IFRS

STAFF PAPER

13–14 May 2014

IFRS Interpretations Committee Meeting

IFRS IC Sep and Nov 2013

Project	**Finalisation of agenda decision**
Paper topic	IFRS 2 *Share-based Payment*—price difference between the institutional offer price and the retail offer price for shares in an initial public offering

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This paper has been prepared by the staff of the IFRS Foundation for discussion at a public meeting of the IFRS Interpretations Committee. Comments made in relation to the application of an IFRS do not purport to be acceptable or unacceptable application of that IFRS—only the IFRS Interpretations Committee or the IASB can make such a determination. Decisions made by the IFRS Interpretations Committee are reported in IFRIC *Update*. The approval of a final Interpretation by the Board is reported in IASB *Update*.

Introduction

1. In November 2013, the IFRS Interpretations Committee (the Interpretations Committee) published a tentative agenda decision not to add to its agenda a request to clarify how an entity should account for a price difference between the retail offer price and the institutional offer price (when the retail offer price is lower) for shares issued in an initial public offering (IPO). This difference could arise by either:
   (a) an unintentional difference derived from the book-building process or derived from a change in the fair value of the shares between the time the indicative offer price is set and the time the institutional price is determined; or
   (b) an intentional difference arising from a discount given to retail investors as indicated in the prospectus.
2. The Interpretations Committee observed the guidance in IFRS 2 *Share-based Payment* was not applicable to the fact pattern analysed and observed that consideration received by the issuer from retail investors and from institutional

investors should be recorded in equity in accordance with paragraph 33 of IAS 32 *Financial Instruments: Presentation*[1].

3. The Interpretations Committee considered that in the light of its analysis of the existing IFRS requirements, neither an interpretation nor an amendment to a Standard was necessary and consequently decided to issue a tentative agenda decision that can be found in the IFRIC Update of November 2013.

Purpose of the paper

4. The purpose of this paper is to:

   (a) provide an analysis of the comments received on the tentative agenda decision; and

   (b) set out the wording for the final agenda decision (refer to Appendix A).

Comment letter analysis

5. The comment period for the tentative agenda decision ended on 20 January 2014. We received **three** responses. These comment letters are attached to this paper as **Appendix B**.

6. The first letter (Deloitte) and second letter (AcSB Canada) agree with the Interpretations Committee's decision not to add this item onto its agenda for the reasons set out in the tentative agenda decision.

7. The third letter (PwC) agrees with the Interpretations Committee that it should not to take this issue onto the agenda but not for the reasons set out in the tentative agenda decision.

8. This respondent thinks that the tentative agenda decision, as drafted, will increase the diversity in practice in applying paragraph 13A of IFRS 2 and IFRS 13

[1] The full analysis of this issue was set out in Agenda Paper 15 of September 2013 and in Agenda Paper 8 of November 2013, which can be found on the public website.

Fair Value Measurement and proposes to the Interpretations Committee that it should consider an alternative rationale for not taking this issue onto its agenda.

9. This respondent thinks that the Interpretations Committee should:
   (a) state that the institutional market is likely to be the 'principal market' if the transaction is analysed in accordance with IFRS 13;
   (b) explain the reason why the retail and institutional investors are considered to be trading in two different markets; and
   (c) explain the factors that distinguish the transaction analysed from other transactions that the Interpretations Committee has analysed to which paragraph 13A of IFRS 2 applies.
10. We fully describe and analyse these comments in the following paragraphs.

Staff analysis

The 'principal market' in the transaction analysed

11. The respondent's view is that the institutional market is likely to be the 'principal market'[2] if this transaction is analysed in accordance with paragraph 16 of IFRS 13, because the institutional market will be the one with the greatest volume of activity. Consequently, the respondent thinks that the fair value of the equity instruments issued is the price paid by the institutional investors.

Staff view

12. We note that IFRS 13 provides guidance to assess whether a market is the principal or the most advantageous one for an asset or liability, once a market for an asset or liability has been identified. However, we also note that IFRS 13 does not provide guidance on identifying individual markets.

