STAFF PAPER

17–21 February 2014

IASB Meeting

Project	**Narrow-scope amendments to IFRS 2 *Share-based Payment***		
Paper topic	Proposed wording for the draft amendments to IFRS 2		

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Purpose of this paper

1. This paper contains all of the draft proposed amendments to IFRS 2 from Agenda Papers 12C to 12F.

2. The objective of this paper to:

   (a) present to the IASB our analysis on the transition requirements for the amendments IFRS 2 *Share-based Payment* that are derived from Agenda Paper 12C-12F; and

   (b) get a decision from the IASB on whether it agrees with the proposed amendments to IFRS 2.

3. We have proposed the amendments to IFRS 2 for the following issues:

   (a) <u>Agenda Paper 12C:</u> Accounting for cash-settled share-based payment transactions that include a performance condition

   (b) <u>Agenda Paper 12D:</u> Share based payments in which the manner of settlement is contingent on future events

   (c) <u>Agenda Paper 12E:</u> Share-based payments settled net of tax withholdings

   (d) <u>Agenda Paper 12F:</u> Modification of a share-based payment transaction from cash settled to equity-settled

Transition provisions

Consideration of the draft amendments individually

4. The proposed amendments in Agenda Paper 12C may 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 because this amount is ultimately remeasured to the amount of cash paid at settlement date. Accordingly, the Interpretations Committee recommended that the proposed amendments should be applied on a prospective basis for new awards and outstanding awards because it thought that the cost of retrospective application would outweigh the benefits from doing so.

5. We note the concern that the proposed amendment in Agenda Paper 12D would be difficult for most entities to determine the classification of the share-based payment with contingent settlement feature at a point of time in the past without using hindsight. This is because the classification depends on the entity's estimates at that point of time in the past for the manner of settlement in the future. Accordingly, we think that the IASB should propose prospective application of this amendment.

6. We think that most entities that are affected by the proposed amendments in Agenda Papers 12E and 12F would have information necessary to apply the amendments retrospectively. The proposed amendments would affect only the classification of the share-based payments and the accounting for changes in classification. They would not require an entity to change estimates or judgements previously made by the entity. Accordingly, if the amendments in Agenda Papers 12E and 12F were considered alone, we think that it would be practicable for most entities to apply the amendments retrospectively.

Consideration of the draft amendments as a group

7. When all the amendments in Agenda Paper 12C-12F are considered collectively, we think that requiring retrospective application only for the amendments in Agenda Papers 12E and 12F could be confusing. We think that, in order to make the transition requirements straight-forward, the IASB should propose a single

transition method for the all of proposed amendments, which is prospective application for new awards and outstanding awards.

8. Notwithstanding the above, we think that an entity should be permitted to apply the amendments applicable to it retrospectively if the entity has information necessary to do so. This would allow better comparability of the entity's results from period to period.

9. On the basis of the analysis above, we recommend that the IASB should propose that the entity applies the amendments prospectively but allow retrospective application when it has the necessary information available.

Questions for the IASB

Questions for the IASB
1. Does the IASB agree with the transition requirements recommended by the staff? 2. Does the IASB agree with the wording of the proposed amendments to IFRS 2?

[Draft] Amendments to IFRS 2 *Share-based Payment*

Paragraphs 33A-33F, 63C, B41A-B41C and headings before paragraph 33E and B41A are added. Paragraphs 30 and 33 are amended. New text is underlined and deleted text is struck-through. Paragraph 32 is not proposed for amendment but is included here 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.

31 ….

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.

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 share appreciation rights 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.

