CPA Hong Kong Institute of Certified Public Accountants 香港會計師公會

MEMBERS' HANDBOOK

Update No. 52

(Issued June 2008)

This Update relates to the issuance of:

- Amendments to HKAS 32 *Financial Instruments: Presentation* and HKAS 1 *Presentation of Financial Statements* – Puttable Financial Instruments and Obligations Arising on Liquidation; and
- Other consequential amendments.

The amendments to HKAS 1 and HKAS 32 are summarised at the end of this update.

Document Reference and Title	***Instructions***	***Explanations***
VOLUME II		
Contents of Volume II	Discard the existing pages i – iii and replace with the new pages i – iii.	Revised contents pages
HONG KONG ACCOUNTING STANDARDS (HKAS)		
HKAS 1 (Revised) *Presentation of Financial Statements*	Insert the revised pages 3, 76A-76C and pages 111A-111B. Discard the replaced pages 3, 76A and 111A.	Amendments to Standards – Note
HKAS 32 *Financial Instruments: Presentation*	Insert the revised pages 2, 4-5, 31A-31N, 32, 55A-55J and 77-78. Discard the replaced pages 2, 4-5, 31A-31B, 32, 55A-55B and 77.	Amendments to Standards – Note
Amendments to other HKFRSs		
HKAS 39 *Financial Instruments: Recognition and Measurement* (Standard)	Insert page 87F after page 87E.	Amendments to Standards – Note

HKFRS 7 *Financial Instruments: Disclosures* (Standard)	Insert page 36 after page 35.	Amendments to Standards – Note
HK(IFRIC)-Int 2 *Members' Shares in Co-operative Entities and Similar Instruments*	Insert the revised pages 2 and 5 and discard the replaced pages 2 and 5. Insert pages 8A-8B after page 8 and insert page 13 after page 12.	Amendments to Interpretation – Note

Note:

SUMMARY OF MAIN CHANGES:

1. Amendments to HKAS 32 and HKAS 1 are relevant to entities that have issued financial instruments that are:

   (a) puttable financial instruments, and

   (b) instruments, or components of instruments, that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation.

2. In accordance with the amendments, even if the above-mentioned financial instruments impose on the entity an obligation to deliver cash or another financial asset, these instruments should be classified as equity instruments if the specified conditions set out below are met.

<u>Puttable financial instruments</u>

3. Puttable financial instruments is classified as an equity instrument only if all of the following criteria are met:

   (a) the holder of the instrument is entitled to a pro rata share of the entity's net assets in the event of the entity's liquidation;

   (b) the instrument is in the class of instruments that is subordinate to all other classes of instruments and all financial instruments in that class of instruments have identical features;

   (c) the instrument does not include any contractual obligation that would meet the definition of a financial liability; and

   (d) the total expected cash flows attributable to the instrument over its life are based substantially on the profit or loss, the change in the recognised net assets or the change in the fair value of the recongised and unrecognised net assets of the entity over the life of the instrument (excluding any effects of the instrument). Profit or loss and the change in recongnised net assets need to be measured in accordance with relevant HKFRSs.

   In addition to the criteria set out above, the issuer must have no other financial instrument or contract that has terms equivalent to (d) above and has the effect of substantially restricting or fixing the residual return to the puttable instrument holders.

Financial instruments puttable only on liquidation

4. The criteria for equity classification for instruments, or components of instruments, that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation are the same as above except the criteria (c) and (d) set out in paragraph 3 do not apply.

5. The distinction between these two types of instruments lies in the difference in the timing of settlement of the obligation under both instruments.

6. HKAS 1 *Presentation of Financial Statements* (as revised in 2007) has been amended to include additional disclosure requirements, including:

   (a) general disclosure for puttable financial instruments classified as equity (e.g. amount, objectives, policies and processes for managing its obligation to repurchase or redeem the instruments, the expected cash outflows on redemption or repurchase and how it was determined);

   (b) disclosure about the amount, timing and reason for reclassification of a puttable instrument or an instrument puttable only on liquidation between financial liabilities and equity; and

   (c) for a limited life entity, information regarding the length of its life.

7. Amendments to HKAS 32 *Financial Instruments: Presentation* and HKAS 1 *Presentation of Financial Statements – Puttable Financial Instruments and Obligations Arising on Liquidation* are effective for annual periods beginning on or after 1 January 2009. Earlier application is permitted provided that the related amendments to HKAS 39 *Financial Instruments: Recognition and Measurement*, HKFRS 7 *Financial Instruments: Disclosures* and HK(IFRIC) – Int 2 *Members' Shares in Co-operative Entities and Similar Instruments* are applied at the same time. The amendments shall be applied retrospectively.

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This revised Standard was issued in December 2007 and revised in June 2008. It supersedes HKAS 1, issued in 2004, as amended in 2005.

Appendix D

Amendments to HKAS 32 and HKAS 1 *Puttable Financial Instruments and Obligations Arising on Liquidation* (issued in June 2008) - effective for annual periods beginning on or after 1 January 2009

The following sets out amendments required for this Standard resulting from amendments to HKAS 32 and HKAS 1 that are not yet effective. Once effective, the amendments set out below will be incorporated into the text of this Standard and this appendix will be deleted. In the amended paragraphs shown below, new text is underlined and deleted text is struck through.

Definitions

After paragraph 8, paragraph 8A is added.

8A The following terms are described in HKAS 32 *Financial Instruments: Presentation* and are used in this Standard with the meaning specified in HKAS 32:

(a) puttable financial instrument classified as an equity instrument (described in paragraphs 16A and 16B of HKAS 32)

(b) an instrument that imposes on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation and is classified as an equity instrument (described in paragraphs 16C and 16D of HKAS 32).

Information to be presented either in the statement of financial position or in the notes

After paragraph 80, paragraph 80A is added.

80A If an entity has reclassified

(a) a puttable financial instrument classified as an equity instrument, or

(b) an instrument that imposes on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation and is classified as an equity instrument

between financial liabilities and equity, it shall disclose the amount reclassified into and out of each category (financial liabilities or equity), and the timing and reason for that reclassification.

After paragraph 136, a heading and paragraph 136A are inserted. Paragraph 138 is amended (new text is underlined and deleted text is struck through).

Puttable financial instruments classified as equity

136A For puttable financial instruments classified as equity instruments, an entity shall disclose (to the extent not disclosed elsewhere):

(a) summary quantitative data about the amount classified as equity;

(b) its objectives, policies and processes for managing its obligation to repurchase or redeem the instruments when required to do so by the instrument holders, including any changes from the previous period;

(c) the expected cash outflow on redemption or repurchase of that class of financial instruments; and

(d) information about how the expected cash outflow on redemption or repurchase was determined.

Other disclosures

138 An entity shall disclose the following, if not disclosed elsewhere in information published with the financial statements:

(a) the domicile and legal form of the entity, its country of incorporation and the address of its registered office (or principal place of business, if different from the registered office);

(b) a description of the nature of the entity's operations and its principal activities; ~~and~~

(c) the name of the parent and the ultimate parent of the group~~.~~; and

(d) if it is a limited life entity, information regarding the length of its life.

After paragraph 139A, paragraph 139B is added.

Transition and effective date

139B *Puttable Financial Instruments and Obligations Arising on Liquidation* (Amendments to HKAS 32 and HKAS 1), issued in June 2008, amended paragraph 138 and inserted paragraphs 8A, 80A and 136A. An entity shall apply those amendments for annual periods beginning on or after 1 January 2009. Earlier application is permitted. If an entity applies the amendments for an earlier period, it shall disclose that fact and apply the related amendments to HKAS 32, HKAS 39, HKFRS 7 and HK(IFRIC)-Int 2 *Members' Shares in Co-operative Entities and Similar Instruments* at the same time.

Appendix ~~D~~E

Amendments resulting from other HKFRSs

The following sets out amendments required for this Standard resulting from other newly issued HKFRSs that are not yet effective. Once effective, the amendments set out below will be incorporated into the text of this Standard and this appendix will be deleted. In the amended paragraphs, new text is underlined and deleted text is struck through.

HKAS 27 *Consolidated and Separate Financial Statements* (issued in March 2008) - effective for annual periods beginning on or after 1 July 2009

References to '[a] minority interest' or 'minority interests' are amended to 'non-controlling interests' in paragraphs 54(q), 83(a)(i), and 83(b)(i).

