

STAFF PAPER

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IASB Meeting

Project	Annual Improvements to IFRSs 2010–2012 Cycle (ED/2012/1) comment letter analysis		
Paper topic	IFRS 2 <i>Share-based Payment</i> —definition of ‘vesting conditions’		
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Introduction

1. The Exposure Draft (ED) on *Annual Improvements to IFRSs 2010–2012 Cycle* (ED/2012/1) published in May 2012 includes the IASB’s proposal to clarify the definition of *vesting conditions* in Appendix A of IFRS 2 *Share-based Payment* by separately defining a ‘performance condition’ and a ‘service condition’.

Purpose of this paper

2. The objective of this paper is:
 - (a) to present to the IASB the IFRS Interpretation Committee’s (the Interpretation Committee) recommendations on the proposal to amend the definition of *vesting conditions* in Appendix A of IFRS 2 including:
 - (i) a summary of changes that the Interpretations Committee recommends for finalisation in response to the comments received;
 - (ii) the proposed wording for the final amendments as set out in Appendix A of this Agenda Paper; and
 - (b) to get a decision from the IASB on this issue to allow it to be included in the final *Improvements to IFRSs* Standard that is planned to be published in 2013.

Summary of the proposed amendment and the comments received

3. A summary of the proposed amendment and the comments received is described in the paragraphs that follow.
4. For a detailed description of the comments received and the source of those comments, the IASB should refer to [Agenda Paper 15A](#), which was presented to the Interpretations Committee at the January 2013 meeting.¹

Proposed amendment

5. In May 2009, the Interpretations Committee took onto its agenda the project Vesting and Non-vesting Conditions, which relates to share-based payments. The Interpretations Committee analysed each of the issues during several meetings² and sought solutions consistent with the underlying principles in IFRS 2.
6. The main concerns identified were:
 - (a) a lack of clarity in the current definition of vesting conditions in IFRS 2, which incorporates the concepts of service conditions and performance conditions including market conditions (and vesting period);
 - (b) the absence of a definition of non-vesting conditions; and
 - (c) insufficient guidance on the interaction of multiple vesting conditions.
7. The IASB agreed with the Interpretations Committee's view and recommendations about what issues should be included in the Annual Improvements project and what other issues should be considered by the IASB in a future agenda proposal for IFRS 2.
8. The IASB proposed to separately define 'performance condition' and 'service condition' and clarify these definitions. The IASB has addressed the following concerns that were raised about these definitions:

¹ For ease of reference, IASB members will receive a copy of this paper.

² The Interpretations Committee discussed this project at its May 2010 meeting (Agenda Papers 3A–3C); at its July meeting (Agenda Papers 3A–3D); at its September 2010 meeting (Agenda papers 2–2C and Agenda Paper 3); and at its November 2010 meeting (Agenda Paper 2). The IASB discussed the Interpretations Committee's recommendations at the 13–17 September 2010 meeting (Agenda Paper 20) and at the September 2011 meeting (Agenda Paper 7D).

- (a) the correlation between an employee's responsibility and the performance target;
 - (b) whether a share market index target may constitute a performance condition or a non-vesting condition;
 - (c) whether a performance target that refers to a longer period than the required service period may constitute a performance condition; and
 - (d) whether the employee's failure to complete a required service period is considered to be a failure to satisfy a 'service condition'.
9. The IASB decided that it should consider the following issues in a future agenda proposal for IFRS 2:
- (a) to define non-vesting conditions;
 - (b) transactions in which the manner of settlement is contingent on future events;
 - (c) the classification of a non-compete provision; and
 - (d) the accounting for the interaction of multiple vesting conditions.

Summary of the comments received

10. The IASB received 84 comment letters on the ED in total. Approximately two-thirds of the total respondents to this ED expressed their views on the proposed amendment to the definition of vesting conditions in IFRS 2.
11. **Three-quarters** of the respondents who replied to this question (a mix of preparers, users and standard-setters) **agreed** with the proposal to amend the definition of vesting conditions in IFRS 2. This is because they think that the proposed amendment brings clarity and transparency to this definition and eliminates divergence in the application of IFRS 2.
12. **One-quarter** of the respondents agreed in general with the proposal to separately define performance conditions and service conditions; however, they raised some comments on various aspects of the proposed clarifications, as follows:
- (a) whether a performance target can be set by reference to the price (or value) of another entity included within the group;

- (b) whether a performance target that refers to a longer period than the required service period may constitute a performance condition; and whether the specified period of service that the counterparty is required to complete can be either implicit or explicit;
- (c) whether a performance target needs to be influenced by an employee;
- (d) whether a share market index target may constitute a performance condition or a non-vesting condition. If an entity's share price makes up a substantial part of the share market index should it still be considered a non-vesting condition?
- (e) whether the definition of 'performance condition' should indicate that it includes a 'market condition';
- (f) whether a definition of 'non-vesting condition' is needed; and
- (g) whether the employee's failure to complete a required service period is considered to be a failure to satisfy a service condition

13. These comments are discussed below.

(a) Can a performance target also be linked to the performance of another group entity or parent within the group?

14. Respondents observe that it is unclear from the proposed definition of *performance condition* whether conditions linked to the performance of another entity within the same group (ie a parent or another group entity) would be considered to be performance conditions or non-vesting conditions.
15. For instance, in a group structure, some performance targets could be set by reference to the price or value of the equity instruments of another entity included within the group. For example, a subsidiary provides share-based payments to its employees based on the performance of the quoted share price of the parent entity within the group.
16. Respondents note that the proposed definition of a 'performance condition' and 'market condition', as drafted, is capturing performance targets based on the entity's own operations (or activities) or on the price or value of its equity instruments, and not on the performance targets that are set by reference to the

price or value of the equity instruments of another entity that is included within the group.

The Interpretations Committee's view and recommendation

17. The Interpretations Committee recommends that the IASB should amend the second part of the definition of a 'performance condition' and also the definition of a 'market condition' by referring to the equity instruments of both the entity and, if applicable, another entity in the group.
18. This change is in line with the scope of paragraph 3A³ of IFRS 2 and the guidance in paragraphs 43A–43D of IFRS 2 which note that share-based payment transactions also include transactions in which share-based payment transactions might be settled by another group entity (or a shareholder of any group entity) on behalf of the entity receiving the goods or services.
19. Consequently the Interpretations Committee suggests that the IASB state:
 - (a) a performance target should be defined by reference to the entity's (or another group entity's) own operations (or activities) or the price (or value) of the entity's (or another group entity's) equity instruments (including shares and share options); and that
 - (b) a market condition should be based on the market price of the entity's (or another entity in the group's) equity instruments.

(b) Can the period of achieving the performance target exceed the period of service? Should the period of service be implicit or explicit?

20. Some respondents note that:
 - (a) it is unclear whether it was the IASB's intention to exclude performance targets for which the period of achieving the performance target exceeds the period of service in the definitions of 'service condition' and 'performance condition'.

