measurement of certain non-financial liabilities

In the context of the discussion about measuring a liability for a dividend payable relating to a non-cash asset the AIC would like to make reference to a joint comment letter sent by the GASB and the IdW to the IASB relating to the IASB project “liabilities”. This comment letter was sent in May 2007 and discussed the measurement of non-financial liabilities under IFRS, when the reporting entity expects to fulfil the obligation itself in the future using its own human and material resources. Considering that the current IAS 37 is silent on this topic and given the practical relevance and the divergent interpretations, the comment letter asked for an appropriate accounting treatment to be established.

For reference purposes, the joint comment letter sent to the IASB in May 2007 is attached to this document.

Other Issue

In this context we further would like to make aware the IFRIC about the possible application of the guidance as given in D23 by analogy to other but similar issues. Such an application by analogy may not be wanted and should therefore be addressed in the draft Interpretation accordingly.



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

Paragraph 12 of the draft Interpretation proposes that, when the dividend payable is settled, any difference between the carrying amount of the assets distributed and the carrying amount of the dividend payable should be recognized in profit or loss. Paragraphs BC28-BC43 of the Basis for Conclusions explain the reasons for this proposal. The Basis for Conclusions also includes an alternative view that the difference should be recognized directly in equity (see paragraph BC44).

Which view do you support and why?

As explained in D23.BC29, the difference will generally represent a credit balance because the carrying amount of the assets distributed would not normally be greater than the carrying amount of the liability. With respect to where the difference should be recognised, the IFRIC discusses two accounting views in D23:

- (a) **view 1:** The view proposed in D23.12 and as explained in BC28-BC43 (difference to be recognized in profit or loss).
- (b) **view 2:** The alternative view – as explained in D23.BC44 (difference to be recognized directly in equity).

AIC members are divided between these different views on this issue.

The majority of the AIC members support **view 2** and argue that the distribution of a dividend (non-cash asset) represents a transaction between an entity and its owners. According to paragraph 70(b) of the Framework and IAS 1.106(c) (revised 2007), such transactions between an entity and its owners do not represent expense but rather need to be reflected in equity:

FW para. 70: The elements of income and expenses are defined as follows:

- (a) ...
- (b) Expenses are decreases in economic benefits during the accounting period in the form of outflows or depletions of assets or incurrences of liabilities that result in decreases in equity, other than those relating to distributions to equity participants.

IAS 1.106 (rev. 2007): An entity shall present a statement of changes in equity showing in the statement:

- (a) ...;
- (b) ...;
- (c) the amounts of transactions with owners in their capacity as owners, showing separately contributions by and distributions to owners; and
- (d)

Therefore, any increase in the value of the asset that arises from the transaction with an owner should be recognised in equity. The AIC-members in favour of view 2 consider a non-cash asset to be distributed to an owner not to be the same as a distribution of the proceeds from a sale of that asset to the owner (assuming the asset had first been sold to a third party and then the resulting proceeds distributed to the owners).



A difference existing between the carrying amount of the assets distributed and the carrying amount of the dividend payable should be presented within “other comprehensive income”.

The AIC members supporting view 2 argue further that only the effect of market-based transactions should be reflected in the income statement. A distribution of a non-cash asset to owners as presented in the illustrative example of D23 differs from a market based transaction with a third party. In this context it should be emphasized that the IFRIC itself acknowledges in D23.BC45–BC48 that a distribution of non-cash assets to owners is not a sale.

On the other hand, a minority of the AIC members support **view 1** and argue the other perspective - if the entity had chosen to sell the asset in the first place and then distributed the proceeds to the owners, it would recognise the difference between the proceeds and the carrying amount of the assets in profit and loss (in accordance with IAS 16.68 and IAS 16.71). It would then follow, by analogy, that the distribution of the appreciated asset to the owners should be recorded similarly. An additional argument brought up by these AIC-members is that the appreciation of the asset does not meet the definition of a transaction with an entity shareholder. They instead consider it to be income which has accumulated while holding the asset and which has to be recognised in profit and loss. Thus, their view is that the distribution of the assets to owners triggers the recognition of the increase in value in the income statement. They do not consider the distribution to be the cause of appreciation. This view is consistent with the IFRIC in D23.BC31.

The AIC-members favouring view 1 also support the separate line disclosure – net of tax - as described in D23.12 (alternatively – at least some detailed description in the notes shall be required).



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

Both the Board and the IFRIC concluded that the requirements in IFRS 5 *Non-current Assets Held for Sale and Discontinued Operations* should be applied to non-current assets held for distribution to owners as well as to non-current assets held for sale (see paragraphs BC45–BC48 of the Basis for Conclusions).

