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Mr. Kevin Stevenson, Chairman
International Financial Reporting Interpretations Committee
30 Cannon Street
London EC4M 6XH
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Dear Kevin,

Changes in Contributions to Employee Share Purchase Plans

Deloitte Touche Tohmatsu is pleased to comment on the International Financial Reporting Interpretations Committee's (IFRIC) Draft Interpretation 11 – *Changes in Contributions to Employee Share Purchase Plans* (the draft interpretation or D11).

With regard to the issue addressed by the draft interpretation, set out in paragraph 3(a) of D11, IFRS 2 – *Share-based payment* (IFRS 2, or the Standard) seems to allow only two possible alternatives for the accounting treatment of an employee ceasing to contribute to a "Save-As-You-Earn" (SAYE) scheme, either that:

(i) the cessation of employee contributions to the plan is a failure to satisfy a vesting condition under paragraphs 19 and 20 of the Standard; or

(ii) it is a cancellation.

Accordingly, we understand how, by restricting the definition of vesting condition as set out in BC7, one could conclude that an employee ceasing to contribute to an employee share purchase plan (ESPP) and thus foregoing the right to buy shares under the plan is not a failure to meet a vesting condition. In that case, cessation by the employee to contribute to the ESPP can only be treated as a cancellation. However, we believe that there may be characteristics of a SAYE plan that were not contemplated in the IASB's deliberations of IFRS 2.

The IFRS 2 definition of vesting conditions - "conditions that must be satisfied for the counterparty to become entitled to receive cash, other assets or equity instruments of the entity, under a share based payment arrangement" - includes service and performance conditions, but does not seem to restrict vesting conditions to these types of conditions. We believe that the principle in IFRS 2 is based on a vesting condition resulting in a benefit to the entity, i.e. the employee's services. D11 restricts the definition of vesting conditions, as acknowledged by the IFRIC in the Basis of Conclusions. However, we find the rationale for this narrowing of the definition as expressed in BC7 concerning because it may have unintended consequences for other share-based payment arrangements. We believe that the definition of vesting conditions is currently insufficient and leads to problems of application in practice. We are aware of other share-based payment arrangements in existence, for example where a director of a company is required to hold shares in the company in order to receive share options of the entity.

In addition, we believe that IFRIC needs to clarify the arguments in D11 for concluding that an employee ceasing to contribute to an ESPP is a cancellation. Paragraph BC4 of D11 states that:

> "IFRS 2 discusses cancellations in the context of cancellations by the entity, not the employee. However it is debatable whether the employee's participation in the plan was cancelled by the entity or the employee. (The cancellation occurred as a consequence of the employee ceasing to contribute to the plan, but that potential consequence was specified by the entity when establishing the plan)."

The employee's decision to withdraw from a SAYE scheme is outside of the control of the employer, and may be based on considerations other than the performance of the underlying shares. For example, an employee may be motivated to cease contributing to the SAYE plan and liquidate their cash account in order to purchase a home, or because their mortgage payments have increased. An employee participating in a SAYE scheme bears no downside risk in deciding to pull out of the scheme, as they will receive the cash they have set aside and interest (which may be tax-free). It is the employee that decides to cease to contribute to the ESPP, not the entity.

Treating the employee's ceasing to contribute to the scheme as a failure to satisfy a non-market vesting condition would result in no IFRS 2 remuneration expense, which seems inappropriate as the entity continues to receive services from those employees. Treating it as a cancellation would result in the immediate recognition in profit or loss of the amount that would otherwise have been recognised for services received over the remainder of the vesting period while the entity continues to receive those services. We think that treating the employee's ceasing to contribute as a cancellation may not be the best reflection of the transaction.

It appears that a more faithful representation of the employee's decision to cease contributing to the scheme is to recognise an expense for the share-based payment component up until the date that the employee decides to withdraw their cash deposit. However, this accounting treatment is not supported by the current version of IFRS 2.

In addition, the draft interpretation is written from the perspective of ensuring consistency of application of IFRS 2 between those employees that take up the opportunity to participate in the scheme, by contributing cash to the scheme but then decide to exit the scheme and those employees that continue to participate until the end of the scheme. However it does not consider those employees that were invited to join the scheme, and did not participate by contributing cash to the scheme.

Because of their unique characteristics, we question whether the current versions of IFRS 2 or D11 provide the best accounting for these types of schemes. Hence we believe that the accounting treatment where an employee ceases to contribute to such an ESPP requires further analysis and potentially an amendment to IFRS 2 (or a recommendation from the IFRIC to the IASB), particularly in respect of the additional questions it raises regarding what the definition of vesting condition encapsulates and whether there is another model besides that for failing to vest or cancellation.

With regards to the issue set out in paragraph 3(b) of D11, we concur with the IFRIC consensus set out in paragraph 5.

We question the necessity of the proposed amendments to IFRS 1 *First-time Adoption of International Financial Reporting Standards* as set out in the Appendix to the draft interpretation.

We appreciate the opportunity to provide our comments. If you have any questions concerning our comments, please contact the undersigned at (020) 7007 0907.

Sincerely,

Ken Wild
Global IFRS Leader