33A To apply the requirements of paragraph 33, the entity shall recognise an amount for the goods or services received during the vesting period based on the best available estimate of the number of share appreciation rights expected to vest and shall revise that estimate, if necessary, if subsequent information indicates that the number of awards expected to vest differs from previous estimates. On vesting date, the entity shall revise the estimate to equal the number of share appreciation rights 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 share appreciation rights 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 result of applying paragraphs 30-33B the cumulative amount ultimately recognised for goods or services received as consideration for the share appreciation rights is equal to the cash paid

33D An entity may be obliged by the tax laws or regulations to withhold a certain amount of the employee's tax obligation associated with share-based payments, and transfer the amount in cash to the taxation authorities. The terms of some employee share-based payment arrangements permit the entity to deduct from the total number of equity instruments the number of equity instruments needed to equal the monetary value of the employee's tax obligation in order to meet the tax withholding obligation. For the purpose of classifying a share-based payment as either cash-settled or equity-settled, a share-based payment transaction with employees in which the terms of the arrangement permit an entity to settle the share-based payment transaction net by withholding a specified portion of the equity instruments to meet its minimum statutory tax withholding requirements shall be accounted for in accordance with the requirements applying to equity-settled share-based payment transactions in paragraphs 10-29, if the entire share-based payment transaction would otherwise be classified as an equity-settled share-based payment transaction without the net settlement feature.

Share-based payment transactions with contingent cash settlement provisions

33E For a share-based payment transaction in which the terms of the arrangement require the entity to settle the transaction in cash or other assets in the event of the occurrence or non-occurrence of future events that are beyond the control of both the entity and the counterparty, the entity shall account for the transaction in accordance with the requirements applying to cash-settled share-based payment transactions if it is probable that the entity will settle the transaction in cash or other assets. Otherwise, the entity shall account for the transaction in accordance with the requirements applying to equity-settled share-based payment transactions.

33F The classification of such a transaction may need to change as a result of changes in the probability of cash settlement. In that case, the entity shall remeasure the goods and services received before the reclassification in accordance with the requirements that apply to the share-based payment transaction after the reclassification, with any change in the measurement being recognised in the period in which the reclassification occurs.

Effective date

…

63C [Draft] *Clarifications of Classification and Measurement of Share-based payment Transactions* (Amendments to IFRS 2), issued in [date to be inserted after exposure], added paragraphs 33A-33F and B41A-B41B. An entity shall apply the amendments prospectively for annual periods beginning on or after [date to be inserted after exposure]. However, an entity may apply the amendments retrospectively in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provided that the entity has information necessary to do so. Earlier application is permitted. If an entity applies those amendments for an earlier period it shall disclose that fact.

[Draft] Amendments to the Application guidance on IFRS 2 *Share based Payment*

Modifications to cash-settled share-based payment arrangements

B41A Paragraph 30 requires the entity to 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 being recognised in profit or loss for the period. The effects of modifications to terms and conditions of cash-settled share-based payment transactions should be included in the remeasurement at the end of each reporting period. Modifications to the terms and conditions of cash-settled share-based payment arrangements may involve a change in the settlement method.

B41B If a cash-settled share-based payment transaction changes to an equity-settled share-based payment transaction by a modification to the terms and conditions of the arrangement, 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, which is the grant date of the equity-settled share-based payment transaction. An increase in equity is recognised at the amount determined on the basis of the modification date fair value of the equity instruments granted and the extent to which the services have been received until the modification date. At the date of the modification, the liability previously recognised is settled by the grant of the equity-settled share-based payment. Accordingly, the liability is remeasured immediately before the modification at the amount of settlement, which is an amount of the increase in equity, with any change in the amount of the liability recognised in profit or loss for the period.

B41C A cash-settled share-based payment may be cancelled followed by the granting of new equity instruments. If, 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 cash-settled share-based payment, the entity should account for the granting of the new equity instruments in the same way as a modification of the original cash-settled share-based payments.

[Draft] Basis for Conclusions on the Exposure Draft *Clarifications of Classification and Measurement of Share based payment Transactions* (Proposed amendments to IFRS 2)

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

Cash-settled share-based payment transactions

BC1 The IASB received a request to clarify the accounting for cash-settled share-based payment transactions that include a performance condition under IFRS 2.

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 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.

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 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 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.

