

# Alerte de votre conseiller – IFRS

## Aperçu d'IFRS 2 *Paiement fondé sur des actions*

Février 2026

### Résumé

Grant Thornton International Ltd a publié deux nouveaux bulletins de la série *Insights into IFRS 2* (en anglais seulement) :

- *Cash-settled share-based payment arrangements with employees;*
- *Employee share-based payment arrangements with settlement alternatives.*

La norme IFRS 2 *Paiement fondé sur des actions* a été publiée en 2004, et les principes comptables sont restés essentiellement les mêmes depuis. Les paiements fondés sur des actions sont devenus de plus en plus populaires au fil des ans, de nombreuses entités utilisant des instruments de capitaux propres ou de la trésorerie et d'autres actifs fondés sur la valeur des instruments de capitaux propres comme forme de paiement aux administrateurs, aux dirigeants, aux salariés et à d'autres fournisseurs de biens et de services.

La comptabilisation des paiements fondés sur des actions est une question qui reste mal comprise, comme en témoigne le grand nombre d'interprétations et de décisions publiées par l'IFRS Interpretations Committee (IFRIC). Il convient de faire preuve d'une grande prudence lors de l'évaluation des exigences énoncées dans IFRS 2 et dans d'autres indications faisant autorité en ce qui concerne les accords de paiement fondés sur des actions de plus en plus complexes et novateurs.

La série *Insights into IFRS 2* vise à démystifier la norme en expliquant les principes fondamentaux de la comptabilisation des paiements fondés sur des actions dans un langage relativement simple et en fournissant des indications pour aider les entités à surmonter certaines des complexités associées à la comptabilisation de ces types d'accords. Les deux nouveaux bulletins sont les suivants :

- *Cash-settled share-based payment arrangements with employees;*
- *Employee share-based payment arrangements with settlement alternatives.*

### Ressources

Les bulletins mentionnés ci-dessus sont joints à la présente *Alerte de votre conseiller – IFRS*.



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Traduction : en cas de divergence, la version originale anglaise a préséance.

# Insights into IFRS 2



## Cash-settled share-based payment arrangements with employees

Cash-settled share-based payment arrangements are a form of compensation where entities pay in cash or other assets based on the value of equity instruments. These arrangements differ significantly from equity-settled payments in their classification, measurement, and accounting treatment under IFRS 2.

While the accounting for both of these types of arrangements has not changed significantly in recent years, it is an area that is not well understood in practice and confusion often arises between the different types of arrangements and how to treat them.

Our ‘**Insights into IFRS 2**’ series is aimed at demystifying IFRS 2 by explaining the fundamentals of accounting for share-based payments using relatively simple language and providing insights to help entities cut through some of the complexities associated with accounting for these types of arrangements.

As explained in our article ‘**Insights into IFRS 2 – Classification of share-based payment transactions and vesting conditions**’, a share-based payment arrangement must be classified as either an equity-settled transaction or a cash-settled transaction. This article discusses the accounting for cash-settled share-based payment transactions. The accounting for equity-settled transactions is discussed in our article, ‘**Insights into IFRS 2 – Equity-settled share-based payment arrangements with employees**’. The accounting for share-based payment transactions with non-employees is discussed in our article ‘**Insights into IFRS 2 – Share-based payment arrangements with non-employees**’.

## Cash-settled share-based payment arrangements

As explained in our article ‘**Insights into IFRS 2 – Classification of share-based payment transactions and vesting conditions**’, share-based payment transactions that are within the scope of IFRS 2 are classified based on whether the entity’s obligation is to deliver:

- its own equity instruments (equity-settled), or
- cash or other assets (cash-settled).

### Cash-settled share-based payment transaction:

A share-based payment transaction in which the entity acquires goods or services by incurring a liability to transfer cash or other assets to the supplier of those goods or services for amounts that are based on the price (or value) of equity instruments (including shares or share options) of the entity or another group entity.

“Our ‘Insights into IFRS 2’ series is aimed at demystifying IFRS 2 by explaining the fundamentals of accounting for share-based payments.”

