

AASB Exposure Draft

ED 257
November 2014

Classification and Measurement of Share-based Payment Transactions

(Proposed amendments to AASB 2)

Comments to the AASB by 25 February 2015



Australian Government

**Australian Accounting
Standards Board**

Commenting on this AASB Exposure Draft

Constituents are strongly encouraged to respond to the AASB and the IASB. The AASB is seeking comment by 25 February 2015. This will enable the AASB to consider Australian constituents' comments in the process of formulating its own comments to the IASB, which are due by 25 March 2015. Comments should be addressed to:

The Chair
Australian Accounting Standards Board
PO Box 204
Collins Street West Victoria 8007
AUSTRALIA
E-mail: standard@asb.gov.au

Respondents to the IASB are asked to send their comments electronically to the IFRS Foundation website (www.ifrs.org), using the 'Comment on a proposal' page.

All submissions will be placed on the public record unless the Chair of the AASB agrees to submissions being treated as confidential. The latter will occur only if the public interest warrants such treatment.

While comments may be lodged by email or by post, email lodgement is preferred. To enable the submissions to be accessible to all users of the website, including those with disabilities, please submit comments via email in an accessible Word format. An additional accessible and unsecured PDF version may also be submitted.

Enquiries

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AASB REQUEST FOR COMMENTS

The proposed amendments to IFRS 2 *Share-based payment* (incorporated into AASB 2 of the same name):

- (a) clarify that accounting for the effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payment should follow the approach used for measuring equity-settled share-based in paragraphs 19-21A of IFRS 2;
- (b) specify that if an entity settles a share-based payment arrangement net by withholding a specified portion of the equity instruments to meet the statutory tax withholding obligation, then the transaction should be classified as equity-settled in its entirety, if the entire share-based payment would otherwise be classified as equity-settled if it had not included the net settlement feature; and
- (c) specify the accounting for modifications to the terms and conditions of a cash-settled share-based payment transaction that results in a change in its classification from cash-settled to equity-settled, so that:
 - (i) the share-based payment transaction is measured by reference to the modification-date fair value of the equity instruments granted as a result of the modification;
 - (ii) the liability recognised in respect of the original cash-settled share-based payment is de-recognised upon the modification, and the equity-settled share-based payment is recognised to the extent that services have been rendered up to the modification date; and
 - (iii) the difference between the carrying amount of the liability as at the modification date and the amount recognised in equity at the same date is recorded in profit and loss immediately.

In light of the Australian Accounting Standards Board's (AASB's) policy of incorporating International Financial Reporting Standards (IFRSs) into Australian Accounting Standards, the AASB is inviting comments on:

- (a) any of the proposals in the attached International Accounting Standards Board (IASB) Exposure Draft, including the specific questions on the proposals as listed in the Invitation to Comment section of the attached IASB Exposure Draft; and
- (b) the 'AASB Specific Matters for Comment' listed below.

Submissions play an important role in the decisions that the AASB will make in regard to a Standard. The AASB would prefer that respondents supplement their opinions with detailed comments, whether supportive or otherwise, on the major issues. The AASB regards supportive and non-supportive comments as essential to a balanced review and will consider all submissions, whether they address some or all specific matters, additional issues or only one issue.

Due Date for Comments to the AASB

Comments should be submitted to the AASB by 25 February 2015. This will enable the AASB to consider those comments in the process of formulating its own comments to the IASB. Constituents are also strongly encouraged to send their response to the IASB.

Reduced Disclosure Requirements

AASB 1053 *Application of Tiers of Australian Accounting Standards* establishes a differential reporting framework consisting of two tiers of reporting requirements for preparing general purpose financial statements:

- (a) Tier 1: Australian Accounting Standards; and
- (b) Tier 2: Australian Accounting Standards – Reduced Disclosure Requirements.

Tier 2 comprises the recognition and measurement requirements of Tier 1 and substantially reduced disclosures corresponding to those requirements.

The proposals in this Exposure Draft would not make amendments to any disclosure requirements. Accordingly, this Exposure Draft does not give rise to any particular implications for Tier 2 disclosures.