Paragraph 106 of HKAS 1 (as revised in 2007) is amended as follows:

106 An entity shall present a statement of changes in equity showing in the statement:

(a) total comprehensive income for the period, showing separately the total amounts attributable to owners of the parent and to <u>non-controlling</u> ~~minority~~ interest<u>s</u>;

(b) for each component of equity, the effects of retrospective application or retrospective restatement recognised in accordance with HKAS 8; <u>and</u>

(c) <u>[deleted]</u> **~~the amounts of transactions with owners in their capacity as owners, showing separately contributions by and distributions to owners; and~~**

(d) for each component of equity, a reconciliation between the carrying amount at the beginning and the end of the period, separately disclosing ~~each~~ change<u>s resulting from:</u>

<u>(i) profit or loss;</u>

<u>(ii) each item of other comprehensive income; and</u>

<u>(iii) transactions with owners in their capacity as owners, showing separately contributions by and distributions to owners and changes in ownership interests in subsidiaries that do not result in a loss of control.</u>

Paragraph 139A is added as follows:

139A HKAS 27 (as amended in 2008) amended paragraph 106. An entity shall apply that amendment for annual periods beginning on or after 1 July 2009. If an entity applies HKAS 27 (amended 2008) for an earlier period, the amendment shall be applied for that earlier period. The amendment shall be applied retrospectively.

Appendix

Amendments to Basis for Conclusions on HKAS 32 and HKAS 1 *Puttable Financial Instruments and Obligations Arising on Liquidation* (issued in June 2008) - effective for annual periods beginning on or after 1 January 2009

The following sets out amendments required for this Basis for Conclusions resulting from amendments to HKAS 32 and HKAS 1 that are not yet effective. Once effective, the amendments set out below will be incorporated into the text of this Conclusions and this appendix will be deleted. In the amended paragraphs shown below, new text is underlined and deleted text is struck through.

In the Basis for Conclusions, after paragraph BC6, a heading and paragraph BC6A are added. After paragraph BC100, a heading and paragraphs BC100A and BC100B are added.

Amendments to IAS 32 and IAS 1 –*Puttable Financial Instruments and Obligations Arising on Liquidation* (2008)

BC6A In July 2006 the Board published an exposure draft of proposed amendments to IAS 32 and IAS 1 relating to the classification of puttable instruments and instruments with obligations arising only on liquidation. The Board subsequently confirmed the proposals and in February 2008 issued an amendment that now forms part of IAS 1.

Puttable financial instruments and obligations arising on liquidation

BC100A The Board decided to require disclosure of information about puttable instruments and instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation that are reclassified in accordance with paragraphs 16E and 16F of IAS 32. This is because the Board concluded that this disclosure allows users of financial statements to understand the effects of any reclassifications.

BC100B The Board also concluded that entities with puttable financial instruments classified as equity should be required to disclose additional information to allow users to assess any effect on the entity's liquidity arising from the ability of the holder to put the instruments to the issuer. Financial instruments classified as equity usually do not include any obligation for the entity to deliver a financial asset to another party. Therefore, the Board concluded that additional disclosures are needed in these circumstances. In particular, the Board concluded that entities should disclose the expected cash outflow on redemption or repurchase of those financial instruments that are classified as equity and information about how that amount was determined. That information allows liquidity risk associated with the put obligation and future cash flows to be evaluated.

Appendix

Amendments resulting from other Basis for Conclusions

The following sets out amendments required for this Basis for Conclusions resulting from other newly issued HKFRSs that are not yet effective. Once effective, the amendments set out below will be incorporated into the text of this Basis for Conclusions and this appendix will be deleted. In the amended paragraphs shown below, new text is underlined and deleted text is struck through.

HKAS 27 *Consolidated and Separate Financial Statements* (issued in March 2008) - effective for annual periods beginning on or after 1 July 2009

Paragraph BC 4(e) and the heading above paragraph BC 59 are footnoted as follows:

> In January 2008 the IASB issued an amended IAS 27 *Consolidated and Separate Financial Statements*, which amended 'minority interest' to 'non-controlling interests'.

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Appendix A

Amendments to HKAS 32 and HKAS 1 *Puttable Financial Instruments and Obligations Arising on Liquidation* (issued in June 2008) - effective for annual periods beginning on or after 1 January 2009

The following sets out amendments required for this Standard resulting from amendments to HKAS 32 and HKAS 1 that are not yet effective. Once effective, the amendments set out below will be incorporated into the text of this Standard and this appendix will be deleted. In the amended paragraphs shown below, new text is underlined and deleted text is struck through.

In paragraph 11 of the Standard, the definitions of a financial asset and a financial liability are amended and the definition of a puttable instrument is added after the definition of fair value (new text is underlined and deleted text is struck through).

Definitions (see also paragraphs AG3–AG23)

11. The following terms are used in this Standard with the meanings specified:

…

A *financial asset* is any asset that is:

(a) …

(d) a contract that will or may be settled in the entity's own equity instruments and is:

(i) …

(ii) a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose the entity's own equity instruments do not include puttable financial instruments classified as equity instruments in accordance with paragraphs 16A and 16B, instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation and are classified as equity instruments in accordance with paragraphs 16C and 16D, or instruments that are themselves contracts for the future receipt or delivery of the entity's own equity instruments.

A *financial liability* is any liability that is:

(a) a contractual obligation:

(i) to deliver cash or another financial asset to another entity; or

(ii) to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the entity; or

(b) a contract that will or may be settled in the entity's own equity instruments and is:

(i) a non-derivative for which the entity is or may be obliged to deliver a variable number of the entity's own equity instruments; or

(ii) a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose the entity's own equity instruments do not include puttable financial instruments that are classified as equity instruments in accordance with paragraphs 16A and 16B, instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation and are classified as equity instruments in accordance with paragraphs 16C and 16D, or instruments that are ~~themselves~~ contracts for the future receipt or delivery of the entity's own equity instruments.

As an exception, an instrument that meets the definition of a financial liability is classified as an equity instrument if it has all the features and meets the conditions in paragraphs 16A and 16B or paragraphs 16C and 16D.

…

A *puttable instrument* is a financial instrument that gives the holder the right to put the instrument back to the issuer for cash or another financial asset or is automatically put back to the issuer on the occurrence of an uncertain future event or the death or retirement of the instrument holder.

The heading before paragraph 15 and paragraph 16 are amended (new text is underlined and deleted text is struck through). After paragraph 16, a heading, paragraphs 16A and 16B, another heading, paragraphs 16C and 16D, another heading and paragraphs 16E and 16F are added.

Presentation

Liabilities and equity (see also paragraphs AG13–AG14J and AG25–AG29A)

…

16 When an issuer applies the definitions in paragraph 11 to determine whether a financial instrument is an equity instrument rather than a financial liability, the instrument is an equity instrument if, and only if, both conditions (a) and (b) below are met.

(a) …

(b) If the instrument will or may be settled in the issuer's own equity instruments, it is:

(i) …

(ii) a derivative that will be settled only by the issuer exchanging a fixed amount of cash or another financial asset for a fixed number of its own equity instruments. For this purpose the issuer's own equity instruments do not include instruments that have all the features and meet the conditions described in paragraphs 16A and 16B or paragraphs 16C and 16D, or instruments that are ~~themselves~~ contracts for the future receipt or delivery of the issuer's own equity instruments.

A contractual obligation, including one arising from a derivative financial instrument, that will or may result in the future receipt or delivery of the issuer's own equity instruments, but does not meet conditions (a) and (b) above, is not an equity instrument. As an exception, an instrument that meets the definition of a financial liability is classified as an equity instrument if it has all the features and meets the conditions in paragraphs 16A and 16B or paragraphs 16C and 16D.

Puttable instruments

16A A puttable financial instrument includes a contractual obligation for the issuer to repurchase or redeem that instrument for cash or another financial asset on exercise of the put. As an exception to the definition of a financial liability, an instrument that includes such an obligation is classified as an equity instrument if it has all the following features:

(a) It entitles the holder to a pro rata share of the entity's net assets in the event of the entity's liquidation. The entity's net assets are those assets that remain after deducting all other claims on its assets. A pro rata share is determined by:

(i) dividing the entity's net assets on liquidation into units of equal amount; and

(ii) multiplying that amount by the number of the units held by the financial instrument holder.

(b) The instrument is in the class of instruments that is subordinate to all other classes of instruments. To be in such a class the instrument:

(i) has no priority over other claims to the assets of the entity on liquidation, and

(ii) does not need to be converted into another instrument before it is in the class of instruments that is subordinate to all other classes of instruments.