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 to state that non-market vesting conditions shall not be taken into account when estimating the fair value of the share appreciation rights and instead, shall be taken into account by adjusting the number of share appreciation rights to receive cash. This is so that, ultimately, the amount recognised for goods or services received as consideration for the cash granted shall be based on the number of share appreciation rights that eventually 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 add IG Example 12A to the Implementation Guidance of IFRS 2 to illustrate the impact of a performance condition on the measurement of a cash-settled share-based payment transaction.

Share-based payment transactions with net settlement features

BC8 Some jurisdictions have tax laws or regulations that oblige an entity to withhold a certain amount of the employee's taxes associated with share-based payments, and transfer the amount in cash to the taxation authority. Share-based payment transactions in those jurisdictions may have provisions that require or permit the entity to deduct from the total number of equity instruments the number of equity instruments needed to equal the monetary value of the employee's tax obligation in order to meet the tax withholding requirements. The tax withholding scheme in respect of share-based payments varies from arrangement to arrangement, but one of the common schemes is the net settlement provision, which permits the entity to deduct from the total number of equity instruments the number of equity instruments needed to equal the monetary value of the employee's tax liability incurred as a result of the share-based payment transaction. The entity pays the amount withheld to taxation authorities from its own cash reserves.

BC9 The IFRS Interpretations Committee (the 'Interpretations Committee') received a request to clarify the classification of an equity-settled share-based payment transaction with a net settlement provision. More specifically, 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 be classified as equity-settled share-based payment transactions without the net settlement feature.

BC10 The IASB was informed that there were divergent views on this issue:

(a) View 1: the portion withheld by the entity should be accounted for separately and be classified as a cash-settled share-based payment transaction in accordance with the manner of settlement.

(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 repurchase of a portion of the equity instruments issued to the counterparty (paragraph 29 of IFRS 2)

BC11 Those who supported View 1 asserted that the entity is acting as an agent on behalf of the counterparty in transferring cash to the taxation authority to settle the counterparty's tax obligation. However, at the same time, the entity is fulfilling its obligation to settle the share-based payment for the services received from the counterparty as a principal by transferring cash to the taxation authority. 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 On the other hand, View 2 is based on the observation that the entity is acting as an agent in paying cash to the taxation authorities because the tax obligation is the counterparty's obligation. In this sense, it should be assumed that the share-based payment transaction was settled entirely in equity instruments with a separate, yet simultaneous, repurchase of a portion of those equity instruments.

BC13 The IASB noted that under US GAAP such a share-based payment transaction is classified as equity-settled in its entirety if an entity withholds a portion of the equity instruments that otherwise would be issued to the employees to meet the employer's minimum statutory tax withholding requirements.

BC14 To mitigate the diversity in practice and achieve further convergence with US GAAP, the IASB proposes to add guidance to specify that a net settlement feature does not, by itself, result in classifying a portion of the share-based payment transaction as a cash-settled share-based payment transaction, if the amount is withheld in order to meet the minimum statutory tax withholding requirements.

Share-based payment transactions with contingent cash settlement provisions

Classification of share-based payment transactions with contingent cash settlement provisions

BC15 The IFRS Interpretations Committee received a request to clarify the classification of a share-based payment transaction in which the manner of settlement is contingent on a future event that is outside the control of both the entity and the counterparty. The terms and conditions of some employee share-based payment transactions have contingent cash settlement provisions that require an entity to settle the share-based payment transaction either in cash (or other assets) or by issuing equity instruments, depending on the occurrence or non-occurrence of an uncertain future event such as a successful initial public offering and change in control. The Interpretations Committee reported to the IASB that practice differed significantly in the accounting for this type of share-based payment transaction.

BC16 The IASB noted that the diversity arises primarily because IFRS 2 does not provide specific guidance on this type of share-based payment transaction. Paragraphs 34-43 of IFRS 2 provide guidance only on share-based payment transactions in which the terms of the arrangements provide the counterparty or the entity with a choice of settlement.

