STAFF PAPER

November 2015

REG IASB Meeting

IFRS IC meeting: July 2015

Project	**Narrow-scope amendment—IFRS 2 (ED/2014/5) Classification and Measurement of Share-based Payment Transactions**
Paper topic	Summary of the Interpretations Committee's recommendations

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Introduction

1. In November 2014 the IASB published the Exposure Draft ('the ED') ED/2014/5 *Classification and Measurement of Share-based Payment Transactions (Proposed amendments to IFRS 2 Share-based Payment)*, which contained proposals to address:

   (a) the effects of vesting conditions on the measurement of a cash-settled share-based payment;

   (b) the classification of share-based payment transactions with net settlement features; and

   (c) the accounting for a modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled.

2. At the July 2015 meeting, the Interpretations Committee was presented with a summary and an analysis of the 70 comment letters received on the ED. The Interpretations Committee discussed the comments received and the staff recommendations and decided to propose that the IASB should finalise the three proposed amendments, subject to some revisions to the proposed wording. The *IFRIC Update* for the Interpretations Committee meeting in July 2015 summarises all the decisions made at that meeting.

3. For a detailed description of the comments received and of the comment letter analysis discussed by the Interpretations Committee, refer to Agenda Paper 2 and Agenda Paper 2A (suggested wording), both papers presented at the July 2015 meeting.

4. **Appendix A** of this paper summarises the issues raised by respondents to the ED for which the Interpretations Committee did not consider that further clarification was needed.

Purpose of this paper

5. The purpose of this paper is to:

   (a) present to the IASB the Interpretations Committee's recommendations on the proposed amendments to IFRS 2 that it discussed at its meeting in July 2015;

   (b) address some specific concerns raised by some members of the Interpretations Committee that they thought should be addressed when finalising the amendments; and

   (c) obtain an IASB decision on the finalisation of these proposed amendments.

6. Agenda Paper 12A is provided to illustrate the wording changes described in this paper and to provide context for the discussion. However, we are not asking the IASB to approve specific wording or to provide specific comments on the wording unless those comments are about the principles. We will collect editorial comments from IASB members later and not in the meeting.

Description of the issues

Effects of vesting conditions on the measurement of a cash-settled share-based payment

7. Paragraph 33 of IFRS 2 requires an entity to measure the liability for a cash-settled share-based payment initially and at the end of each reporting period until settled, at the fair value of the cash-settled share-based payment. This measurement involves

taking into account the terms and conditions on which the cash-settled share-based payment was granted and the extent to which the employees have rendered service to date. However, IFRS 2 does not specifically address the impact of vesting and non-vesting conditions on the measurement of the fair value of the liability incurred in a cash-settled share-based payment transaction.

8. The IASB proposed to clarify that accounting for the effects of vesting and non-vesting conditions on the measurement of a cash-settled share-based payment should follow the approach used for measuring equity-settled share-based payments in paragraphs 19-21A of IFRS 2. In accordance with this guidance the fair value of the individual equity instruments granted at grant date is not adjusted for the probability of satisfying service and/or a non-market performance condition and requires adjusting that fair value for the probability of satisfying market conditions and non-vesting conditions. At grant date the entity estimates the number of awards for which the service and/or a non-market performance condition is expected to be satisfied. Subsequently, the entity adjusts the number of awards to reflect the number of awards for which the service and/or performance condition is expected to be satisfied and finally for the number of awards for which the service and/or performance condition is actually satisfied.

Classification of share-based payment transactions with net settlement features

9. An entity may be obliged by tax laws or regulations to withhold an amount for an employee's tax obligation associated with share-based payments and then transfer the amount, normally in cash, to the taxation authorities. To fulfil this obligation, the terms of some employee share-based payment arrangements permit or require the entity to deduct (from the total number of equity instruments that would otherwise be issued to the employee upon exercise (or vesting) of the share-based payment), the number of equity instruments needed to equal the monetary value of the employee's tax obligation in order to meet the statutory tax withholding obligation.

10. Under the current requirements in paragraph 34 of IFRS 2, the transaction with net settlement features would have been bifurcated into an equity-settled component and a

cash-settled component and each would be accounted for in accordance with how each component is settled.

11. The amendments propose an exception to the requirements in IFRS 2 to remove the requirement to bifurcate if certain conditions are met. These amendments were proposed to reduce operational complexity and avoid an undue burden in applying the requirements in IFRS 2. The IASB proposes to specify that if the entity settles the share-based payment arrangement net by withholding a specified portion of the equity instruments to meet the statutory tax withholding obligation, then the transaction should be classified as equity-settled in its entirety. However, this would only be applicable if the entire share-based payment would otherwise have been classified as equity-settled if it had not included the net settlement feature.

