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Belgium

Ref: The IASB's Exposure Draft *Classification and Measurement of Share-based Payment Transactions*: Proposed amendments to IFRS 2

Dear ~~Ms Flores~~, Dear Françoise,

The European Securities and Markets Authority (ESMA) thanks you for the opportunity to contribute to the EFRAG's due process. ESMA has considered EFRAG's draft comment letter to the IASB's Exposure Draft (ED) *Classification and Measurement of Share-based Payment Transactions*: Proposed amendments to IFRS 2. We are pleased to provide you with the following comments with the aim of improving the enforceability of IFRSs and the transparency and decision usefulness of financial statements.

ESMA agrees that the proposed amendments address the issues identified by the IFRS Interpretations Committee (IFRS IC) and would contribute to the consistent application of IFRS 2 *Share-based Payments*. However, ESMA considers that the wording of paragraph 33 of IFRS 2 should be clarified to enhance its consistent application and enforceability.

Specifically, ESMA believes that the proposed exception to the classification principles for transactions with net settlement features is justified as it reduces operational complexity and provides useful information to users of financial statements. At the same time, ESMA is concerned that the suggestion in paragraph 13 of the EFRAG Draft Comment Letter not to label the proposed amendment as an exception to the existing definition of cash-settled share-based payments could have unintended consequences and thus might lead to diversity in practice. Furthermore, by giving precedence to the substance of the arrangements rather than to the (existing) definition of cash-settled share-based payments in absence of strict conditions and criteria could undermine the nature of existing guidance in IFRSs more broadly as well as have an impact on consistency of their application in practice.

Regarding the proposal for prospective application, ESMA would prefer that all three proposed amendments are applied retrospectively in order to increase comparability of information in financial statements. Our view is that entities have the information necessary to apply the proposed amendments retrospectively and this information is available without the use of hindsight.

While agreeing with the proposed amendments, in light of the frequent changes to IFRS 2, ESMA suggests that the IASB specifically asks constituents in its upcoming triennial Agenda Consultation, whether it should undertake a post-implementation review of IFRS 2.

Our detailed comments on the ED are set out in the Appendix I to this letter. Please do not hesitate to contact us should you wish to discuss all or any of the issues we have raised.

Yours sincerely,

Steven Maijoor

Appendix I – ESMA's detailed answers to the questions in the ED

Question 1

The IASB proposes 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.

Do you agree? Why or why not?

1. ESMA agrees with the proposed clarifications and the fact that the principles of fair value measurement included in paragraph 6A of IFRS 2 apply equally to cash-settled and equity-settled share-based payments. ESMA conceptually agrees that while the difference in economic substance rationalizes their different accounting treatment, it does not justify different approaches to measure their fair value.

2. ESMA notes that, in the absence of guidance on accounting for the effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payments, different approaches could have developed in practice. Accordingly, ESMA is of the view that the proposed clarifications will contribute to the consistent application of IFRS 2 principles when reflecting the impact of vesting and non-vesting conditions in the fair value of share-based payment transactions.

   <u>Clarifications on the wording of paragraph 33 of IFRS 2</u>

3. ESMA notes that in paragraph BC 4 of the ED the IASB observed that the guidance in paragraph 6A of IFRS 2 refers to the same notion of 'fair value' for cash-settled and equity-settled awards. However, the measurement requirements for fair value of equity-settled share-based payments in paragraphs 16 and 17 of IFRS 2 and cash-settled share-based payments in paragraph 33 of IFRS 2 differ. Whereas fair value of equity-settled share-based payments is determined with reference to the fair value of the equity instruments granted or, if not available, by using a valuation technique, fair value of cash-settled share-based payment shall be determined by using option pricing model.

4. Furthermore, while paragraph 31 of IFRS 2 indicates that share appreciation rights (SARs) are an example of cash-settled share-based payment transactions, based on the current wording of paragraph 33 of IFRS 2, some might consider that the guidance regarding the measurement of the cash-settled share-based payments is limited to SARs only. While we understand that the intention of the IASB was to refer to SARs only as an example of cash-settled share-based payments, questions might be raised whether the guidance in paragraph 33 is applicable to the measurement of all cash-settled share-based payments or to SARs only. Therefore, adding new guidance applicable to all cash-settled share-based payments to paragraph 33 of IFRS 2 might lead to enforceability issues and inconsistent application in relation to cash-settled share-based payments other than SARs.