(c) All financial instruments in the class of instruments that is subordinate to all other classes of instruments have identical features. For example, they must all be puttable, and the formula or other method used to calculate the repurchase or redemption price is the same for all instruments in that class.

(d) Apart from the contractual obligation for the issuer to repurchase or redeem the instrument for cash or another financial asset, the instrument does not include any contractual obligation to deliver cash or another financial asset to another entity, or to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavourable to the entity, and it is not a contract that will or may be settled in the entity's own equity instruments as set out in subparagraph (b) of the definition of a financial liability.

(e) The total expected cash flows attributable to the instrument over the life of the instrument are based substantially on the profit or loss, the change in the recognised net assets or the change in the fair value of the recognised and unrecognised net assets of the entity over the life of the instrument (excluding any effects of the instrument).

16B For an instrument to be classified as an equity instrument, in addition to the instrument having all the above features, the issuer must have no other financial instrument or contract that has:

(a) total cash flows based substantially on the profit or loss, the change in the recognised net assets or the change in the fair value of the recognised and unrecognised net assets of the entity (excluding any effects of such instrument or contract) and

(b) the effect of substantially restricting or fixing the residual return to the puttable instrument holders.

For the purposes of applying this condition, the entity shall not consider non-financial contracts with a holder of an instrument described in paragraph 16A that have contractual terms and conditions that are similar to the contractual terms and conditions of an equivalent contract that might occur between a non-instrument holder and the issuing entity. If the entity cannot determine that this condition is met, it shall not classify the puttable instrument as an equity instrument.

Instruments, or components of instruments, that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation

16C Some financial instruments include a contractual obligation for the issuing entity to deliver to another entity a pro rata share of its net assets only on liquidation. The obligation arises because liquidation either is certain to occur and outside the control of the entity (for example, a limited life entity) or is uncertain to occur but is at the option of the instrument holder. As an exception to the definition of a financial liability, an instrument that includes such an obligation is classified as an equity instrument if it has all the following features:

(a) It entitles the holder to a pro rata share of the entity's net assets in the event of the entity's liquidation. The entity's net assets are those assets that remain after deducting all other claims on its assets. A pro rata share is determined by:

  (i) dividing the net assets of the entity on liquidation into units of equal amount; and

  (ii) multiplying that amount by the number of the units held by the financial instrument holder.

(b) The instrument is in the class of instruments that is subordinate to all other classes of instruments. To be in such a class the instrument:

  (i) has no priority over other claims to the assets of the entity on liquidation, and

  (ii) does not need to be converted into another instrument before it is in the class of instruments that is subordinate to all other classes of instruments.

(c) All financial instruments in the class of instruments that is subordinate to all other classes of instruments must have an identical contractual obligation for the issuing entity to deliver a pro rata share of its net assets on liquidation.

16D For an instrument to be classified as an equity instrument, in addition to the instrument having all the above features, the issuer must have no other financial instrument or contract that has:

(a) total cash flows based substantially on the profit or loss, the change in the recognised net assets or the change in the fair value of the recognised and unrecognised net assets of the entity (excluding any effects of such instrument or contract) and

(b) the effect of substantially restricting or fixing the residual return to the instrument holders.

For the purposes of applying this condition, the entity shall not consider non-financial contracts with a holder of an instrument described in paragraph 16C that have contractual terms and conditions that are similar to the contractual terms and conditions of an equivalent contract that might occur between a non-instrument holder and the issuing entity. If the entity cannot determine that this condition is met, it shall not classify the instrument as an equity instrument.

Reclassification of puttable instruments and instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation

16E An entity shall classify a financial instrument as an equity instrument in accordance with paragraphs 16A and 16B or paragraphs 16C and 16D from the date when the instrument has all the features and meets the conditions set out in those paragraphs. An entity shall reclassify a financial instrument from the date when the instrument

ceases to have all the features or meet all the conditions set out in those paragraphs. For example, if an entity redeems all its issued non-puttable instruments and any puttable instruments that remain outstanding have all the features and meet all the conditions in paragraphs 16A and 16B, the entity shall reclassify the puttable instruments as equity instruments from the date when it redeems the non-puttable instruments.

16F An entity shall account as follows for the reclassification of an instrument in accordance with paragraph 16E:

(a) It shall reclassify an equity instrument as a financial liability from the date when the instrument ceases to have all the features or meet the conditions in paragraphs 16A and 16B or paragraphs 16C and 16D. The financial liability shall be measured at the instrument's fair value at the date of reclassification. The entity shall recognise in equity any difference between the carrying value of the equity instrument and the fair value of the financial liability at the date of reclassification.

(b) It shall reclassify a financial liability as equity from the date when the instrument has all the features and meets the conditions set out in paragraphs 16A and 16B or paragraphs 16C and 16D. An equity instrument shall be measured at the carrying value of the financial liability at the date of reclassification.

Paragraphs 17–19 are amended (new text is underlined and deleted text is struck through).

No contractual obligation to deliver cash or another financial asset (paragraph 16(a))

17 With the exception of the circumstances described in paragraphs 16A and 16B or paragraphs 16C and 16D, ~~A~~a critical feature in differentiating a financial liability from an equity instrument is the existence of a contractual obligation of one party to the financial instrument (the issuer) either to deliver cash or another financial asset to the other party (the holder) or to exchange financial assets or financial liabilities with the holder under conditions that are potentially unfavourable to the issuer. …

18 The substance of a financial instrument, rather than its legal form, governs its classification in the entity's statement of financial position. Substance and legal form are commonly consistent, but not always. Some financial instruments take the legal form of equity but are liabilities in substance and others may combine features associated with equity instruments and features associated with financial liabilities. For example:

(a) …

(b) a financial instrument that gives the holder the right to put it back to the issuer for cash or another financial asset (a 'puttable instrument') is a financial liability, except for those instruments classified as equity instruments in accordance with paragraphs 16A and 16B or paragraphs 16C

and 16D. ~~This is so~~ The financial instrument is a financial liability even when the amount of cash or other financial assets is determined on the basis of an index or other item that has the potential to increase or decrease~~, or when the legal form of the puttable instrument gives the holder a right to a residual interest in the assets of an issuer~~. The existence of an option for the holder to put the instrument back to the issuer for cash or another financial asset means that the puttable instrument meets the definition of a financial liability, except for those instruments classified as equity instruments in accordance with paragraphs 16A and 16B or paragraphs 16C and 16D. For example, open-ended mutual funds, unit trusts, partnerships and some co-operative entities may provide their unitholders or members with a right to redeem their interests in the issuer at any time for cash ~~equal to their proportionate share of the asset value of the issuer~~, which results in the unitholders' or members' interests being classified as financial liabilities, except for those instruments classified as equity instruments in accordance with paragraphs 16A and 16B or paragraphs 16C and 16D. However, classification as a financial liability does not preclude the use of descriptors such as 'net asset value attributable to unitholders' and 'change in net asset value attributable to unitholders' in the financial statements of an entity that has no contributed equity (such as some mutual funds and unit trusts, see Illustrative Example 7) or the use of additional disclosure to show that total members' interests comprise items such as reserves that meet the definition of equity and puttable instruments that do not (see Illustrative Example 8).

19 If an entity does not have an unconditional right to avoid delivering cash or another financial asset to settle a contractual obligation, the obligation meets the definition of a financial liability, except for those instruments classified as equity instruments in accordance with paragraphs 16A and 16B or paragraphs 16C and 16D. For example:

…

Paragraphs 22, 23 and 25 are amended (new text is underlined and deleted text is struck through). After paragraph 22, paragraph 22A is added.

Settlement in the entity's own equity instruments (paragraph 16(b))

22 Except as stated in paragraph 22A, ~~A~~a contract that will be settled by the entity (receiving or) delivering a fixed number of its own equity instruments in exchange for a fixed amount of cash or another financial asset is an equity instrument. For example, …

22A If the entity's own equity instruments to be received, or delivered, by the entity upon settlement of a contract are puttable financial instruments with all the features and meeting the conditions described in paragraphs 16A and 16B, or instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation with all the features and meeting the conditions described in paragraphs 16C and 16D, the contract is a financial asset or a financial liability. This includes a contract that will be settled by the entity receiving or delivering a fixed number of such instruments in exchange for a fixed amount of cash or another financial asset.

23 With the exception of the circumstances described in paragraphs 16A and 16B or paragraphs 16C and 16D, ~~A~~a contract that contains an obligation for an entity to purchase its own equity instruments for cash or another financial asset gives rise to a financial liability for the present value of the redemption amount (for example, for the present value of the forward repurchase price, option exercise price or other redemption amount). This is the case even if the contract itself is an equity instrument. One example ...