Accounting for a modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled

12. Modifications to the terms and conditions of a cash-settled share-based payment may cause its classification to change to an equity-settled share-based payment. In other circumstances, an entity might replace a cash-settled share-based payment with a new equity-settled share-based payment. IFRS 2 does not specifically address such situations.

13. The IASB proposed to amend IFRS 2 so that:

   (a) the share-based payment transaction is measured by reference to the modification-date fair value of the equity instruments that are granted as a result of the modification;

   (b) the liability recognised in respect of the original cash-settled share-based payment is derecognised upon the modification, and the equity-settled share-based payment is recognised in equity to the extent that the services have been rendered up to the modification date; and

   (c) the difference between the carrying amount of the liability as at the modification date, and the amount recognised in equity at the same date, is recorded in profit or loss immediately.

Transition guidance

14. The IASB also proposed to require prospective application for the proposed amendments and allow entities to perform retrospective application if the necessary information to do so is available without the use of hindsight.

Main comments raised by respondents

15. The IASB received 70 comment letters on the ED[1].

16. Most respondents broadly support the proposals. They think that the proposed amendments provide practical solutions and reduce the risk of diversity in practice in the application of IFRS 2. However, some respondents requested further clarification or simplification of the proposed amendments.

17. A majority of respondents agreed with the proposed prospective application of the amendments, but requested further guidance on the transition and on the application of the proposed amendments to new awards and existing unvested awards.

18. Some respondents expressed concern about the number of recent separate narrow-scope amendments that the IASB has recently made to IFRS 2 or that had been proposed for the future. They think that the IASB should instead undertake a Post-implementation Review of IFRS 2.

The Interpretations Committee's recommendations

19. The Interpretations Committee discussed the issues that had been identified by respondents in respect of the three amendments included in the ED. The Interpretations Committee recommends finalising these amendments subject to some clarifications and revisions to the wording. In the following section we describe the recommendations from the Interpretations Committee.

[1] These comment letters can be accessed via the following link: http://www.ifrs.org/Current-Projects/IASB-Projects/IFRS-2-Clarifications-Classification-and-Measurement/ED-November-2014/Pages/Comment-letters.aspx

Effects of vesting conditions on the measurement of a cash-settled share-based payment

20. The following paragraphs describe the Interpretations Committee's recommendations with respect to the proposed amendments about the effects of vesting conditions on the measurement of a cash-settled share-based payment.

Include some wording changes in paragraphs 19 and 33 of IFRS 2

21. Some respondents to the ED observed that the proposed wording added to paragraph 33 of IFRS 2 (regarding the effects of vesting conditions on the measurement of a cash-settled share-based payment) could imply that all vesting conditions (ie including market and non-vesting conditions) should be taken into account when adjusting the number of instruments included in the measurement of a share-based payment transaction.

22. The Interpretations Committee agreed that the proposed amendments to paragraph 33 of IFRS 2 were potentially misleading. Consequently, it recommends to the IASB that it should include some wording changes in paragraph 33 of IFRS 2 (and make some similar changes in paragraph 19 of IFRS 2) to clarify that the impact of market and non-vesting conditions should not be taken into account when adjusting the number of instruments included in the measurement of a share-based payment transaction.

State that the proposed guidance to account for the effects of vesting and non-vesting conditions applies to all cash-settled share-based payments

23. Respondents to the ED noted that the guidance in paragraph 33 for measuring the liability incurred in a cash-settled share-based payment appeared to apply more specifically to 'share appreciation rights' whereas the proposed guidance in paragraphs 33A–33C of the ED (which provided guidance on measuring the effects of vesting and non-vesting conditions on a cash-settled share-based payment) appeared to apply more broadly to all cash-settled share-based payments.

24. The Interpretations Committee agreed with the respondents that there seemed to be an inconsistency between the proposed guidance in paragraphs 33A–33C of the ED and the wording in paragraph 33. Consequently, it recommends to the IASB that it should indicate in the main body of the Standard that the guidance on measuring the liability

incurred (ie included in paragraphs 30–33D, refer to Agenda Paper 12A) should be applied to all cash-settled awards and that share appreciation rights are an example of cash-settled share-based payment transactions.

Classification of share-based payment transactions with net settlement features

25. The following paragraphs describe the Interpretations Committee's recommendations with respect to the proposed amendments about the classification of share-based payment transactions with net settlement features.

The proposed classification for a share-based payment transaction with net settlement features is an exception to the requirements to IFRS 2

26. Some respondents observed that the proposed classification for the share-based payment transaction with net settlement features should not be categorised as an exception to the requirements in IFRS 2, because the employer does not control or bear risks associated with the portion of equity instruments withheld and the entity transfers cash to a third party (ie the tax authority) rather than to the counterparty in the share-based payment (ie the employee).