AASB Specific Matters for Comment

The AASB would particularly value comments on the following:

1. whether there are any regulatory issues or other issues arising in the Australian environment that may affect the implementation of the proposals, particularly any issues relating to:
 - (a) not-for-profit entities; and
 - (b) public sector entities;
2. whether, overall, the proposals would result in financial statements that would be useful to users;
3. whether the proposals are in the best interests of the Australian economy; and
4. unless already provided in response to specific matters for comment 1 – 3 above, the costs and benefits of the proposals relative to the current requirements, whether quantitative (financial or non-financial) or qualitative. In relation to quantitative financial costs, the AASB is particularly seeking to know the nature(s) and estimated amount(s) of any expected incremental costs, or cost savings, of the proposals relative to the existing requirements.

November 2014

Exposure Draft ED/2014/5

Classification and Measurement of Share-based Payment Transactions

Proposed amendments to IFRS 2

Comments to be received by 25 March 2015

IASB[®]

 IFRS[®]

Classification and Measurement of Share-based Payment Transactions

(Proposed amendments to IFRS 2)

Comments to be received by 25 March 2015

Exposure Draft ED/2014/5 *Classification and Measurement of Share-based Payment Transactions* (Proposed amendments to IFRS 2) is published by the International Accounting Standards Board (IASB) for comment only. The proposals may be modified in the light of the comments received before being issued in final form. Comments need to be received by **25 March 2015** and should be submitted in writing to the address below or electronically using our 'Comment on a proposal' page.

All comments will be on the public record and posted on our website unless the respondent requests confidentiality. Such requests will not normally be granted unless supported by good reason, for example, commercial confidence. Please see our website for details on this and how we use your personal data.

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Introduction

The International Accounting Standards Board (IASB) has published this Exposure Draft of proposed amendments to IFRS 2 *Share-based Payment* to address:

- (a) the effects of vesting conditions on the measurement of a cash-settled share-based payment;
- (b) the classification of share-based payment transactions with net settlement features; and
- (c) the accounting for a modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled.

Effects of vesting conditions on the measurement of a cash-settled share-based payment

Paragraph 33 of IFRS 2 requires an entity to measure the liability for a cash-settled share-based payment initially and at the end of each reporting period until settled, at the fair value of the cash-settled share-based payment, taking into account the terms and conditions on which the cash-settled share-based payment was granted and the extent to which the employees have rendered service to date. However, IFRS 2 does not specifically address the impact of vesting and non-vesting conditions on the measurement of the fair value of the liability incurred in a cash-settled share-based payment transaction.

The IASB proposes to clarify that accounting for the effects of vesting and non-vesting conditions on the measurement of a cash-settled share-based payment should follow the approach used for measuring equity-settled share-based payments in paragraphs 19–21A of IFRS 2.

Classification of share-based payment transactions with net settlement features

An entity may be obliged by tax laws or regulations to withhold an amount for an employee's tax obligation associated with share-based payments and transfer the amount, normally in cash, to the taxation authorities. To fulfil this obligation, the terms of some employee share-based payment arrangements permit or require the entity to deduct from the total number of equity instruments that would otherwise be issued to the employee upon exercise (or vesting) of the share-based payment, the number of equity instruments needed to equal the monetary value of the employee's tax obligation in order to meet the statutory tax withholding obligation.

The amendments propose an exception to the requirements in IFRS 2. The IASB proposes to specify that if the entity settles the share-based payment arrangement net by withholding a specified portion of the equity instruments to meet the statutory tax withholding obligation, then the transaction should be classified as equity-settled in its entirety, if the entire share-based payment would otherwise be classified as equity-settled if it had not included the net settlement feature.

Accounting for a modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled

A cash-settled share-based payment may change to an equity-settled share-based payment because of modifications to the terms and conditions of the arrangement. In addition, there are transactions in which a cash-settled share-based payment is settled and replaced by a new equity-settled share-based payment. IFRS 2 does not specifically address such situations.