³ Paragraph 3A is part of the amendment made to IFRS 2 in 2009, to incorporate the consensus originally contained in *IFRIC Interpretation 11 IFRS 2—Group and Treasury Share Transactions* (released in 2006). Paragraphs BC268A–BC268S summarise the IASB's considerations when finalising its proposals contained in the Exposure Draft *Group Cash-settled Share-based Payment Transactions* published in December 2007.

- (b) the definition of a ‘performance condition’ includes a requirement to satisfy the ‘performance condition’ while rendering services; that is, “specified performance targets have to be met while the counterparty is rendering the service”. They think that the interaction between a ‘performance condition’ and ‘service condition’ should be made more evident to remain consistent.

The Interpretations Committee’s view and recommendation

- 21. The Interpretations Committee agreed with the views expressed by respondents. It observed that the duration of the performance condition needs to be ‘wholly within the period’ of the related service requirement. This means that the period of the performance target cannot start before the start of the service period and cannot end after the service period. Consequently, the duration of the performance target needs to be within the period of the related service requirement
- 22. The Interpretations Committee therefore, recommends that the IASB should clarify in the definition of a ‘performance condition’:
 - (a) that the duration of the performance target should be wholly within the period of the related service requirement (ie an employee must be rendering a service for the entire period that the performance target is being measured). The Basis for Conclusions should further clarify that performance targets for which the period of achieving the performance target exceeds the period of service are excluded from the definition of performance condition;
 - (b) that the service requirement can either be explicit or implicit. This means that if the share-based payment arrangement does not contain an explicit requirement to provide services, the arrangement may still contain an implicit service condition. The Basis for Conclusions should also explain that this clarification was made to highlight a feature that distinguishes a performance condition from a non-vesting condition: a performance condition has an explicit or implicit service requirement and a non-vesting condition does not, which is consistent with the explanation given in paragraph BC171A of IFRS 2; and

- (c) the words “(ie a ‘service condition’)” should be added after criterion (a) of the proposed definition of performance condition in order to create a cross-reference to the definition of a ‘service condition’.

(c) Does the performance target need to be “influenced by an employee”?

23. Some respondents question why the performance target needs to be within the influence of the employee and one notes that the existence of this level of influence is not always clear. Others are concerned that the wording in the proposed Basis for Conclusions in the ED (paragraphs BC3–BC4) might imply that an entity should give evidence of the correlation between the award and an increase in the performance.

The Interpretations Committee’s view and recommendation

24. The Interpretations Committee observed that in a ‘performance condition’, a performance target is defined “by reference to the entity’s own operations (or activities) or the price (or value) of its equity instruments”. Consequently:
- (a) a performance target needs to reflect the performance of the entity (or the performance of the group or part of the group of which the entity is part); and
 - (b) an entity is not required to demonstrate the correlation between an employee’s responsibility and the performance target in order for that target to be a performance condition.
25. In line with the above, the Interpretations Committee thinks that the IASB should omit the requirement that the target “needs to be within the influence of the employee” to avoid further confusion.

(d) If an entity’s share price makes up a substantial part of the share market index should it still be considered a non-vesting condition?

26. One respondent observes that it is not clear from the drafting in paragraph BC5 of the ED whether a share market index target would still be considered a non-vesting condition if the entity’s share price makes up a substantial part of the index.

27. In addition, one respondent observes that the fact that a share market index target is affected by many external variables and factors should not be given as a reason to support the view that such a target is a non-vesting condition. This is because this respondent thinks that determining whether a performance target is affected by external variables or factors is questionable. In the respondent's view, the fact that a share market index is not related to the performance of the entity should be enough to determine that it is a non-vesting condition.

The Interpretations Committee's view and recommendation

28. The Interpretations Committee observed that a share market index that is related substantially (but not entirely) to the performance of the entity is not a performance target, because it partly reflects the performance of other entities outside the group and the proposed definition of 'performance condition' clearly states that a performance target is defined "by reference to the entity's own operations (or activities) or the price (or value) of its equity instruments".
29. The Interpretations Committee also agreed that the fact that the target might be affected by external variables or factors need not be cited as another decisive reason for not considering it as a performance condition and proposes that the IASB should clarify this fact as part of the amendment.
30. The Interpretations Committee further recommended the IASB to clarify that in *any* circumstance in which a share market index is used as a performance target, it is considered a non-vesting condition because a share market reflects the performance of other entities *outside* the group.

(e) Should the definition of performance condition indicate that it includes a market condition?

31. Some respondents think that the last sentence under the definition of vesting condition (ie "a 'performance condition' might include a 'market condition'") should be moved to the definition of 'performance condition' to improve clarity.

The Interpretations Committee's view and recommendation

32. The Interpretations Committee agrees with the view of those respondents who think that, to avoid confusion, the definition of a 'performance condition' should clearly state that performance conditions include market conditions.
33. This is because it observed that the definition of performance condition implies that if a performance condition is subject to a performance target that is related to the market price of an entity's equity instruments **and** to the completion of a specified period of service, then the market condition becomes a subcomponent of a performance condition.
34. Consequently, the Interpretations Committee suggests that the IASB should:
- (a) delete the last sentence under the definition of vesting condition (ie "a 'performance condition' might include a 'market condition'"); and
 - (b) indicate within the definition of 'performance condition' that performance conditions are either market conditions or non-market conditions.

(f) Is a definition of non-vesting condition needed?

35. A few respondents mentioned that clarity could be improved further in IFRS 2 by defining a 'non-vesting condition'.

The Interpretations Committee's view and recommendation

36. The Interpretations Committee observed that there is no formal definition of non-vesting condition in IFRS 2, but implementation guidance on the difference between vesting and non-vesting conditions is provided in a flowchart in paragraph IG24 of IFRS 2 ("Summary of conditions that determine whether a counterparty receives an equity instrument granted").
37. The Interpretations Committee also observed that the definition of non-vesting condition could be inferred from paragraphs BC170–BC184 of IFRS 2, which clarify the definition of vesting conditions.
38. Consequently the Interpretations Committee does not recommend the IASB to add a definition of 'non-vesting condition' to IFRS 2.

(g) Is the employee's failure to complete a required service period considered to be a failure to satisfy a service condition?

39. Some respondents questioned the IASB's clarification in paragraph BC7 that if the employee fails to complete a service period, the employee fails to satisfy a 'service condition', *regardless of what the reason for that failure is*. They also observe that the accounting consequence is that the compensation expense would therefore need to be reversed if an employee fails to complete a specified service period.
40. The reason why some respondents questioned this issue is because they noted that in some circumstances where an employee is unable to perform the service condition by completing the stipulated service period (such as when the employee is ill or dies in service) it would normally be expected that part of the award would be capable of vesting and that the related compensation expense should not be reversed. They noted that, to the extent that a portion of the award remains capable of vesting, that portion should be recognised as an expense.