Common forms of cash-settled share-based payment transactions include:

- Share-appreciation rights (SARs), where employees are entitled to a future cash payment equal to the increase in the entity's share price from a specified level over a specified period of time
- Phantom shares, where employees are entitled to a cash payment equal to the fair value of a specified number of shares at the date of exercise, and
- Phantom options, where employees are entitled to a cash payment equal to the gain that would have been made by exercising options at a specified price over a specified number of shares and then selling the shares at the date of exercise.

#### **Practical insight – Classification of share-based payment transactions based on cash flows**

Each situation should be assessed to determine whether a share-based payment transaction is equity-settled or cash-settled. There may be circumstances where there are cash outflows incurred by the entity or cash inflows received by the employee which may suggest that the transaction is cash-settled. For example:

- An entity may incur a cash outflow to purchase shares in the market to settle equity-settled share-based payment transactions, rather than issuing new shares from treasury. In our view, this transaction is not classified as cash-settled, as there is no liability to transfer cash or other assets to the employee. In this instance, the transaction should be accounted as two separate transactions consisting of a buy-back of treasury shares recognised in accordance with IAS 32 'Financial Instruments: Presentation' and an equity-settled share-based payment transaction accounted for in terms of the principles explained in our article '[Insights into IFRS 2 – Equity-settled share-based payment arrangements with employees](#)'.
- An entity may immediately repurchase shares granted to an employee, even though the entity has not committed to do so. In our view, if an entity creates an expectation by the employee that it will systematically reacquire the shares granted (for example, because of the illiquidity of the market) this could result in the arrangement being accounted for as cash-settled.

#### **Example 1 – Repurchase arrangement at the entity's option**

Entity A is an unlisted company that has issued shares to its employees as part of their compensation packages. Since it expects that not every employee will wish to become long-term investors in the company, Entity A also established an arrangement in which the employees must offer their shares for sale to Entity A upon ceasing employment.

Entity A may, but is not obligated to, repurchase the offered shares at their then-current market price. To date, Entity A has accepted all past offers to buy back the shares. This arrangement is not available to any of Entity A's non-employee shareholders.

#### **Analysis**

In practice different approaches may be acceptable, depending on the facts and circumstances. For example:

- Some entities may determine that the arrangement should be classified as cash-settled so long as the entity has created a valid expectation that the awards will be settled in cash. Due to Entity A's past practice of repurchasing the shares, the employees may have an expectation that the awards will be settled in cash. Entity A could also have a stated policy to accept repurchase offers from its employees.
- Other entities may also consider whether the repurchase arrangement is limited to employees:
  - When the repurchase arrangement only relates to employees who receive shares in their role as employees, the entity may determine that the repurchase arrangement is part of the terms and conditions of the share-based payment. When there is also a valid expectation that such awards (ie where the terms include the repurchase arrangement) will be settled in cash, then the entity may determine that they should be classified as cash-settled.
  - In contrast, if the repurchase arrangement was available to all of an entity's shareholders (ie not just its employees), the entity may determine that the repurchase arrangement is a shareholder condition, rather than part of the share-based payment arrangement with its employees. If so, the entity may consider it appropriate to ignore the repurchase arrangement when classifying the awards, and thus classify them as equity-settled. For equity-settled awards, any payment made to the employee should be accounted for as the repurchase of an equity interest (ie as a deduction from equity), except to the extent that the payment exceeds the fair value of the equity instruments measured at the repurchase date. Any excess would be an expense.

Transactions where either the entity or the counterparty has the choice of settlement in equity instruments or in cash or other assets are discussed in our article, '[Insights into IFRS 2 – Employee share-based payment agreements with settlement alternatives](#)'.

## Accounting for cash-settled share-based payment arrangements with employees

For cash-settled share-based payment transactions with employees, the services received are initially measured on the grant date at fair value. The entity also recognises a corresponding liability that represents its obligation to make a payment of cash or other assets. At each reporting date and until the final settlement date, the liability for a cash-settled share-based payment transaction is remeasured at its fair value (which is equal to the fair value of the award). Any differences in the fair value of the liability are recognised in profit or loss.