3.1) Do you agree that an entity should apply IFRS 5 to non-current assets that are held for distribution to owners? If not, why and what alternative would you propose?

The Board noted that IFRS 5 requires an entity to classify a non-current asset as held for sale when the sale is highly probable and the entity is committed to a plan to sell (emphasis added). For assets held for distribution to owners, this raises the following three questions:

3.2(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?

3.2(b) Do you think there is a difference between those dates?

3.2(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?

ad 3.1) The classification, presentation and disclosure requirements as presented in IFRS 5 should be applied to non-current assets that are held for distribution to owners since it would enable financial statements users to evaluate the financial effects of such distributions. In any case, separate disclosure with regard to distributions of non-cash assets to owners should be required in the notes.

We do not support an application of the measurement guidance of IFRS 5 in its current version to non-current assets that are held for distribution to owners since we think that applying IFRS 5 might produce inappropriate results. This is mainly the case because the application of IFRS 5.15-29 would not solve the accounting mismatch situation; the asset to be distributed remains at book value while the dividend payable is recorded at the fair value of the assets to be distributed.

However, as explained above, the IFRIC might wish to consider asking the IASB to amend IFRS 5 to permit an entity to remeasure the assets to be distributed so that it equals the amount of the corresponding liability. We believe that such an amendment might indeed be helpful since it would also solve some of the key concerns with the proposals as made in D23.

In any case, if an entity in the future has to apply IFRS 5 to non-current assets that are held for distribution to owners, it should be clarified whether this relates to distributions under the scope of D23 only or to all non-current assets that are held for distribution to owners, even if the transactions are outside of the scope of D23.

ad 3.2(a): The AIC members consider it appropriate that an entity should apply IFRS 5 (with the limitations as outlined above – non-application of the measurement requirements of IFRS 5) when it has an obligation to distribute the assets to equity holders. For distributions to equity holders the entity is not subject to a time-schedule similar to that when selling to a third party (i.e. commitment of management to the



plan, activating the programme to locate a buyer, conducting negotiations, completing the plan). Therefore, it appears appropriate to apply IFRS 5 as outlined above to distributions of non-cash assets to owners once an obligation has been established.

ad 3.2(b): The AIC members believe that in practice differences may arise between the commitment and the obligation dates – however, based on the answer given on 3.2(a) it has not been further pursued.

ad 3.2(c): As outlined above the AIC members do not believe that an entity should apply IFRS 5 at the commitment date.



Other comments and suggestions for drafting the Interpretation (besides the 3 questions as raised by the IFRIC in the “Invitation to Comment” – section):

Paragraph 3 – scope

According to D23.3 the Interpretation should be applied to unconditional non-reciprocal distributions of non-cash assets by an entity to its owners and to similar distributions that give owners a cash alternative. However, the IFRIC provides no guidance as to how “unconditional” and “non-reciprocal” are defined or in which circumstance a distribution is “unconditional” and / or “non-reciprocal”. Therefore, we suggest that some clarifying guidance should be provided.

In addition, we suggest that the IFRIC should include some guidance with regards to “distribute-contribute schemes” (or “pay-out-take-back“-method) in order to avoid any misuse in the context of distributions to owners (e.g. by distributing an asset that had been measured at cost and may be taken back on the balance sheet after (re-) contribution based on fair value).

According to D23.3(b) the draft interpretation shall be applied to “distributions that give owners a choice of receiving either non-cash assets or a cash-alternative.” We recommend that this section of the scope should be amended to also include distributions that give owners a choice of receiving either non-cash assets or a cash-alternative, or combinations of these.

Wording of D23.11

Currently the wording of D23.11 with regard to the subsequent measurement of a dividend payable reads as follows: “..., with any changes in the carrying amount of the dividend payable recognized as adjustments to the amount of the distribution.” The AIC-members consider this wording not to be sufficiently clear and suggest using the more precise wording of D23.BC27. Hence, D23.11 would read as follows: “..., with any changes in the carrying amount of the dividend payable recognized as adjustments to the amount of the distribution with the offsetting entry to be recognized directly in the statement of changes in equity.”

Concerns regarding the possible impact on related party accounting

The AIC members have additional concerns that the guidance of D23 may have an indirect impact on the accounting for transactions with related parties. On one hand, the AIC observed that the IFRIC concluded that the draft Interpretation should not address exchange transactions between an entity and its owners because that would probably result in addressing all related party transactions. Such a scope would be too broad for an Interpretation (D23.BC4). On the other hand, the AIC has concerns that especially the measurement guidance of D23.9-11 could be required to be applied in analogy to similar transactions with related parties.



If you would like further clarification of the issues set out in this comment letter, please do not hesitate to contact me.

Best regards

Prof. Dr. Manfred Bolin
AIC, Chairman