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International Accounting Standards Board

INFORMATION FOR OBSERVERS

Board Meeting: **17 October 2008, London**

Project: **ED OF PROPOSED AMENDMENTS TO IFRS 2 AND IFRIC 11 – Group cash-settled share-based payment transactions**

Subject: **Comment analysis (Agenda Paper 14A)** ***(Originally posted as observer note 7A for the September 2008 IASB Meeting)***

INTRODUCTION

1 This is the Board's first redeliberation since publishing the ED. The purpose of this agenda paper is to briefly recap the background of the proposals in the ED, the IFRIC discussions of the comment analysis presented by the staff, and the main areas of concerns that the IFRIC reconsidered before making its recommendations to the Board.

2 Appendix A contains the comment letter analysis paper presented at the May 2008 IFRIC meeting and Appendix B contains the respondents list.

3 At this meeting, the staff will ask if the Board identified additional issues in its review of the comment letters that should be reconsidered before finalising the amendments.

BACKGROUND

4 For group *equity-settled* share-based payment arrangements, paragraph 3 of IFRS 2 requires an entity to apply IFRS 2 when its shareholders transfer equity instruments of the entity or the entity's parent (or another entity in the same group) to parties that have supplied goods or services to the entity. IFRIC 11 provides guidance on how the entity that receives the goods or services from its suppliers should account for such *equity-settled* transactions in its financial statements.

5 The ED addresses how an entity that receives goods and services from its suppliers (including employees) should account for similar share-based arrangements that are *cash-settled* when the entity itself does not have any obligation to make the required payments to its employees. Paragraph 3 of the Introduction in the ED described two examples:

- Arrangement 1 – the suppliers of the entity will receive cash payments that are linked to the price of the equity instruments of the *entity*
- Arrangement 2 – the suppliers of the entity will receive cash payments that are linked to the price of the equity instruments of the *parent of the* entity.

For either arrangement, the parent (not the entity itself) has an obligation to make the required cash payments to the suppliers of the entity.

6 In the financial statements of the subsidiary, neither arrangement meets the definition of either a cash-settled share-based payment transaction or an equity-settled share-based payment transaction. Paragraph 6 of IFRIC 8 *Scope of IFRS 2* does suggest that Arrangement 1 is within the scope of IFRS 2 in the financial statements of the subsidiary. However, IFRS 2 does not specify how to account for the cash-settled arrangements described above in the financial statements of the subsidiary.

7 In the IFRIC's July and September 2007 meetings, and the Board's October 2007 meeting, both the Board and the IFRIC noted that these arrangements are: (a) for the purpose of providing benefits to the employees of the subsidiary in return for employee services, and (b) share-based and cash-settled.

PROPOSALS – ED

8 To clarify the scope and accounting for these types of share-based payment transactions, the ED proposes that in the standalone financial statements of a subsidiary that receives goods or services from its suppliers under the arrangements described in new paragraph 3A of IFRIC 11,

(a) With respect to scope, the subsidiary should apply IFRS 2 to account for the transactions with its suppliers. In other words, in the financial statements of the subsidiary, such cash-settled share-based payments are within the scope of IFRS 2 (see Agenda Paper 14D);

(b) With respect to measurement, the subsidiary should measure the goods or services in accordance with the requirements applicable to cash-settled share-based payment transactions. Specifically, the subsidiary should measure the services received from its employees on the basis of the fair value of the corresponding liability incurred by the parent. Until the liability incurred by the parent is settled, the subsidiary should recognise any change in the fair value of the liability in profit or loss and in the subsidiary's equity as adjustments to contributions from the parent. (See Agenda Paper 14D)

9 Therefore, as proposed, an entity that receives goods or services from its suppliers must apply IFRS 2 and recognise the remeasurement of the liability reflected by the parent even though it has no obligation to make the required share-based cash payments itself, regardless of whether there is a reimbursement arrangement between the parent and its subsidiary (see Agenda Paper 14D).

