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Clarifying share-based payment accounting

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"The amendments resolve some long-standing ambiguities in share-based payment accounting and go a long way toward improving consistency."

– Kim Heng, KPMG's global IFRS employee benefits leader

Amendments to IFRS 2 clarify the accounting for certain types of arrangements

Highlights

- Measurement of cash-settled awards – Use same approach as equity-settled awards
- Classification of awards settled net of tax withholdings – Account for as equity-settled if certain conditions are met
- Modification of awards from cash-settled to equity-settled – Specific approach to follow
- Next steps, effective date and transition

Currently, there is ambiguity over how a company should account for certain types of share-based payment arrangements. The IASB has responded by publishing amendments to IFRS 2 *Share-based Payment*.

The amendments cover three accounting areas:

- measurement of cash-settled share-based payments;
- classification of share-based payments settled net of tax withholdings; and
- accounting for a modification of a share-based payment from cash-settled to equity-settled.

The new requirements could affect the classification and/or measurement of these arrangements – and potentially the timing and amount of expense recognised for new and outstanding awards.

Measurement of cash-settled awards

There is currently no guidance in IFRS 2 on how to measure the fair value of the liability incurred in a cash-settled share-based payment. As a result, diversity in practice exists between measuring the liability using the same approach as for equity-settled awards and using full fair value.

The amendments clarify that a cash-settled share-based payment is measured using the same approach as for equity-settled share-based payments – i.e. the modified grant date method. Therefore, in measuring the liability:

- market and non-vesting conditions are taken into account in measuring its fair value; and

- the number of awards to receive cash is adjusted to reflect the best estimate of those expected to vest as a result of satisfying service and any non-market performance conditions.

The new requirements do not change the cumulative amount of expense that is ultimately recognised, because the total consideration for a cash-settled share-based payment is still equal to the cash paid on settlement.

Classification of awards settled net of tax withholdings

In some countries, the company may be obligated to collect or withhold tax related to a share-based payment, even though the tax obligation is often a liability of the employee and not the company.

Some share-based payment arrangements permit or require the company to withhold a portion of the shares that would otherwise be issued to the employee, and to pay the tax authorities on the employee's behalf.

Currently, it is unclear whether the portion of the share-based payment that is withheld in these instances should be accounted for as equity-settled or cash-settled.

The amendments introduce an exception stating that, for classification purposes, a share-based payment transaction with employees is accounted for as equity-settled if:

- the terms of the arrangement permit or require a company to settle the transaction net by withholding a specified portion of the equity instruments to meet the statutory tax withholding requirement (the net settlement feature); and
- the entire share-based payment transaction would otherwise be classified as equity-settled if there were no net settlement feature.

The exception does not apply to equity instruments that the company withholds in excess of the employee's tax obligation associated with the share-based payment.

Modification of awards from cash-settled to equity-settled

There is no specific guidance in IFRS 2 that addresses the accounting when a share-based payment is modified from cash-settled to equity-settled. The amendments clarify that companies are to apply the following approach.

- At the modification date:
  - the liability for the original cash-settled share-based payment is derecognised; and
  - the equity-settled share-based payment is measured at its fair value as at the modification date, and recognised to the extent that the goods or services have been received up to that date.
- The difference between the carrying amount of the liability derecognised as at the modification date, and the amount recognised in equity as at that date, is recognised in profit or loss immediately.

Next steps, effective date and transition

The amendments are effective for annual periods commencing on or after 1 January 2018.

Companies should consider whether the new requirements will result in a change to their accounting for share-based payment transactions.

As a practical simplification, the amendments can be applied prospectively so that prior periods do not have to be restated. Retrospective, or early, application is permitted if companies have the required information.

For more information on the amendments, read the IASB press release or speak to your usual KPMG contact.

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