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[2] Appendix A in IFRS 13 defines the *principal market* as "The market with the greatest volume and level of activity for the asset or liability".

13. Moreover we observe that applying IFRS 13 to identify the principal market in which the shares are offered could lead some to conclude that the institutional offer price is the fair value of the shares and that IFRS 2 could be applied to explain the difference between the retail price and the fair value of the shares. However, we do not think that this conclusion sits easily with the guidance in IFRS 13 and IFRS 2. This is because in accordance with paragraph 6 of IFRS 13, the measurement and disclosure requirements in IFRS 13 do not apply to share-based payment transactions within the scope of IFRS 2.

14. Because the guidance in IFRS 13 should not be applied by analogy to identify the existence of different markets, we think that the agenda decision should not include references to the guidance in IFRS 13. More specifically, we think that the final agenda decision should not refer to the guidance in paragraph B4(d) in IFRS 13 , which clarifies that a transaction price may differ from fair value if the "market in which the transaction takes place is different from the principal market (and most advantageous market)".

The existence of different markets in the transaction analysed

15. The respondent thinks it is unclear why the Interpretations Committee concluded that the retail and institutional investors are considered to be trading in two different markets (the institutional market and the retail market) and that the retail price and institutional price represented the fair value of the equity instruments issued in each of these two markets.

Staff view

16. We agree that the basis for concluding that two different markets exist is not clear in the tentative agenda decision.

17. After publishing the tentative agenda decision we informally queried the submitter (of the original fact pattern analysed) to clarify whether retail and institution investors were able to transact with each other prior to the shares being listed on the stock exchange, because the submission itself did not include this information.

18. The submitter replied that retail and institutional investors are not able to transact with each other before the shares are listed. The submitter also clarified that the offer of shares to institutional and retail investors (prior to the listing of these shares) generally starts at the same time (upon issuance of prospectus) but the institutional offering would generally close later. The submitter observed that all shares will be listed at the same time and that after the shares are listed there is only one market (ie the stock exchange) in which the shares can be traded.

19. We think that the fact that retail and institutional investors are not able to transact with each other before the shares are listed, could provide some evidence of the existence of two different markets (for the retail and institutional investors) before the shares are listed. Nevertheless, we think that such identification is not necessary following the Interpretations Committee's conclusion that paragraph 33 of IAS 32 applies to the fact pattern analysed.

20. We observe that the basic principles in paragraph 33 of IAS 32 to account for an issue of an entity's own equity instruments are that:

    (a) no gain or loss shall be recognised in profit or loss; and

    (b) consideration paid shall be recognised directly in equity.

21. Consequently, when applying the guidance in paragraph 33 of IAS 32 to the fact pattern analysed, the relevant facts are that an entity:

    (a) is issuing its own equity instruments;

    (b) to two different types of investors;

    (c) at different prices.

22. As a result, an entity identifies two distinct transactions (ie the issue of shares to retail and institutional investors) and accounts for them at the amount of the consideration paid by each investor.

23. Consequently we think that the final agenda decision should refrain from mentioning that the difference (if any) between the retail price and the fair value of a share appears to relate to the existence of different markets.

Factors that distinguish the transaction analysed from other transactions

24. The respondent thinks that if the Interpretations Committee decides to proceed with an agenda decision that states that the fact pattern analysed is outside the scope of IFRS 2, the agenda decision should clearly explain the factors that distinguish this transaction from other transactions to which paragraph 13A of IFRS 2 applies, such as for example:

    (a) the Black Economic Empowerment (BEE) arrangements in South Africa that offer a discount on the price of the shares offered to specifically attract a particular investor or class of investor; and

    (b) the fact pattern analysed by the Interpretations Committee back in March 2013 regarding the 'Accounting for reverse acquisitions that do not constitute a business', in which the Interpretations Committee had observed that on the basis of paragraph 13A of IFRS 2, any difference in the fair value of the shares deemed to have been issued by the accounting acquirer and the fair value of the accounting acquiree's identifiable net assets represents a service received by the accounting acquirer (refer to the IFRIC Update from March 2013)

25. The respondent further observes that in the fact pattern analysed, similar to the conclusion reached for the transaction on 'reverse acquisitions that do not constitute a business' (refer to (b) above), the shares are offered to retail investors as a way to ensure that the listing requirements would be met and to ensure that the IPO would be successful. Consequently the respondent thinks that the issuer is receiving a service for the shares offered (ie a stock exchange listing) and disagrees with the Interpretations Committee's conclusion that "the stock exchange listing was not received in exchange for, or conditional on, the issue of the shares for less than fair value".

