Illustrative example accompanying agenda decision *IAS 33 Earnings per Share—Tax arising from payments on participating equity instruments*

Reference—IAS 33, paragraphs A13 and A14

This example illustrates how an entity (Entity Y) determines profit or loss attributable to ordinary shareholders (ie the numerator in the basic earnings per share (EPS) calculation) over three reporting periods. Entity Y has two classes of equity instruments outstanding—ordinary shares and participating equity instruments. Other facts assumed are as follows:

Participation rights: Participating equity holders participate in dividends with ordinary shareholders according to a 10:1 ratio (except for any distribution relating to the tax benefit—see **Tax deductibility** and **Attribution of the tax benefit** assumptions below).

Tax deductibility: The dividends on participating equity instruments are deductible for tax purposes. Accordingly, such payments reduce taxable income and thus reduce income taxes payable to the taxation authority ('tax benefit').

Attribution of the tax benefit: Ordinary shareholders, not participating equity holders, benefit from the tax benefit.

Tax rate: The tax rate is 30 per cent.

Profit for the year: Entity Y's profit applying IFRS Standards for years 1, 2 and 3 are CU330, CU550 and CU110 respectively—before considering any tax benefit that arises from paying dividends to participating equity holders.

Dividends declared:

Year 1—Entity Y does not declare or pay dividends.

Year 2—at the end of year 2, Entity Y declares and pays dividends for (a) all the profit in year 1 of CU330 and (b) the tax benefit that arises from paying dividends to the participating equity holders.

Year 3—at the end of year 3, Entity Y declares and pays dividends for (a) all the profit in years 2 and 3 and (b) the tax benefit that arises from paying dividends to the participating equity holders.

This table summarises Entity Y's profit, dividends paid and tax benefit in each of the three years:

	Year 1 CU	Year 2 CU	Year 3 CU	Total CU
Profit (before tax benefit)	**330**	**550**	**110**	**990**
Dividends declared and paid (before considering the tax benefit):				
To participating equity holders (in ratio of 10:1) [A]	0	300	600	900
To ordinary shareholders (in ratio of 10:1)	0	30	60	90
	0	**330**	**660**	**990**
Tax benefit from paying dividends [A x 30%]	**0**	**90**	**180**	**270**
Dividends declared and paid relating to the tax benefit:				
To participating equity holders	0	0	0	0
To ordinary shareholders [(a)]	0	90	180	270
	0	**90**	**180**	**270**
Total dividends declared and paid:				
To participating equity holders	0	300	600	900
To ordinary shareholders	0	120	240	360
	0	**420**	**840**	**1,260**

(a) In this example, ordinary shareholders (and not participating equity holders) benefit from the tax benefit. However, if that were not the case, and ordinary shareholders and participating equity holders were to share the tax benefit according to the same ratio as other dividend payments (for example, 10:1 ratio), an entity would allocate the dividend related to the tax benefit using the relevant ratio.

Step 1—adjust profit for the dividends declared

Paragraph A14(a) of IAS 33 states:

> (a) profit or loss attributable to ordinary equity holders of the parent entity is adjusted (a profit reduced and a loss increased) by the amount of dividends declared in the period for each class of shares and by the contractual amount of dividends (or interest on participating bonds) that must be paid for the period (for example, unpaid cumulative dividends).

This table illustrates how Entity Y applies this requirement:

	Year 1 CU	Year 2 CU	Year 3 CU	Total CU
Profit (before tax benefit)	**330**	**550**	**110**	**990**
Tax benefit from paying dividends	0	90	180	270
Profit (after tax benefit) [(a)]	**330**	**640**	**290**	**1,260**
Less total dividends declared and paid (including the tax benefit):				
To participating equity holders	0	(300)	(600)	(900)
To ordinary shareholders	0	(120)	(240)	(360)
	0	**(420)**	**(840)**	**(1,260)**
Remaining profit	**330**	**220**	**(550)**	**0**

(a) In this example, Entity Y recognises the tax benefit arising from the payment of dividends in profit or loss. If an entity were to recognise the tax benefit directly in equity, the entity would adjust profit or loss for the period by the amount of the tax benefit when calculating basic EPS. Paragraph 11 of IAS 33 states: 'The objective of basic earnings per share information is to provide a measure of the interests of each ordinary share of a parent entity in the performance of the entity over the reporting period.' Adjusting profit or loss by the amount of any tax benefit is consistent with the view that the tax benefit represents an interest of the ordinary shareholder.

Step 2—allocate the remaining profit

Paragraph A14(b) of IAS 33 states:

> (b) the remaining profit or loss is allocated to ordinary shares and participating equity instruments to the extent that each instrument shares in earnings as if all of the profit or loss for the period had been distributed….

This table illustrates how Entity Y applies this requirement:

	Year 1 CU	Year 2 CU	Year 3 CU	Total CU
Remaining profit	**330**	**220**	**(550)**	**0**
Allocation:				
To participating equity holders (in ratio of 10:1) [B]	**300**	**200**	**(500)**	**0**
To ordinary shareholders:				
Allocation of remaining profit (in ratio of 10:1)	30	20	(50)	0
Add—tax benefit on hypothetical distribution of profit to participating equity holders [(a)] [B x 30%]	90	60	(150)	0
	120	**80**	**(200)**	**0**

(a) Adjustment to reflect the Committee's conclusion that Entity Y adjusts profit or loss attributable to ordinary shareholders for the portion of any tax benefit attributable to those ordinary shareholders. This tax benefit would arise on the hypothetical distribution of profit to the participating equity holders if all the profit or loss for the period had been distributed. The tax benefit is calculated as the hypothetical distribution to participating equity holders multiplied by the tax rate (ie 30%).

Step 3—add the amount allocated for dividends and for a participation feature

Paragraph A14(b) of IAS 33 states:

> (b) …The total profit or loss allocated to each class of equity instrument is determined by adding together the amount allocated for dividends and the amount allocated for a participation feature.

This table illustrates how Entity Y applies this requirement to calculate profit or loss attributable to ordinary shareholders (ie the numerator for calculating basic EPS):

	Year 1	Year 2	Year 3	Total
	CU	CU	CU	CU
Profit or loss attributable to ordinary shareholders:				
Dividends declared	0	120	240	360
Remaining profit allocated	120	80	(200)	0
	120	**200**	**40**	**360**

Profit or loss attributable to ordinary shareholders

The total profit or loss attributable to ordinary shareholders in each year reflects the ordinary shareholders' share of (i) profit for the year plus (ii) the tax benefit that would arise on the hypothetical distribution of profit for the year to the participating equity holders.

This table illustrates the outcome:

	Year 1	Year 2	Year 3	Total
	CU	CU	CU	CU
Profit or loss attributable to ordinary shareholders:				
(i) Ordinary shareholders' share of profit for the year	30	50	10	90
(ii) Tax benefit on hypothetical distribution of profit to participating equity holders [(a)]	90	150	30	270
	120	**200**	**40**	**360**

(a) Calculated as participating equity holder's share of profits of CU300, CU500 and CU100 in years 1, 2 and 3 respectively multiplied by the tax rate of 30%.