Contingent settlement provisions

25 A financial instrument may require the entity to deliver cash or another financial asset, or otherwise to settle it in such a way that it would be a financial liability, in the event of the occurrence or non-occurrence of uncertain future events (or on the outcome of uncertain circumstances) that are beyond the control of both the issuer and the holder of the instrument, such as a change in a stock market index, consumer price index, interest rate or taxation requirements, or the issuer's future revenues, net income or debt-to-equity ratio. The issuer of such an instrument does not have the unconditional right to avoid delivering cash or another financial asset (or otherwise to settle it in such a way that it would be a financial liability). Therefore, it is a financial liability of the issuer unless:

(a) the part of the contingent settlement provision that could require settlement in cash or another financial asset (or otherwise in such a way that it would be a financial liability) is not genuine; ~~or~~

(b) the issuer can be required to settle the obligation in cash or another financial asset (or otherwise to settle it in such a way that it would be a financial liability) only in the event of liquidation of the issuer~~.~~; or

(c) the instrument has all the features and meets the conditions in paragraphs 16A and 16B.

Before paragraph 96, the heading is amended (new text is underlined). After paragraph 96, paragraphs 96A–96C are added. After paragraph 97B, paragraph 97C is added.

Effective date and transition

96A *Puttable Financial Instruments and Obligations Arising on Liquidation* (Amendments to HKAS 32 and HKAS 1), issued in June 2008, required financial instruments that contain all the features and meet the conditions in paragraphs 16A and 16B or paragraphs 16C and 16D to be classified as an equity instrument, amended paragraphs 11, 16, 17–19, 22, 23, 25, AG13, AG14 and AG27, and inserted paragraphs 16A–16F, 22A, 96B, 96C, 97C, AG14A–AG14J and AG29A. An entity shall apply those amendments for annual periods beginning on or after 1 January 2009. Earlier application is permitted. If an entity applies the changes for an earlier period, it shall disclose that fact and apply the related amendments to HKAS 1, HKAS 39, HKFRS 7 and HK(IFRIC)-Int 2 at the same time.

96B *Puttable Financial Instruments and Obligations Arising on Liquidation* introduced a limited scope exception; therefore, an entity shall not apply the exception by analogy.

96C The classification of instruments under this exception shall be restricted to the accounting for such an instrument under HKAS 1, HKAS 32, HKAS 39 and HKFRS 7. The instrument shall not be considered an equity instrument under other guidance, for example HKFRS 2 *Share-based Payment*.

97C When applying the amendments described in paragraph 96A, an entity is required to split a compound financial instrument with an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation into separate liability and equity components. If the liability component is no longer outstanding, a retrospective application of those amendments to HKAS 32 would involve separating two components of equity. The first component would be in retained earnings and represent the cumulative interest accreted on the liability component. The other component would represent the original equity component. Therefore, an entity need not separate these two components if the liability component is no longer outstanding at the date of application of the amendments.

In the Appendix *Application Guidance*, paragraphs AG13 and AG14 are amended (new text is underlined and deleted text is struck through). After paragraph AG14, a heading, paragraphs AG14A–AG14D, another heading, paragraph AG14E, another heading, paragraphs AG14F–AG14I, another heading and paragraph AG14J are added.

Equity instruments

AG13 Examples of equity instruments include non-puttable ordinary shares, some puttable instruments (see paragraphs 16A and 16B), some instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation (see paragraphs 16C and 16D), some types of preference shares (see paragraphs AG25 and AG26), and warrants or written call options that allow the holder to subscribe for or purchase a fixed number of non-puttable ordinary shares in the issuing entity in exchange for a fixed amount of cash or another financial asset. An entity's obligation to issue or purchase a fixed number of its own equity instruments in exchange for a fixed amount of cash or another financial asset is an equity instrument of the entity (except as stated in paragraph 22A). However, if such a contract contains an obligation for the entity to pay cash or another financial asset (other than a contract classified as equity in accordance with paragraphs 16A and 16B or paragraphs 16C and 16D), it also gives rise to a liability for the present value of the redemption amount (see paragraph AG27(a)). 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 may be the case following the declaration of a dividend or when the entity is being wound up and any assets remaining after the satisfaction of liabilities become distributable to shareholders.

AG14 A purchased call option or other similar contract acquired by an entity that gives it the right to reacquire a fixed number of its own equity instruments in exchange for delivering a fixed amount of cash or another financial asset is not a financial asset of the entity (except as stated in paragraph 22A). Instead, any consideration paid for such a contract is deducted from equity.

The class of instruments that is subordinate to all other classes (paragraphs 16A(b) and 16C(b))

AG14A One of the features of paragraphs 16A and 16C is that the financial instrument is in the class of instruments that is subordinate to all other classes.

AG14B When determining whether an instrument is in the subordinate class, an entity evaluates the instrument's claim on liquidation as if it were to liquidate on the date when it classifies the instrument. An entity shall reassess the classification if there is a change in relevant circumstances. For example, if the entity issues or redeems another financial instrument, this may affect whether the instrument in question is in the class of instruments that is subordinate to all other classes.

AG14C An instrument that has a preferential right on liquidation of the entity is not an instrument with an entitlement to a pro rata share of the net assets of the entity. For example, an instrument has a preferential right on liquidation if it entitles the holder to a fixed dividend on liquidation, in addition to a share of the entity's net assets, when other instruments in the subordinate class with a right to a pro rata share of the net assets of the entity do not have the same right on liquidation.

AG14D If an entity has only one class of financial instruments, that class shall be treated as if it were subordinate to all other classes.

Total expected cash flows attributable to the instrument over the life of the instrument (paragraph 16A(e))

AG14E The total expected cash flows of the instrument over the life of the instrument must be substantially based on the profit or loss, change in the recognised net assets or fair value of the recognised and unrecognised net assets of the entity over the life of the instrument. Profit or loss and the change in the recognised net assets shall be measured in accordance with relevant HKFRSs.

Transactions entered into by an instrument holder other than as owner of the entity (paragraphs 16A and 16C)

AG14F The holder of a puttable financial instrument or an instrument that imposes on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation may enter into transactions with the entity in a role other than that of an owner. For example, an instrument holder may also be an employee of the entity. Only the cash flows and the contractual terms and conditions of the instrument that relate to the instrument holder as an owner of the entity shall be considered when assessing whether the instrument should be classified as equity under paragraph 16A or paragraph 16C.

AG14G An example is a limited partnership that has limited and general partners. Some general partners may provide a guarantee to the entity and may be remunerated for providing that guarantee. In such situations, the guarantee and the associated cash flows relate to the instrument holders in their role as guarantors and not in their roles as owners of the entity. Therefore, such a guarantee and the associated cash flows would not result in the general partners being considered subordinate to the limited partners, and would be disregarded when assessing whether the contractual terms of the limited partnership instruments and the general partnership instruments are identical.

AG14H Another example is a profit or loss sharing arrangement that allocates profit or loss to the instrument holders on the basis of services rendered or business generated during the current and previous years. Such arrangements are transactions with instrument holders in their role as non-owners and should not be considered when assessing the features listed in paragraph 16A or paragraph 16C. However, profit or loss sharing arrangements that allocate profit or loss to instrument holders based on the nominal amount of their instruments relative to others in the class represent transactions with the instrument holders in their roles as owners and should be considered when assessing the features listed in paragraph 16A or paragraph 16C.

AG14I The cash flows and contractual terms and conditions of a transaction between the instrument holder (in the role as a non-owner) and the issuing entity must be similar to an equivalent transaction that might occur between a non-instrument holder and the issuing entity.

No other financial instrument or contract with total cash flows that substantially fixes or restricts the residual return to the instrument holder (paragraphs 16B and 16D)

AG14J A condition for classifying as equity a financial instrument that otherwise meets the criteria in paragraph 16A or paragraph 16C is that the entity has no other financial instrument or contract that has (a) total cash flows based substantially on the profit or loss, the change in the recognised net assets or the change in the fair value of the recognised and unrecognised net assets of the entity and (b) the effect of substantially restricting or fixing the residual return. The following instruments, when entered into on normal commercial terms with unrelated parties, are unlikely to prevent instruments that otherwise meet the criteria in paragraph 16A or paragraph 16C from being classified as equity:

(a) instruments with total cash flows substantially based on specific assets of the entity.

(b) instruments with total cash flows based on a percentage of revenue.

(c) contracts designed to reward individual employees for services rendered to the entity.