The entity recognises the services received (ie the share-based payment cost), along with the corresponding liability, as the employee provides the service. Where the employee is required to complete a specified period of service, the services and the corresponding liability are recognised over the vesting period. Where the award vests immediately, the service is recognised immediately. For further information on determining the vesting period, refer to our article '[Insights into IFRS 2 – Basic principles of share-based payment arrangements with employees](#)'.

As discussed in our article '[Insights into IFRS 2 – Classification of share-based payment transactions and vesting conditions](#)', share-based payment awards may include conditions that determine whether an employee is entitled to receive the payment (ie vesting and non-vesting conditions). The entity accounts for the effects of these conditions at the end of each reporting period and upon settlement as follows:

- Market and non-vesting conditions are taken into account when estimating the fair value of the cash-settled share-based payment.
- Conversely, service and non-market performance vesting conditions are not taken into account when estimating the fair value of the cash-settled share-based payment. Instead, service and non-market performance vesting conditions are taken into account by adjusting the number of awards that are expected to vest – that is, the entity shall not recognise amounts relating to awards that are not expected to and ultimately do not vest because of a failure to satisfy a service or non-market performance vesting condition.



In summary:

Type of Condition	Impact on fair value and expense
<b>Non-vesting condition</b> (eg non-compete restriction, requirement to hold shares for a specified period)	<ul style="list-style-type: none"><li>• Reflected in grant date fair value</li><li>• Fair value remeasured at the end of each reporting period</li><li>• (True-up reflected in fair value remeasurement)</li></ul>
<b>Market performance condition</b> (eg achieving a specified share price)	<ul style="list-style-type: none"><li>• Reflected in grant date fair value</li><li>• Fair value remeasured at the end of each reporting period</li><li>• (True-up reflected in fair value remeasurement)</li></ul>
<b>Non-market performance condition</b> (eg achieving a specified earnings before interest, taxes, depreciation, and amortisation (EBITDA) level)	<ul style="list-style-type: none"><li>• Not reflected in grant date fair value</li><li>• Reflected in number of awards expected to vest</li><li>• True-up for failure to meet condition</li></ul>
<b>Service condition</b> (eg vesting after three year service period)	<ul style="list-style-type: none"><li>• Not reflected in grant date fair value</li><li>• Reflected in number of awards expected to vest</li><li>• True-up for failure to meet condition</li></ul>

Ultimately, the cumulative amount recognised for goods or services received for a cash-settled share-based award is equal to the cash paid. Accordingly, if at the end of the vesting period, a vesting condition is not met, the award is forfeited due to the failure to vest, and any amounts previously recognised in profit or loss are reversed.

#### Key difference with accounting for equity-settled share-based payment arrangements with employees

This treatment differs from an equity-settled award where an entity recognises, at a minimum, the grant date fair-value of the equity instruments, unless they fail to vest because a service or non-market performance vesting condition is not satisfied.

This difference occurs because a cash-settled award is remeasured at the end of each reporting period at its fair value, and therefore continues to incorporate the effects of market and non-vesting conditions at each remeasurement date. In contrast, the fair value of equity-settled awards, including the effects of market and non-vesting conditions, is determined at the grant date and then is not subsequently remeasured.

As a result, an IFRS 2 expense would be recognised for an equity-settled share-based payment even though the market condition is not met (to the extent that the services condition and any other non-market performance conditions are satisfied). In the case of a cash-settled award, there would be no IFRS 2 expense recognised in that situation.

#### Fair value versus intrinsic value

As discussed above, an entity is required to remeasure a cash-settled share-based payment award to its fair value at the end of each reporting period. A cash-settled award, however, is sometimes settled at its intrinsic value.

Intrinsic value:
The difference between the fair value of the shares to which the counterparty has the (conditional or unconditional) right to subscribe or to which it has the right to receive, and the price (if any) the counterparty is (or will be) required to pay for those shares.

For example, a share appreciation right (SAR) gives the holder the right to receive the increase in value of a share between two dates. If the grant date share price is CU15 and the settlement date share price is CU20, then the intrinsic value is CU5.