BC17 The IASB considered whether it would be appropriate to apply guidance in other IFRSs by analogy, to the share-based payment transaction. The IASB noted that paragraph 25 of IAS 32 addresses a financial instrument with a contingent settlement feature. However, the IASB observed that the guidance in IAS 32 does not provide guidance for the classification of this type of share-based payment transaction because there are differences in principles for classification between IFRS 2 and IAS 32 (see paragraph BC106-110 of IFRS 2). The IASB further noted that paragraph 4 of IAS 32 states that share-based payment transactions are, for the most part, outside the scope of IAS 32.

BC18 The IASB also observed that the requirements for recognition of a liability in IAS 37 are not applicable to a share-based payment transaction. This is because IAS 37 has different recognition requirements from those in IFRS 2 (ie there is a probability threshold in addition to an existence threshold). In addition, the IASB noted that the *Conceptual Framework* does not provide clear guidance for the distinction between a liability and equity.

BC19 Consequently, the IASB observed that the existing guidance in other IFRSs and the *Conceptual Framework* does not provide guidance for the classification of share-based payment transactions. Accordingly, the IASB decided to add guidance to IFRS 2 to specify how to classify share-based payment transactions with contingent cash settlement provisions in order to solve the significant diversity in practice.

BC20 When the IASB developed the proposed guidance, it considered:

(a) whether the share-based payment transaction should be classified as:

  (i) equity-settled;

  (ii) cash-settled; or

  (iii) a combination of equity-settled and cash-settled.

(b) if the share-based payment transaction should be classified as a combination of equity-settled and cash-settled, how that bifurcation should be made.

BC21 The IASB observed that the share-based payment transaction should be viewed as representing a single share-based payment (either cash-settled or equity-settled). Two share-based payment transactions (ie both cash-settled and equity-settled) do not exist at the same time because no parties to the arrangement can dictate the manner of settlement.

BC22 The IASB noted that the single share-based payment is settled in its entirety either in cash (or other assets) or by issuing equity instruments depending on the occurrence or non-occurrence of an uncertain future event. Thus, the IASB observed that the classification of the share-based payment should be determined on the basis of the most likely settlement scenario.

BC23 Accordingly, the IASB decided that the share-based payment transaction should be classified as either cash-settled or equity-settled in its entirety, depending on which settlement method is the most likely (ie probable) to occur.

Accounting for changes in classification of share-based payment transactions with contingent cash settlement provisions

BC24 The IASB discussed how changes in classification of the share-based payment transaction should be accounted for. The IASB noted that two approaches could be derived, by analogy, from the existing guidance in IFRS 2 as follows:

(a) Approach 1–account for the change in classification by applying the requirements for failure to satisfy a non-market vesting condition in paragraph 19; and

(b) Approach 2–account for the change in classification by applying the requirements for modifications to terms and conditions of a share-based payment transaction in paragraphs 26-29.

BC25 Approach 1 treats the changes in classification as if the original settlement alternative had failed to satisfy a non-market vesting condition. For example, if the share-based payment transaction is reclassified from equity-settled to cash-settled, the entity would derecognise the amount recorded in equity for the equity-settled share-based payment transaction, with a credit to profit or loss in accordance with paragraph 19. At the same time, the entity would record a liability with a corresponding expense at an amount determined as if the share-based payment had been accounted for as a cash-settled share-based payment transaction.

BC26 Accordingly, the total amount of expense recognised in this approach would represent the measurement determined in accordance with the requirements for either a cash-settled or equity-settled share-based payment transaction.

