



Global Rewards Update

Amendments to IFRS 2 for net-settlement of share-based payment transactions

Background

This update discusses the accounting standard for share plans and the impact of net settling, which has now been clarified. This is of interest for companies because treating awards cash-settled rather than equity-settled can impact the accounting cost.

Many jurisdictions oblige companies to withhold an employee's tax on a share award or option and to transfer the tax amount to the tax authority. There are various processes a company can use to collect the funds from employees.

Some companies deduct from the award enough shares with a value equal to the value of the employee's tax liability. The company then pays the amount withheld to the tax authorities from its own cash. This is known as 'net-settlement'. This is different from a 'sell to cover' arrangement where the full number of shares is transferred or issued on vesting/exercise of an award but sufficient shares are then sold on the employee's behalf to cover their tax.

Whilst the value received by the employee is the same under both arrangements, the number of shares and an entity's cash liability is different.

Among companies which net settle awards, the accounting treatment of the net-settled portion currently varies, with some companies accounting for the withheld portion as cash-settled and some as equity-settled.

The IASB was asked to consider whether the portion of the share award that is used to pay taxes under **net-settlement** should be classified as *cash-settled* (which requires the company to re-measure that portion of the award at the end of

each reporting period and the date of settlement, with any changes in fair value recognised in the entity's profit and loss account) or *equity-settled* (with no requirement to re-measure).

On 15 December 2015, the IASB agreed amendments to the wording of IFRS 2 to clarify the position. A copy of the agreed wording can be found [here](#).

Application

The new standard is expected to be finalised in late February 2016, and will be mandatory for new and unvested share awards and option in accounting periods beginning on or after 1 January 2018. Companies can choose to apply the amendment for an earlier period.

Effect

The agreed wording confirms that where a share-based payment is net-settled by withholding a specified portion of the shares to meet a statutory withholding obligation, the transaction should normally be accounted for as equity-settled in its entirety.

For existing unvested share awards, companies will need to reclassify any proportion that was being accounted for as cash-settled as equity-settled at the beginning of the accounting period in which the amendment is first applied.

This will not apply to shares withheld in excess of the amount required to satisfy the tax obligation.

Impact

Where companies currently net-settle, and treat the net-settled amount within an equity-settled transaction, there should be no impact.

However, this will only be the case where the company net-settles based on the statutory withholding requirement. Where a company net-settles based on a higher amount (for example the highest marginal rate of tax in a jurisdiction) and the excess between the amount net-settled and the statutory withholding requirement is settled in cash, the excess should be treated as a cash-settled share-based payment transaction. This may result in an additional expense to be recognised on settlement.

Where companies currently net-settle share-based payment transactions and treat the net-settled amount as a separate cash-settled share-based payment transaction, from 1 January 2018 they will need to start accounting for the net-settled amount as equity-settled.

Where a company net-settles their share-based payments it is still important to consider the other implications, for example the impact on cash, the availability of a corporate tax deduction and the impact on dilution.

Deloitte's view

Clarification of the treatment of the withheld portion of share awards is to be welcomed, although companies will need to ensure that they only withhold the appropriate amount of shares to cover the actual tax due, if equity-settled treatment is to be available in its entirety. For those companies with a significant number of employees receiving share-based payments, this could result in additional complexity, but choosing to net-settle at the highest marginal rate of income tax could result in a further accounting expense in respect of any excess settled in cash.

Companies should review their current approach to classification of share-based payments to consider the impact of these changes on their plans.

Contacts

For assistance with these issues, or any other issue related to the operation of your global equity plans, please contact your usual Deloitte adviser or email us at globalshareplans@deloitte.co.uk, and an adviser will contact you.

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