10 For convenience, the proposal to amend IFRIC 11 only discusses the issues in terms of a parent and its subsidiary, however, IFRIC 11 as amended also applies to similar arrangements between an entity and another entity in the same group (See Agenda Paper 14D).

IFRIC DISCUSSIONS

11 At the May 2008 IFRIC meeting, the staff presented a summary of the comment analysis (see Appendix A) and identified the main areas of concern

about the proposed scope and measurement in the ED that the staff believed should be reconsidered before finalising the amendments.

12 Many respondents acknowledged that the principal objective of the proposals was to align the accounting for share-based transactions of similar economic substance, no matter whether they are equity-settled or cash-settled, and to remove structuring incentives. However, many respondents either expressed concern about the scope, or disagreed with some aspects of the measurement proposal. Some questioned some of the bases for the consensus reached.

13 The IFRIC agreed with the staff's analysis of the main issues to be reconsidered, which are:

(a) the scope for these arrangements with similar substance should be set out more clearly and consistently among IFRSs;

(b) the amended scope for these arrangements should be consistent with the definitions of share-based payments in IFRS 2;

(c) the classification and measurement for these arrangements as cash-settled transactions by the entity when it does not have any obligation;

(d) the attribution of the parent's liability and remeasurement by the subsidiary in the absence of existing concepts in IFRSs and the risk of unintended analogy for other transactions.

QUESTION TO THE BOARD

14 **Are there additional issues that the Board identified in its review of the comment letters that should be reconsidered before finalising the amendments?**

REVISED PROPOSALS

15 Agenda Paper 14B includes the IFRIC's recommended changes from the proposed scope in Question 1(a) of the ED.

16 Agenda Paper 14C includes the IFRIC's recommended changes from the proposed classification for accounting in Question 1(b) of the ED.

Appendix A

Extracts from the paper presented as Agenda Paper 4 at the May 2008 IFRIC meeting

NOTE TO THE BOARD – Paragraphs 1-10 of that IFRIC paper is omitted due to redundant background information (see paragraphs 4-10 of this Agenda Paper)

PRELIMINARY COMMENT ANALYSIS

Scope (Question 1a of the ED)

11 Respondents generally agreed that the narrow category of cash-settled transactions between a parent and a subsidiary described in the ED's Introduction and paragraph 4 of this Agenda Paper should be within the scope of IFRS 2. Supporters believed that including these arrangements is consistent with IFRS 2's main principle of recognizing the goods and services that an entity receives in a share-based transaction. Because such cash-settled transactions have similar economic substance as group equity-settled transactions explicitly addressed in paragraph 3(a) of IFRIC 11, accounting for them consistently also removes an incentive to structure arrangements to be outside of IFRS 2's scope. [1]

12 However, respondents also expressed the following concerns about the proposed scope, as further explained in the paragraphs below:

- Lack of clarity and inconsistency in scope among IFRSs
- Inconsistency with definitions of share-based payments

Lack of clarity and inconsistency in scope among IFRSs

13 Most respondents noted that the proposal's principle objective is to align the subsidiary's accounting for similar share-based arrangements that are *cash-settled*, when the subsidiary itself does not have any obligation to make the required payments to its suppliers of goods and services, with the existing accounting already addressed in IFRIC 11 for those that are *equity-settled*.

[1] CL 3

14 For example, the proposed amendment to paragraph 4 of IFRIC 11 states as follows:

> "This Interpretation addresses how the share-based payment arrangements set out in paragraphs 3 and 3A should be accounted for in the financial statements of the subsidiary that receives services from the employees. For convenience, this Interpretation discusses the issues in terms of a parent and its subsidiary. However, this Interpretation also applies to similar arrangements between an entity and another entity in the same group."

15 This proposed amendment results in existing IFRIC 11 accounting guidance, if discussed in examples between a parent and subsidiary, to be applicable to arrangements between an entity and another entity in the same group, regardless of the arrangements' substance and the group entities' relationship.