5. Consequently, ESMA recommends the IASB to provide further clarifications in this respect in order to avoid divergence in practice and/or enforceability issues.

Question 2

The IASB proposes to specify that a share-based payment transaction in which 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 should be classified as equity-settled in its entirety. This is required if the entire share-based payment transaction would otherwise have been classified as an equity-settled share-based payment transaction if it had not included the net settlement feature.

Do you agree? Why or why not?

6. ESMA points out that when the IFRS IC analysed this fact pattern in September 2010, it recalled that, according to IFRS 2, an award is classified as cash-settled if the entity incurs a liability to transfer cash or other assets as a result of acquiring goods or services. Consequently, it concluded that as cash is transferred to the tax authority in settlement of the counterparty's tax obligation in respect of the shares withheld, the portion corresponding to the future withholding tax is classified as cash-settled share-based payment. As the IFRS IC identified a number of issues arising from the submission for which the application of the requirements of IFRS 2 caused concern, such as separately classifying components of a single award, the IFRS IC recommended to the IASB to determine whether the introduction of an exception in IFRS 2, to permit equity-settled classification of the portion of the share-based payment withheld, would be appropriate.

7. ESMA agrees with the proposed amendment. ESMA concurs that the proposed exception to the classification principles is justified as it reduces operational complexity, compared to the alternative solution and contributes to the convergence of the accounting treatment with US GAAP. ESMA is of the view that the proposed accounting treatment provides useful information to users of financial statements.

8. However, ESMA suggests that the IASB clarifies the accounting for the settlement of the withholding tax in these circumstances and exemplify such treatment in the Guidance on implementing IFRS 2.

Question 3

The IASB proposes to specify the accounting for modifications to the terms and conditions of a cash-settled share-based payment transaction that results in a change in its classification from cash-settled to equity-settled. The IASB proposes that these transactions should be accounted for in the following manner:

(a) the share-based payment transaction is measured by reference to the modification-date fair value of the equity instruments 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 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.

Do you agree? Why or why not?

9. ESMA agrees with these proposed amendments as we believe they will contribute to consistency in accounting for these types of modifications. We concur with the view that when modifications to the terms and conditions of a cash-settled share-based payment transaction are so significant that they result in a change in its classification from cash-settled to equity-settled, the proposed accounting treatment correctly reflects the nature of the change that is more akin to the settlement of the original award.

Question 4

The IASB proposes prospective application of these amendments, but also proposes to permit the entity to apply the amendments retrospectively if it has the information needed to do so and this information is available without the use of hindsight.

Do you agree? Why or why not?

10. In general, ESMA prefers retrospective application of amendments to IFRSs, unless such application is impracticable, as it enhances consistency and comparability of financial statements. ESMA is of the view that, in most cases, entities have the information necessary to apply all three proposed amendments retrospectively and that this information is available without the use of hindsight.

11. ESMA does not agree that the argument included in paragraph 22 of the Basis for Conclusions of the ED[1] could justify that full retrospective application of the 'vesting conditions' amendment is not required as its retrospective application will increase comparability of the information in financial statements. However, if the IASB were not to require full retrospective application of this amendment to IFRS 2, ESMA considers that this, on its own, cannot justify the prospective application for the other two proposed

[1] that the proposed amendment related to accounting for the effects of vesting and non-vesting conditions will result only in changes to the timing and amount of the expense recognized at each reporting date, but will not result in changes to the cumulative expense

amendments included in the ED as suggested in paragraph BC 23 of the ED, as they concern three different issues. Indeed, ESMA does not agree that prospective application of these proposed amendments will result in better information for users.

Question 5

Do you have any other comments on the proposals?

12. In light of the frequent changes made to IFRS 2, and of a good number of submissions discussed by the IFRS IC, ESMA suggests the IASB to specifically asks constituents, as part of its upcoming triennial Agenda Consultation, whether it should undertake a comprehensive post-implementation review of IFRS 2.