26. The respondent says that if the Interpretations Committee decides not to provide a definite conclusion on whether the fact pattern analysed is within the scope of IFRS 2, then the agenda decision could state that the fact pattern analysed is very specific and narrow.

27. The respondent also thinks that the scope of paragraph13A in IFRS 2 is not clear and is subject to divergent views and application in practice and thinks that the Interpretations Committee should recommend to the IASB to reconsider that paragraph in a future project.

Staff view

28. We observe that the respondent thinks that the fact pattern analysed (ie raising finance through an IPO) can be analogised to the fact pattern analysed in Example 1 of the Implementation Guidance of IFRS 2 (IG Example 1).

29. In that example, an entity grants shares to parties other than employees, representing historically disadvantaged individuals, as a means of enhancing its image as a good citizen, but the entity is unable to identify the specific consideration received in exchange (ie a service or cash received)[3]. We observe that the transaction described in this example was introduced by IFRIC 8 *Scope of IFRS 2* (which was later incorporated into the guidance of IFRS 2 by amending paragraph 2 and adding paragraph 13A), because the IFRIC and the IASB determined that an entity was unable to specifically identify some or all of the services or goods received.

30. We think that a situation in which an entity raises finance through an IPO is different from the fact pattern analysed in IG Example 1 because the objective is different: in the fact pattern analysed the entity grants shares to investors to raise finance, whereas in IG Example 1 the entity grants shares to enhance its image as a good corporate citizen.

31. However we acknowledge that in the fact pattern analysed some could argue that, similarly to IG Example 1, the issuer of the shares obtained a service from the counterparty in the transaction. This is because some could claim[4] that the discount provided to the retail investors provides a specific benefit to the entity issuing shares. This benefit is the ability to achieve the regulatory requirement of

[3] These arrangements were referred to as 'black economic empowerment', or 'BEE', and were introduced in South Africa.

[4] Some of our staff took this view. Refer to the section on 'Alternative staff view' in Agenda Paper 15 of September 2013.

a minimum number of shareholders, and so the discount provided to the retail investor is the 'cost' of meeting that regulatory requirement. Consequently, some could argue that the entity has issued shares in exchange for a 'service' (ie a listing requirement) from the retail investors and the success of the IPO is conditional on the listing requirements being met.

32. We observe that the Interpretations Committee reached a similar conclusion (ie that the shares had been issued in exchange for a 'service') when it analysed the issue on the 'Accounting for reverse acquisitions that do not constitute a business' (refer to IFRIC Update from March 2013). For this issue the Interpretations Committee stated that (emphasis added):

    (a) any difference in the fair value of the shares deemed to have been issued by the accounting acquirer and the fair value of the accounting acquiree's identifiable net assets represents a service received by the accounting acquirer; and

    (b) regardless of the level of monetary or non-monetary assets owned by the non-listed operating entity, the entire difference should be considered to be payment for a service of a stock exchange listing for its shares, and that no amount should be considered a cost of raising capital.

33. We however, think that IG Example 1 and the two fact patterns analysed by the Intepretations Committee all lead to different accounting because they contain different facts and circumstances. Consequently, in our view if a fact pattern reflects a transaction where an entity is issuing its own shares:

    (a) for cash, this transaction would be accounted for in accordance with IAS 32; and

(b) for receipt of a 'service' (ie obtaining a stock exhange listing from another entity), this transaction would be accounted for in accordance with IFRS 2[5].