While the fair value and intrinsic value of a SAR are equal upon settlement, disparities between the two values exist on dates prior to settlement because the fair value is determined by applying an option pricing model and takes into account the current intrinsic value and a premium for the possibility of future increases in intrinsic value (ie time value). This is illustrated in the example below, where the fair value of the SARs are different from the intrinsic values.

### Example 2 – Cash-settled share-based arrangements

On 1 January 20X2, Entity C grants five SARs to each of its 100 employees, on the condition that the employees remain in its employ for the next three years.

- During year one, 10 employees leave. The entity estimates that, in total, a further 25 will leave during years two and three.
- During year two, 15 employees leave. The entity estimates that a further 20 will leave during year three.
- During year three, 25 employees leave. Following the end of year three, the remaining 50 employees exercise their SARs, and receive their intrinsic value on the settlement date of 31 January 20X5.

Entity C estimates the fair value of the SARs as follows:

#### Analysis

Entity C estimates the fair value of the SARs as follows:

Year	Fair value (CU)	Intrinsic value (CU)
Grant date	10	
1	12	
2	14	
3	16	
Settlement date		15

Entity C recognises the following:

Year	Calculation of liability	Liability (ending balance) (CU)	Expense (CU)
1 – 31 December 20X2	5 SARs X (100-35) employees X CU12 X 1/3	1,300	1,300
2 – 31 December 20X3	5 SARs X (100-45) employees X CU14 X 2/3	2,567	1,267
3 – 31 December 20X4	5 SARs X (100-50) employees X CU16 X 3/3	4,000	1,433
31 January 20X5	5 SARs X (100-50) employees X CU15 X 3/3	3,750	(250)
<b>Total</b>			<b>3,750</b>

Note: the expense is calculated as the change in the liability balance between reporting periods.

# Summary of differences in accounting for equity-settled and cash-settled share-based payment arrangements

Below are the key differences in accounting for equity-settled and cash-settled share-based payment arrangements:

	Equity-settled	Cash-settled:
Accounting entry	The credit in the transaction entry is recorded in equity.	The credit in the transaction entry is recorded as a liability.
Remeasurement of fair value	The grant date fair value is never remeasured.	Until the liability is settled, the fair value is remeasured at each reporting period and at the settlement date.
Cumulative net cost	The cumulative net cost is trued-up only for changes in the estimates regarding service and non-market performance conditions.	The cumulative net cost is equal to the settlement amount (ie the cash that is paid).
Period accounted for	The expense and corresponding equity adjustment are recognised over the vesting period.	The expense and corresponding liability are recognised until settlement.

## How we can help

We hope you find the information in this article helpful in giving you insight into aspects of IFRS 2. If you would like to discuss any of the points raised, please speak to your usual Grant Thornton contact or visit [www.grantthornton.global/locations](http://www.grantthornton.global/locations) to find your local member firm.

# Insights into IFRS 2

## Employee share-based payment agreements with settlement alternatives



The use of share-based payments has grown significantly over time, with many organisations opting to compensate directors, senior executives, employees and other providers of goods and services through equity instruments or cash and other assets linked to the value of equity instruments.

IFRS 2 ‘Share-based Payment’ governs the accounting for share-based payment arrangements including employee agreements, and those with settlement alternatives allowing either equity instruments or cash settlements. The accounting treatment varies depending on whether the employee or the entity has the choice of settlement, with distinct approaches for compound financial instruments and present obligations to settle in cash.

Our ‘**Insights into IFRS 2**’ series is aimed at demystifying IFRS 2 by explaining the fundamentals of accounting for share-based payments using relatively simple language and providing insights to help entities cut through some of the complexities associated with accounting for these types of arrangements.

This article discusses share-based payment arrangements that provide either the entity or the employee with a choice as to whether settlement occurs in equity instruments or in cash or other assets (hereafter ‘cash’). The accounting treatment for agreements with settlement alternatives depends on which party has the choice of settlement.

### Employee has the choice of settlement

When the employee has been granted an award where they have the right to choose whether the transaction is settled in cash or equity instruments, the entity has granted a compound financial instrument that includes a debt component and an equity component. The debt component reflects the employee’s right to demand payment in cash, and the equity component reflects the employee’s right to demand settlement in equity instruments rather than cash.

