Australian Government
Australian Accounting Standards Board

Memorandum

To:	**AASB Members**	**Date:**	13 May 2014
From:	**Kala Kandiah**	**Agenda Item:**	12.2 (M138)
Subject:	**Narrow Scope Amendments – IFRS 2**	**File:**	

Action

Receive an update on recent tentative decisions made by the IASB on narrow scope amendments to IFRS 2 *Share Based Payments* and decide whether there are any issues that need to be raised with the IASB on those tentative decisions at this stage.

Staff recommendation

Staff do not consider that there are any issues that warrant being raised with the IASB prior to the AASB drafting its submission on the forthcoming IASB ED.

Question to Board members:

Do you agree with staff's recommendation?

Background

1 The IFRS Interpretations Committee (the Interpretations Committee) recommended to the IASB that it should expose together a collection of four proposed amendments to IFRS 2 in an Exposure Draft *("Clarifications of Classification and Measurement of Share-based payment transactions").* These proposed amendments were tentatively approved by the Interpretations Committee at previous meetings.

2 Those four issues are:

(a) Issue 1: Accounting for cash-settled share-based payment transactions that include a performance condition;

(b) Issue 2: Share-based payments in which the manner of settlement is contingent on future events;

(c) Issue 3: Share-based payments settled net of tax withholdings; and

(d) Issue 4: Modification of a share-based payment transaction from cash-settled to equity-settled.

Issue 1: Accounting for cash-settled share-based payment transactions that include a performance condition

3 In September 2013, the Interpretations Committee discussed a request to clarify the accounting for cash-settled share based payment (SBP) transactions that include a performance condition under IFRS 2 *Share-based Payment*. The submitter noted that IFRS 2 does not specifically address the impact of vesting conditions (including the effect of a performance condition) within the context of cash-settled SBP transactions and asked the Interpretations Committee to clarify the accounting for cash-settled awards that include a performance condition, because the guidance in IFRS 2 is leading to divergent interpretations.

4 The Interpretations Committee tentatively decided that the guidance in IFRS 2 for the measurement of equity-settled awards that include a performance condition should be applied by analogy to account for cash-settled SBP transactions that include a performance condition.

5 The Interpretation Committee's decision above was based on the view that:

(a) the 'fair value' of share-based payment transactions should be measured in accordance with the specific guidance in IFRS 2 for measuring the impact of vesting and non-vesting conditions and not in accordance with IFRS 13 (on the basis of paragraph 6A of IFRS 2[1]); and

(b) the accounting for a cash-settled award that includes a service condition in Example 12 of the Implementation Guidance in IFRS 2 is consistent with the accounting for the effect of a vesting condition (other than a market condition) in an equity-settled award and is not consistent with the remeasurement for all the uncertainties at each reporting date.

6 At its February 2014 meeting, the IASB discussed the recommendations of the Interpretations Committee and decided that accounting for the effects of vesting conditions on a cash-settled share-based payment should follow the approach used for equity-settled share-based payments. Consequently the IASB decided to add:

(a) further guidance to IFRS 2 on accounting for a cash-settled share-based payment transaction that includes a performance condition. This guidance will describe how a vesting or a non-vesting condition should be reflected in the measurement of cash-settled share-based payments; and

(b) an example in the Implementation Guidance of IFRS 2 to illustrate the effect of a performance condition on the measurement of a cash-settled share-based payment transaction.

AASB Staff view on Issue 1

7 AASB staff agree with the Interpretation Committee's views as outlined in paragraph 5 above as it is consistent with the measurement of equity settled share based payments.

---

[1] Paragraph 6A in IFRS 2 states that "this IFRS uses the term 'fair value' in a way that differs in some respects from the definition of fair value in IFRS 13 Fair Value Measurement. Therefore, when applying IFRS 2 an entity measures fair value in accordance with this IFRS, not IFRS 13".

AASB staff consider that the IASB's proposed amendment to IFRS 2 on Issue 1 is needed to (i) clarify the accounting for cash-settled share-based payment transactions that include a performance condition and (ii) alleviate diversity in practice.

Issue 2: Share based payments in which the manner of settlement is contingent on future events

8 The Interpretations Committee received a request to clarify the classification of share-based payment transactions in which the manner of settlement is contingent on a future event that is outside the control of both the entity and the counterparty.

9 The Interpretations Committee considered an equity-settled share-based payment arrangement that has a contingent cash settlement provision in which the granted equity instruments will vest immediately and be settled in cash at the fair value of the equity instruments at the date of settlement, if a specified event that is outside the control of both the entity and the employees occurs. Examples of such contingent events include (i) a successful IPO and (ii) death or disability of the employee.

10 The Interpretations Committee learnt that there is significant diversity in practice on this issue. This is primarily because IFRS 2 does not provide specific guidance on the classification of this type of share-based payment. Hence, the Interpretations Committee recommended to the IASB that it should clarify in a narrow-scope amendment project the classification of a share-based payment with a contingent settlement feature.

11 The Interpretations Committee recommended clarifying that:

(a) the share-based payment should be classified as either cash-settled or equity-settled in its entirety depending on which outcome is **probable** (the probable approach); and

(b) a change in classification of the share-based payment arising from a change in the most likely settlement method should be accounted for by recording a cumulative adjustment at the point in time that the change in classification occurs, in such a way that the cumulative cost will be the same as if the change in classification had occurred at the inception of the arrangement.

12 The IASB discussed the above approach at its April 2014 meeting. Some IASB members were concerned that the proposed amendment would introduce a principle for distinguishing between a liability and equity that would be inconsistent with the requirements in IAS 32. They also note that the definition of a liability is being discussed in the Conceptual Framework project. Accordingly, the IASB decided **not** to propose an amendment to IFRS 2 for this issue.