34. We think that the current wording in the tentative agenda decision reflects our conclusions above mentioned.

Other considerations identified by the staff

35. We observe that the penultimate paragraph in the tentative agenda decision should be revised because paragraph 33 of IAS 32 does not mention that the equity instruments should be measured at the fair value of the consideration received. We recommend that this paragraph should be corrected as follows:

> The Intepretations Committee noted that in accordance with paragraph 33 of IAS 32 *Financial Instruments: Presentation*, consideration received shall be recognised directly in equity. Furthermore it observed that in accordance with this same paragraph 'no gain or loss shall be recognised in profit or loss on the purchase, sale, issue or cancellation of an entity's own equity instruments'. ~~the equity instruments issued by the entity to the investors should be recognised in equity in accordance with paragraph 33 of IAS 32 Financial Instruments: Presentation and be measured at the fair value of the consideration received.~~

Staff recommendation

36. On the basis of our analysis above, we recommend to the Intepretations Committee that in the final agenda decision it should:

[5] We think that if the purpose is to enlarge the entity's shareholder base (ie not to raise cash), this transaction would also be accounted for in accordance with IFRS 2.

(a) reaffirm its conclusion that IAS 32 applies to account for the fact pattern analysed;

(b) delete any reference to the application of IFRS 13 to the fact pattern analysed to avoid any confusion; more specifically we think that it should delete the reference to paragraph B4(d) in IFRS 13, which specified that a transaction price may differ from fair value if the "market in which the transaction takes place is different from the principal market (and most advantageous market)"; and

(c) refrain from mentioning that the difference (if any) between the retail price and the fair value of a share appears to relate to the existence of different markets; and

(d) revise the penultimate paragraph in the tentative agenda decision.

37. We have set out the wording for the final agenda decision in **Appendix A** of this paper.

Questions for the Interpretations Committee

Questions for the Interpretations Committee
1. Does the Interpretations Committee agree with our recommendations to reaffirm that IFRS 2 does not apply to the fact pattern analysed and to refrain from mentioning the application of the guidance in IFRS 13? 2. Does the Interpretations Committee agree with the revised wording proposed for the agenda decision in Appendix A of this paper?

Appendix A—Tentative agenda decision

A1. We propose the following wording for agenda decision showing changes from the tentative agenda decision. New text is underlined and deleted text is struck through.

IFRS 2 *Share-based Payment*—price difference between the institutional offer price and the retail offer price for shares in an initial public offering

The Interpretations Committee received a request to clarify how an entity should account for a price difference between the institutional offer price and the retail offer price for shares issued in an initial public offering (IPO).

The submitter refers to the fact that the final retail price could be different from the institutional price because of:

(a) an unintentional difference arising from the book-building process; or

(b) an intentional difference arising from a discount given to retail investors by the issuer of the equity instruments as indicated in the prospectus.

The submitter described a situation in which the issuer needs to fulfil a minimum public spread of its shareholdings to qualify for a listing under the stock exchange's regulations in its jurisdiction. This minimum number was achieved through offering shares to retail investors at a discount from the price at which shares were sold to institutional investors.

The submitter asked the Interpretations Committee to clarify whether the transaction should be analysed within the scope of IFRS 2 *Share-based Payment*.

The Interpretations Committee considered whether the transaction analysed involves the receipt of identifiable or unidentifiable goods or services from the retail shareholder group, and therefore whether it is a share-based payment transaction within the scope of IFRS 2. Paragraph 13A of IFRS 2 requires that if consideration received by the entity appears to be less than the fair value of the equity instruments granted or liability incurred, then this situation typically indicates that other consideration (ie unidentified goods or services) has been (or will be) received by the entity. The Interpretations Committee noted that applying this guidance requires judgement and consideration of the specific facts and circumstances of each transaction.

In the circumstances underlying the submission, the Interpretations Committee concluded that IFRS 2 is not applicable because there is no share-based payment transaction. This is because no identified or unidentified goods or services have been (or will be) received. ~~This is because~~ Moreover, it noted that the price agreed ~~between~~ with each shareholder group reflected a transaction to raise funds. Furthermore the retail shareholder group did not provide any goods or services, only the cash consideration to acquire the shares.