BC27 On the other hand, Approach 2 is based on the requirements applying to modifications of terms and conditions of a share-based payment transaction. For example, if the share-based payment is reclassified from equity-settled to cash-settled, the cumulative amount of compensation expenses recognised for the equity-settled share-based payment would not be adjusted. After the reclassification date, an amount of the compensation expense is determined in accordance with the requirements for cash-settled share-based payment transactions in paragraphs 30-33 and with the requirements for modifications to terms and conditions of equity-settled share-based payment transactions in paragraphs 26-29 and B42-B44. Thus, if the modification date fair value is greater than the grant date fair value of the equity-settled share-based payment transaction, the incremental fair value would be recognised as an expense over the remainder of the service period (paragraph B43 of IFRS 2). If not, there would be no adjustment to expenses recognised for the equity-settled share-based payment transaction before the reclassification (paragraph B44).

BC28 Adopting Approach 2, the total amount of expense recognised would represent a mix of measurements determined in accordance with the requirements for both cash-settled share-based payment transactions and equity-settled share-based payment transactions.

BC29 The IASB noted that neither approach can directly be derived from the existing requirements in IFRS 2 because the change in classification does not arise from either a failure to satisfy a non-market vesting condition or a modification to terms and conditions of the share-based payment arrangement.

BC30 However, the IASB observed that the measurement in accordance with a new classification better matches the share-based payment transaction, that is a single share-based payment transaction with two settlement alternatives from the inception of the arrangement. The IASB also noted that a change in the estimate for the most probable settlement method is a change in an accounting estimate. The change in the estimate would give rise to changes in liabilities and equity. Thus, the IASB observed that the effects of the change attributable to the period before the change should be recognised in the period of the change (rather than over the remainder of the vesting period) in accordance with paragraph 37 of IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*. Accordingly, the IASB proposes that the entity should measure the goods and services received before the reclassification in accordance with the requirements that apply to a new classification, with any change in the measurement recognised in the period in which the reclassification occurs.

Modifications to cash-settled share-based payment arrangements

Accounting for a change from cash-settled to equity-settled

BC31 The IASB was asked to clarify the accounting for a modification to 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 is replaced by a new equity-settled share-based payment. The IASB learnt that there is significant diversity in practice because IFRS 2 does not provide specific guidance for such situations or general guidance for modifications to terms and conditions of cash-settled share-based payment arrangements.

BC32 The IASB noted that the entity is required to remeasure the liability incurred for a cash-settled share-based payment transaction at the fair value of the liability at the end of each reporting period until the liability is settled (paragraph 30). Accordingly, the IASB observed that the effects of the modifications to terms and conditions of the cash-settled share-based payment would be included in the remeasurement of the fair value of the liability incurred.

BC33 Analysing the situation described in paragraph BC29, the IASB noted that the cancellation of the original cash-settled share-based payment is compensated for by the promise to issue equity instruments. Thus, the IASB observed that the cancellation of the original share-based payment followed by the granting the replacement share-based payment should be viewed as a modification to the terms and conditions of the share-based payment arrangement rather than as a cancellation of the original arrangement followed by the beginning of a new share-based payment. This is consistent with the requirement in paragraph 28, which requires an entity to account for the granting of replacement equity instruments in the same way as a modification of the original grant of equity instruments.

BC34 The IASB considered how the replacement equity-settled share-based payment should be measured. The IASB noted that an equity-settled share-based payment transaction with employees is measured at the fair value of the equity instruments at grant date (paragraph 11). Grant date is defined as “the date at which the entity and another party (including an employee) agree to a share-based payment arrangement, being when the entity and the counterparty have a shared understanding of the terms and conditions of the arrangement". The IASB observed that, in the transaction analysed, the entity and the counterparty have a shared understanding of the terms and conditions of the replacement share-based payment on the date of the modification. At the original grant date, the shared understanding was that the entity would pay cash for services to be rendered by the counterparty. Accordingly, the replacement equity-settled share-based payment should be measured by reference to the modification date fair value of the equity instruments granted.

BC35 Because the share-based payment transaction changes from cash-settled to equity-settled, the transaction should be accounted for as an equity-settled share-based payment from the date of the modification. The IASB observed that the entity should recognise an increase in equity by the amount determined on the basis of the modification date fair value of the equity instruments granted and the extent to which the services have been received before the date of the modification.