(d) contracts requiring the payment of an insignificant percentage of profit for services rendered or goods provided.

Paragraph AG27 is amended (new text is underlined) and after paragraph AG29, paragraph AG29A is added.

AG27 The following examples illustrate how to classify different types of contracts on an entity's own equity instruments:

(a) A contract that will be settled by the entity receiving or delivering a fixed number of its own shares for no future consideration, or exchanging a fixed number of its own shares for a fixed amount of cash or another financial asset, is an equity instrument (except as stated in paragraph 22A). Accordingly, any consideration received or paid for such a contract is added directly to or deducted directly from equity. One example is an issued share option that gives the counterparty a right to buy a fixed number of the entity's shares for a fixed amount of cash. However, if the contract requires the entity to purchase (redeem) its own shares for cash or another financial asset at a fixed or determinable date or on demand, the entity also recognises a financial liability for the present value of the redemption amount (with the exception of instruments that have all the features and meet the conditions in paragraphs 16A and 16B or paragraphs 16C and 16D). One example is an entity's obligation under a forward contract to repurchase a fixed number of its own shares for a fixed amount of cash.

(b) An entity's obligation to purchase its own shares for cash gives rise to a financial liability for the present value of the redemption amount even if the number of shares that the entity is obliged to repurchase is not fixed or if the obligation is conditional on the counterparty exercising a right to redeem (except as stated in paragraphs 16A and 16B or paragraphs 16C and 16D). One example of a conditional obligation is an issued option that requires the entity to repurchase its own shares for cash if the counterparty exercises the option.

(c) A contract that will be settled in cash or another financial asset is a financial asset or financial liability even if the amount of cash or another financial asset that will be received or delivered is based on changes in the market price of the entity's own equity (except as stated in paragraphs 16A and 16B or paragraphs 16C and 16D). One example is a net cash-settled share option.

(d) …

AG29A Some types of instruments that impose a contractual obligation on the entity are classified as equity instruments in accordance with paragraphs 16A and 16B or paragraphs 16C and 16D. Classification in accordance with those paragraphs is an exception to the principles otherwise applied in this Standard to the classification of an instrument. This exception is not extended to the classification of non-controlling interests in the consolidated financial statements. Therefore, instruments classified as equity instruments in accordance with either paragraphs 16A and 16B or paragraphs 16C and 16D in the separate or individual financial statements that are non-controlling interests are classified as liabilities in the consolidated financial statements of the group.

Appendix B

Amendments resulting from other HKFRSs

The following sets out amendments required for this Standard resulting from other newly issued HKFRSs that are not yet effective. Once effective, the amendments set out below will be incorporated into the text of this Standard and this appendix will be deleted. In the amended paragraphs shown below, new text is underlined and deleted text is struck through.

HKAS 1 *Presentation of Financial Statements* (issued in December 2007) - effective for annual periods beginning on or after 1 January 2009

In paragraph 18, 'on the entity's balance sheet' is amended to 'in the entity's statement of financial position'.

In paragraph 29, last sentence, 'on its balance sheet' is amended to 'in its statement of financial position'.

In paragraph 40, 'income statement' is amended to 'statement of comprehensive income or separate income statement (if presented)' (twice).

Paragraph 97A is added as follows:

97A HKAS 1 (as revised in 2007) amended the terminology used throughout HKFRSs. In addition it amended paragraph 40. An entity shall apply those amendments for annual periods beginning on or after 1 January 2009. If an entity applies HKAS 1 (revised 2007) for an earlier period, the amendments shall be applied for that earlier period.

The Application Guidance is amended as described below.

In paragraph AG31, 'on the balance sheet' is amended to 'in the statement of financial position'.

In paragraph AG39, 'on an entity's balance sheet' is amended to 'in an entity's statement of financial position'.

HKFRS 3 *Business Combinations* (issued in March 2008) - effective for annual periods beginning on or after 1 July 2009

Paragraph 4(c) is deleted.

Paragraph 97B is added as follows:

97B HKFRS 3 (as revised in 2008) deleted paragraph 4(c). An entity shall apply that amendment for annual periods beginning on or after 1 July 2009. If an entity applies HKFRS 3 (revised 2008) for an earlier period, the amendment shall also be applied for that earlier period.

HKAS 27 *Consolidated and Separate Financial Statements* (issued in March 2008) - effective for annual periods beginning on or after 1 July 2009

References to '[a] minority interest' or 'minority interests' are amended to 'non-controlling interests' in paragraph AG29.

Appendix C

Comparison with International Accounting Standards

This comparison appendix, which was prepared as at 20 April 2004 and deals only with significant differences in the standards extant, is produced for information only and does not form part of the standards in HKAS 32.

The International Accounting Standard comparable with HKAS 32 is IAS 32 *Financial Instruments: Presentation*.

There are no major textual differences between HKAS 32 and IAS 32.

Appendix A

Amendments to Basis for Conclusions on HKAS 32 and HKAS 1 *Puttable Financial Instruments and Obligations Arising on Liquidation* (issued in June 2008) - effective for annual periods beginning on or after 1 January 2009

The following sets out amendments required for this Basis for Conclusions resulting from amendments to HKAS 32 and HKAS 1 that are not yet effective. Once effective, the amendments set out below will be incorporated into the text of this Conclusions and this appendix will be deleted. In the amended paragraphs shown below, new text is underlined and deleted text is struck through.

In the Basis for Conclusions, after paragraph BC3, paragraph BC3A is added. After paragraph BC7, paragraph BC7A is added. After paragraph BC49, two headings, paragraphs BC50–BC63, another heading, paragraphs BC64–BC67, another heading, paragraph BC68, another heading and paragraphs BC69–BC74 are added.

BC3A In July 2006 the Board published an exposure draft of proposed amendments to IAS 32 relating to the classification of puttable instruments and instruments with obligations arising on liquidation. The Board subsequently confirmed the proposals and in 2008 issued an amendment that now forms part of IAS 32. A summary of the Board's considerations and reasons for its conclusions is in paragraphs BC50–BC74.

Puttable instruments (paragraph 18(b))

BC7A The Board reconsidered its conclusions with regards to some puttable instruments and amended IAS 32 in February 2008 (see paragraphs BC50–BC74).

Amendments for some puttable instruments and some instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation

Amendment for puttable instruments

BC50 As discussed in paragraphs BC7 and BC8, puttable instruments meet the definition of a financial liability and the Board concluded that all such instruments should be classified as liabilities. However, constituents raised the following concerns about classifying such instruments as financial liabilities if they represent the residual claim to the net assets of the entity:

(a) On an ongoing basis, the liability is recognised at not less than the amount payable on demand. This can result in the entire market capitalisation of the entity being recognised as a liability depending on the basis for which the redemption value of the financial instrument is calculated.

(b) Changes in the carrying value of the liability are recognised in profit or loss. This results in counter-intuitive accounting (if the redemption value is linked to the performance of the entity) because:

(i) when an entity performs well, the present value of the settlement amount of the liabilities increases, and a loss is recognised.

(ii) when the entity performs poorly, the present value of the settlement amount of the liability decreases, and a gain is recognised.

(c) It is possible, again depending on the basis for which the redemption value is calculated, that the entity will report negative net assets because of unrecognised intangible assets and goodwill, and because the measurement of recognised assets and liabilities may not be at fair value.

(d) The issuing entity's statement of financial position portrays the entity as wholly, or mostly, debt funded.

(e) Distributions of profits to shareholders are recognised as expenses. Hence, it may appear that profit or loss is a function of the distribution policy, not performance.

Furthermore, constituents contended that additional disclosures and adapting the format of the statement of comprehensive income and statement of financial position did not resolve these concerns.

BC51 The Board agreed with constituents that many puttable instruments, despite meeting the definition of a financial liability, represent a residual interest in the net assets of the entity. The Board also agreed with constituents that additional disclosures and adapting the format of the entity's financial statements did not resolve the problem of the lack of relevance and understandability of that current accounting treatment. Therefore, the Board decided to amend IAS 32 to improve the financial reporting of these instruments.

BC52 The Board considered the following ways to improve the financial reporting of instruments that represent a residual interest in the net assets of the entity:

(a) to continue to classify these instruments as financial liabilities, but amend their measurement so that changes in their fair value would not be recognised;

(b) to amend IAS 32 to require separation of all puttable instruments into a put option and a host instrument; or

(c) to amend IAS 32 to provide a limited scope exception so that financial instruments puttable at fair value would be classified as equity, if specified conditions were met.