27. The Interpretations Committee disagreed with the respondents, because the entity settles the employee's tax obligation by using its own cash resources rather than by issuing equity. Moreover, it observed that the amount to be withheld and paid to the tax authorities is a liability for the entity.

28. The Interpretations Committee recommends to the IASB that it should retain the existing scope of the proposed exception to require the share-based payment transaction with net settlement features to be classified as equity-settled in its entirety. In addition, the Interpretations Committee suggests to the IASB that it should reinforce the reasons in the Basis for Conclusions why the proposed classification represents an exception to the requirements in IFRS 2. In this respect, the Interpretations Committee proposes that this could be done by stating that (a) the payment to the tax authority represents in substance a payment to the employee, regardless of the fact that the tax authority is the one receiving the cash payment; and

(b) the entity settles the employee's tax obligation by using its own cash rather than by issuing equity.

Include an example illustrating the accounting for a share-based payment transaction with net settlement features

29. Some respondents thought that it would be useful if the IASB were to add an example illustrating the application of the proposed guidance in paragraph 33E of the ED (which sets out the accounting for a share-based payment transaction with net settlement features).

30. The Interpretations Committee agreed with this suggestion and recommends that the IASB should add Example 12B (refer to Agenda Paper 12A) to the implementation guidance in IFRS 2 to illustrate the accounting for the transaction with net settlement features described in paragraph 33D.

Provide guidance to account for any difference that may arise between the compensation cost recognised during the vesting period and the amount of the cash that needs to be paid to the tax authority

31. Some respondents to the ED observed that paragraph 33D (which sets out the accounting for a share-based payment transaction with net settlement features) in the ED did not specifically address the accounting for any difference that may arise between the compensation cost recognised during the vesting period and the amount of the cash that needs to be paid to the tax authority (ie the proposed paragraph 33D in the ED broadly referred to the application of paragraphs 10–29 of IFRS 2).

32. The Interpretations Committee agreed that former paragraph 33D (now paragraph 33E) is silent about the accounting for the cash paid to the tax authority. Consequently, it recommends to the IASB that it should clarify that if there is a difference between the compensation cost recognised during the vesting period and the amount of cash paid to the tax authority this difference should be accounted for in accordance with paragraph 29 of IFRS 2 (ie as a deduction from equity, but with any

amount paid in excess of the fair value of the shares that were withheld being recognised as an expense in profit or loss)[2].

33. The Interpretations Committee further noted that as explained in paragraph BC12 of the ED, paragraph 29 of IFRS 2 is applied on the assumption that the share-based payment transaction is considered as being settled entirely in equity instruments with a separate, yet simultaneous, repurchase of a portion of those equity instruments. The entity then remits the cash for the repurchased equity instruments to the taxation authority on behalf of the employee to settle the employee's tax obligation.

Add a disclosure to inform users about the expected tax withholding obligation incurred as a result of a share-based payment transaction

34. The Interpretations Committee observed that a consequence of applying equity-settled accounting to a share-based payment transaction with net settlement features is that an entity recognises:

(a) compensation cost over the vesting period based on grant-date fair value; and

(b) an adjustment in equity (in accordance with paragraph 29 of IFRS 2) when entity pays cash to the tax authority. This adjustment reflects the difference between the compensation cost recognised during the vesting period and the settlement-date fair value of the shares that are net-settled (ie the amount of cash paid).

35. Some members of the Interpretations Committee expressed concern that there could be a significant true-up adjustment (that would be recorded in equity in accordance with paragraph 29 of IFRS 2). This is because the cash payable would reflect settlement-date fair value, whereas the compensation cost recognised during the vesting period would reflect grant-date fair value. Moreover, some members observed that because the adjustment in equity is not recorded until settlement date, this results in a misleading representation of the cost over the vesting period.[3]

[2] Refer to paragraph 33G in Agenda Paper 12A (November 2015).

[3] Example 12B in Agenda Paper 12A (November 2015) provides an illustration of the accounting for a share-based payment transaction with net settlement features.

36. To address the concern raised, some members of the Interpretations Committee recommended to the IASB that it should require a disclosure of the estimated amount of cash that an entity will pay in connection with the withholding of the employee's tax obligation for a share-based payment, indicating when such amount of cash is expected to be paid. The Interpretations Committee observed that such disclosure will be useful to inform users of the amount and timing of the expected cash payment.

37. The Interpretations Committee observed that some may argue that requiring such disclosure might not be necessary, because paragraph 50 of IFRS 2 contains a general disclosure requirement to 'disclose information that enables users of the financial statements to understand the effect of share-based payment transactions on the entity's profit or loss for the period and on its financial position'. In this respect, the Interpretations Committee observed that the disclosure requirement in paragraph 50 is too general and that the IASB should require a specific disclosure.

