**30 Cannon Street, London EC4M 6XH, United Kingdom**
**Phone: +44 (0)20 7246 6410 Fax: +44 (0)20 7246 6411**
**Email: iasb@iasb.org Website: http://www.iasb.org**

**International Accounting Standards Board**



# INFORMATION FOR OBSERVERS

**IASB Meeting:** **18 September 2008, London (Agenda Paper 12A)**

**Project:** **IFRS 2: Category A issues**

---

## *Introduction*

1. This paper sets out a summary of the Category A IFRS 2 issues that have arisen. These are issues that would require a reconsideration of the key principles underlying IFRS 2. They include:

   - seven 'new' arguments for the review or repeal of IFRS 2
   - accounting for cancellations
   - the measurement date
   - accounting for modifications that are not intended to be beneficial to the employee.

## *Staff Recommendation*

2. In all cases, no new arguments or reasons that would form a basis for a reconsideration of the principles underlying the standard were raised. Therefore the staff does not think that any of the issues in Category A meet the criteria for inclusion as a Board project.

3. A more detailed analysis of the issues raised is set out below.

**Seven ‘new’ arguments**

4. Earlier this year, a petition was submitted to the IASB asking for the repeal or review of IFRS 2.

5. The proposers identified seven arguments that, in their view, are new and prove that the accounting required by IFRS 2 is inappropriate.

6. A similar request was sent to the SEC on 27 February for the repeal of FASB Statement No. 123(R), *Share-Based Payment.* The FASB staff concluded that the issues raised do not provide a basis to reconsider the standard.

7. [Paragraph omitted from Observer Notes].

8. The staff has analysed the issues presented in order to assess whether they do indeed raise new arguments or reasons that would be a basis for reconsideration of IFRS 2. The staff conclusion is that the substance of issues/arguments raised are not new, were carefully considered by both the IASB and the FASB and do not provide a basis to reconsider the standard.

**Accounting for cancellations**

9. Some disagree with the IFRS 2 approach for accounting for cancellations. They would support, instead, a reversal of expense on cancellation. The IASB discussed this issue at length during its deliberations on IFRS 2. In particular, they discussed whether the cancellation should be accounted for as:

(a) an accelerated recognition of costs;

(b) a non-event, in which case the employer would continue to recognise the services received from that employee over the remainder of the vesting period; or

(c) a forfeiture, in which case the employer would reverse the compensation expense previously recognised.

10. The key principle underlying IFRS 2 is that the employer should recognise a compensation expense for the services received as determined at the grant date fair value of the share-based payment. If a share-based payment is cancelled, this does not imply that the employer does not receive the services, therefore treating a cancellation as a reversal of expense would undermine the requirements of IFRS 2. The IASB concluded that the employer should accelerate the recognition of the expense for the services (to be) received when the share-based payment is cancelled. The FASB also agreed with this approach for cancellations and included similar requirements in its revised standard on share-based payments.

**The Measurement Date**

11. Some think that the grant date is not the appropriate measurement date for accounting for share-based payments. They argue that the grant date model leads to different accounting outcomes for the same economic events and prefer, instead, a vesting date measurement model.

12. [Paragraph omitted from Observer Notes].

13. In paragraph BC 103 of IFRS 2, the Board noted that vesting date measurement is inconsistent with the *Framework* because it requires the remeasurement of equity. Moreover, IFRS 2 focuses on measuring the goods or services received in return for the share-based payment using the fair value of the share-based payment as a surrogate measure when necessary. Paragraphs BC 91 – 96 of IFRS 2 explain why the Board thought that the grant date is the most appropriate measurement date given this measurement objective. [Part of paragraph omitted from Observer Notes].

14. The staff does not think that those who disagree with the grant date model have put forward any new arguments that would form a basis for a reconsideration of the key principles for a grant date measurement date.

**Modifications that are not intended to be beneficial to the employee**

15. Paragraph 27 of IFRS 2 requires an employer to recognise the effects of modifications that increase the fair value of share-based payments. Some questioned why the same treatment should be required for modifications that are not beneficial to the employees. Their main concern was that there are cases where modifications are made that are not, and were not intended to be, beneficial to employees. For example some purport that in the case where the market value of a share falls and the entity reduces the exercise price so that the employee would be no worse off that the effect of the modification should not be taken into account since the intent of the employer was not to improve the employee's compensation.

16. The staff thinks that reducing the exercise price when the share price falls is an improvement to the employee's compensation, since otherwise the value of the option would have decreased or even gone underwater. The effect of this improvement should be taken into account.

17. In any case, ignoring the effect of the modification would be inconsistent with IFRS 2. IFRS 2 *Basis for Conclusions* paragraph BC 228 (b) explains that the effect of the modification should be taken into account because a share-based payment that could be modified as a result of market changes is more valuable than a share-based payment that could not be modified. The grant date fair value does not take into account the possibility of future modifications to the share-based payment (to make the employee no worse off). Therefore, the employer effectively underestimated the value of the share-based payment. Therefore, when such a modification does occur, the incremental fair value should be recognised even if that modification is not intended to be beneficial to the employee.