The IASB proposes to amend IFRS 2 so that:

- (a) the share-based payment transaction is measured by reference to the modification-date fair value of the equity instruments granted as a result of the modification;
- (b) the liability recognised in respect of the original cash-settled share-based payment is derecognised upon the modification, and the equity-settled share-based payment is recognised to the extent that the services have been rendered up to the modification date; and
- (c) the difference between the carrying amount of the liability as at the modification date and the amount recognised in equity at the same date is recorded in profit or loss immediately.

Invitation to comment

The IASB invites comments on the proposals in this Exposure Draft, particularly on the questions set out below. Comments are most helpful if they:

- (a) comment on the questions as stated;
- (b) indicate the specific paragraph or group of paragraphs to which they relate;
- (c) contain a clear rationale; and
- (d) include any alternative that the IASB should consider, if applicable.

The IASB is not requesting comments on matters in IFRS 2 that are not addressed in this Exposure Draft.

Comments should be submitted in writing so as to be received no later than 25 March 2015.

Questions for respondents

Question 1
<p>The IASB proposes to clarify that accounting for the effects of vesting and non-vesting conditions on the measurement of a cash-settled share-based payment should follow the approach used for measuring equity-settled share-based payments in paragraphs 19–21A of IFRS 2.</p> <p>Do you agree? Why or why not?</p>

Question 2

The IASB proposes to specify that a share-based payment transaction in which the entity settles the share-based payment arrangement net by withholding a specified portion of the equity instruments to meet the statutory tax withholding obligation should be classified as equity-settled in its entirety. This is required if the entire share-based payment transaction would otherwise have been classified as an equity-settled share-based payment transaction if it had not included the net settlement feature.

Do you agree? Why or why not?

Question 3

The IASB proposes to specify the accounting for modifications to the terms and conditions of a cash-settled share-based payment transaction that results in a change in its classification from cash-settled to equity-settled. The IASB proposes that these transactions should be accounted for in the following manner:

- (a) the share-based payment transaction is measured by reference to the modification-date fair value of the equity instruments granted as a result of the modification;
- (b) the liability recognised in respect of the original cash-settled share-based payment is derecognised upon the modification, and the equity-settled share-based payment is recognised to the extent that the services have been rendered up to the modification date; and
- (c) the difference between the carrying amount of the liability as at the modification date and the amount recognised in equity at the same date is recorded in profit or loss immediately.

Do you agree? Why or why not?

Question 4

The IASB proposes prospective application of these amendments, but also proposes to permit the entity to apply the amendments retrospectively if it has the information needed to do so and this information is available without the use of hindsight.

Do you agree? Why or why not?

Question 5

Do you have any other comments on the proposals?

How to comment

Comments should be submitted using one of the following methods.

Electronically Visit the 'Comment on a proposal page', which can be found at:
(our preferred method) go.ifrs.org/comment

Email Email comments can be sent to: commentletters@ifrs.org

Postal IFRS Foundation
30 Cannon Street
London EC4M 6XH
United Kingdom

All comments will be on the public record and posted on our website unless confidentiality is requested. Such requests will not normally be granted unless supported by good reason, for example, commercial confidence. Please see our website for details on this and how we use your personal data.

Proposed amendments to IFRS 2 *Share-based Payment*

Paragraphs 30 and 33 are amended and paragraphs 33A–33D and 63D are added. Headings before paragraphs 33 and 33D are added. New text is underlined. Paragraph 32 has not been amended but is included for ease of reference.

Cash-settled share-based payment transactions

30 For cash-settled share-based payment transactions, the entity shall measure the goods or services acquired and the liability incurred at the fair value of the liability (subject to the requirements of paragraphs 32–33C). Until the liability is settled, the entity shall remeasure the fair value of the liability at the end of each reporting period and at the date of settlement, with any changes in fair value recognised in profit or loss for the period.

...

32 The entity shall recognise the services received, and a liability to pay for those services, as the employees render service. For example, some share appreciation rights vest immediately, and the employees are therefore not required to complete a specified period of service to become entitled to the cash payment. In the absence of evidence to the contrary, the entity shall presume that the services rendered by the employees in exchange for the share appreciation rights have been received. Thus, the entity shall recognise immediately the services received and a liability to pay for them. If the share appreciation rights do not vest until the employees have completed a specified period of service, the entity shall recognise the services received, and a liability to pay for them, as the employees render service during that period.