38. Consequently, the Interpretations Committee recommends the IASB to add the proposed disclosure to paragraph 51, because this paragraph requires some disclosures that give effect to the general principle in paragraph 50 of IFRS 2. This proposed disclosure is shown in Agenda Paper 12A.

Provide guidance when an entity withholds a higher number of shares

39. Some respondents noted that the proposed amendment did not clarify the accounting when an entity withholds from the employee's compensation a higher number shares (than it needed) to satisfy the employee's tax obligation. For example, one respondent noted that in its jurisdiction a flat statutory rate does not exist and entities often do not know the precise amount of the tax withholding obligation. This respondent noted that in this case, entities calculate the number of shares needed to meet the tax withholding obligation on the basis of the maximum tax rate applicable, which results in the withholding of a number of shares that is too high in relation to the actual tax withholding when it becomes payable[4].

40. The Interpretations Committee recommends to the IASB that it should address the accounting for the situation raised by the respondents in circumstances in which such

[4] Refer to paragraphs 86–101 in Agenda Paper 2 (July 2015).

an amount is paid in cash or other assets to the employee, rather than paid in shares. In this respect the Interpretations Committee observes that if the entity withholds a higher number of shares in this circumstance, the entity should reverse, after the vesting period, the amount recognised in equity for the shares withheld in excess and account for this excess as a cash-settled share-based payment[5].

Accounting for a modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled

41. The following paragraphs describe the Interpretations Committee's recommendations with respect to the proposed amendments about the accounting for a modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled.

Recognising the difference in value between the original and the new award in profit or loss is consistent with the accounting for the extinguishment of a financial liability

42. Some respondents were of the view that the difference between the carrying amount of the liability at the modification date and the amount recognised in equity at the same date should not be recognised in profit or loss and should instead be recognised over the remaining service period. This is because they observed that this accounting was more consistent with the guidance in paragraphs 26–27 of IFRS 2 (and corresponding application guidance in paragraphs B42–B44) for modifications to equity-settled share-based payment arrangements in which incremental fair value has been granted.

43. The Interpretations Committee disagreed with the respondents' view because as paragraph BC18 of the ED explains, the IASB decided not to apply by analogy the guidance in paragraphs 27 and B42–B44 of IFRS 2 (applicable to modifications of equity-settled share-based payments).

44. Moreover, the Interpretations Committee observed that recognising the difference in value between the original and the new award in profit or loss is consistent with the

[5] Refer to paragraph 33H in Agenda Paper 12A (November 2015).

accounting for the extinguishment of a financial liability (that has been extinguished fully or partially by the issue of equity instruments) in paragraph 3.3.3 of IFRS 9 *Financial Instruments* and with paragraph 9 of IFRIC Interpretation 19 *Extinguishing Financial Liabilities with Equity Instruments*.

45. The Interpretations Committee recommends to the IASB that it should reinforce the reasons why the difference between the liability derecognised and the amount of equity recorded at the modification date is recognised in profit or loss. The Interpretations Committee suggests that this could be done by explaining in the Basis for Conclusions that recognising the difference in value between the original and the new award in profit or loss is consistent with the accounting for the extinguishment of a financial liability (that has been extinguished fully or partially by the issue of equity instruments) in paragraph 3.3.3 of IFRS 9 and with paragraph 9 of IFRIC Interpretation 19.

Add an example illustrating the accounting for a modification of a share-based payment transaction

46. Some respondents thought that it would be useful if the IASB was to add an example illustrating the accounting for a modification of a share-based payment transaction that changes the classification from cash-settled to equity-settled (in accordance with the requirements in proposed paragraph B41A of the ED).[6]

47. The Interpretations Committee agreed with the respondents' suggestion and recommends to the IASB that it should add Example 12C to the implementation guidance in IFRS 2. This example (shown in Agenda Paper 12A) illustrates a modification of the terms and conditions of a cash-settled share-based payment that results in a change in the classification of the share-based payment transaction from cash-settled to equity-settled as a result of issuing replacement awards.

The modifications guidance applies when the modification occurs outside or within the vesting period or when the vesting period is extended or shortened

48. Some respondents to the ED questioned whether the guidance in proposed paragraph B41A of the ED would also apply to a situation in which the modification extends the

[6] This paragraph was renumbered as paragraph B44A. Refer to Agenda Paper 12A.

vesting period of the share-based payment transaction or when the modification occurs outside the vesting period.[7]

49. The Interpretations Committee observed that the proposed accounting for a modification that changes its classification for cash-settled to equity-settled would apply when:

    (a) the change in classification (from a cash-settled to equity-settled) occurs outside or within the vesting period; or

    (b) the vesting period is extended or shortened.