Amend the measurement of some puttable financial instruments so that changes in their fair value would not be recognised

BC53 The Board decided against this approach because:

(a) it is inconsistent with the principle in IAS 32 and IAS 39 that only equity instruments are not remeasured after their initial recognition;

(b) it retains the disadvantage that entities whose instruments are all puttable would have no equity instruments; and

(c) it introduces a new category of financial liabilities to IAS 39, and thus increases complexity.

Separate all puttable instruments into a put option and a host instrument

BC54 The Board concluded that conducting further research into an approach that splits a puttable share into an equity component and a written put option component (financial liability) would duplicate efforts of the Board's longer-term project on liabilities and equity. Consequently, the Board decided not to proceed with a project at this stage to determine whether a puttable share should be split into an equity component and a written put option component.

Classify as equity instruments puttable instruments that represent a residual interest in the entity

BC55 The Board decided to proceed with proposals to amend IAS 32 to require puttable financial instruments that represent a residual interest in the net assets of the entity to be classified as equity provided that specified conditions are met. The proposals represented a limited scope exception to the definition of a financial liability and a short-term solution, pending the outcome of the longer-term project on liabilities and equity. In June 2006 the Board published an exposure draft proposing that financial instruments puttable at fair value that meet specific criteria should be classified as equity.

BC56 In response to comments received from respondents to that exposure draft, the Board amended the criteria for identifying puttable instruments that represent a residual interest in the entity, to those included in paragraphs 16A and 16B. The Board decided on those conditions for the following reasons:

(a) to ensure that the puttable instruments, as a class, represent the residual interest in the net assets of the entity;

(b) to ensure that the proposed amendments are consistent with a limited scope exception to the definition of a financial liability; and

(c) to reduce structuring opportunities that might arise as a result of the amendments.

BC57 The Board decided that the instrument must entitle the holder to a pro rata share of the net assets on liquidation because the net assets on liquidation represent the ultimate residual interest of the entity.

BC58 The Board decided that the instrument must be in the class of instruments that is subordinate to all other classes of instruments on liquidation in order to represent the residual interest in the entity.

BC59 The Board decided that all instruments in the class that is subordinate to all other classes of instruments must have identical contractual terms and conditions. In order to ensure that the class of instruments as a whole is the residual class, the Board decided that no instrument holder in that class can have preferential terms or conditions in its position as an owner of the entity.

BC60 The Board decided that the puttable instruments should contain no contractual obligation to deliver a financial asset to another entity other than the put. That is because the amendments represent a limited scope exception to the definition of a financial liability and extending that exception to instruments that also contain other contractual obligations is not appropriate. Moreover, the Board concluded that if the puttable instrument contains another contractual obligation, that instrument may not represent the residual interest because the holder of the puttable instrument may have a claim to some of the net assets of the entity in preference to other instruments.

BC61 As well as requiring a direct link between the puttable instrument and the performance of the entity, the Board also decided that there should be no financial instrument or contract with a return that is more residual. The Board decided to require that there must be no other financial instrument or contract that has total cash flows based substantially on the performance of the entity and has the effect of significantly restricting or fixing the return to the puttable instrument holders. This criterion was included to ensure that the holders of the puttable instruments represent the residual interest in the net assets of the entity.

BC62 An instrument holder may enter into transactions with the issuing entity in a role other than that of an owner. The Board concluded that it is inappropriate to consider cash flows and contractual features related to the instrument holder in a non-owner role when evaluating whether a financial instrument has the features set out in paragraph 16A or paragraph 16C. That is because those cash flows and contractual features are separate and distinct from the cash flows and contractual features of the puttable financial instrument.

BC63 The Board also decided that contracts (such as warrants and other derivatives) to be settled by the issue of puttable financial instruments should be precluded from equity classification. That is because the Board noted that the amendments represent a limited scope exception to the definition of a financial liability and extending that exception to such contracts is not appropriate.

Amendment for obligations to deliver to another party a pro rata share of the net assets of the entity only on liquidation

BC64 Issues similar to those raised by constituents relating to classification of puttable financial instruments apply to some financial instruments that create an obligation only on liquidation of the entity.

BC65 In the exposure draft published in June 2006, the Board proposed to exclude from the definition of a financial liability a contractual obligation that entitles the holder to a pro rata share of the net assets of the entity only on liquidation of the entity. The liquidation of the entity may be:

(a) certain to occur and outside the control of the entity (limited life entities); or

(b) uncertain to occur but at the option of the holder (for example, some partnership interests).

BC66 Respondents to that exposure draft were generally supportive of the proposed amendment.

BC67 The Board decided that an exception to the definition of a financial liability should be made for instruments that entitle the holder to a pro rata share of the net assets of an entity only on liquidation if particular requirements are met. Many of those requirements, and the reasons for them, are similar to those for puttable financial instruments. The differences between the requirements are as follows:

(a) there is no requirement that there be no other contractual obligations;

(b) there is no requirement to consider the expected total cash flows throughout the life of the instrument;

(c) the only feature that must be identical among the instruments in the class is the obligation for the issuing entity to deliver to the holder a pro rata share of its net assets on liquidation.

The reason for the differences is the timing of settlement of the obligation. The life of the financial instrument is the same as the life of the issuing entity; the extinguishment of the obligation can occur only at liquidation. Therefore, the Board concluded that it was appropriate to focus only on the obligations that exist at liquidation. The instrument must be subordinate to all other classes of instruments and represent the residual interests only at that point in time. However, if the instrument contains other contractual obligations, those obligations may need to be accounted for separately in accordance with the requirements of IAS 32.

Non-controlling interests

BC68 The Board decided that puttable financial instruments or instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation should be classified as equity in the separate financial statements of the issuer if they represent the residual class of instruments (and all the relevant requirements are met). The Board decided that such instruments were not the residual interest in the consolidated financial statements and therefore that non-controlling interests that contain an obligation to transfer a financial asset to another entity should be classified as a financial liability in the consolidated financial statements.

Analysis of costs and benefits

BC69 The Board acknowledged that the amendments made in February 2008 are not consistent with the definition of a liability in the *Framework*, or with the underlying principle of IAS 32, which is based on that definition. Consequently, those amendments added complexity to IAS 32 and introduced the need for detailed rules. However, the Board also noted that IAS 32 contains other exceptions to its principle (and the definition of a liability in the *Framework*) that require instruments to be classified as liabilities that otherwise would be treated as equity. Those exceptions highlight the need for a comprehensive reconsideration of the distinctions between liabilities and equity, which the Board is undertaking in its long-term project.

BC70 In the interim, the Board concluded that classifying as equity the instruments that have all the features and meet the conditions in paragraphs 16A and 16B or paragraphs 16C and 16D would improve the comparability of information provided to the users of financial statements. That is because financial instruments that are largely equivalent to ordinary shares would be consistently classified across different entity structures (eg some partnerships, limited life entities and co-operatives). The specified instruments differ from ordinary shares in one respect; that difference is the obligation to deliver cash (or another financial asset). However, the Board concluded that the other characteristics of the specified instruments are sufficiently similar to ordinary shares for the instruments to be classified as equity. Consequently, the Board concluded that the amendments will result in financial reporting that is more understandable and relevant to the users of financial statements.

BC71 Furthermore, in developing the amendments, the Board considered the costs to entities of obtaining information necessary to determine the required classification. The Board believes that the costs of obtaining any new information would be slight because all of the necessary information should be readily available.

BC72 The Board also acknowledged that one of the costs and risks of introducing exceptions to the definition of a financial liability is the structuring opportunities that may result. The Board concluded that financial structuring opportunities are minimised by the detailed criteria required for equity classification and the related disclosures.

BC73 Consequently, the Board believed that the benefits of the amendments outweigh the costs.

BC74 The Board took the view that, in most cases, entities should be able to apply the amendments retrospectively. The Board noted that IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provides relief when it is impracticable to apply a change in accounting policy retrospectively as a result of a new requirement. Furthermore, the Board took the view that the costs outweighed the benefits of separating a compound financial instrument with an obligation to deliver a pro rata share of the net assets of the entity only on liquidation when the liability component is no longer outstanding on the date of initial application. Hence, there is no requirement on transition to separate such compound instruments.

Appendix B

Amendments resulting from other Basis for Conclusions

The following sets out amendments required for this Basis for Conclusions resulting from other newly issued HKFRSs that are not yet effective. Once effective, the amendments set out below will be incorporated into the text of this Basis for Conclusions and this appendix will be deleted. In the amended paragraphs shown below, new text is underlined and deleted text is struck through.

