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Wayne Upton
Chairman
IFRS Interpretations Committee
30 Cannon Street
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Email: ifric@ifrs.org

25 September 2013

Dear Mr Upton

Tentative Agenda Decision - IAS 32 *Financial Instruments: Presentation*: Classification of a financial instrument that is mandatorily convertible into a variable number of shares upon a contingent 'non-viability' event

Deloitte Touche Tohmatsu Limited is pleased to respond to the IFRS Interpretations Committee's publication in the July IFRIC Update of the tentative decision not to take onto the Committee's agenda a request for clarification of the classification as equity or as a liability of a financial instrument that has no stated maturity date, pays interest at the discretion of the issuer and is mandatorily convertible into a variable number of equity shares upon breach of the issuer's Tier 1 Capital ratio ('the contingent non-viability event').

We believe that the tentative agenda decision as currently drafted is not sufficiently clear about the two distinct issues relevant to this instrument (its classification and the measurement of any liability component to be recognised) and does not recognise that for each of these issues more than one valid view exists. Before proceeding, we believe the Committee should consider more explicitly these two questions and the alternative views.

Classification of the instrument

We agree with the statement in the tentative agenda decision that the instrument is a compound instrument due to the discretionary nature of interest payments (which are, as a result, an equity feature) and the contingent mandatory conversion into a variable number of equity shares (which is a liability feature).

We disagree, however, that the only appropriate characterisation of the liability component of the instrument is as a non-derivative liability akin to a demand obligation. We believe that consideration of this liability as a derivative (and, therefore, of the instrument as an embedded derivative with an equity host contract) would also be appropriate as the issuer's obligation to redeem the instrument can be characterised as a derivative that is an exchange of a fixed number of equity host contracts for a variable number of shares that are contingent on a future event. Such an instrument would fail the fixed-for-fixed criteria and therefore would be a financial liability.

Measurement of the financial liability component

On this issue we similarly believe that other valid views exist in addition to the analysis presented in the tentative agenda decision.

If the liability component is considered to be a derivative, then it must be measured at its fair value which will reflect the probability of the contingent feature being exercised in its fair valuation.

If it is considered a non-derivative (as in the tentative agenda decision) we do not consider the standard is clear about how such a non-derivative shall be characterised, specifically whether it is akin to a demand deposit that is not contingent (as in the tentative agenda decision) or a liability with a contingent feature. The characterisation is critical as it determines what the terms are that are subject to fair valuation.

Although we agree that one of the conclusions, as stated in the tentative agenda decision, could be that it is a non-derivative liability that is akin to a demand deposit and therefore fair valued assuming the contingent feature will occur is reasonable, we also believe a contrary view can validly be argued. The alternative view is that the analogy to the measurement of a demand deposit in IAS 39 is not relevant as the holder does not have the right to demand redemption. We believe it can be argued that measuring a demand deposit at the minimum amount that the holder can demand applies only when that amount is capable of being demanded, i.e. it is not contingent other than the passage of time and the holder's right to demand redemption. The financial instrument that the Committee is considering is not capable of being redeemed on demand unless the issuer is regarded as non-viable. Under this view, until the issuer is non-viable, the liability is not akin to a demand deposit and consequently is not fair valued assuming the contingent feature will occur. Its fair valuation would include the probability of the event occurring.

We believe that the Committee's agenda decision should more explicitly acknowledge these two questions and that there is more than one valid view for each.

If you have any questions concerning our comments, please contact Veronica Poole in London at +44 (0)20 7007 0884.

Yours sincerely

Veronica Poole
Global IFRS Leader