16 While most supported the scope extension to the narrow cases explicitly described between parent and subsidiary, there are conflicting views about the appropriateness, and the Board's intent (or the lack thereof), to require application of the proposed amendments beyond these narrow cases to other group entities such as transfers by shareholders, fellow subsidiaries, or joint ventures. Some questioned if the proposed 'push-down' accounting and recording a contribution in equity from parent should always apply to arrangements other than those between a parent and subsidiary.[2] For example, a respondent commented on the implications to existing guidance in paragraph 8 of IFRIC 11 for equity-settled share-based payments if the entities are not in a parent-subsidiary relationship.[3]

17 Many also expressed concerns about the inconsistent scopes between IFRS 2 and IFRIC 11 as proposed. Different terminologies are used in IFRS 2, IFRIC 8, and IFRIC 11. For example, the proposed amendments to both paragraphs 3A of IFRS 2 and IFRIC 11 for cash-settled share-based transactions do not mirror the reference to the entity's *shareholders* as the grantor that is in the existing paragraph 3 of IFRS 2 and paragraph 7(b) of IFRIC 11, which specifically include such transfers in the scope. Instead, the proposals only include in the scope those cases when the entity's *parent (or another entity in the group)* incurs a liability for the cash-settled share-based payments to the subsidiary's employees.

[2] CL 5, 6, 10, 14, 15, 18, 19, 21, 22, 23, 25, 26, 27, 29, 35, 37, 41, 43, 44
[3] CL 19

18 For example, the comment letter from the Institute for the Accountancy Profession in Sweden (CL 19) includes a one-page table and bullets on page two as their attempt to illustrate their understanding of the different scopes between equity-settled and cash-settled share-based transactions as required by IFRS 2 and IFRIC 11 with the proposed amendments.

19 According to this table, equity-settled share-based transactions, where the grantor is *the entity's shareholder*, are within the scope pursuant to paragraph 3 of IFRS 2 (and paragraph 7(b) of IFRIC 11, which was not mentioned by the comment letter). However, neither IFRS 2 nor IFRIC 11 specifies the scope for similar cash-settled transactions. On the other hand, cash-settled share-based transactions where the grantor is *the entity itself* are within the scope pursuant to paragraph 2(b) of IFRS 2, and paragraphs 3(b) and 4 of IFRIC 11 with the proposed amendment. However, neither IFRS 2 nor IFRIC 11 specifies the scope for similar equity-settled transactions.

20 These inconsistencies result in unexplained scope differences applicable to equity-settled and cash-settled arrangements that are of the same substance. Generally, most recommended aligning the scope and terminology consistently among these IFRSs. [4]

Inconsistency with definitions of share-based payments

21 A number of respondents emphasized the importance of consistency for definitions in IFRSs. Many expressed concerns of the rule-based approach of the ED to extend the scope on a case-by-case basis. They also noted that such cases, as amended, do not meet the definitions of share-based payments in Appendix A of IFRS 2, similar to specific cases previously addressed by IFRIC 11. [5]

22 These respondents recommended a direct amendment to broaden the definitions of 'equity-settled share-based payments' and 'cash-settled share-based payments' in Appendix A of IFRS 2 so that transactions between group entities with similar characteristics are included in the scope of IFRS 2. Some respondents also recommended that, because the proposals amend both IFRS 2 and IFRIC 11, the Board should take this opportunity to incorporate the main

[4] Same CLs as footnote 2
[5] CL 5, 12, 18, 24, 26, 27, 30, 40, 41, 44

principles of IFRIC 11 (and IFRIC 8) into IFRS 2, and move the specific cases described to the appendix of Implementation Guidance or Illustrative Examples sections? of IFRS 2 to avoid fragmented guidance.[6]

Measurement by the entity receiving goods and services (Question 1b of the ED)

23 The proposal amends paragraph 11B of IFRIC 11 and requires the subsidiary to measure the goods and services received from its employees as cash-settled share-based payments, and to recognise any changes in the fair value of the parent's liability in profit or loss and in the subsidiary's equity as adjustments to contributions from the parent until the parent's liability is settled.