50. It further noted that in accordance with the proposed paragraph B41A of the ED, any difference between the fair value of the liability at the modification date and the fair value of the equity instruments promised in settlement should be recognised immediately in profit or loss at the date of the modification by reference to the modified vesting period.

51. The Interpretations Committee recommends to the IASB that it should make the aspects mentioned above explicit in the proposed amendment (ie paragraph B44A). Consequently, the Interpretations Committee recommends to the IASB that it should specify that a change in classification from a cash-settled award to an equity-settled award can occur during or outside the vesting period and that when the vesting period is extended or shortened; when these situations occur an entity should follow the requirements in paragraph B44A. The entity should consequently recognise any difference between the cash-settled award (recognised as a liability) and the amount of the equity-settled award (recognised in equity) immediately in profit or loss for the accrued portion of each award by reference to the modified vesting period[8].

52. In addition, at its July 2015 meeting, the Interpretations Committee analysed an example of the accounting for a modification in which the vesting period is extended (the solution provided in this example is in accordance with paragraph B44A). The Interpretations Committee did not propose adding this example to the implementation

[7] Ibid.

[8] We have included this guidance in paragraph B44A of the amendment. Refer to Agenda Paper 12A.

guidance in IFRS 2, but we show this example below to illustrate the Interpretations Committee's views.

Example of a modification from cash-settled to equity-settled when the vesting period is extended

An employee is granted a cash-settled share-based payment with a vesting period of one year. The total fair value of the cash-settled liability is CU100[9]. The cash-settled award is replaced by an equity-settled award shortly before the end of Year 1, which has a further one-year vesting period from the modification date.
The fair value of the equity-settled award at the modification date is CU150.
In the period prior to modification the entity has recorded a cumulative expense of CU100.

<u>Solution</u>

- At the modification date the entity determines the difference between: the value of the original award (CU 100) and the proportionate amount of the equity-settled award based on this award, which is 50 per cent through its total vesting period of two years CU75 (CU150 × ½).
- The difference is a gain of CU 25 (CU 100 – CU 75) which is recognised immediately in profit or loss.
- The entity derecognises the liability and reclassifies it to equity.
- A future expense of CU 75 (CU150 × ½) is recognised over the remaining vesting period from the modification date (ie Year 2).

Dr Liability	100	
Cr Expense (gain)		*25*
Cr Equity		*75*

Recognition of a credit in profit or loss.
Reclassification of the liability to equity in Year 1.

Dr Expense	75	
Cr Equity		*75*

For the recognition of incremental expense in Year 2.

State that when new equity instruments are granted as replacement equity instruments for a cash-settled SBP that has been cancelled or settled, the entity should apply the guidance for modification accounting

53. The Interpretations Committee expressed concern that the wording in paragraph B41B of the ED (which applies to cash-settled awards that have been cancelled or settled and replaced by equity-settled awards) appeared to be introducing an accounting policy choice about whether or not an entity has designated an equity-settled award as

[9] In this paper, currency accounts are denominated in 'currency units' (CU).

a replacement of a cancelled or settled cash-settled award.[10] This paragraph is reproduced below (emphasis added):

> B41B A cash-settled share-based payment may be cancelled or settled (other than a grant that is cancelled by forfeiture when the vesting conditions are not satisfied). If equity instruments are granted and, **on the date when those equity instruments are granted, the entity identifies them as replacement equity instruments for the cancelled cash-settled share-based payment,** the entity shall account for the granting of the replacement equity instruments in accordance with the guidance in paragraph B41A.

54. Moreover, the members of the Interpretations Committee noted that the proposed amendment did not provide specific guidance:

    (a) that would help in the identification of whether the new equity instruments granted are in fact replacing the cash-settled award; or

    (b) in situations in which the cash-settled award has not been, in fact, been identified as being replaced with the new grant of equity instruments.

55. The Interpretations Committee was of the view that it was not the intention of the IASB to introduce an accounting policy choice. The Interpretations Committee also observed that the wording in the proposed paragraph B41B of the ED is consistent with the use of the word 'identifies' in paragraph 28(c) of IFRS 2.[11] This paragraph is reproduced below (emphasis added):

> (c) if new equity instruments are granted to the employee and, on the date when those new equity instruments are granted, **the entity identifies the new equity instruments granted as replacement equity instruments for the cancelled equity instruments**, the entity shall account for the granting of replacement equity instruments in the same way as a modification of the original grant of equity instruments, in

[10] This paragraph has been renumbered as paragraph B44B.