HKAS 1 *Presentation of Financial Statement*s (issued in December 2007) – effective for annual periods beginning on or after 1 January 2009

Paragraphs BC8 and BC22 are footnoted as follows:

BC8 The Board … also agreed that it should provide examples of how such entities might present their income statement* and balance sheet† (see Illustrative Examples 7 and 8).

* IAS 1 *Presentation of Financial Statements* (as revised in 2007) requires an entity to present all income and expense items in one statement of comprehensive income or in two statements (a separate income statement and a statement of comprehensive income).

† IAS 1 (revised 2007) replaced the term 'balance sheet' with 'statement of financial position'.

BC22 The Standard requires the separate presentation ~~on~~ in an entity's balance sheet* of liability and equity components of a single financial instrument. …

* IAS 1 (as revised in 2007) replaced the term 'balance sheet' with 'statement of financial position'.

HKAS 27 *Consolidated and Separate Financial Statements* (issued in February 2008) - effective for annual periods beginning on or after 1 July 2009

Paragraph BC49(h) ‘minority interest’ is footnoted as follows:

> In January 2008 the IASB issued an amended IAS 27 *Consolidated and Separate Financial Statements*, which amended ‘minority interest’ to ‘non-controlling interests’.

Appendix C

Dissenting opinions (2008 Amendment)

Dissent of Mary E Barth and Robert P Garnett

DO1 Professor Barth and Mr Garnett voted against the publication of the Amendments to IAS 32 Financial Instruments: Presentation and IAS 1 Presentation of Financial Statements—*Puttable Financial Instruments and Obligations Arising on Liquidation*. The reasons for their dissent are set out below.

DO2 These Board members believe that the decision to permit entities to classify as equity some puttable financial instruments and some financial instruments that entitle the holder to a pro rata share of the net assets of the entity only on liquidation is inconsistent with the *Framework*. The contractual provisions attached to those instruments give the holders the right to put the instruments to the entity and demand cash. The *Framework*'s definition of a liability is that it is a present obligation of the entity arising from a past event, the settlement of which is expected to result in an outflow of resources of the entity. Thus, financial instruments within the scope of the amendments clearly meet the definition of a liability in the *Framework*.

DO3 These Board members do not agree with the Board that an exception to the *Framework* is justified in this situation. First, the Board has an active project on the *Framework*, which will revisit the definition of a liability. Although these Board members agree that standards projects can precede decisions in the *Framework* project, the discussions to date in the *Framework* project do not make it clear that the Board will modify the existing elements definitions in such a way that these instruments would be equity. Second, the amendments would require disclosure of the expected cash outflow on redemption or repurchase of puttable instruments classified as equity. These disclosures are similar to those for financial liabilities; existing standards do not require similar disclosure for equity instruments. The Board's decision to require these disclosures reveals its implicit view these instruments are, in fact, liabilities. Yet, the *Framework* is clear that disclosure is not a substitute for recognition. Third, these Board members see no cost-benefit or practical reasons for making this exception. The amendments require the same or similar information to be obtained and disclosed as would be the case if these obligations were classified as liabilities. Existing standards offer presentation alternatives for entities that have no equity under the *Framework*'s definitions.

DO4 These Board members also do not agree with the Board that there are benefits to issuing these amendments. First, paragraph BC70 in the Basis for Conclusions states that the amendments will result in more relevant and understandable financial reporting. However, as noted above, these Board members do not believe that presenting as equity items that meet the *Framework*'s definition of a liability results in relevant information. Also as noted above, existing standards offer presentation alternatives that result in understandable financial reporting.

DO5 Second, paragraph BC70 states that the amendments would increase comparability by requiring more consistent classification of financial instruments that are largely equivalent to ordinary shares. These Board members believe that the amendments decrease comparability. These instruments are not comparable to ordinary shares because these instruments oblige the entity to transfer its economic resources; ordinary shares do not. Also, puttable instruments and instruments that entitle the holder to a pro rata share of the net assets of the entity only on liquidation will be classified as equity by some entities and as liabilities by other entities, depending on whether the other criteria specified in the amendments are met. Thus, these amendments account similarly for economically different instruments, which decreases comparability.

DO6 Finally, these Board members do not believe that the amendments are based on a clear principle. Rather, they comprise several paragraphs of detailed rules crafted to achieve a desired accounting result. Although the Board attempted to craft these rules to minimise structuring opportunities, the lack of a clear principle leaves open the possibility that economically similar situations will be accounted for differently and economically different situations will be accounted for similarly. Both of these outcomes also result in lack of comparability.

Appendix A

Amendments to Illustrative Examples on HKAS 32 and HKAS 1 *Puttable Financial Instruments and Obligations Arising on Liquidation* (issued in June 2008) - effective for annual periods beginning on or after 1 January 2009

The following sets out amendments required for this Guidance resulting from amendments to HKAS 32 and HKAS 1 that are not yet effective. Once effective, the amendments set out below will be incorporated into the text of this Guidance and this appendix will be deleted. In the amended paragraphs shown below, new text is underlined and deleted text is struck through.

Paragraphs IE1 and IE33 are amended (new text is underlined).

Accounting for contracts on equity instruments of an entity

IE1 The following examples* illustrate the application of paragraphs 15 – 27 and HKAS 39 to the accounting for contracts on an entity's own equity instruments (other than the financial instruments specified in paragraphs 16A and 16B or paragraphs 16C and 16D).

* In these examples, monetary amounts are denominated in 'currency units' (CU).

Example 8: Entities with some equity

IE33 The following example illustrates a format of a statement of comprehensive income and statement of financial position that may be used by entities whose share capital is not equity as defined in HKAS 32 because the entity has an obligation to repay the share capital on demand but does not have all the features or meet the conditions in paragraphs 16A and 16B or paragraphs 16C and 16D. Other formats are possible.

Appendix B

Amendments resulting from other Illustrative Examples

The following sets out amendments required for this Guidance resulting from other newly issued HKFRSs that are not yet effective. Once effective, the amendments set out below will be incorporated into the text of this Guidance and this appendix will be deleted. In the amended paragraphs shown below, new text is underlined and deleted text is struck through.

HKAS 1 *Presentation of Financial Statements* (issued in December 2007) – effective for annual periods beginning on or after 1 January 2009

In paragraphs IE32 and IE33, 'an income statement and balance sheet format' is amended to 'a format of a statement of comprehensive income and statement of financial position'.

In the statement of financial position following paragraph IE33, '**RESERVES**' is amended to '**OTHER COMPONENTS OF EQUITY**'.

In paragraph IE45, 'income statement' is amended to 'profit or loss'.

Amendments to HKAS 32 and HKAS 1 *Puttable Financial Instruments and Obligations Arising on Liquidation* (issued in June 2008) - effective for annual periods beginning on or after 1 January 2009

Entities shall apply the following amendments when they apply the related amendments to HKAS 32 and HKAS 1.

Paragraph 2(d) is amended (new text is underlined and deleted text is struck through).

Scope

2 **This Standard shall be applied by all entities to all types of financial instruments except:**

(d) **financial instruments issued by the entity that meet the definition of an equity instrument in HKAS 32 (including options and warrants) <u>or that are required to be classified as an equity instrument in accordance with paragraphs 16A and 16B or paragraphs 16C and 16D of HKAS 32</u>. However, the holder of such equity instruments shall apply this Standard to those instruments, unless they meet the exception in (a) above.**

After paragraph 103E, paragraph 103F is added.

Effective date and transition

103F An entity shall apply the amendment in paragraph 2 for annual periods beginning on or after 1 January 2009. If an entity applies *Puttable Financial Instruments and Obligations Arising on Liquidation* (Amendments to HKAS 32 and HKAS 1) issued in June 2008, for an earlier period, the amendment in paragraph 2 shall be applied for that earlier period.

Amendments to HKAS 32 and HKAS 1 *Puttable Financial Instruments and Obligations Arising on Liquidation* (issued in June 2008) - effective for annual periods beginning on or after 1 January 2009

Entities shall apply the following amendments when they apply the related amendments to HKAS 32 and HKAS 1.

Paragraph 3 is amended (new text is underlined).

Scope

3 This HKFRS shall be applied by all entities to all types of financial instruments, except:

(a) …

<u>(f)</u> <u>instruments that are required to be classified as equity instruments in accordance with paragraphs 16A and 16B or paragraphs 16C and 16D of HKAS 32.</u>

After paragraph 44B, paragraph 44C is added.