24 Most respondents supported the proposed classification and measurement for the narrow category of cash-settled transactions between a parent and a subsidiary as described the ED's Introduction and paragraph 4 of this Agenda Paper. However, several respondents objected to the proposals[7] and a number of others questioned the bases underlying the consensus reached, citing different reasons.[8]

25 Some also questioned if the proposed 'push-down' accounting and recording a contribution in equity from parent should always apply to arrangements other than those between a parent and subsidiary.[9]

26 The main concerns expressed by respondents are as follows:

- Classification and measurement as cash-settled share-based payments by the entity receiving the goods and services
- Attribution of the parent's liability by the subsidiary

Classification and measurement as cash-settled share-based payments

27 Several respondents opposed the classification of these arrangements as cash-settled share-based payments in the subsidiary's financial statements on the basis that the subsidiary has no liability in either of the arrangements explicitly described in the ED.[10] Classifying them as cash-settled share-based payments conflicts with the rationales in paragraphs BC238, BC240-BC241 of IFRS 2,

[6] CL 6, 14, 17, 23, 28, 34, 35
[7] CL 20, 24, 36, 40
[8] CL 17, 18, 19, 35, 37
[9] Same CLs as footnote 2
[10] CL 24, 35, 37

and BC8-BC9 and BC16-BC18 of IFRIC 11, which distinguish cash-settled from equity-settled share-based payments as those where the subsidiary has the obligation to transfer cash to suppliers of goods and services.[11]

28 Some respondents expressed concerns about the proposed measurement of the goods and services received by the subsidiary in its financial statements. Many questioned and several objected to the remeasurement of changes in fair value of the parent's liability in the subsidiary's profit and loss.[12]

29 Respondents objected to this proposal on the basis that it conflicts with paragraphs 70, 78, 94-98 of the *Framework,* and is prohibited by IFRSs, because the subsidiary itself does not have any obligation. Therefore, the change in fair value is not a change in the subsidiary's own liability but rather, a change in the fair value of an equity owner's (parent's) liability.[13]

30 One respondent commented that paragraph IG19 of IFRS 2 defines the value of goods and services received in a cash-settled share-based payment as the fair value of the award on the date of grant, and that the remeasurement of the parent's liability does not have to be attributed to the entity. In addition, this respondent also commented that the lack of obligation of the subsidiary suggests that the share-based payments in these arrangements would be classified as equity-settled in the subsidiary's financial statements even though it will be classified as cash-settled in the consolidated financial statements.[14]

31 One respondent commented that IFRS 2 requires remeasurement until the liability is settled, whereas the proposals require remeasurement after settlement has effectively taken place.[15] This respondent believed that the proposals conflicts with paragraph 30 of IFRS 2 because settlement occurs when the parent commits to making the payment to the subsidiary's employees and not when the employees are paid.

32 Other constituents have different understandings about when the 'contribution' from the parent takes place, and the related accounting at initial recognition and subsequent measurement. They requested clarification of whether the fair value of the parent's liability should be recognized by the subsidiary as a

[11] Same CLs as footnote 10, CL 26
[12] CL 17, 20, 21, 23, 24, 25, 26, 35, 37
[13] CL 17, 20, 24, 25
[14] CL 37
[15] CL 23

liability initially, then subsequently as a contribution from parent in equity when settled, or whether the amount should initially be recognized in the subsidiary's equity, similar to the changes in the fair value of the parent's liability.[16]

33 In addition to concerns related to the appropriateness of accounting for the credit entry as a contribution from parent in the subsidiary's equity at initial recognition and subsequent measurement, a number of respondents questioned whether the credit entry should always be a contribution of equity either for parent or non-parent contributors.[17]

Attribution of the parent's liability by the subsidiary

34 Several respondents commented that the Basis for Conclusions in the ED has not articulated the IFRS principle that results in applying 'push-down' accounting of the parent's liability in the subsidiary's financial statements and recording changes in fair value of the parent's liability through the subsidiary's profit and loss, when the subsidiary has no obligation to make a cash payment.[18]