[11] Paragraph 28(c) includes guidance for new equity instruments that are granted as replacement equity instruments for the cancelled equity instruments.

accordance with paragraph 27 and the guidance in Appendix B.

56. Furthermore, the Interpretations Committee was not of the view that the IASB should provide further guidance on how an entity should perform such an identification. In the Interpretations Committee's view, the facts and circumstances should be analysed in order to determine whether the cash-settled award has been replaced by the 'new' equity-settled award. Consequently, if an entity:

(a) identifies the new equity instruments as replacement for the cash-settled award, the entity should apply the guidance in paragraph B44A (previously paragraph B41A).

(b) does not identify the new equity instruments granted as a replacement for the cash-settled award, the entity should remeasure the fair value of the cash-settled award at the date of cancellation or settlement (in line with paragraph 30 of IFRS 2). Because the cash-settled award has been cancelled (or settled) the cash-settled award will be remeasured to an amount of zero. The entity would thereby reverse the cumulative expense that had been previously recognised, and the entity would account for the new equity instruments as a new grant of equity instruments.

57. To address the views of the Interpretations Committee, we propose adding to the Basis for Conclusions a paragraph explaining that in applying the accounting in accordance with paragraph B44B[12], the facts and circumstances should be analysed in order to determine whether the cash-settled award has been replaced by the equity-settled award. We also suggest adding that if the entity identifies the new equity instruments as a replacement for the cash-settled award, the entity should follow the requirements in paragraph B44A. Otherwise, the entity would have to remeasure the fair value of the cash-settled award at the date of cancellation or settlement to an amount of zero; reverse the cumulative expense that had been previously recognised; and account for the new equity instruments as a new grant of equity instruments.

[12] Previously, paragraph B41B in the ED.

Transition arrangements for the proposed amendments

58. Some respondents were of the view that the proposed transition guidance was unclear about whether the proposed amendments were intended to be applied only to new awards or to new and outstanding (non-vested) awards. Some respondents were also unclear about how the proposed amendments would be applied to unvested, share-based payments.

59. The Interpretations Committee agreed with the respondents who think that the transition provisions were not clear. This is because it observed that the proposed effective date paragraph in the ED (paragraph 63D) was silent about whether the proposed amendments would be applied to new or unvested awards (or both); whereas the explanations in paragraph BC22 of the ED stated that the three amendments included in the ED should be applied to new awards and outstanding awards.

60. The Interpretations Committee observed that modifications are event-driven, so it proposes that for modifications that change the classification from cash-settled to equity-settled, the new accounting would apply to the modifications that occur after the date the amendments are first applied.

61. The Interpretations Committee observed that for existing unvested cash-settled awards that are subject to vesting and non-vesting conditions, an entity would need to adjust the carrying amount of the liability in the statement of financial position in the period of change on the date the amendment is first applied and to recognise the effect of the change, ie any cumulative catch-up adjustment, in equity (ie retained earnings) at the beginning of the annual period in which the amendment is first applied.

62. The Interpretations Committee observed that the amendment for awards with net settlement features addresses not only a change in measurement but also a change in classification. Consequently, the Interpretations Committee observed that at the date the amendment is first applied an entity would need to assess the existing unvested arrangements with net settlement features that have been classified as cash-settled or that have been classified using a ‘bifurcation’ approach (ie in accordance with paragraph 34 of IFRS 2). If the entity reaches the conclusion that such arrangements should be classified as equity-settled, the entity would reclassify the current carrying value of the liability into equity. An entity would need to adjust the measurement of

the unvested award due to the new classification. This adjustment should be recognised in equity (ie retained earnings) at the beginning of the period when the amendment is first applied

63. The Interpretations Committee also recommends to the IASB that it should state that for all the three proposed amendments no adjustment should be made to comparative information.

64. The Interpretations Committee further noted that the IASB allows an entity to apply the three amendments retrospectively (in accordance with IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors*) provided that the entity has the information necessary to do so and this information is available without the use of hindsight.

Summary of proposed changes to respond to recommendations from the Interpretations Committee

65. The Interpretations Committee recommends to the IASB that it should finalise the proposed three amendments, subject to some clarifications and revisions to the wording. The changes to the draft wording in the proposed amendments to IFRS 2 that respond to recommendations from the Interpretations Committee are summarised below.

66. Regarding the proposed amendment about the effects of vesting conditions on the measurement of a cash-settled share-based payment, the Interpretations Committee recommends to the IASB that it should:

    (a) include some wording changes in paragraphs 19 and 33 of IFRS 2 to clarify that the impact of market and non-vesting conditions should not be taken into account when adjusting the number of instruments included in the measurement of a share-based payment transaction.