Effective date and transition

44C An entity shall apply the amendment in paragraph 3 for annual periods beginning on or after 1 January 2009. If an entity applies *Puttable Financial Instruments and Obligations Arising on Liquidation* (Amendments to HKAS 32 and HKAS 1), issued in June 2008, for an earlier period, the amendment in paragraph 3 shall be applied for that earlier period.

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HK(IFRIC) Interpretation 2 Members' Shares in Co-operative Entities and Similar Instruments

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A Examples of application of the conclusions

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B Amendments resulting from other HKFRSs

BASIS FOR CONCLUSIONS ON HK(IFRIC)-Int 2

APPENDIX

Amendments resulting from other Basis for Conclusions

HK(IFRIC) Interpretation 2 *Members' Shares in Co-operative Entities and Similar Instruments* (HK(IFRIC)-Int 2) is set out in paragraphs 1–14 and ~~the~~ Appendi~~x~~ces A and B. HK(IFRIC)-Int 2 is accompanied by a Basis for Conclusions. The scope and authority of Interpretations are set out in the *Preface to Hong Kong Financial Reporting Standards*.

Appendix A

Examples of application of the conclusions

This appendix is an integral part of the Interpretation.

A1 This appendix sets out seven examples of the application of the HK(IFRIC)-Int conclusions. The examples do not constitute an exhaustive list; other fact patterns are possible. Each example assumes that there are no conditions other than those set out in the facts of the example that would require the financial instrument to be classified as a financial liability.

Unconditional right to refuse redemption (paragraph 7)

Example 1

Facts

A2 The entity's charter states that redemptions are made at the sole discretion of the entity. The charter does not provide further elaboration or limitation on that discretion. In its history, the entity has never refused to redeem members' shares, although the governing board has the right to do so.

Classification

A3 The entity has the unconditional right to refuse redemption and the members' shares are equity. HKAS 32 establishes principles for classification that are based on the terms of the financial instrument and notes that a history of, or intention to make, discretionary payments does not trigger liability classification. Paragraph AG26 of HKAS 32 states:

> When preference shares are non-redeemable, the appropriate classification is determined by the other rights that attach to them. Classification is based on an assessment of the substance of the contractual arrangements and the definitions of a financial liability and an equity instrument. When distributions to holders of the preference shares, whether cumulative or non-cumulative, are at the discretion of the issuer, the shares are equity instruments. The classification of a preference share as an equity instrument or a financial liability is not affected by, for example:
>
> (a) a history of making distributions;
>
> (b) an intention to make distributions in the future;
>
> (c) a possible negative impact on the price of ordinary shares of the issuer if distributions are not made (because of restrictions on paying dividends on the ordinary shares if dividends are not paid on the preference shares);
>
> (d) the amount of the issuer's reserves;
>
> (e) an issuer's expectation of a profit or loss for a period; or
>
> (f) an ability or inability of the issuer to influence the amount of its profit or loss for the period.

Example 2

Facts

A4 The entity's charter states that redemptions are made at the sole discretion of the entity. However, the charter further states that approval of a redemption request is automatic unless the entity is unable to make payments without violating local regulations regarding liquidity or reserves.

Appendix B

Amendments resulting from other HKFRSs

The following sets out amendments required for this Interpretation resulting from other newly issued HKFRSs that are not yet effective. Once effective, the amendments set out below will be incorporated into the text of this Interpretation and this appendix will be deleted. In the amended paragraphs shown below, new text is underlined and deleted text is struck through.

Amendments to HKAS 32 and HKAS 1 *Puttable Financial Instruments and Obligations Arising on Liquidation* (issued in June 2008) - effective for annual periods beginning on or after 1 January 2009

Entities shall apply the following amendments when they apply the related amendments to HKAS 32 and HKAS 1.

In the References section, the footnote is amended (new text is underlined).

* HKAS 32 was amended as HKAS 32 *Financial Instruments: Presentation* for annual periods beginning on or after 1 January 2007. In June 2008 the HKICPA amended HKAS 32 by requiring instruments to be classified as equity if those instruments have all the features and meet the conditions in paragraphs 16A and 16B or paragraphs 16C and 16D of HKAS 32.

Paragraphs 6 and 9 are amended (new text is underlined) and paragraph 14A is added.

Conclusions

6 Members' shares that would be classified as equity if the members did not have a right to request redemption are equity if either of the conditions described in paragraphs 7 and 8 is present or the members' shares have all the features and meet the conditions in paragraphs 16A and 16B or paragraphs 16C and 16D of HKAS 32. Demand deposits, including current accounts, deposit accounts and similar contracts that arise when members act as customers are financial liabilities of the entity.

9 An unconditional prohibition may be absolute, in that all redemptions are prohibited. An unconditional prohibition may be partial, in that it prohibits redemption of members' shares if redemption would cause the number of members' shares or amount of paid-in capital from members' shares to fall below a specified level. Members' shares in excess of the prohibition against redemption are liabilities, unless the entity has the unconditional right to refuse redemption as described in paragraph 7 or the members' shares have all the features and meet the conditions in paragraphs 16A and 16B or paragraphs 16C and 16D of HKAS 32. In some cases, the number of shares or the amount of paid-in capital subject to a redemption prohibition may change from time to time. Such a change in the redemption prohibition leads to a transfer between financial liabilities and equity.

Effective date

14A An entity shall apply the amendments in paragraphs 6, 9, A1 and A12 for annual periods beginning on or after 1 January 2009. If an entity applies *Puttable Financial Instruments and Obligations Arising on Liquidation* (Amendments to HKAS 32 and HKAS 1), issued in June 2008, for an earlier period, the amendments in paragraphs 6, 9, A1 and A12 shall be applied for that earlier period.

In Appendix A (Examples of application of the conclusions), paragraphs A1 and A12 are amended (new text is underlined and deleted text is struck through).

Examples of application of the conclusions

A1 This appendix sets out seven examples of the application of the HK(IFRIC)-Int conclusions. The examples do not constitute an exhaustive list; other fact patterns are possible. Each example assumes that there are no conditions other than those set out in the facts of the example that would require the financial instrument to be classified as a financial liability and that the financial instrument does not have all the features or does not meet the conditions in paragraphs 16A and 16B or paragraphs 16C and 16D of HKAS 32.

Example 4

Classification

A12 In this case, CU750,000 would be classified as equity and CU150,000 would be classified as financial liabilities. In addition to the paragraphs already cited, paragraph 18(b) of HKAS 32 states in part:

> …a financial instrument that gives the holder the right to put it back to the issuer for cash or another financial asset (a 'puttable instrument') is a financial liability, except for those instruments classified as equity instruments in accordance with paragraphs 16A and 16B or paragraphs 16C and 16D. ~~This is so~~ The financial instrument is a financial liability even when the amount of cash or other financial assets is determined on the basis of an index or other item that has the potential to increase or decrease~~, or when the legal form of the puttable instrument gives the holder a right to a residual interest in the assets of an issuer~~. The existence of an option for the holder to put the instrument back to the issuer for cash or another financial asset means that the puttable instrument meets the definition of a financial liability, except for those instruments classified as equity instruments in accordance with paragraphs 16A and 16B or paragraphs 16C and 16D.

Appendix

Amendments resulting from other Basis for Conclusions

The following sets out amendments required for this Basis for Conclusions resulting from other newly issued HKFRSs that are not yet effective. Once effective, the amendments set out below will be incorporated into the text of this Basis for Conclusions and this appendix will be deleted. In the amended paragraphs shown below, new text is underlined and deleted text is struck through.

Amendments to HKAS 32 and HKAS 1 *Puttable Financial Instruments and Obligations Arising on Liquidation* (issued in June 2008) - effective for annual periods beginning on or after 1 January 2009

Paragraph BC7 is amended (new text is underlined and deleted text is struck through).

Basis for Conclusions

BC7 In many jurisdictions, local law or regulations state that members' shares are equity of the entity. However, paragraph 17 of IAS 32 states:

> With the exception of the circumstances described in paragraphs 16A and 16B or paragraphs 16C and 16D, ~~A~~a critical feature in differentiating a financial liability from an equity instrument is *the existence of a contractual obligation of one party to the financial instrument (the issuer) either to deliver cash or another financial asset to the other party (the holder)* or to exchange financial assets or financial liabilities with the holder under conditions that are potentially unfavourable to the issuer. Although the holder of an equity instrument may be entitled to receive a pro rata share of any dividends or other distributions of equity, the issuer does not have a contractual obligation to make such distributions because it cannot be required to deliver cash or another financial asset to another party. [Emphasis added]