The Interpretations Committee's view and recommendation

41. The Interpretations Committee noted that the circumstances that the proposed amendments were referring to were the ones in which the share-based payment did not vest, whereas the comments received all relate to circumstances in which the share-based payments either partly or fully vest on cessation of employment.
42. Consequently, in circumstances where the share-based payment does not vest because of failure to satisfy a vesting condition, paragraph 19 of IFRS 2 states that "on a cumulative basis no amount is recognised for goods or services received if the equity instruments granted do not vest because of a failure to satisfy a vesting condition".
43. The Interpretations Committee observed that in circumstances where:
- (a) the equity instruments either partly or fully vest on cessation of employment, paragraph 23 of IFRS 2 states that "the entity shall make no subsequent adjustment to total equity after vesting date".
 - (b) a grant of equity instruments is cancelled or settled during the vesting period (other than a grant cancelled by forfeiture when the vesting conditions are not satisfied) paragraph 28(a) of IFRS 2

states that: “if the entity shall account for the cancellation or settlement as an acceleration of vesting, and shall therefore recognise immediately the amount that otherwise would have been recognised for services received over the remainder of the vesting period”.

44. Noting the guidance already provided in IFRS 2, the Interpretations Committee’s recommendation to the IASB is that further guidance in IFRS 2 is not necessary.

Transition and effective date

45. Respondents broadly **agreed** with the transition requirements and the effective date of the proposed amendment to IFRS 2. This proposed amendment will be applied in annual periods beginning on or after 1 January 2014 with earlier application permitted.
46. Nevertheless, a small minority of respondents considered that the proposed amendment to IFRS 2 should be applied on a prospective basis rather than retrospectively because they are concerned that changes to the definitions of performance condition and/or service condition may result in changes to the grant date fair value.

The Interpretations Committee’s view and recommendation

47. In view of the comments received, the Interpretations Committee suggests that the amendment to IFRS 2 be applied on a prospective basis rather than on a retrospective basis.

Interpretations Committee recommendation

48. On the basis of the analysis in the previous section, the Interpretations Committee recommends the IASB to proceed with the proposed amendments to the definitions of a ‘vesting condition’, a ‘performance condition’ and a ‘service condition’, but add some further amendments that would make them clearer. The Interpretations Committee also suggests that the amendment to IFRS 2 be applied on a prospective basis rather than on a retrospective basis.
49. The recommended changes are included as appendices:

- (a) **Appendix A** shows the proposed amendment, highlighting differences from the currently effective Standard; and
- (b) **Appendix B** shows revisions to the wording in the previously published Exposure Draft, following the recommendations in this paper.

Question to the IASB

1. Does the IASB agree with the Interpretations Committee's view and recommendations on finalising the amendment to IFRS 2 on the definition of 'vesting conditions', including the proposed wording changes, as described in Appendix A and Appendix B?

Appendix A—Changes for finalising the amendment

C1. The amendment to the definition of vesting conditions is presented below.

The IASB amended IFRS 2 by adding paragraph 63B and amending paragraphs 15 and 19 and Appendix A Defined terms, which is an integral part of the Standard. In Appendix A, the definition of ‘vesting conditions’ and ‘market condition’ are amended and the definitions of ‘performance condition’, ‘service condition’ are added.

The amendment is marked up in the text of IFRS 2 (new text is underlined and deleted text is struck through).

The following Basis for Conclusions accompanies, but is not part of, the amendment. It sets out the reasons why the IASB decided to amend IFRS 2. This basis is included in the Basis for Conclusions on IFRS 2 *Share-based Payment*, which is not part of the Standard.

Equity-settled share-based payment transactions

Transactions in which services are received

- 15 If the equity instruments granted do not vest until the counterparty completes a specified period of service, the entity shall presume that the services to be rendered by the counterparty as consideration for those equity instruments will be received in the future, during the *vesting period*. The entity shall account for those services as they are rendered by the counterparty during the vesting period, with a corresponding increase in equity. For example:
- (a) if an employee is granted share options conditional upon completing three years’ service (ie a *service condition*), then the entity shall presume that the services to be rendered by the employee as consideration for the share options will be received in the future, over that three-year vesting period.
 - (b) if an employee is granted share options conditional upon the achievement of a ~~performance condition~~ *performance condition* and remaining in the entity’s employ until that performance condition is satisfied, and the length of the vesting period varies depending on when that performance condition is satisfied, the entity shall presume that the services to be rendered by the employee as consideration for the share options will be received in the future, over the expected vesting period. ...

Transactions measured by reference to the fair value of the equity instruments granted

Treatment of vesting conditions

- 19 A grant of equity instruments might be conditional upon satisfying a specified *vesting condition* or specified ~~vesting conditions~~ vesting conditions. ...

Effective date

63B *Annual Improvements to IFRSs 2010–2012 Cycle* issued in [date] amended paragraphs 15 and 19 and the definitions of *vesting conditions* and *market condition* and added definitions for *performance condition*, and *service condition* to Appendix A *Defined terms*. An entity shall prospectively apply that amendment to share-based payment transactions for which the grant date is on or after 1 January 2014. Earlier application is permitted. If an entity applies that amendment for an earlier period it shall disclose that fact.

Appendix A

Defined terms

market condition

A condition upon which the exercise price, vesting or exercisability of an **equity instrument** depends that is related to the market price (or value) of the entity's **equity instruments** (or the equity instruments of another entity in the same group), such as:

- (a) attaining a specified share price or a specified amount of **intrinsic value** of a **share option**, or
- (b) achieving a specified target that is based on the market price (or value) of the entity's **equity instruments** (or the equity instruments of another entity in the same group), relative to an index of market prices of **equity instruments** of other entities.

performance condition

A **vesting condition** that requires:

- (a) the counterparty to complete a specified period of service (ie a 'service condition'); and
- (b) specified performance targets to be met while the counterparty is rendering the service required in (a).

The duration of a performance target should be wholly within the period of the related service requirement for it to constitute a performance condition (ie an employee must be rendering service for the duration of the period that the performance target is being measured). The related service requirement can be implicit or explicit.

A performance target is defined by reference to:

- (a) the entity's own operations (or activities) or the operations or activities of another entity in the same group or
- (b) the price (or value) of the entity's **equity instruments** or the equity instruments of another entity in the same group (including shares and **share options**).

A performance target might relate either to the performance of the entity as a whole or to some part of the entity (or part of the group), such as a division or an individual employee.

A performance condition can be a **market condition**

or a non-market performance condition. In a market condition that is a performance condition, the performance target relates to the market price of the equity instruments of an entity. In a non-market performance condition, the performance target is not related to the market price of the equity instruments of an entity.

service condition

A **vesting condition** that requires the counterparty to complete a specified period of service. If the counterparty, regardless of the reason, ceases to provide service during the **vesting period**, the counterparty has failed to satisfy the condition. A 'service condition' does not require a performance target to be met.

vesting conditions

The A conditions that determines whether the entity receives the services that entitle the counterparty to receive cash, other assets or **equity instruments** of the entity, under a **share-based payment arrangement**. A ~~V~~vesting conditions are is either ~~service conditions~~ a **service condition** or ~~performance conditions~~ a **performance condition**. ~~Service conditions require the counterparty to complete a specified period of service. Performance conditions require the counterparty to complete a specified period of service and specified performance targets to be met (such as a specified increase in the entity's profit over a specified period of time). A performance condition~~ **performance condition** might include a **market condition**.

