COMMENTS ON IASB EXPOSURE DRAFT ON PROPOSED AMENDMENTS TO IAS 32 "CLASSIFICATION OF RIGHTS ISSUES" (ED/2009/9)

Question 1 – Specifying the characteristics of the rights issue

The proposed amendment applies to instruments (rights) to be offered pro rata to all existing owners of the same class of equity instruments and the exercise price to be a fixed amount of cash in any currency.

Do you agree with the proposal to limit the amendment to instruments with these characteristics? If not, why? Are there any other instruments that should be included and why?

Answer 1
I broadly agree with the proposal to limit the amendment to the proposed change.

It is common for international entities to make rights issues to existing shareholders in a currency other than the entities' functional currency. If such rights issues are accounted for as derivative liabilities with changes in fair value recognized in profit and loss, the entities' results will be significantly impacted as a result of the fluctuations in share prices and foreign exchange rates. The classification of such will not truly reflect the substance of the rights issue transaction; on the contrary, it may cause distortion when providing decision-useful information for users of financial statements.

I assume that the proposed amendment will cover those rights issues that are issued under the equality principle, which give holders an equal opportunity to participate. However, I suggest the IASB mention specifically the treatment of non-traditional rights issues, such as accelerated rights issue to institutional investors, long-dated rights issues, and any issues that are not entirely equity in nature.

I agree that foreign currency convertible bonds should be excluded from equity classification. It may be helpful if IASB could explain the reasoning behind, which boils down to the fact that isolating interrelated equity and foreign currency elements in the convertible bonds will be complicated and arbitrary. This is also necessary to comply with IAS 39 Financial Instruments: Recognition and Measurement.

When the proposed amendments in the ED have been implemented, it should be noted that the possible foreign exchange risk arising from foreign currency rights issues will not be reflected in the financial statements, unless proper disclosure is required to be made in the financial statements by the revised standard.

Question 2 – Specifying the currency of the exercise price

The proposed amendment specifies that the fixed amount of cash the entity will receive can be denominated in any currency. If that currency is not the entity's functional or reporting currency, the proceeds it receives from the issue of its shares will vary depending on foreign exchange rates.

Do you agree with the proposal to permit an entity to classify rights with the characteristics set out above as equity instruments even when the exercise price is not fixed in its functional or reporting currency? If not, why?

Answer 2
I agree.

Question 3 – Transition

The proposed change would be required to be applied retrospectively with early adoption permitted. Is the requirement to apply the proposed change retrospectively appropriate? If not, what do you propose and why?

Answer 3
I support the proposed change with retrospective effect is appropriate.

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Note : The above views represent those of Paul Mok only, not of any organisations to which he is related.