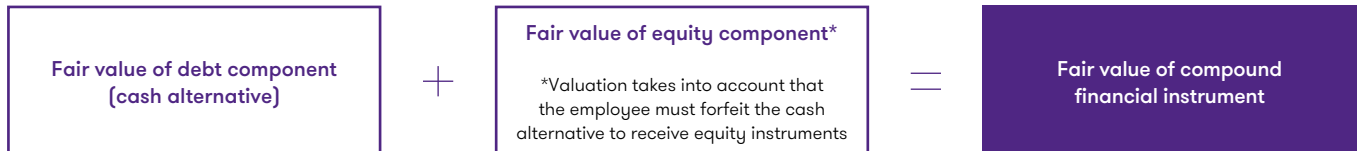
“This article discusses share-based payment arrangements that provide either the entity or the employee with a choice as to whether settlement occurs in equity instruments or in cash or other assets (hereafter ‘cash’).”

### How is the value of a compound financial instrument granted to an employee determined?

At the measurement date, the entity determines the fair value of the compound financial instrument (ie the value of the services received) by taking into account the terms and conditions on which the rights to the equity or cash alternatives were granted.

As discussed in our article '[Insights into IFRS 2 – Basic principles of share-based payment arrangements with employees](#)', the measurement date is the grant date for share-based payment transactions with employees.

The fair value of a compound financial instrument can be illustrated as follows:



The fair value of the debt component is measured first and is equal to the fair value of the cash liability. The fair value of the equity component is then determined and takes into account the fact that the employee must forfeit the cash alternative in order to receive equity instruments. In other words, the fair value of the cash alternative is deducted from the fair value of the equity alternative in order to determine the fair value of the equity component.

In practice, it is common for share-based payment transactions where the employee has the choice of settlement to be structured so that the fair value of the cash and equity alternatives are equal. This structure results in the fair value of the equity component being equal to zero, and therefore the value of the compound instrument is equal to the fair value of the debt component.

To illustrate, assume an entity grants an employee the right to receive either share options or cash-settled share appreciation rights (SARs) upon vesting. Also assume that the exercise price of the share options is equal to the grant date fair value of the entity's shares. The fair value of the cash and equity alternatives will always be equal because the value the employee receives under both alternatives is equal to the difference between the share price at vesting and the grant date fair value (ie the grant date share price). Consequently, the fair value of the equity component will be equal to zero, and the fair value of the compound instruments will be equal to the fair value of the debt component.

Arrangements may also be structured so that the fair value under the settlement alternatives differ. Usually, the fair value of the equity component under these arrangements will be greater than zero and therefore the value of the compound instrument will exceed the fair value of the debt component. An example of such an arrangement and the required accounting treatment can be found in Example 1 below.

### How should the compound financial instrument be accounted for?

Each component of the compound financial instrument is accounted for separately in accordance with the requirements for cash-settled and equity-settled share-based payments, as discussed in our articles '[Insights into IFRS 2 – Cash-settled share-based payment arrangements with employees](#)' and '[Insights into IFRS 2 – Equity-settled share-based payment arrangements with employees](#)'.

In summary, the accounting treatment for the debt and equity components is as follows:

Component	Accounting treatment
<p><b>Debt component</b></p>	<p>Accounting for cash-settled share-based payments:</p> <ul style="list-style-type: none"> <li>• Recognise the services as received over the vesting period in profit and loss (other than amounts that qualify for capitalisation) with a corresponding credit to a liability. Do not recognise amounts relating to awards that are not expected to and ultimately do not vest, because of a failure to satisfy a service or non-market performance vesting condition specified at the grant date.</li> <li>• Remeasure the liability to its fair value at the end of each reporting period and upon settlement, taking any differences to profit or loss. Market performance and non-vesting conditions are taken into account when estimating the fair value of the cash-settled share-based payment; if such conditions are not met, any amounts previously recognised in profit or loss are reversed.</li> </ul>
<p><b>Equity component</b></p>	<p>Accounting for equity-settled share-based payments:</p> <ul style="list-style-type: none"> <li>• Recognise the services as received over the vesting period in profit and loss (other than amounts that qualify for capitalisation) with a corresponding credit to equity. Do not recognise amounts relating to awards that are not expected to and ultimately do not vest, because of a failure to satisfy a service or non-market performance vesting condition specified at the grant date.</li> </ul>