Basis for Conclusions on amendments to IFRS 2 *Share-based Payment*

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

Definition of vesting condition⁴ (2012 amendments)

- BC334 The IASB identified the need to clarify the definition of ‘vesting conditions’ in IFRS 2 to ensure the consistent classification of conditions attached to a share-based payment. Previously, this Standard did not separately define ‘performance condition’ or ‘service condition’, but instead described both concepts within the definition of ‘vesting conditions’.
- BC335 The IASB decided to separate the definitions of ‘performance condition’ and ‘service condition’ from the definition of ‘vesting condition’ to make the description of each condition clearer.
- BC336 In response to the comments received on the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* (Proposed amendments to International Financial Reporting Standards) the IASB addresses the following concerns that have been raised about the definitions of ‘performance condition’, ‘service condition’ and ‘market condition’:
- (a) whether a performance target can be set by reference to the price (or value) of another entity included within the group;
 - (b) whether a performance target that refers to a longer period than the required service period may constitute a performance condition;
 - (c) whether the specified period of service that the counterparty is required to complete can either be implicit or explicit;
 - (d) whether a performance target needs or not to be influenced by an employee;
 - (e) whether a share market index target may constitute a performance condition or a non-vesting condition;
 - (f) whether the definition of ‘performance condition’ should indicate that it includes a ‘market condition’;
 - (g) whether a definition of ‘non-vesting condition’ is needed; and
 - (h) whether the employee’s failure to complete a required service period is considered to be a failure to satisfy a service condition.

⁴Paragraphs BC333 –BC369 are added as a consequence of Annual Improvements to IFRSs 2010–2012 Cycle.

(a) Whether a performance target can be set by reference to another entity (or entities) within the group

- BC337 The IASB decided to clarify that within the context of a share-based payment transaction that is amongst entities in the same group, a performance target can be defined by the price (or value) of the equity instruments of another entity in that group. This amendment is consistent with the guidance in paragraphs 3A and 43A–43D of IFRS 2. Paragraph 3A, which provides guidance about the scope of IFRS 2, states that “a share-based payment transaction may be settled by another group entity (or a shareholder of any group entity) on behalf of the entity receiving or acquiring the goods or services”.
- BC338 The IASB decided to make a similar amendment to the definition of ‘market condition’ to indicate that a market condition can be based on the market price of the entity’s equity instruments or the equity instruments of another entity in the same group.

(b) Whether a performance target that refers to a longer period than the required service period may constitute a performance condition

- BC339 The IASB observed that IFRS 2 did not explicitly require a performance target to coincide with a service requirement for it to constitute a performance condition. Consequently, it does not explicitly require the duration of a performance target to be wholly within the period of the related service requirement for it to constitute a performance condition. For example, some believe that a performance target should be taken to constitute a performance condition even if the achievement of the performance target is assessed over a period that exceeds the period for which the employee is required to provide service.
- BC340 The IASB decided to clarify that the duration of the performance condition needs to be ‘wholly within the period’ of the related service requirement. This means that the period of the performance target cannot start before the start of the service period and cannot end after the service period. Consequently, the duration of the performance target needs to be within the period of the related service requirement. The IASB observed that, otherwise, the generic definition of ‘vesting conditions’ may be compromised where a service is not received during a portion of the performance target period.
- BC341 The IASB also decided to add the words “ie a ‘service condition’” after criterion (a) of the proposed definition of ‘performance condition’ in order to create a cross reference to the definition of ‘service condition’.

(c) whether the specified period of service that the counterparty is required to complete can either be implicit or explicit

BC342 The IASB decided to highlight in the definition of ‘performance condition’ a feature that distinguishes a performance condition from a non-vesting condition in accordance with paragraph BC171A of IFRS 2, namely, that a performance condition has an explicit or implicit service requirement and a non-vesting condition does not. This is so that, in order to constitute a performance condition, a performance target needs to be accompanied by a service requirement that can be implicit or explicit. The IASB observed that if the share-based payment arrangement does not contain an explicit requirement to provide services, the arrangement may still contain an ‘implicit’ service condition.

(d) Whether a performance target needs to be influenced by an employee

BC343 During its deliberations the IASB observed that for a target to constitute a performance condition, the target needs to be “within the influence” of the employee and also in the interest of the entity. Consequently, the IASB proposed that the definition of ‘performance condition’ should make clear that a performance target is defined by reference to the entity’s own operations (or activities) or the price (or value) of its equity instruments (including shares and share options).

BC344 In response to the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* some respondents noticed that the reason why the performance target needed to be within the influence of the employee was unclear and found it to be contradictory to the proposed definition of ‘performance condition’, where the performance target is defined by reference to the performance of the entity, this is, by reference to the entity’s own operations (or activities) or the price (or value) of its equity instruments. Some other respondents also raised some difficulties expected in applying the proposed guidance. In this respect, these respondents noticed that determining whether a performance target is within the influence of the employee would be difficult to apply in the case of a group of entities; for example, the profit or share price of a group of companies could be seen to be ‘remote from the influence of’ an employee of a particular subsidiary of the group.

BC345 The IASB observed that requiring a performance target to be within the influence of the employee could be misinterpreted as meaning that the IASB’s intention was to challenge management to explain how the performance of the employee affects the performance target. The IASB confirmed that it was not its intention to ask an entity to demonstrate how an employee’s performance affects a performance target. The IASB observed that the link between the employee’s service/performance against a given performance target is management’s sole responsibility. It noted that each employee has, in varying degrees, an influence over an entity’s (or group’s) overall performance, that is, over an entity’s (or group’s) own operations (or activities) or the price (or value) of its equity instruments. Consequently, the IASB decided to omit the requirement

that the target “needs to be within the influence of the employee” to avoid further confusion.

- BC346 In its review of the definition of ‘performance condition’ the IASB also considered what, if any, level of correlation is required between an employee’s responsibility and the performance target. Potential diversity in practice had emerged, because some were of the view that if share-based payment awards are granted to employees conditionally on the entity-wide profit, it is not clear that the profit target constitutes a ‘performance condition’ on the basis that the employee might have so little influence on the entity-wide profit that it is not clear whether the target is able to sufficiently incentivise an individual employee’s actions. Others held the view that because the entity is in business in order to make a profit, it is reasonable to assume that all employees contribute directly or indirectly to the entity-wide profit, ie that the whole body of employees contribute towards the entity-wide profit.
- BC347 In the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* the IASB observed that it is reasonable to assume that the performance target that is set by management for an employee’s share-based payment appropriately incentivises the employee to provide an increased quality and/or quantity of service to benefit the entity. Consequently, the IASB decided that the definition of ‘performance condition’ should make clear that a performance target may relate either to the performance of the entity as a whole or to some part it, such as a division or an individual employee.
- BC348 Respondents to the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* questioned whether it was the IASB’s intention to require an entity to demonstrate, or provide evidence of, the correlation between an employee’s responsibility and the performance target in order for that target to be a ‘performance condition’. During its deliberations, the IASB confirmed that it was not the IASB’s intention to require an entity to prove this correlation.