BC36 The IASB noted that, as a result of the modification, the liability incurred for the original cash-settled share-based payment is 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. The IASB noted that the liability incurred for the cash-settled share-based payment is ultimately measured at the amount of settlement when it is settled (see paragraph BC249). 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 for the period in accordance with paragraph 30.

Effective date and transition

BC37 The IASB proposes to amend the requirements for measurement of cash-settled share-based payments in some circumstances. It also proposes to require an entity to classify a share-based payment transaction with a contingent settlement feature on the basis of the entity's estimate, as at a point of time in the past, for the manner of settlement in the future. Thus, the IASB was concerned that it could be difficult for most entities to determine the classification of the share-based payment with a contingent settlement feature as at a point of time in the past without using hindsight. Accordingly, the IASB proposes prospective application of these amendments, but permit the entity to apply the amendments retrospectively if it has the information needed to do so without using hindsight.

[Draft] Amendments to the Implementation guidance on IFRS 2 *Share-based Payment*

Paragraphs IG19A, 19B, IG19C, ID19D, IG Example 12A, IG Example 12B and IG Example 12C and a heading before paragraph IG19B are added. Paragraph IG19 is amended. New text is underlined.

Cash-settled share-based payment transactions

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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<u>, on the basis of paragraphs 33-33C,</u> 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~~.~~ <u>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 performance condition.</u>

IG Example 12
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IG Example 12 A
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 (CU1B in sales) at the end of year 3. For simplicity, it is assumed that no employees are expected to leave and that none leave. 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.

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 in which a liability exists as shown below. At the end of Year 3, all SARs held by the remaining employees vest. The intrinsic values of the SARs at the date of exercise (which equal the cash paid out) at the end of Years 3–5 are also shown below.

Year	Fair value of one SAR	Intrinsic value of one SAR
1	CU14.40	
2	CU15.50	
3	CU18.20	CU15.00
4	CU21.40	CU20.00
5		CU25.00

Application of requirements	Num. of employees expected to satisfy the service condition	Estimate of whether the profit target will be met
Year 1	500	No
Year 2	500	Yes
Year 3	350	Yes

Year	Calculation		Expense CU	Liability CU
1	Vesting is not probable: no expense is recognised		0	0
2	Vesting is probable: 500 employees × 100 SARs × CU15.50 × ⅔		516,667	516,667
3	(500 –150) employees × 100 SARs × CU18.20 – CU516,667	120,333		637,000
	+ 150 employees × 100 SARs × CU15.00	225,000		

	Total		345,333	
4	(350 – 150) employees × 100 SARs × CU21.40 – CU637,000	(209,000)		428,000
	+ 150 employees × 100 SARs × CU20.00	300,000		
	Total		91,000	
5	CU0 – CU428,000	(428,000)		0
	+ 200 employees × 100 SARs × CU25.00	500,000		
	Total		72,000	
	Total		1,025,000	

IG19A An entity may modify the terms and conditions of a cash-settled share-based payment transaction. The effects of the modification on the fair value of the liability are recognised in profit or loss as part of the remeasurement of the liability at each reporting date. The modifications of the terms and conditions of the cash-settled share-based payment transaction might involve a change in the settlement method of the share-based payment transaction. The following example illustrates the application of IFRS 2 to modifications of the terms and conditions of cash-settled share-based payments that result in the share-based payment transaction being settled by issuing equity instruments rather than in cash or other assets.

IG Example 12 B

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. The entity estimates that the fair value of the SARs at the end of Year 1 is CU14.40.

At the end of Year 2, the entity cancels the grant of the SARs. At the same time, as a replacement for the cancelled SARs, the entity grants 100 share options with a fair value of CU15.00 to each of its employees remaining at the end of Year 2 on the condition that the employees remain in its employment for the next year.

During year 1, 35 employees leave. The entity estimates that a further 60 will leave during Years 2 and 3. During Year 2, 40 employees leave and the entity estimates that a further 25 will leave during Year 3. During Year 3, 22 employees leave.