The Interpretations Committee noted that in accordance with paragraph 33 of IAS 32 *Financial Instruments: Presentation* consideration received shall be recognised directly in equity. Furthermore it observed that in accordance with this same paragraph "no gain or loss shall be recognised in profit or loss on the purchase, sale, issue or cancellation of an entity's own equity instruments".

~~The Interpretations Committee also noted that the entity has issued shares in two different markets (the institutional market and the retail market). It was unclear from the submission which price (the retail price or the institutional price) represents the fair value of a share in accordance with IFRS 13 Fair Value Measurement. However, IFRS 13 paragraph B4(d) states that a transaction price may differ from fair value if the transaction takes place in a~~

~~market other than the principal market (or most advantageous market). The Interpretations Committee concluded that the difference, if any, between the retail price and the fair value of a share in the fact pattern considered appeared to relate to the existence of different markets rather than the receipt of additional goods or services. Consequently, the Interpretations Committee observed that the guidance in IFRS 2 is not applicable because there is no share-based payment transaction.~~

The Interpretations Committee noted that ~~this situation~~ the issue analysed is different to the issue on which it had issued an agenda decision in March 2013. In that agenda decision ('Accounting for reverse acquisitions that do not constitute a business') the Interpretations Committee had concluded that any difference in the fair value of the shares deemed to have been issued by the accounting acquirer and the fair value of the accounting acquiree's identifiable net assets represents a service received by the accounting acquirer. The Interpretations Committee observed that in that fact pattern, the service received from the other entity was a stock exchange listing for its shares, whereas in the fact pattern considered there is no share-based payment transaction. ~~in this submission the stock exchange listing was received in exchange for, or conditional on, the issue of the shares for less than fair value~~.

~~The Interpretations Committee noted that the equity instruments issued by the entity to the investors should be recognised in equity in accordance with paragraph 33 of IAS 32 *Financial Instruments: Presentation* and be measured at the fair value of the consideration received.~~

On the basis of the analysis above, the Interpretations Committee determined that, in the light of the existing IFRS requirements, sufficient guidance exists and that neither an Interpretation nor an amendment to a Standard was necessary. Consequently, the Interpretations Committee ~~[~~decided~~]~~ not to add this issue to its agenda.

Appendix B – comment letters submitted

(included in the next pages)

Mr Michael Stewart
Director of Implementation Activities
International Accounting Standards Board
30 Cannon Street
London
EC4M 6XH

20 January 2014

Dear Mr Stewart

Tentative agenda decision: IFRS 2 *Share-based Payment* – price difference between the institutional offer price and the retail offer price for shares in an initial public offering

We are responding to your invitation to comment on the above tentative agenda decision, published in the November 2013 edition of IFRIC Update, on behalf of PricewaterhouseCoopers. Following consultation with members of the PricewaterhouseCoopers network of firms, this response summarises the views of member firms who commented on the tentative agenda decision. 'PricewaterhouseCoopers' refers to the network of member firms of PricewaterhouseCoopers International Limited, each of which is a separate and independent legal entity.

We support the committee's decision not to take this question onto the agenda but not for the reasons given. We understand there are different views about the accounting for this type of transaction and we are concerned that the reasons given for the agenda decision will increase diversity in practice regarding the application of IFRS 2 para 13A and may also lead to diversity in the application of IFRS 13.

The tentative agenda decision says that 'it was unclear from the submission which price (the retail price or the institutional price) represents the fair value of a share in accordance with IFRS 13 *Fair Value Measurement*. However, IFRS 13 paragraph B4(d) states that a transaction price may differ from fair value if the transaction takes place in a market other than the principal market (or most advantageous market).' IFRS 13 defines the principal market as the market with the greatest volume and level of activity for the asset or liability. It seems likely in this case that the institutional market is the principal market and thus the fair value of a share is the price paid by the institutional investors.

The tentative agenda decision does not explain clearly the factors that distinguish between the transaction that is the subject of this submission and transactions that are within the scope of IFRS 2, such as the Black Economic Empowerment arrangements in South Africa and similar arrangements in many territories that require local nationals as investors. For example, what distinguishes the lower price offered to retail investors in this case and an IPO that offers a lower price to black investors in South Africa? The price at which the shares are offered reflects a transaction between independent parties in both cases.