(e) Whether a share market index target may constitute a performance condition or a non-vesting condition

- BC349 The IASB analysed the case in which a share-based payment is conditional on a share market index target and decided whether it would be considered a performance condition or a non-vesting condition. For example, a grant might be conditional on a stock exchange index reaching a specified target and the employee remaining in service up to the date that the target is met.
- BC350 The IASB observed that some might argue that the share market index target with the implicit service requirement constitutes a ‘performance condition’ because an employee is required to provide service to the entity and the time estimated to affect the share market index target implicitly determines how long the entity receives the required service. Others might argue that the share market index target is a non-vesting condition because it is not related to the performance of the entity (ie

instead it is related to or based on the entity's share price and the share price of other unrelated entities).

- BC351 In the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* the IASB observed that the share market index target would be considered a non-vesting condition because it is not related to the performance of the entity or of another entity in the same group, even if the shares of the entity or of another entity in the same group form part of that index. The IASB also observed that a share market index target may be predominantly affected by many external variables or factors involved in its determination, including macroeconomic factors such as the risk-free interest rate or foreign exchange rates, and consequently, it is remote from the influence of the employee.
- BC352 Respondents to the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* agreed that it would be reasonable to assume that the share market index target is a non-vesting condition but some respondents thought that it should not be based on the level of influence exercised by an employee over the performance target or on whether the target is affected by external variables or factors. This is because, in their view, the level of influence and the effect of external variables are subjective reasons that are difficult to measure.
- BC353 The IASB decided to reaffirm its position that a share market index is a non-vesting condition, but, on the basis of the comments received, it will clarify that the reason why it is a non-vesting condition is because a share market index does not only reflect the performance of an entity but, instead, also reflects the performance of other entities outside the group.
- BC354 The IASB also considered a similar case in which the entity's share price makes up a substantial part of the share market index. The IASB determined that even if the entity makes up a substantial part of the share market index it would still be considered a non-vesting condition because it reflects the performance of other entities that are outside the group.

(f) Whether the definition of 'performance condition' should indicate that it includes 'market condition'

- BC355 A respondent to the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* noted that the final sentence of the definition of 'vesting condition' which states that "a performance condition might include a market condition" is contradictory. This is because the respondent observes that a market condition:
- (a) is a target that is related to the market price of the entity's equity instruments; and
 - (b) includes no explicit requirement for the counterparty to complete a specified period of service.
- BC356 The IASB observed that, on the basis of the definition of performance condition, a performance target that is related to the market price of an entity's equity instruments and to the completion of a specified period of service is considered a market (performance) condition. Consequently,

the IASB disagreed that an inconsistency existed in the definitions of performance condition and market condition.

BC357 To avoid confusion in the definitions of ‘performance condition’ and ‘market condition’, the IASB decided to:

- (a) delete the last sentence under the definition of ‘vesting condition’ (ie “a ‘performance condition’ might include a ‘market condition’”); and
- (b) indicate within the definition of ‘performance condition’ that performance conditions are either market conditions or non-market conditions.

(g) Whether a definition of ‘non-vesting condition’ is needed

BC358 Respondents to the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* thought that clarity could be improved further in IFRS 2 by defining a ‘non-vesting condition’.

BC359 The IASB noted that there is no formal definition of non-vesting condition in IFRS 2, but implementation guidance on the split between vesting and non-vesting conditions is provided in a flowchart in paragraph IG24 of IFRS 2 (“Summary of conditions that determine whether a counterparty receives an equity instrument granted”).

BC360 The IASB determined that the creation of a stand-alone definition of non-vesting condition would not be the best alternative for providing clarity on this issue. This is because the IASB observed that the concept of a non-vesting condition can be inferred from paragraphs BC170–BC184 of IFRS 2, which clarify the definition of vesting conditions. In accordance with this guidance it can be inferred that a non-vesting condition is any condition that does not determine “whether the entity receives the services that entitle the counterparty to receive cash, other assets or equity instruments of the entity, under a share-based payment arrangement”. In other words, a non-vesting condition is one that is not a vesting condition. On the basis of its analysis the IASB decided to not add a definition of non-vesting condition.

(h) Whether the employee’s failure to complete a required service period is considered to be a failure to satisfy a service condition

BC361 In considering a possible revision of the definition of ‘service condition’, the IASB observed that in IFRS 2 there is no specific guidance on how to account for a share-based payment award resulting from the entity’s termination of an employee’s employment.

BC362 The IASB noted, however, that paragraph 19 of this Standard regards the employee’s failure to complete a specified service period as a failure to satisfy a service condition. In the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* the IASB proposed to clarify within the definition of ‘service condition’ that if the employee fails to complete a specified service period, the employee fails to satisfy a service condition, regardless of what the reason for that failure is. The

IASB also noted that the accounting consequence is that the compensation expense would therefore need to be reversed if an employee fails to complete a specified service period.

- BC363 Some respondents to the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* thought that more clarity could be provided in the proposed guidance. This is because they noted that in some circumstances where an employee is unable to perform the service condition by completing the stipulated service period (such as when the employee is ill or dies in service) it would normally be expected that part of the award would be capable of vesting and that the related compensation expense should not be reversed. They noted that, to the extent that a portion of the award remains capable of vesting, that portion should be recognised as an expense.
- BC364 In response to the comments received, the IASB noted that the objective of the proposed amendment to the definition of ‘service condition’ is to clarify that the termination of an employee’s employment is a situation where the employee fails to complete a specified service period, and consequently, is considered a situation where the service condition is not met.
- BC365 The IASB observed that in circumstances where equity instruments do not vest because of failure to satisfy a vesting condition, paragraph 19 of IFRS 2 states that “on a cumulative basis no amount is recognised for goods or services received if the equity instruments granted do not vest because of a failure to satisfy a vesting condition”.
- BC366 The IASB observed that in circumstances where the equity instruments either partly or fully vest on cessation of employment, paragraph 23 of IFRS 2 states that “the entity shall make no subsequent adjustment to total equity after vesting date”.
- BC367 The IASB also noted that in accordance with paragraph 28(a), “if a grant of equity instruments is cancelled or settled during the vesting period (other than a grant cancelled by forfeiture when the vesting conditions are not satisfied) the entity shall account for the cancellation or settlement as an acceleration of vesting, and shall therefore recognise immediately the amount that otherwise would have been recognised for services received over the remainder of the vesting period”.
- BC368 Noting the guidance already provided in IFRS 2, the IASB concluded that further guidance was not necessary.

Transition and effective date of the 2012 amendments

- BC369 In response to the comments received the IASB also decided to provide relief in the application of the amendments to the definition of vesting conditions in IFRS 2 by requiring the prospective application of such amendments to share-based payment transactions for which the grant date is on or after 1 January 2014.