35 One respondent limited their support to attribution of the grant-date fair value only. The main concern about requiring attribution of the remeasurement in the subsidiary's financial statements is the broader issue that no clear concept in IFRSs addresses when, and if so how, a transaction with shareholders should be attributed to an entity. The respondent acknowledged that paragraph 3 of IFRS 2 is the first time that IFRSs provides for such attribution although that change in concept only focused on equity-settled share-based payments. Many other circumstances where a parent provides benefits for or on behalf of a subsidiary would not require attribution, but rather, disclosures according to IAS 24 *Related Party Disclosures*.[19]

36 Other respondents shared similar concerns about the risk of analogy to this proposal for other types of corporate allocation expenses among group entities.[20]

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[16] CL 21
[17] CL 5, 7, 17, 19, 21, 36, 44
[18] CL 18, 35, 37, 42
[19] CL 37
[20] CL 3, 6, 25

Transition (Question 2 of the ED)

37 Most respondents agreed with the retrospective application of the proposals except for minor clarifications. For example, respondents requested clarification about whether the transition would apply only to outstanding cash-settled share-based payment plans as of the effective date of this amendment, whether the same relief to first-time adopters in IFRS 1 *First-time Adoption of International Financial Reporting Standards* applies to the entity receiving the goods and services and identifying the specific transitional paragraphs under IFRS 2 to which the proposal is linked..[21]

Other issues

38 There are some additional issues raised by respondents besides those on which the Board and the IFRIC requested comments. For example, many respondents requested clarification about when the entity itself has an obligation to the employees for the cash-settled share-based payments, whether the proposed accounting should apply. Other similar requests include additional guidance for other intra-group transactions, arrangements with reimbursements from the subsidiary, contributor accounting, hybrid share-based payments that are partially cash-settled and equity-settled, or when the employees or grantors have a choice in the method of settlement, and so on.

39 Once the IFRIC reaches consensus on the issues discussed in this Agenda Paper we will decide whether some of these additional issues need to be addressed. The staff proposes to bring an analysis of these remaining issues in a subsequent paper.

PROJECT PLAN

40 Expected timetable for subsequent redeliberations:

Tasks	Expected Time
Preliminary comment analysis	May 2008 IFRIC meeting
Redeliberations of issues raised - Scope - Classification	 July 2008 IFRIC meeting July 2008 IFRIC meeting

[21] CL 4, 12, 17, 19, 23, 26, 28, 35, 41, 44

- Measurement	September 2008 IFRIC meeting
Redeliberations of consensus reached	October 2008 IASB meeting
Review of revised amendments	October 2008
Balloting and drafting	November 2008
Publication of revised amendments to IFRS 2 and IFRIC 11	December 2008 Expected effective date: —to be determined

QUESTIONS FOR THE IFRIC

41 **Are there additional issues that the IFRIC identified in its review of the comment letters that it would like the staff to consider?**