Effects of vesting conditions on the measurement of a cash-settled share-based payment

33 The liability shall be measured, initially and at the end of each reporting period until settled, at the fair value of the share appreciation rights, by applying an option pricing model, taking into account the terms and conditions on which the share appreciation rights were granted, and the extent to which the employees have rendered service to date. Vesting conditions, other than market conditions, shall not be taken into account when estimating the fair value of the cash-settled share-based payment at the measurement date. Instead, vesting conditions shall be taken into account by adjusting the number of awards included in the measurement of the transaction amount so that, ultimately, the amount recognised for goods and services received as consideration for the awards granted shall be based on the number of awards that eventually vest and are settled.

33A To apply the requirements in paragraph 33, the entity shall recognise an amount for the goods or services received during the vesting period. That amount shall be based on the best available estimate of the number of awards

that are expected to vest. It shall revise that estimate, if necessary, if subsequent information indicates that the number of awards that are expected to vest differs from previous estimates. On the vesting date, the entity shall revise the estimate to equal the number of awards that ultimately vested.

33B Market conditions, such as a target share price upon which vesting (or exercisability) is conditioned, as well as non-vesting conditions, shall be taken into account when estimating the fair value of the cash-settled share-based payment granted and when remeasuring the fair value of the awards at the end of each reporting period and at the date of settlement.

33C As a result of applying paragraphs 30–33B, the cumulative amount ultimately recognised for goods or services received as consideration for the cash-settled share-based payment is equal to the cash paid.

Classification of share-based payment transactions with net settlement features

33D An entity may be obliged by tax laws or regulations to withhold an amount for an employee’s tax obligation associated with share based payments and transfer the amount, normally in cash, to the taxation authorities. To fulfil this obligation the terms of some employee share-based payment arrangements permit or require the entity to deduct from the total number of equity instruments, which would otherwise be issued to the employee upon exercise (or vesting) of the share-based payment, the number of equity instruments needed to equal the monetary value of the statutory tax withholding obligation. In such cases, if, in the absence of such a net settlement feature, the entire share-based payment transaction would have been classified as an equity-settled share-based payment, the share-based payment shall be accounted for in accordance with the requirements that apply to equity-settled share-based payment transactions in paragraphs 10–29.

...

Effective date

...

63D [Draft] *Classification and Measurement of Share-based Payment Transactions* (Amendments to IFRS 2), issued in [date to be inserted after exposure], amended paragraphs 30 and 33 and added paragraphs 33A–33D and B41A–B41B and their related headings. An entity shall apply those amendments prospectively for annual periods beginning on or after [date to be inserted after exposure]. However, an entity may instead apply the amendments retrospectively in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provided that the entity has the information necessary to do so and this information is available without the use of hindsight. Earlier application is permitted. If an entity applies the amendments for an earlier period it shall disclose that fact.

In Appendix B, paragraphs B41A–B41B and their related heading are added. New text is underlined.

Accounting for a modification to the terms and conditions of a share-based payment transaction that changes the classification of the transaction from cash-settled to equity-settled

- B41A** If the terms and conditions of a cash-settled share-based payment transaction are modified in such a way that it becomes an equity-settled share-based payment transaction, the transaction is accounted for as an equity-settled share-based payment transaction from the date of the modification. The equity-settled share-based payment transaction is measured at the fair value of the equity instruments granted as of the modification date. The portion of the equity-settled share-based payment transaction for which goods or services have been received is recognised as an increase in equity. The liability for the cash-settled share-based payment transaction is derecognised and any difference between the amount of the liability derecognised and the amount of equity recorded is recognised immediately in profit or loss.
- B41B** A cash-settled share-based payment may be cancelled or settled (other than a grant that is cancelled by forfeiture when the vesting conditions are not satisfied). If equity instruments are granted and, on the date when those equity instruments are granted, the entity identifies them as replacement equity instruments for the cancelled cash-settled share-based payment, the entity shall account for the granting of the replacement equity instruments in accordance with the guidance in paragraph B41A.