Appendix B—Changes from the Exposure Draft published in May 2012 following our recommendations in this paper

B1 The amendment to the definition of vesting conditions is presented below.

The IASB ~~proposes to amend~~ amended IFRS 2 by adding paragraph 63B and amending paragraphs 15 and 19 and Appendix A Defined terms, which is an integral part of the IFRS. In Appendix A, the definitions of ‘vesting conditions’ and ‘market condition’ ~~are~~ is amended and the definitions of ‘performance condition’ and ‘service condition’ are added.

The ~~proposed~~ amendment is marked up in the text of IFRS 2 (new text is underlined and deleted text is struck through). ~~The definition of ‘market condition’ is not proposed for amendment but is included here for ease of reference.~~

The following Basis for Conclusions accompanies, but is not part of, the ~~proposed~~ amendment. It sets out the reasons why the IASB ~~proposes the amendment~~ decided to amend IFRS 2. ~~If the amendment is approved, this~~ This basis will be is included in the Basis for Conclusions on IFRS 2 *Share-based Payment*, which is not part of the IFRS.

Equity-settled share-based payment transactions

...

Transactions in which services are received

...

- 15 If the equity instruments granted do not vest until the counterparty completes a specified period of service, the entity shall presume that the services to be rendered by the counterparty as consideration for those equity instruments will be received in the future, during the *vesting period*. The entity shall account for those services as they are rendered by the counterparty during the vesting period, with a corresponding increase in equity. For example:
- (a) if an employee is granted share options conditional upon completing three years’ service (ie a *service condition*), then the entity shall presume that the services to be rendered by the employee as consideration for the share options will be received in the future, over that three-year vesting period.
 - (b) if an employee is granted share options conditional upon the achievement of a *performance condition* and remaining in the entity’s employ until that performance condition is satisfied, and the length of the vesting period varies depending on when that performance condition is satisfied, the entity shall presume that the services to be rendered by the employee as consideration for the share options will be received in the future, over the expected vesting period. ...

Transactions measured by reference to the fair value of the equity instruments granted

...

Treatment of vesting conditions

- 19 A grant of equity instruments might be conditional upon satisfying a specified *vesting condition* or specified vesting conditions. ...

Effective date

...

- 63B *Annual Improvements to IFRSs 2010–2012 Cycle* issued in [date] amended paragraphs 15 and 19 and the definitions of *vesting conditions* and *market condition* and added definitions for *performance condition*, and *service condition* to Appendix A *Defined terms*. An entity shall prospectively apply that amendment for annual periods beginning to share-based payment transactions for which the grant date is on or after 1 January 2014. Earlier application is permitted. If an entity applies that amendment for an earlier period it shall disclose that fact.

Appendix A (of IFRS 2)

Defined terms

market condition

...

A condition upon which the exercise price, vesting or exercisability of an **equity instrument** depends that is related to the market price (or value) of the entity's **equity instruments** (or the equity instruments of another entity in the same group) such as:

- (a) attaining a specified share price or a specified amount of **intrinsic value** of a **share option**, or
- (b) achieving a specified target that is based on the market price (or value) of the entity's **equity instruments** (or the equity instruments of another entity in the same group), relative to an index of market prices of **equity instruments** of other entities.

...

performance condition

A **vesting condition** that requires:

- (a) the counterparty to complete a specified period of service (ie a 'service condition'); and
- (b) specified performance targets to be met while the counterparty is rendering the service required in (a).

The duration of a performance target should be wholly within the period of the related service requirement for it to constitute a performance condition (ie an employee must be rendering service for the duration of the period that the performance target is being measured). The related service requirement can be implicit or explicit.

A performance target is defined by reference to:

- (a) the entity's own operations (or activities) or the operations or activities of another entity in the same group; or
- (b) the price (or value) of ~~it's~~ the entity's equity instruments or the equity instruments of another entity in the same group (including shares and share options).

A performance target might relate either to the performance of the entity as a whole or to some part of the entity (or part of the group), such as a division

or an individual employee.

A performance condition can be a **market condition** or a non-market performance condition. In a market condition that is a performance condition, the performance target relates to the market price of the equity instruments of an entity. In a non-market performance condition, the performance target is not related to the market price of the equity instruments of an entity.

service condition

A **vesting condition** that requires the counterparty to complete a specified period of service. If the counterparty, regardless of the reason, ceases to provide service during the **vesting period**, the counterparty has failed to satisfy the condition. A ‘service condition’ does not require a performance target to be met.

...

vesting conditions

~~The~~ A conditions that determines whether the entity receives the services that entitle the counterparty to receive cash, other assets or **equity instruments** of the entity, under a **share-based payment arrangement**. A ~~vesting conditions are~~ is either ~~service conditions~~ a **service condition** or ~~performance conditions~~ a **performance condition**. ~~Service conditions require the counterparty to complete a specified period of service. Performance conditions require the counterparty to complete a specified period of service and specified performance targets to be met (such as a specified increase in the entity’s profit over a specified period of time). A performance condition~~ **performance condition** might include a **market condition**.

Basis for Conclusions on amendments to IFRS 2 *Share-based payment*

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

Definition of vesting condition⁵ (2012 amendments)

BC1334 The IASB identified the need to clarify the definition of ‘vesting conditions’ in IFRS 2 to ensure the consistent classification of conditions attached to a share-based payment. Previously, this IFRS did not separately define ‘performance condition’ or ‘service condition’, but instead described both concepts within the definition of ‘vesting condition’.

BC2335 The IASB decided to separate the definitions of a ‘performance condition’ and a ‘service condition’ from the definition of a ‘vesting condition’ and thus make the description of each condition clearer.

BC3336 ~~In its proposed revision, the Board:~~ In response to the comments received on the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* the IASB addresses the following concerns that have been raised about these definitions: of a ‘performance condition’, ‘service condition’ and ‘market condition’:

- ~~(a) the correlation between an employee’s responsibility and the performance target;~~
- ~~(b) whether a share market index target may constitute a performance condition or a non-vesting condition;~~
- ~~(c) whether a performance target that refers to a longer period than the required service period may constitute a performance condition; and~~
- ~~(d) whether the employee’s failure to complete a required service period is considered to be a failure to satisfy a service condition.~~
- (a) whether a performance target can be set by reference to the price (or value) of another entity included within the group;
- (b) whether a performance target that refers to a longer period than the required service period may constitute a performance condition;
- (c) whether the specified period of service that the counterparty is required to complete can either be implicit or explicit;
- (d) whether a performance target needs or not to be influenced by an employee;
- (e) whether a share market index target may constitute a performance condition or a non-vesting condition;
- (f) whether the definition of ‘performance condition’ should indicate that it includes a ‘market condition’;

⁵Paragraphs BC333–BC369 are added as a consequence of *Annual Improvements to IFRSs 2010–2012 Cycle*.

- (g) whether a definition of ‘non-vesting condition’ is needed; and
- (h) whether the employee’s failure to complete a required service period is considered to be a failure to satisfy a service condition.