Application of requirements

The entity identifies the grant of the share options as the replacement share-based payment for the cancelled SARs. Hence, the entity accounts for the granting of share options as a modification of the original cash-settled share-based payment.

At the modification date, the liability is settled by the grant of share options. In accordance with paragraph 11, the share options granted are measured by reference to the fair value of the share options at grant date. Grant date is defined as the date when the entity and the counterparty have a shared understanding of the terms and conditions of the share-based payment arrangement. In this example, the entity and employees share an understanding of the terms and conditions of the grant of share options on the modification date.

Accordingly, at the modification date, the entity recognises equity for the share options granted that are used to settle the liability at the amount determined on the basis of the fair value of the share options at the modification date and the extent to which the services have been received from the employees. The remuneration expense recognised for the granting of SARs equal the amount of settlement in the share options granted.

Year	Calculation	Expense CU	Equity CU	Liability CU
1	(500-95) employees × 100 SARs x CU14.40 × ⅓	194,400		194,400
2	(500-100) employees x 100 × CU15.00 × ⅔ - 194,400	205,600		400,000
	Reclassify liability to equity		400,000	(400,000)

3	(500-97) employees x 100 × CU15.00 – CU400,000	204,500	604,500
	Total	604,500	

Share based payment transactions with contingent cash settlement provisions

IG19B There are employee share-based payment arrangements in which the employee receives either cash or equity instruments depending on the occurrence or non-occurrence of uncertain future events that are outside the control of both the entity and the employee, such as a successful initial public offering and a change in control of the entity. In this situation, neither the entity nor the employee has the choice of whether the share-based payment arrangement is settled in cash or by issuing equity instruments.

IG19C Paragraphs 33A of IFRS 2 requires an entity to account for the transaction as a cash-settled share-based payment transaction if it is probable that the entity will settle the transaction by transferring cash. If not, the transaction is accounted for as an equity-settled share-based payment transaction.

IC19D The share-based payment may subsequently change from a cash-settled share-based payment transaction to an equity-settled share-based payment transaction or vice versa (ie reclassification of the share-based payment transaction) because of changes in the probability of the cash settlement. Paragraph 33B of IFRS 2 requires the entity to measure the employees' services received until the date of the reclassification in accordance with the requirements that applies to the share-based payment transaction after the reclassification, with any change in the measurement being recognised as compensation expense for the period in which the reclassification occurs. Example 12C illustrates those requirements.

IG Example 12 C

Background

An entity grants to an employee a right to receive an amount of cash equal to the fair value of 100 shares of the entity, on condition that the employee remains in service for three years. If a successful initial public offering (IPO) occurs within the three-year period, the share-based payment arrangement immediately vests and the employee receives 1,000 free shares instead of cash. The shares received by the employee are not transferable for three years after a vesting date.

At the grant date and the end of Year 1, it is not probable that a successful IPO will occur in the next two years. At the end of Year 2, the entity concludes that it is probable that a successful IPO will occur in Year 3. At the end of Year 3, a successful IPO occurs and the employee receives the free shares.

At grant date, the fair value of entity's share is CU20 per share. At the end of Years 1, 2, and 3, the fair value is CU22, CU24, and CU21 respectively. The entity does not expect to pay dividends in the next three years. After taking into account the effects of the post-vesting transfer restrictions, the entity estimates that the grant date fair value of the right to receive a unit of the free shares is CU18.

Application of requirements

Year	Calculation	Expense CU	Equity CU	Liability CU
1	1,000 x CU22 × ⅓	7,333		7,333
2	1,000 x CU24 × ⅔ – CU7,333	8,667		16,000
	Derecognition of the cash-settled share-based payment	(16,000)		(16,000)
	Recognition of the equity-settled share-based payment			
	1,000 × CU18 × ⅔	12,000	12,000	
3	1,000 × CU18 x 3/3 – CU12,000	6,000	18,000	
	Total	18,000		