Proposed amendments to the Guidance on implementing IFRS 2 *Share-based Payment*

Paragraph IG19 is amended and IG Example 12A is added. Deleted text is struck through and new text is underlined.

Cash-settled share-based payment transactions

...

IG19 For example, an entity might grant share appreciation rights to employees as part of their remuneration package, whereby the employees will become entitled to a future cash payment (rather than an equity instrument), based on the increase in the entity's share price from a specified level over a specified period of time. If the share appreciation rights do not vest until the employees have completed a specified period of service, the entity recognises the services received, and a liability to pay for them, as the employees render service during that period. The liability is measured, initially and at the end of each reporting period until settled, at the fair value of the share appreciation rights, on the basis of paragraphs 33–33C of IFRS 2, by applying an option pricing model, and the extent to which the employees have rendered service to date. Changes in fair value are recognised in profit or loss. Therefore, if the amount recognised for the services received was included in the carrying amount of an asset recognised in the entity's statement of financial position (eg inventory), the carrying amount of that asset is not adjusted for the effects of the liability remeasurement. Example 12 illustrates these requirements: when a cash-settled share-based payment transaction is subject to the completion of a service condition. Example 12A illustrates these requirements when a cash-settled share-based payment transaction is subject to the attainment of a non-market performance condition.

IG Example 12

...

IG Example 12A

Background

An entity grants 100 cash-settled share appreciation rights (SARs) to each of its 500 employees on the condition that the employees remain in its employment for the next three years and the entity reaches a revenue target (CU1 billion in sales) by the end of Year 3.

For simplicity, it is assumed that no employees are expected to leave and that none of the employee compensation is capitalised as part of the cost of an asset.

continued...

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IG Example 12A		
<p>During Year 1, the entity estimates a 40 per cent probability that the revenue target will be attained at the end of Year 3. During Year 2, the entity estimates a 70 per cent probability that the revenue target will be attained at the end of Year 3. At the end of Year 3, the revenue target was attained and 150 employees exercise their SARs, another 150 employees exercise their SARs at the end of Year 4 and the remaining 200 employees exercise their SARs at the end of Year 5.</p> <p>Using an option pricing model, the entity estimates the fair value of the SARs, ignoring the revenue target performance condition, at the end of each year until the cash-settled share-based payments are settled. At the end of Year 3, all SARs held by the employees vest. The intrinsic values of the SARs at the date of exercise (which equals the cash paid out) at the end of Years 3-5 are also shown in the following table.</p>		
<u>Year</u>	<u>Fair value of one SAR</u>	<u>Intrinsic value of one SAR</u>
1	CU14.40	=
2	CU15.50	=
3	CU18.20	CU15.00
4	CU21.40	CU20.00
5	=	CU25.00
<u>Application of requirements</u>	<u>Number of employees expected to satisfy the service condition</u>	<u>Best estimate of whether the profit target will be met</u>
Year 1	500	No
Year 2	500	Yes
Year 3	500	Yes

continued...

...continued

IG Example 12A			
<u>Year</u>	<u>Calculation</u>	<u>Expense</u> <u>CU</u>	<u>Liability</u> <u>CU</u>
1	<u>Vesting is not probable: no expense is recognised</u>	=	=
2	<u>Vesting is probable: 500 employees x 100 SARs x CU15.50 x $\frac{2}{3}$</u>	=	<u>516.667</u>
3	<u>Vesting is probable: (500 – 150) employees x 100 SARs x CU18.20 – CU516.667</u>	<u>120.333</u>	=
	<u>+ 150 employees x 100 SARs x CU15.00</u>	<u>225.000</u>	=
	<u>Total</u>	=	<u>345.333</u>
4	<u>(350 – 150) employees x 100 SARs x CU21.40 – CU637.000</u>	<u>(209.000)</u>	=
	<u>+ 150 employees x 100 SARs x CU20.00</u>	<u>300.000</u>	=
	<u>Total</u>	=	<u>91.000</u>
5	<u>CU0 – CU428.000</u>	<u>(428.000)</u>	=
	<u>+ 200 employees x 100 SARs x CU25.00</u>	<u>500.000</u>	=
	<u>Total</u>	=	<u>72.000</u>
	<u>Total</u>	=	<u>1,025,000</u>

Approval by the Board of *Classification and Measurement of Share-based Payment Transactions* (Proposed amendments to IFRS 2) published in November 2014

The Exposure Draft *Classification and Measurement of Share-based Payment Transactions* was approved for publication by the fourteen members of the International Accounting Standards Board.