42 **Does the IFRIC agree with the staff's project plan?**

Appendix B

Respondents to the Invitation to Comment

1 This appendix contains the following:

Table 1 contains a full list of the respondents to the invitation to comment

Table 2 categorises the respondents by type and geography

TABLE 1: LIST OF RESPONDENTS

CL#	Respondents	Respondent Type	Respondent Industry	Country
1	PKF (UK) LLP	Accounting Firm	Accounting	United Kingdom
2	Malaysian Accounting Standards Board (MASB)	Standard Setter	Accounting	Malaysia
3	Grant Thornton	Accounting Firm	Accounting	International
4	CPA Australia	Professional Body	Accounting	Australia
5	German Accounting Standards Committee (DRSC)	Standard Setter	Accounting	Germany
6	Institute of Chartered Accountants in Australia (ICAA)	Professional Body	Accounting	Australia
7	CINIF	Professional Body	Accounting	Mexico
8	Dutch Accounting Standards Board (DASB)	Standard Setter	Accounting	Netherlands
9	Bank of Russia Russia	Preparer (Bank)	Banking	Russia
10	Institut der Wirtschaftsprüfer (IDW)	Professional Body	Accounting	Germany
11	Financial Executives Institute (FEIC)	Preparers (Representative Body)	Accounting	Canada
12	Accounting Standards Board (ASB)	Standard Setter	Accounting	United Kingdom
13	Canadian Accounting Standards Board	Standard Setter	Accounting	Canada
14	Ernst & Young	Accounting Firm	Accounting	International
15	Institute of Chartered Accountants in Ireland (ICAI)	Professional Body	Accounting	Ireland
16	Institute of Chartered Accountants of Pakistan (ICAP)	Professional Body	Accounting	Pakistan
17	FirstRand Banking Group	Preparer (Bank)	Banking	South Africa
18	Institute of Chartered Accountants in England & Wales (ICAEW)	Professional Body	Accounting	United Kingdom
19	FAR SRS	Professional Body	Accounting	Sweden
20	Norsk RegnskapsStiftelse - Norwegian Accounting Standards Board	Standard Setter	Accounting	Norway
21	International Organization of Securities Commissions (IOSCO)	Regulators	Unspecified	International
22	Korea Accounting Standards Board (KASB) (International Financial Reporting Standards Review Committee) (IFRSRC)	Standard Setter	Accounting	Korea
23	South African Institute of Chartered Accountants (SAICA)	Standard Setter	Accounting	South Africa
24	Mazars	Accounting Firm	Accounting	International
25	BDO	Accounting Firm	Accounting	International
26	Deloitte Touche Tohmatsu	Accounting Firm	Accounting	International
27	PricewaterhouseCoopers	Accounting Firm	Accounting	International
28	Association of Chartered Certified Accountants (ACCA)	Professional Body	Accounting	United Kingdom

CL#	Respondents	Respondent Type	Respondent Industry	Country
29	Polish Accounting Standards Committee	Standard Setter	Accounting	Poland
30	National Accounting Standards Board of Russia (NASB)	Standard Setter	Accounting	Russia
31	UBS	Preparer (Bank)	Banking	International
32	The Body of Experts and Licensed Accountants of Romania	Professional Body	Accounting	Romania
33	Institute of Chartered Accountants of Scotland (ICAS)	Professional Body	Accounting	United Kingdom
34	The Chartered Institute of Management Accountants (CIMA)	Professional Body	Accounting	United Kingdom
35	Conseil National de la Comptabilité (CNC)	Professional Body	Accounting	France
36	BHP Billiton	Preparers (Company)	Mining	Australia
37	KPMG	Accounting Firm	Accounting	International
38	Accounting Research and Development Foundation	Standard Setter	Accounting	Taiwan
39	Accounting Standards Council of Singapore	Standard Setter	Accounting	Singapore
40	ACTEO, MEDEF and AFEP	Preparers (Representative Body)	Accounting	France
41	Australian Accounting Standards Board	Standard Setter	Accounting	Australia
42	London Society of Chartered Accountants (LSCA)	Professional Body	Accounting	United Kingdom
43	Swedish Financial Reporting Board	Standard Setter	Accounting	Sweden
44	European Financial Reporting Advisory Group (EFRAG)	Professional Body	Accounting	International

TABLE 2: RESPONDENTS BY GEOGRAPHY

Respondent type: Industry	**Africa**	**Asia-Pacific**	**Europe**	**North America**	**International**	**Total**
Professional Body	-	3	10	1	1	**15**
Accounting Firm	-	-	1	-	7	**8**
Preparer (Bank)	1	-	1	-	1	**3**
Preparer (Company)	-	1	-	-	-	**1**
Preparer (Representative Body)	-	-	1	1	-	**2**
Regulator	-	-	-	-	1	**1**
Standard Setter	1	5	7	1	-	**14**
Total	2	9	20	3	10	**44**