AASB staff view on Issue 2

13 AASB staff consider that introducing a principle now in IFRS 2 to distinguish between cash-settled and equity-settled share based payment would not be appropriate, given that the overall definition of a liability is being discussed in the Conceptual Framework project. AASB staff agree with the IASB not to propose an amendment for Issue 2 at this stage.

Issue 3: Share-based payments settled net of tax withholdings

14 The Interpretations Committee received a request to clarify the classification of a share-based payment transaction in which the entity withholds a specified portion of the shares

that would otherwise be issued to the counterparty upon exercise (or vesting) of the share-based payment. Instead of delivering all of the shares due under the terms of the share-based payment, the entity withholds a portion and makes a payment to the tax authorities in respect of the counterparty's tax due in relation to the share-based payment.

15 The Interpretations Committee decided to recommend to the IASB that, to mitigate diversity in practice on this issue, it should amend IFRS 2 in a narrow-scope amendment by adding specific guidance. The guidance would be to clarify that a share-based payment in which the entity settles the share-based payment net by withholding a specified portion of the equity instruments to meet its minimum statutory tax withholding requirements would be classified as equity-settled in its entirety, if the entire share-based payment would otherwise be classified as equity-settled without the net settlement feature. This amendment would result in more converged guidance with US GAAP.

16 At its February 2014 meeting, the IASB agreed with the Interpretations Committee's recommendation to propose amendments to IFRS 2, subject to revisions to the wording proposed by the staff.

AASB staff view on Issue 3

17 AASB staff agree with the proposed amendments to IFRS 2 on Issue 3 as AASB staff consider that the economic substance of the share-based payment transaction in Issue 3 is that the entity settled the share based payment entirely in equity instruments and separately, yet simultaneously, repurchased a portion of those equity instruments to settle the tax obligations of the counterparty, to which paragraph 29[2] of IFRS 2 applies

Issue 4: Modification of a share-based payment transaction from cash-settled to equity-settled

18 The Interpretations Committee received a request to clarify the accounting for a modification to the terms and conditions of a cash-settled share-based payment that involves a change in the classification from cash-settled to equity-settled. The request received sought clarification of the accounting for a share-based payment arrangement with employees in situations in which:

(a) a cash-settled award is cancelled and is replaced by a new equity-settled award; and

(b) the replacement award has a higher fair value than the original award as at the replacement date.

19 The Interpretations Committee recommended that the IASB should specify the accounting for the change in classification from cash-settled to equity-settled that arises from the replacement because at present IFRS 2 does not provide specific guidance. The Interpretations Committee recommended that this change be made in a narrow-scope amendment project.

20 The Interpretations Committee recommended to the IASB that it should amend IFRS 2 to clarify that:

---

[2] Paragraph 29 of IFRS 2 states that "If an entity repurchases vested equity instruments, the payment made to the employee shall be accounted for as a deduction from equity, except to the extent that the payment exceeds the fair value of the equity instruments repurchased, measured at the repurchase date. Any such excess shall be recognised as an expense".

(a) the cancellation of a share-based payment followed by a replacement equity-settled share-based payment should be accounted for consistently with a change in the classification that arises from a modification to the terms and conditions of the share-based payment. This is consistent with the requirements in paragraph 28(c) of IFRS 2, which require replacement of an equity-settled share-based payment to be accounted for in the same manner as a modification to the original grant of equity instruments;

(b) the share-based payment should be accounted for as an equity-settled share-based payment after the modification date;

(c) the replacement equity-settled share-based payment should be measured by reference to the modification-date fair value of the equity-settled share-based payment, because the modification-date should be viewed as the grant date of the replacement equity-settled share-based payment in accordance with the definition of 'grant date' in IFRS 2;

(d) the liability recorded in respect of the original cash-settled share-based payment should be derecognised upon the modification and the equity-settled share-based payment should be recognised to the extent that service has been rendered up to the modification date; and

(e) the difference between the carrying amount of the liability as at the modification date and the amount recognised in equity as at the same date should be recorded in profit or loss immediately. This reflects the remeasurement of the liability to the settlement amount in accordance with paragraph 30 of IFRS 2.

21 The IASB discussed the approach recommended by the Interpretations Committee and decided to add guidance to IFRS 2 in line with the Interpretation Committee's recommendation in 16(c)-16(e) above.

AASB staff views on Issue 4

22 AASB staff agree with the proposed amendment to IFRS 2 on Issue 4 as AASB staff consider that the modification of a cash settled award to an equity settled award should be treated in a manner consistent with the modification of a equity settled award, as outlined in paragraph 28(c)[3] of IFRS 2. AASB staff also consider, consistent with the views of the IASB staff, that the compensation expense in respect of the new equity-settled award should be measured at the modification date fair value of the equity instruments. This is because there would have been a shared understanding at the original grant date that the entity would pay cash for services to be rendered by the employees.

Transition requirements for the narrow-scope amendments to IFRS 2

23 The IASB tentatively decided that the proposed amendments to IFRS 2 should be applied on a prospective basis. Notwithstanding that decision, the IASB tentatively decided that an

---

[3] Paragraph 28(c) of IFRS 2 states that "if new equity instruments are granted to the employee and, on the date when those new equity instruments are granted, the entity identifies the new equity instruments granted as replacement equity instruments for the cancelled equity instruments, the entity shall account for the granting of replacement equity instruments in the same way as a modification of the original grant of equity instruments….".

entity should be permitted to apply retrospectively all the amendments that are applicable to it if the entity has the information necessary to do so.

AASB staff views on the transition requirements

24 AASB staff agree with the proposed transition requirements, when considering the proposed amendments collectively. This makes the transition requirements straight-forward and also enables an entity to apply the amendments applicable to it retrospectively if the entity has information necessary to do so.