Hans Hoogervorst	Chairman
Ian Mackintosh	Vice-Chairman
Stephen Cooper	
Philippe Danjou	
Amaro Luiz De Oliveira Gomes	
Martin Edelmann	
Patrick Finnegan	
Gary Kabureck	
Suzanne Lloyd	
Takatsugu Ochi	
Darrel Scott	
Chungwoo Suh	
Mary Tokar	
Wei-Guo Zhang	

Basis for Conclusions on the proposed amendments to IFRS 2 *Share-based Payment*

This Basis for Conclusions accompanies, but is not part of, the proposed amendments.

Effects of vesting conditions on the measurement of a cash-settled share-based payment

- BC1 The International Accounting Standards Board (IASB) received a request regarding the accounting under IFRS 2 *Share-based Payment* for cash-settled share based payment transactions that include a performance condition.
- BC2 The IASB noted that IFRS 2 requires the use of fair value as a principle in measuring share-based payment transactions. The IASB observed that paragraphs 19–21A of IFRS 2 provide guidance on the measurement of the fair value of equity-settled share-based payment transactions that include vesting and non-vesting conditions. The IASB also observed that in the case of cash-settled share-based payment transactions, paragraph 33 of IFRS 2 requires an entity to measure the liability, initially and at the end of each reporting period until settled, at the fair value of the cash-settled share-based payments. The entity is required to apply an option pricing model, taking into account the terms and conditions on which the cash-settled share-based payments were granted and the extent to which the employees have rendered service to date.
- BC3 However, IFRS 2 does not specifically address the impact of vesting and non-vesting conditions on the measurement of the fair value of the liability incurred in a cash-settled share-based payment transaction and it was unclear whether:
- (a) by analogy to the guidance for the measurement of equity-settled share-based payment transactions that include vesting conditions, only market and non-vesting conditions should be taken into account in measuring the fair value of the cash-settled liability; or
 - (b) all conditions, including service and non-market performance conditions, should be taken into account in measuring that fair value.
- BC4 The IASB observed that the guidance in paragraph 6A of IFRS 2, which requires an entity to follow the notion of ‘fair value’ in IFRS 2, requires the same notion of fair value for cash-settled and equity-settled awards. Consequently, the IASB proposes to include guidance on the impact of vesting and non-vesting conditions on the measurement of a cash-settled share-based payment transaction, based on the analogy of the accounting treatment for an equity-settled share-based payment transaction. The IASB further observed that measuring the fair value of the liability incurred in a cash-settled share-based payment transaction by analogy to the guidance for equity-settled share-based payment transactions would be easier to apply in practice. The IASB also referred to some explanations in the Basis for Conclusions on IFRS 2, which explain why a distinction has been drawn in the accounting for different types of conditions affecting equity-settled awards; in this respect it referred to paragraph BC184 of IFRS 2 and noted that the same considerations applied.

- BC5 The IASB proposes to amend paragraphs 30 and 33 of IFRS 2 and add paragraphs 33A–33C to clarify the effect that vesting and/or non-vesting conditions have on the measurement of the liability. The IASB proposes that non-market vesting conditions shall not be taken into account when estimating the fair value of the cash-settled share-based payment and, instead, shall be taken into account by adjusting the number of awards expected to vest.
- BC6 The IASB further observed that a failure to satisfy any condition should trigger a remeasurement of the liability to zero through profit or loss. Consequently, the cumulative expense recognised for the cash-settled liability should be reversed for the failure to satisfy any condition.
- BC7 The IASB also proposes to amend paragraph IG19 and add IG Example 12A to the Guidance on implementing IFRS 2 to illustrate the impact of a performance condition on the measurement of a cash-settled share-based payment transaction.

