



SAS Quadra 05. Bloco J. CFC
Brasília, Distrito Federal – Brazil
www.cpc.org.br

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ifric@ifrs.org

International Accounting Standards Board
IFRS Interpretations Committee
30 Cannon Street
London EC4M 6XH
United Kingdom

RE: Outreach Request: Foreign currency embedded derivatives (IAS 39)

Dear Board Members,

The Comitê de Pronunciamentos Contábeis - CPC (Brazilian Accounting Pronouncements Committee)¹ welcomes the opportunity to respond to the Outreach Request – **Foreign currency embedded derivatives(IAS 39)**.

We are a standard-setting body engaged in the study, development and issuance of accounting standards, interpretations and guidance for Brazilian companies.

Background of the issue

The entity conducts its license agreements (host contract) for international film productions routinely in US-Dollars, and therefore not in its own functional currency (EUR). To ensure an accurate accounting, it is necessary to determine whether these contracts contain an embedded foreign currency derivative in accordance with IAS 39.10, which must be accounted for separately from the license agreement. The obligation to separate the embedded derivative from the license agreement pursuant to IAS 39.11 depends on the criterion 'closely related', which is defined in IAS 39.AG33d. Since criteria IAS 39.AG33d i) and iii) conform only to license agreements with some contractual partners of the entity, criterion IAS 39.AG33d ii) is relevant to determine whether an embedded foreign currency derivative is closely related to the license agreement (host contract). Criterion ii) applies, if - for international film license agreements - the US-Dollars is "the currency in which the price of the related good or service that is acquired or delivered is routinely denominated in commercial transactions around the world."

¹ The Brazilian Accounting Pronouncements Committee (CPC) is a standard-setting body engaged in the study, development and issuance of accounting standards, interpretations and guidances for Brazilian companies. Our members are nominated by the following entities: ABRASCA (Brazilian Listed Companies Association), APIMEC (National Association of Capital Market Investment Professionals and Analysts), BMFBOVESPA (Brazilian Stock Exchange and Mercantile & Future Exchange), CFC (Federal Accounting Council), FIPECAFI (Financial and Accounting Research Institute Foundation) and IBRACON (Brazilian Institute of Independent Auditors).



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International film productions are projects targeted for worldwide exploitation as opposed to local productions aimed at a single country. Due to their high production cost these international projects need to be refinanced by a worldwide release. Traditionally mainly the U.S. major studios {Walt Disney, Paramount, Sony, Twentieth Century Fox, Universal and Warner Bros., hereinafter referred to as majors) produce international films, but some independent producers such as Lionsgate / Summit or The entity are also part of this business. Refinancing of the production budget is either done by a worldwide sale of distribution and exploitation rights to local film distributors of a respective territory, or through the exploitation of the picture by foreign subsidiaries of the majors. Since the headquarters of the market-dominating majors are in the US, budgeting, exploitation and reporting (Box Office) of international film productions are routinely carried out in US- Dollars.

As part of the wholesale market, the entity pre-sells the worldwide distribution and exploitation rights of its international film productions to foreign film distributors in the respective territories ahead of the start of actual production. These license agreements are regularly denominated in US-Dollars.

The incurred production costs must be pre-financed by the entity during the production phase (1 - 1.5 years), because the entity will only receive payment upon delivery of the completed film. Therefore the entity has concluded US-Dollar credit lines which are repaid at the time of the theatrical releases, when the US-Dollar income of the international license agreements is generated.

Our Comments

Although we have no examples of this case in our jurisdiction, as a function of more frequent observance in the United States, we agree that the application of 'closely related' criterion with international film productions would improve financial accounting. The separation of the embedded derivative in foreign currency of the host contract adds volatility to the balance sheet of the company for the production and marketing of the film. At the closing, financial statement analysts perceive a distorted image due to (positive and / or negative) fluctuations in financial results, even if no actual exposure of the exchange rate.

If you have any questions about our comments, please contact us at operacoes@cpc.org.br.

Yours sincerely,

Idésio da Silva Coelho Júnior
Chair of International Affairs
Comitê de Pronunciamentos Contábeis (CPC)