At the settlement date, the debt component is remeasured to its fair value and the accounting is as follows:

- If the employee chooses to settle in equity instruments, rather than settling in cash, the value of the liability is transferred directly to equity, as consideration for the equity instruments issued.
- If the employee chooses to settle in cash, the payment is used to settle the liability in full. Any equity component previously recognised remains in equity, as the employee has forfeited the right to receive equity instruments. However, the entity may recognise a transfer within equity (ie from one component of equity to another).



### Example 1 – Employee has choice of settlement

Company A grants to an employee the right to choose either 1,000 phantom shares (ie a right to a cash payment equal to the value of 1,000 shares), or 1,200 shares. The grant is conditional upon the completion of three years of service. If the employee chooses the share alternative, the shares must be held for three years after the vesting date.

At the grant date, Company A's share price is CU50 per share. At the end of years one, two and three, the share price is CU52, CU55 and CU60 respectively. Company A does not expect to pay dividends in the next three years. After taking into account the effects of post-vesting transfer restrictions, the entity estimates that the grant date fair value of the share alternative is CU48 per share.

At the end of year three, the employee chooses:

- Scenario one – the cash alternative
- Scenario two – the equity alternative

#### Analysis

Company A first determines the value of the compound financial instrument at the measurement date.

- Fair value of equity alternative = 1,200 shares x CU48 = CU57,600
- Fair value of cash alternative = 1,000 phantom shares x CU50 (grant date share price) = CU50,000

The fair value of the equity component is therefore CU7,600 (CU57,600 less CU50,000).

Company A recognises the following amounts:

Year	Calculation	Expense (CU)	Adjustment to Equity (CU)	Adjustment to Liability (CU)
1	Liability component: (1,000 × CU52 × 1/3 years) Equity component: (CU7,600 × 1/3 years)	17,333 2,533	- 2,533	17,333 -
2	Liability component: (1,000 × CU55 × 2/3 years) – CU17,333 Equity component: (CU7,600 × 2/3 years) – CU2,533	19,333 2,533	- 2,533	19,333 -
3	Liability component: (1,000 × CU60 × 3/3 years) – CU36,666* *(CU17,333 + CU19,333) Equity component: (CU7,600 × 3/3 years) – CU5,066	23,334 2,534	- 2,534	23,334 -
End of Year 3	Scenario 1: Cash alternative – Cash of CU60,000 paid <b>Totals</b>	- <b>67,600</b>	- <b>7,600</b>	(60,000) <b>-</b>
	Scenario 2: Equity alternative – 1,200 shares issued <b>Totals</b>	- <b>67,600</b>	60,000 <b>67,600</b>	(60,000) <b>-</b>

### How should the compound financial instrument be accounted for where each alternative has a different vesting period?

In some situations, arrangements may be structured so that each alternative has a different vesting period. For example, an employee may have the right to choose either 1,000 phantom shares at the end of a three-year vesting period, or 1,200 share options if the employee remains employed for an additional two years following the original vesting period. The IFRS Interpretations Committee (IFRIC) released an Agenda Decision in May 2006 which clarified that IFRS 2 requires that an entity accounts for each component separately, and therefore vesting periods of the debt and equity components should also be determined separately.

### How should an entity account for transactions where the cash alternative is not based on the value of the entity's equity instruments?

An entity may offer an employee the right to receive shares (or another equity alternative), or cash at an amount that is unrelated to the price of the entity's equity instruments. In practice, although the cash alternative in isolation does not fall within the scope of IFRS 2, one acceptable approach is to account for such arrangements as compound financial instruments in accordance with IFRS 2 by analogy. The non-share-based cash alternative would represent the debt component and be accounted for in accordance with the appropriate standard, such as IAS 19 'Employee Benefits'. As discussed above, any excess of the fair value of the equity alternative over the fair value of the debt component represents the fair value of the equity component.