The tentative agenda decision states that the Committtee "noted that the entity has issued shares in two different markets (the institutional market and the retail market)". The tentative decision does not explain why retail and institutional investors in an IPO are different markets but BEE credentialed investors and other investors in South Africa or existing customers and other investors are not. What is the distinguishing feature that creates a separate market when all of the investors will subsequently be selling in a single market?

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The tentative agenda decision also states that this fact pattern differs from the reverse acquisition of a listed shell, considered by the Interpretations Committee in their March 2013 agenda decision, because in this case the listing was not conditional on the issue of the shares for less than fair value. This is not necessarily the case because the successful IPO is conditional on the listing requirements being met and it would fail if sufficient retail investors did not subscribe for shares. We believe that the lower subscription price offered to retail investors is a means of ensuring that the listing requirements are met and the IPO is successful.

We suggest that the Committee considers an alternative rationale in which the item is not taken onto the agenda because the issue is territory specific and very narrow. This would avoid creating additional diversity in practice by issuing an agenda decision that expresses a definite conclusion that this transaction is out of the scope of IFRS 2.

If the Committee decides to proceed with an agenda decision that states this transaction is outside the scope of IFRS 2, it is essential that it includes a clear explanation of why this transaction is different from other transactions to which IFRS 2 paragraph 13A applies. This should specifically address the reverse acquisition of a listed entity that does not constitute a business and other transactions in which an entity offers a discount specifically to attract a particular investor or class of investor, such as BEE arrangements in South Africa.

Finally, we note that the scope of IFRS 2 paragraph13A is not clear and is subject to divergent views and application in practice. The Committee might consider recommending to the IASB that this part of IFRS 2 is reconsidered.

If you have any questions in relation to this letter please do not hesitate to contact John Hitchins (020 7804 2497) or Helen Wise (+27 (11) 797 5293).

Yours sincerely

PricewaterhouseCoopers

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January 13, 2014
(via email to ifric@ifrs.org)

IFRS Interpretations Committee
30 Cannon Street, 1st Floor
London EC4M 6XH
United Kingdom

Dear Sirs:

Re: Tentative agenda decision on IFRS 2 Share Based Payment

This letter is the response of the staff of the Canadian Accounting Standards Board (AcSB) to the IFRS Interpretations Committee's tentative agenda decision regarding the price difference between the institutional offer price and the retail offer price for shares in an initial public offering, as published in the November 2013 IFRIC update.

The views expressed in this letter take into account comments from individual members of the AcSB staff but do not necessarily represent a common view of the AcSB or its staff. Views of the AcSB are developed only through due process.

We agree with the Committee's decision not to add this item to its agenda for the reasons provided in the tentative agenda decision.

If you require further information, please contact me at +1 416 204-3276 (email pmartin@cpacanada.ca), or Katharine Christopoulos, Principal, Accounting Standards at +1 416 204-3270 (email kchristopoulos@cpacanada.ca).

Yours truly,

Peter Martin

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Director, Accounting Standards

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Wayne Upton
Chairman
IFRS Interpretations Committee
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Email: ifric@ifrs.org

21 January 2014

Dear Mr Upton

Tentative agenda decision – IFRS 2 *Share-based Payment*: Price difference between the institutional offer price and the retail offer price for shares in an initial public offering

Deloitte Touche Tohmatsu Limited is pleased to respond to the IFRS Interpretations Committee's publication in the November IFRIC Update of the tentative decision not to take onto the Committee's agenda a request for clarification of the accounting for a price difference between the institutional offer price and the retail offer price for shares issued in an initial public offering (IPO).

We agree with the IFRS Interpretations Committee's decision not to add this item onto its agenda for the reasons set out in the tentative agenda decision.

If you have any questions concerning our comments, please contact Veronica Poole in London at +44 (0)20 7007 0884.

Yours sincerely

Veronica Poole
Global IFRS Leader

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