    (b) indicate in the main body of the Standard that the guidance for measuring the liability incurred (ie in paragraphs 30–33D) should be applied to all cash-settled awards and that share appreciation rights are an example of cash-settled share-based payment transactions.

67. Regarding the proposed amendments about the classification of share-based payment transactions with net settlement features, the Interpretations Committee recommends to the IASB that it should:

(a) retain the existing scope of the proposed exception to require the share-based payment transaction with net settlement features to be classified as equity-settled in its entirety. In addition, the Interpretations Committee suggests to the IASB that it should reinforce the reasons in the Basis for Conclusions why the proposed classification represents an exception to the requirements in IFRS 2. The Interpretations Committee proposes that this could be done by stating that (a) the payment to the tax authority represents in substance a payment to the employee, regardless of the fact that the tax authority is the one receiving the cash payment; and (b) the entity settles the employee's tax obligation by using its own cash rather than by issuing equity

(b) include an example in the implementation guidance of IFRS 2 illustrating the application of the proposed guidance in paragraph 33E (which sets out the accounting for a share-based payment transaction with net settlement features). The Interpretations Committee recommends adding Example 12B for this purpose.

(c) clarify that if there is a difference between the compensation cost recognised during the vesting period and the amount of cash paid to the tax authority this difference should be accounted for in accordance with paragraph 29 of IFRS 2 (ie as a deduction from equity, but with any amount paid in excess of the fair value of the shares that were withheld being recognised as an expense in profit or loss).

(d) add a requirement in a new paragraph 51(c) to require the disclosure of the estimated amount of cash that an entity will pay in connection with the withholding of the employee's tax obligation for a share-based payment transaction, indicating when such an amount of cash is expected to be paid.

(e) clarify that an entity might have withheld a higher number of equity instruments than the number of equity instruments needed to equal the monetary value of the statutory tax withholding obligation. In such a case, after the vesting period, the entity should reverse the amount recognised in equity for the shares withheld in excess and account for this excess as a cash-settled share-based payment (if such an amount was paid in cash or other assets to the employee).

68. Regarding the proposed amendments about the accounting for a modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled, the Interpretations Committee recommends to the IASB that it should:

(a) reinforce the reasons why the difference between the liability derecognised and the amount of equity recorded at the modification date is recognised in profit or loss. This could be done by explaining in the Basis for Conclusions that recognising the difference in value between the original and the new award in profit or loss is consistent with the accounting for the extinguishment of a financial liability (that has been extinguished fully or partially by the issue of equity instruments) in paragraph 3.3.3 of IFRS 9 and with paragraph 9 of IFRIC Interpretation 19.

(b) add an example to the implementation guidance in IFRS 2 to illustrate a modification of the terms and conditions of a cash-settled share-based payment that results in a change in the classification of the share-based payment transaction from cash-settled to equity-settled as a result of issuing replacement awards. The Interpretations Committee recommends adding Example 12C for this purpose.

(c) specify in paragraph B44A that the guidance in this paragraph should be applied when a change in classification from a cash-settled award to an equity-settled award occurs either during or outside the vesting period; and when the vesting period is extended or shortened.

(d) specify in the Basis for Conclusions that in applying paragraph B44B, the facts and circumstances should be analysed in order to determine whether the cash-settled award has been replaced by an equity-settled award.[13] If the entity identifies the new equity instruments as a replacement for the cash-settled award, the entity should follow the requirements in paragraph B44A. Otherwise, the entity would have to remeasure the fair value of the cash-settled award at the date of cancellation or settlement to an amount of zero, reverse the cumulative expense that had been previously recognised, and account for the new equity instruments as a new grant of equity instruments.

69. The Interpretations Committee recommends to the IASB that the transition guidance for the amendments to IFRS 2 should be as follows:

(a) for modifications that change the classification from cash-settled to equity-settled, the new accounting would apply to the modifications that occur after the date the amendments are first applied.

(b) for cash-settled share-based payments that are subject to vesting and non-vesting conditions, an entity shall adjust the carrying amount of the liability in the statement of financial position in the period of change on the date the amendment is first applied, and recognise the effect of the change retained earnings (or another appropriate component of equity) at the beginning of the annual period in which the amendment is first applied.

(c) for awards with net settlement features; an entity shall reclassify the current carrying value of the liability to equity for those awards (or components of awards) that were accounted for as cash-settled awards but which now meet the criteria to be accounted for as equity-settled awards. This reclassification shall be recognised in equity at the beginning of the annual period in which the amendment is first applied.

70. The Interpretations Committee notes that an entity may apply instead the three amendments retrospectively (in accordance with IAS 8) provided that the entity has the information necessary to do so and this information is available without the use of hindsight.

