

XXX May, 2006

IFRIC  
30 Cannon Street  
London EC4M 6XH  
UK

**Draft comment letter for comments by 5 May 2006 to**  
[Commentletter@efrag.org](mailto:Commentletter@efrag.org)

**Re: Exposure Draft of Proposed Amendments to IFRS 2 Share-based Payment  
*Vesting Conditions and Cancellations***

On behalf of the European Financial Reporting Advisory Group (EFRAG) I am writing to comment on the Exposure Draft of Proposed Amendments to IFRS 2 Share-based Payment *Vesting Conditions and Cancellations* (Amendments to IFRS 2). The issue was discussed by IFRIC in 2005 in the context of IFRIC Draft Interpretation 11 *Changes in Contributions to Employee Share Purchase Plans* (D11), but it was decided that this issue requires an amendment to the existing standard rather than an interpretation. EFRAG commented on D11.

This letter is submitted in EFRAG's capacity of contributing to IASB's and IFRIC's due process and does not necessarily indicate the conclusions that would be reached in its capacity of advising the European Commission on endorsement of the definitive IFRIC on the issue.

The document sets out the Board's proposed definition of vesting conditions and guidance on the accounting treatment of cancellations by parties other than the entity. The Exposure draft proposes:

- (a) to restrict vesting conditions to service conditions and performance conditions;
- (b) to require cancellations by parties other than the entity, whether by employees, shareholders or any other parties, to be accounted for in the same way as cancellations by the entity (paragraph 28 of IFRS 2);
- (c) to require these changes to be applied in annual periods beginning on or after 1 January 2007. The amendments are to be applied retrospectively.

In principle we agree that the issues have to be clarified by amending IFRS 2 rather than an interpretation, but we have several concerns.

Our response to the detailed questions is:

### **Question 1 – Vesting conditions**

*The Exposure Draft proposes that vesting conditions should be restricted to performance conditions and service conditions. Do you agree? If not, what changes do you propose, and why?*

#### **EFRAG draft response:**

We agree with the clarification that vesting conditions are restricted to performance conditions and service conditions and therefore support the proposed amendment to the definition in IFRS 2 Appendix A. In particular we agree that contractual requirements for employees to make regular plan contributions over a specified period do not meet that definition.

### **Question 2 – Cancellations**

*The Exposure Draft proposes that cancellations by parties other than the entity should be accounted for in the same way as cancellations by the entity.*

*Do you agree that all cancellations should be treated in the same way? If not, please specify the nature of any differences between types of cancellations and explain how they influence the selection of appropriate accounting requirements.*

#### **EFRAG draft response:**

As we argued in our response to IFRIC Draft interpretation 11 (D11), we disagree that all cancellations of plans to grant equity instruments should be treated in the same way. The proposed solution for employee withdrawals is to account for them as a cancellation according to IFRS 2 paragraph 28(a), meaning that vesting should be accelerated and therefore the amount that otherwise would have been recognised for services received over the remainder of the vesting period should be expensed immediately. In our view there is a fundamental difference in substance between an employer cancellation and an employee withdrawal. An employer can cancel a plan only with the agreement of the counterparty, and that agreement will usually be forthcoming if the employer has agreed to pay some kind of compensation (IFRS 2, BC233). As such, the cancellation can be viewed as an accelerated vesting, thus justifying the accounting treatment required by IFRS 2.28(a).

Employees can decide whether they wish to benefit by the plan at grant date or later on by deciding whether to continue contributing or whether to exercise their rights. We believe that an employee who ceases to contribute for example to a savings plan associated to an employee share plan is an employee who decides not to exercise his rights, although he had previously agreed to participate in the plan. We therefore do not see any difference in economic substance between an employee withdrawing from a plan to grant equity instruments shortly before the end of the savings period and an employee that chooses not to exercise the option to purchase shares. The accounting treatment for both should be the same.

The Basis for Conclusion from BC8 onwards evaluates four possible accounting treatments. We agree with the Board that neither (a) nor (b) are consistent with the general principle of IFRS 2 as expressed in BC11. We note that for cancellations by

the employer alternative (d), immediate expensing (or bullet expense), has been put forward in IFRS 2 in order to limit possibilities to structure around the requirements of the standard (IFRS 2, BC232 and BC233).

For the reasons expressed above, we believe that option (c), the continuation of expense recognition in cases of cancellations by employees, is the accounting treatment which is the most consistent with the IFRS 2 general principle and therefore we support (c) rather than (d).

Although we acknowledge the strong argument of converging IFRS 2 to the US GAAP requirements of SFAS 123, where all cancellations are treated the same way, as accelerations of vesting, on balance, we disagree with the proposed treatment from a technical perspective.

### **Question 3 – Effective date and transition**

*The proposed changes would apply to periods beginning on or after 1 January 2007, and would be required to be applied retrospectively. Earlier application would be encouraged.*

#### **EFRAG draft response:**

We agree with the effective date and transitional requirement of retrospective application.

If you would like further clarification of the points raised in this letter I would be happy to discuss these further with you.

Yours sincerely

Stig Enevoldsen  
**EFRAG, Chairman**