Classification of share-based payment transactions with net settlement features

- BC8 Some jurisdictions have tax laws or regulations that oblige an entity to withhold an amount for an employee's tax obligation associated with share-based payments and to transfer the amount, normally in cash, to the taxation authority. The tax withholding scheme in respect of share-based payments varies from arrangement to arrangement. However one of the common features of schemes is a net settlement feature, which permits or requires the entity to deduct from the total number of equity instruments that would otherwise be delivered to the employee the number of equity instruments needed to equal the monetary value of the statutory tax withholding obligation incurred as a result of the share-based payment transaction. The entity pays the amount withheld to taxation authorities from its own cash or other assets.
- BC9 The IFRS Interpretations Committee (the 'Interpretations Committee') received a request to address the classification of an equity-settled share-based payment transaction with such a net settlement provision. The request received by the Interpretations Committee asked whether the portion of the share-based payment that is withheld should be classified as cash-settled or equity-settled, if the entire share-based payment would otherwise have been classified as an equity-settled share-based payment transaction in the absence of the net settlement feature.
- BC10 The IASB was informed that there were divergent views on this issue:
- (a) View 1—each component of the share-based payment is accounted for in a manner that is consistent with the manner of settlement. The portion withheld by the entity for which the entity has incurred a liability to pay cash should be accounted for separately and be classified as a cash-settled share-based payment transaction in accordance with the manner of settlement. The portion of the share-based payment that the entity settles by the issue of equity instruments is accounted for as an equity-settled share-based payment.

- (b) View 2—the entire share-based payment transaction should be classified as an equity-settled share-based payment transaction, because the net settlement should be viewed as a repurchase of a portion of the equity instruments issued to the employee (see paragraph 29 of IFRS 2).
- BC11 View 1 is based on the view that the entity is fulfilling part of its obligation to settle the share-based payment for the services received from the employee in cash; this cash is transferred to the tax authority to settle the employee’s tax obligation. Paragraph 34 of IFRS 2 requires that a share-based payment transaction, or components of that transaction, should be classified as cash-settled if, and to the extent that, the entity has incurred a liability to settle in cash or other assets. Accordingly, the portion withheld by the entity should be accounted for as a cash-settled share-based payment in accordance with the manner of settlement.
- BC12 View 2 is based on the assumption that the entity is acting as an agent in paying cash to the taxation authorities, because the tax obligation is the employee’s obligation. The share-based payment transaction is considered as being settled entirely in equity instruments with a separate, yet simultaneous, repurchase of a portion of those equity instruments. The entity then remits the cash for the repurchased equity instruments to the taxation authority on behalf of the employee to settle the employee’s tax obligation.
- BC13 In respect of View 1, the Interpretations Committee was concerned that requiring a different classification of the portion that is withheld by the entity (that is, a classification that is different from the classification of the other portion) could cause an undue burden when applying IFRS 2. In reaching this view, the Interpretations Committee considered arguments that View 1 would impose a significant operational challenge, because it would require an entity to estimate changes in tax laws, including changes in tax rates that affect the amount that is required to be withheld and remitted by the entity. As the estimate changes, the entity would need to reclassify a portion of the share-based payment between cash-settled and equity-settled.
- BC14 However, the IASB noted that other circumstances would lead to classification as a cash-settled share-based payment transaction to the extent to which the share-based payment is settled in cash in accordance with paragraph 34 of IFRS 2. For example, the classification as cash-settled would apply when there is a stated intention to purchase, or there is past practice of repurchasing, equity instruments granted in a share-based payment transaction.
- BC15 To reduce the operational complexity identified, the IASB proposes adding guidance to IFRS 2 in the form of an exception to the requirements in IFRS 2. The IASB proposes that this guidance should be limited to a situation in which a net settlement feature is used by an entity to meet statutory tax withholding obligations incurred as a result of the share-based payment transaction.
- BC16 The guidance proposed by the IASB specifies that a share-based payment transaction with employees in which the entity settles the share-based payment arrangement net (by withholding a specified portion of the equity instruments to meet the statutory tax withholding obligation incurred as a result of the share-based payment transaction) should be classified as equity-settled in its

entirety, if the entire share-based payment would otherwise have been classified as equity-settled if it had not included the net settlement feature. The IASB noted that this approach is similar to that taken in US Generally Accepted Accounting Principles (US GAAP) and achieves further convergence with US GAAP.