[13] Formerly paragraph B41B in the ED.

Questions to the IASB

Questions
1. Does the IASB agree with the Interpretations Committee's recommendation to finalise the three proposed amendments to IFRS 2? 2. Does the IASB agree with the recommended revisions to the proposed amendment to IFRS 2 in response to the Interpretations Committee's recommendations as described above?

Appendix A—issues raised by respondents to the ED for which the Interpretations Committee did not consider that further clarification was needed

A1. The following table shows issues raised by respondents to the ED for which the Interpretations Committee did not consider that further clarification was needed.

Request analysed by the Interpretations Committee	Reason why the Interpretations Committee does not propose that the IASB should take any further action
Add guidance to IFRS 2 to determine the best available estimate (of the number of instruments that will effectively vest) in paragraph 20 of IFRS 2 (which provides guidance to account for equity-settled awards subject to vesting conditions) and the proposed paragraph 33A of the ED (which provides guidance to account for cash-settled awards subject to vesting conditions).	The Interpretations Committee observed that adding guidance to determine the best available estimate (of the number of instruments that will effectively vest) is an issue that is too complex to be addressed as part of a narrow-scope amendment to IFRS 2.
Add a stand-alone requirement for the disclosure of a contingent liability when vesting is not probable and no liability is recognised (as illustrated in Example 12A in the ED).	The Interpretations Committee considered that the disclosure of a contingent liability when vesting is not probable is not needed. This is because it observed that IFRS 2 contains a general requirement in paragraph 50 to 'disclose information that enables users of the financial statements to understand the effect of share-based payment transactions on the entity's profit or loss for the period and on its financial position'.
Add examples to the implementation guidance of IFRS 2 to illustrate the effects of vesting and non-vesting conditions on the measurement of cash-settled awards.	The Interpretations Committee observed that the implementation guidance in IFRS 2 includes a number of examples that illustrate the effects of vesting and non-vesting conditions in measuring equity-settled awards. Consequently, the Interpretations Committee considers that these illustrations could be applied by analogy in measuring cash-settled awards.
Clarify whether the classification exception in the proposed paragraph 33D (which provides guidance to account for share-based payment transactions with net settlement features) is available for other arrangements in which entities are obliged to withhold an employee's tax obligation[14].	The Interpretations Committee noted that the proposed classification exception would apply to a limited type of tax withholding arrangement in which an entity has a statutory obligation to withhold the tax associated with an employee's share-based payment.[15] It further noted that the proposed amendment should not specify the circumstances in which the proposed exception would not apply, because management should use its judgement in applying the proposed guidance.

[14] In paragraphs 77–85 of Agenda Paper 2 (July 2015) we analysed some situations that respondents claim are similar in substance to the arrangement with net settlement features described in the ED.

[15] In this respect there was a proposal by some Interpretations Committee members to modify the heading before paragraph 33D to indicate that the proposed exception applies to a limited type of award with net settlement features (as described in paragraph 33D). We amended this heading as proposed (refer to Agenda Paper 12A).

Request analysed by the Interpretations Committee	Reason why the Interpretations Committee does not propose that the IASB should take any further action
Determine whether any further amendments to IFRS 2 are needed to converge with the FASB's potential improvements to the accounting for share-based payment awards with net settlement features under its *Employee Share-Based Payment Accounting Improvements* project. The FASB's proposal allows an employer with a statutory income tax withholding obligation to repurchase an employee's shares to cover income taxes on the award without triggering liability accounting, as long as the value of the shares repurchased does not exceed the amount calculated using the *highest applicable marginal tax rate* in the applicable jurisdiction.	The Interpretations Committee determined that no additional clarification or amendment is needed in the light of the FASB's proposals for changes to US GAAP regarding the accounting for share-based payment awards with net-settlement features. The Interpretations Committee observed that the proposal in paragraph 33D of the ED does not restrict the amount withheld to a minimum or to a maximum amount; and requires the entire award to be classified as equity-settled.
Clarify the accounting treatment when the replacement award has a lower fair value than the original award at the modification date.	The Interpretations Committee observed that no clarification is needed because the proposed paragraph B41A states that (emphasis added) '**any** difference between the liability derecognised and the amount of equity recorded is recognised immediately in profit or loss'. Consequently, the Interpretations Committee thought that this guidance would apply to replacement awards that have either a higher or lower fair value.
Clarify the accounting for other types of modifications of share-based payments.	The Interpretations Committee observed that the implementation guidance in IFRS 2 could be used as guidance to account for modifications from equity-settled to cash-settled (for example, Example 9, which illustrates a grant of shares to which a cash alternative is subsequently added). It further observed other types of modifications could potentially be addressed as part of the IASB's research project on share-based payments.