(a) Whether a performance target can be set by reference to another entity (or entities) within the group

BC337 The IASB decided to clarify that within the context of a share-based payment transaction that is amongst entities in the same group, a performance target can be defined by the price (or value) of the equity instruments of another entity in that group. This amendment is consistent with the guidance in paragraphs 3A and 43A–43D of IFRS 2. Paragraph 3A, which provides guidance about the scope of IFRS 2, states that “a share-based payment transaction may be settled by another group entity (or a shareholder of any group entity) on behalf of the entity receiving or acquiring the goods or services”.

BC338 The IASB decided to make a similar amendment to the definition of ‘market condition’ to indicate that a market condition can be based on the market price of the entity’s equity instruments or the equity instruments of another entity in the same group.

(b) Whether a performance target that refers to a longer period than the required service period may constitute a performance condition

BC6339 The IASB observed that the IFRS 2 did not explicitly require a performance target to coincide with a service requirement for it to constitute a performance condition. However, the Board noted that the definition of ‘vesting conditions’ makes clear that a vesting condition (including a performance condition) must “determine whether the entity receives the services that entitle the counterparty to receive” the share-based payment. In addition, paragraph BC171A elaborates on the definition of a ‘vesting condition’ by highlighting a feature that distinguishes a performance condition from a non-vesting condition: a performance condition has an explicit or implicit service requirement and a non-vesting condition does not. Consequently, the Board proposes to make clear the length of the performance period within the definition of ‘performance condition’. This is so that, in order to constitute a performance condition, any performance target needs to have an explicit or implicit service requirement for at least the period during which the performance target is being measured. Consequently, it does not explicitly require the duration of a performance target to be wholly within the period of the related service requirement for it to constitute a performance condition. For example, some believe that a performance target should be taken to constitute a performance condition even if the achievement of the performance target is assessed over a period that exceeds the period for which the employee is required to provide service.

BC340 The IASB decided to clarify that the duration of the performance condition needs to be ‘wholly within the period’ of the related service requirement. This means that the period of the performance target cannot start before the start of the service period and cannot end after the service period. Consequently, the duration of the performance target needs to be within the period of the related service requirement. The IASB observed that, otherwise, the generic definition of ‘vesting conditions’ may be compromised where a service is not received during a portion of the performance target period.

BC341 The IASB also decided to add the words “(ie a ‘service condition’)” after criterion (a) of the proposed definition of ‘performance condition’ in order to create a cross reference to the definition of a ‘service condition’.

(c) whether the specified period of service that the counterparty is required to complete can be either implicit or explicit

BC342 The IASB decided to highlight in the definition of ‘performance condition’ a feature that distinguishes a performance condition from a non-vesting condition in accordance with paragraph BC171A of IFRS 2, namely, that a performance condition has an explicit or implicit service requirement and a non-vesting condition does not. This is so that, in order to constitute a performance condition, a performance target needs to be accompanied by a service requirement that can be implicit or explicit. The IASB observed that if the share-based payment arrangement does not contain an explicit requirement to provide services, the arrangement may still contain an ‘implicit’ service condition.

(d) whether a performance target needs to be influenced by an employee

BC343 During its deliberations the IASB observed that for a target to constitute a performance condition, the target needs to be “within the influence” of the employee and also in the interest of the entity. Consequently, the IASB proposed that the definition of ‘performance condition’ should clarify that a performance target is defined by reference to the entity’s own operations (or activities) or the price (or value) of its equity instruments (including shares and share options).

BC344 In response to the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* some respondents noticed that the reason why the performance target needed to be within the influence of the employee was unclear and found it to be contradictory to the proposed definition of ‘performance condition’, where the performance target is defined by reference to the performance of the entity, this is, by reference to the entity’s own operations (or activities) or the price (or value) of its equity instruments. Some other respondents also raised some difficulties expected in applying the proposed guidance. In this respect, these respondents noticed that determining whether a performance target is within the influence of the employee would be difficult to apply in the case of a group of entities; for example, the profit or share price of a

group of companies could be seen to be ‘remote from the influence of’ an employee of a particular subsidiary of the group.

BC345 The IASB observed that requiring a performance target to be within the influence of the employee could be misinterpreted as meaning that the IASB’s intention was to challenge management to explain how the performance of the employee affects the performance target. The IASB confirmed that it was not its intention to ask an entity to demonstrate how an employee’s performance affects a performance target. The IASB observed that the link between the employee’s service/performance against a given performance target is management’s sole responsibility. It noted that each employee has, in varying degrees, an influence over an entity’s (or group’s) overall performance, that is, over an entity’s (or group’s) own operations (or activities) or the price (or value) of its equity instruments. Consequently, the IASB decided to omit the requirement that the target “needs to be within the influence of the employee” to avoid further confusion.

BC346 In its review of the definition of a ‘performance condition’ the IASB also considered what, if any, level of correlation is required between an employee’s responsibility and the performance target. Potential diversity in practice had emerged because some were of the view that if share-based payment awards are granted to employees conditional on the entity-wide profit, it is not clear that the profit target constitutes a ‘performance condition’ on the basis that the employee might have so little influence on the entity-wide profit that it is not clear that the target is able to sufficiently incentivise an individual employee’s actions. Others held the view that because the entity is in business in order to make a profit, it is reasonable to assume that all employees contribute directly or indirectly to the entity-wide profit, ie that the whole body of employees contribute towards the entity-wide profit.

Correlation between an employee’s responsibility and the performance target

BC4347 In the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* In its review of the definition of a ‘performance condition’, the Board IASB observed that it is reasonable to assume that the performance target set by management for an employee’s share-based payment appropriately incentivises the employee to provide an increased quality and/or quantity of service to benefit the entity. Consequently, the Board IASB ~~proposed~~ decided that the definition of a ‘performance condition’ should make clear that a performance target may relate either to the performance of the entity as a whole or to some part of the entity, such as a division or an individual employee.

BC348 Respondents to the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* questioned whether it was the IASB’s intention to require an entity to demonstrate, or provide evidence of, the correlation between an employee’s responsibility and the performance target in order for that target to be a ‘performance condition’. During its deliberations, the IASB confirmed that it was not the IASB’s intention to require an entity to prove this correlation.