Accounting for a modification to the terms and conditions of a share-based payment transaction that changes the classification of the transaction from cash-settled to equity-settled

- BC17 The IASB was asked to provide guidance for the accounting for a modification to the terms and conditions of a share-based payment transaction that changes the transaction from cash-settled to equity-settled. The IASB was informed that there are situations in which a cash-settled share-based payment is settled and replaced by a new equity-settled share-based payment and the replacement award has a higher fair value than the original award at the replacement date. The IASB was told that there is diversity in practice because IFRS 2 does not provide specific guidance for such situations.
- BC18 The IASB decided that the principles for the modification of equity-settled share-based payments in paragraphs 27 and B42–B44 of IFRS 2 should not be applied by analogy to account for the fact pattern analysed. This is because it observed that the requirement in paragraph 27 of IFRS 2, for the recognition of a minimum amount for the share-based payment following modifications to the terms and conditions of an equity-settled share-based payment transaction, is inconsistent with the requirement in paragraph 30 of IFRS 2. Paragraph 30 of IFRS 2 requires, for a cash-settled share-based payment transaction, the remeasurement of the fair value of the liability at the end of each reporting date until the liability is settled.
- BC19 The IASB observed that in the transaction described in paragraph BC17, the original cash-settled share-based payment is considered to be settled and replaced by the promise to issue equity instruments. In this respect, the IASB noted that at the original grant date there was a shared understanding that the entity would pay cash for services to be rendered by the counterparty. However, at the modification date, the entity and its counterparty have a new shared understanding that the entity would issue equity instruments to the counterparty.
- BC20 Accordingly, the IASB determined that the portion of the equity-settled share-based payment transaction for which goods or services have been received is recognised as an increase in equity and is measured by reference to the modification-date fair value of the equity instruments granted.
- BC21 Furthermore, the IASB noted that the liability incurred for the original cash-settled share-based payment is considered to be settled by the granting of the equity-settled share-based payment. Hence, the liability should be derecognised as of the modification date, because the entity is no longer obliged to transfer cash or other assets to the counterparty, and the equity-settled share-based payment should be recognised to the extent that the services have been rendered up to the modification date. The IASB noted that the liability

incurred for a cash-settled share-based payment is ultimately remeasured to the amount paid at the settlement date (see paragraph BC249 of IFRS 2). Accordingly, the liability recognised for the original cash-settled share-based payment should be remeasured at the settlement amount, which is the amount of the increase in equity. Any change in the amount of the liability until the settlement should be recognised in profit or loss in accordance with paragraph 30 of IFRS 2. Consequently, the IASB decided that any difference between the fair value of the liability at the modification date and the fair value of the equity instruments promised in settlement should be recognised immediately in profit or loss.

Effective date and transition

- BC22 The IASB proposes prospective application of the amendment included in the Exposure Draft to clarify the effects of vesting conditions on the measurement of a cash-settled share-based payment, for both new and outstanding awards, because it will result only in changes to the timing and amount of the expense recognised at each reporting date, but will not result in changes to the cumulative expense. This is because this amount is ultimately remeasured to the amount of cash paid at the settlement date.
- BC23 The IASB also proposes prospective application for the other two amendments included in the Exposure Draft ('the classification of share-based payment transactions with net settlement features' and 'the accounting for a modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled'). Although the IASB noted that retrospective application of these two amendments is achievable, it noted that it would be preferable for an entity to apply the same transition method for all the amendments in this Exposure Draft and that this would give better information for users. The IASB also proposes to permit an entity to apply all of the amendments retrospectively if the necessary information to do so is available without the use of hindsight.