(e) Whether a share market index target may constitute a performance condition or a non-vesting condition

- BC5 ~~The Board noted that for a target to constitute a performance condition, the target needs to be ‘within the influence of’ the employee and also in the interest of the entity. The Board observed that a share market index target may be predominantly affected by many external variables or factors involved in its determination, including macroeconomic factors such as the risk-free interest rate or foreign exchange rates. It is therefore remote from the influence of the employee. Accordingly, the Board observed that the share market index target is a non-vesting condition because it is not related to the performance of the entity, even if the entity’s shares form part of that index. Consequently, the Board proposes that the definition of a ‘performance condition’ should make clear that a performance target is defined by reference to the entity’s own operations (or activities) or the price (or value) of its equity instruments (including shares and share options).~~
- BC349 The IASB analysed the case in which a share-based payment is conditional on a share market index target and decided whether it would be considered a performance condition or a non-vesting condition. For example, a grant might be conditional on a stock exchange index reaching a specified target and the employee remaining in service up to the date that the target is met.
- BC350 The IASB observed that some might argue that the share market index target with the implicit service requirement constitutes a ‘performance condition’ because an employee is required to provide service to the entity and the time estimated to affect the share market index target implicitly determines how long the entity receives the required service. Others might argue that the share market index target is a non-vesting condition because it is not related to the performance of the entity (ie instead it is related to or based on the entity’s share price and the share price of other unrelated entities).
- BC351 In the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* the IASB observed that the share market index target would be considered a non-vesting condition because it is not related to the performance of the entity or of another entity in the same group, even if the shares of the entity or of another entity in the same group form part of that index. The IASB also observed that a share market index target may be predominantly affected by many external variables or factors involved in its determination, including macroeconomic factors such as the risk-free interest rate or foreign exchange rates, and consequently, it is remote from the influence of the employee.
- BC352 Respondents to the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* agreed that it would be reasonable to assume that the share market index target is a non-vesting condition but some respondents thought that it should not be based on the level of influence exercised by an employee over the performance target or on whether the target is affected by external variables or factors. This is because, in their view,

the level of influence and the effect of external variables are subjective reasons that are difficult to measure.

BC353 The IASB decided to reaffirm its position that a share market index is a non-vesting condition, but, on the basis of the comments received, it will clarify that the reason why it is a non-vesting condition is because a share market index does not only reflect the performance of an entity but, instead, also reflects the performance of other entities outside the group.

BC354 The IASB also considered a similar case in which the entity's share price makes up a substantial part of the share market index. The IASB determined that even if the entity makes up a substantial part of the share market index it would still be considered a non-vesting condition because it reflects the performance of other entities outside the group.

(f) whether the definition of 'performance condition' should indicate that it includes a 'market condition'

BC355 A respondent to the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* noted that the final sentence of the definition of 'vesting condition' which states that "a performance condition might include a market condition" is contradictory. This is because the respondent observes that a market condition:

(a) is a target that is related to the market price of the entity's equity instruments; and

(b) includes no explicit requirement for the counterparty to complete a specified period of service.

BC356 The IASB observed that, on the basis of the definition of performance condition, a performance target that is related to the market price of an entity's equity instruments and to the completion of a specified period of service, is considered a market (performance) condition. Consequently, the IASB disagreed that an inconsistency existed in the definitions of performance condition and market condition.

BC357 To avoid confusion in the definitions of 'performance condition' and 'market condition', the IASB decided to:

(a) delete the last sentence under the definition of 'vesting condition' (ie "a 'performance condition' might include a 'market condition'"); and

(b) indicate within the definition of 'performance condition' that performance conditions are either market conditions or non-market conditions.

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BC358 Respondents to the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* thought that clarity could be improved further in IFRS 2 by defining 'non-vesting condition'.

- BC359 The IASB noted that there is no formal definition of non-vesting condition in IFRS 2, but implementation guidance on the difference between vesting and non-vesting conditions is provided in a flowchart in paragraph IG24 of IFRS 2 (“Summary of conditions that determine whether a counterparty receives an equity instrument granted”).
- BC360 The IASB determined that the creation of a stand-alone definition of non-vesting condition would not be the best alternative for providing clarity on this issue. This is because the IASB observed that the concept of a non-vesting condition can be inferred from paragraphs BC170–BC184 of IFRS 2, which clarify the definition of vesting conditions. In accordance with this guidance it can be inferred that a non-vesting condition is any condition that does not determine “whether the entity receives the services that entitle the counterparty to receive cash, other assets or equity instruments of the entity, under a share-based payment arrangement”. In other words, a non-vesting condition is one that is not a vesting condition. On the basis of its analysis the IASB decided to not add a definition of non-vesting condition.

(h) Whether the employee’s failure to complete a required service period is considered to be a failure to satisfy a service condition

- BC7361 In considering a possible revision of the definition of ‘service condition’, the IASB observed that in IFRS 2 there is no specific guidance on how to account for a share-based payment award resulting from the entity’s termination of an employee’s employment. ~~The Board noted, however, that paragraph 19 of this IFRS regards the employee’s failure to complete a specified service period as a failure to satisfy a service condition. Consequently, the Board proposes to make clear within the definition of a ‘service condition’ that if the employee fails to complete a specified service period, the employee fails to satisfy a service condition, regardless of what the reason for that failure is. The accounting consequence is that the compensation expense would therefore need to be reversed if an employee fails to complete a specified service period.~~
- BC362 The IASB noted, however, that paragraph 19 of this Standard regards the employee’s failure to complete a specified service period as a failure to satisfy a service condition. In the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* the IASB proposed to clarify within the definition of ‘service condition’ that if the employee fails to complete a specified service period, the employee fails to satisfy a service condition, regardless of what the reason for that failure is. The IASB also noted that the accounting consequence is that the compensation expense would therefore need to be reversed if an employee fails to complete a specified service period.
- BC363 Some respondents to the Exposure Draft *Annual Improvements to IFRSs 2010–2012 Cycle* thought that more clarity could be provided in the proposed guidance. This is because they noted that in some circumstances where an employee is unable to perform the service

condition by completing the stipulated service period (such as when the employee is ill or dies in service) it would normally be expected that part of the award would be capable of vesting and that the related compensation expense should not be reversed. They noted that, to the extent that a portion of the award remains capable of vesting, that portion should be recognised as an expense.

BC364 In response to the comments received, the IASB noted that the objective of the proposed amendment to the definition of ‘service condition’ is to clarify that the termination of an employee’s employment is a situation where the employee fails to complete a specified service period, and consequently, is considered a situation where the service condition is not met.

BC365 The IASB observed that in circumstances where equity instruments do not vest because of failure to satisfy a vesting condition, paragraph 19 of IFRS 2 states that “on a cumulative basis no amount is recognised for goods or services received if the equity instruments granted do not vest because of a failure to satisfy a vesting condition”.

BC366 The IASB observed that in circumstances where the equity instruments either partly or fully vest on cessation of employment, paragraph 23 of IFRS 2 states that “the entity shall make no subsequent adjustment to total equity after vesting date”.

BC367 The IASB also noted that in accordance with paragraph 28(a), “if a grant of equity instruments is cancelled or settled during the vesting period (other than a grant cancelled by forfeiture when the vesting conditions are not satisfied) the entity shall account for the cancellation or settlement as an acceleration of vesting, and shall therefore recognise immediately the amount that otherwise would have been recognised for services received over the remainder of the vesting period”.

BC368 Noting the guidance already provided in IFRS 2, the IASB concluded that further guidance was not necessary.

Transition and effective date of the 2012 amendments

BC369 In response to the comments received the IASB also decided to provide relief in the application of the amendments to the definition of vesting conditions in IFRS 2 by requiring the prospective application of such amendments to share-based payment transactions for which the grant date is on or after 1 January 2014.