## Entity has the choice of settlement

Where the entity has the choice of settlement, the treatment is binary – that is, the entity accounts for the entire share-based payment transaction as either cash-settled or equity-settled, depending on whether it has a present obligation to settle in cash.

### When does an entity have a present obligation to settle in cash?

An entity has a present obligation to settle in cash if:

- the choice of settlement in equity instruments has no commercial substance (eg because the entity is legally prohibited from issuing shares)
- the entity has a past practice or stated policy of settling in cash (eg an entity settles awards in cash for employees that leave before the vesting date for reasons outside their control (a ‘good leaver’)), or
- the entity generally settles in cash whenever the counterparty asks for a cash settlement.

An entity also has an obligation to settle in cash if the shares issued (including shares issued upon the exercise of share options) are redeemable, either mandatorily (eg upon cessation of employment) or at the counterparty’s option.

If an entity has a present obligation to settle in cash, it accounts for the transaction in accordance with the requirements for cash-settled share-based payment transactions.

### Practical insight – Commercial substance of equity settlements

Some practical examples of circumstances that bring into question the commercial substance of settlement in equity instruments include:

- Group share-based payment schemes where settlement in equity could be restricted due to the practices or laws in the jurisdiction in which the award is granted, that make it illegal or difficult to hold shares in the parent
- Unlisted entities where there are difficulties for the beneficiaries to transfer the shares to third parties, other than existing shareholders, resulting in there being little to no benefit for an employee to receive a share, or
- Entities that are owned by a small number of shareholders eg where the entity is owned by members of a family. In this instance, there may be an assumption that the existing shareholders would not want to dilute their interests and would opt for the cash settlement

### What if an entity does not have a present obligation to settle in cash?

An entity that does not have a present obligation to settle in cash accounts for the entire transaction in accordance with the requirements for equity-settled share-based payment transactions.

Upon settlement:

- (a) If the entity chooses to settle in cash, the cash payment is accounted for as a repurchase of an equity instrument – ie as a deduction from equity, except as noted in (c) below.
- (b) If the entity chooses to settle by issuing equity instruments, no further accounting is required (other than a transfer from one component of equity to another, if necessary), except as noted in (c) below.
- (c) If the entity chooses the settlement alternative with the higher fair value, as at the date of settlement, the entity recognises an additional expense for the excess value (ie the difference between the fair value of the liability (ie cash paid) and the fair value of the equity instruments issued).

### Example 2 – Entity has the choice of settlement

Company C grants an employee a share-based payment arrangement, subject to a service condition of two years. Company C has a choice to settle the transaction in either equity or cash. Company C has accounted for the transaction as equity-settled on the basis that it does not have a present obligation to settle in cash as its stated policy, intention and past practice indicates that the transaction will be settled in equity.

The grant date fair value of the cash alternative is CU1,500 and the grant date fair value of the equity alternative is CU1,800.

#### Analysis – fair value of cash alternative at settlement exceeds fair value of equity alternative

Assume the employee satisfies the service condition. At the end of year two, the fair value of the cash and equity alternatives are CU2,000 and CU1,900 respectively.

If at the end of year two, Company C chooses to settle in equity, the following amounts are recognised:

Year	Calculation	Expense (CU)	Adjustment to Equity (CU)	Adjustment to Liability (CU)
1	Equity component: (CU1,800 × 1/2 years)	900	900	-
2	Equity component: (CU1,800 × 2/2 years) – CU900 No further entries are required as the fair value of the equity alternative at the settlement date is less than the fair value of the cash alternative	900	900	-
<b>Total</b>		<b>1,800</b>	<b>1,800</b>	<b>-</b>

If at the end of year two, Company C chooses to settle in cash, the following amounts are recognised:

Year	Calculation	Expense (CU)	Adjustment to Equity (CU)	Adjustment to Liability (CU)
1	Equity component: (CU1,800 × 1/2 years)	900	900	-
2	Equity component: (CU1,800 × 2/2 years) – CU900 Repurchase of equity: CU1,900 (fair value of equity alternative at settlement date) Additional expense for excess value: CU2,000 (fair value of cash alternative at settlement) less CU1,900 (fair value of equity alternative at the settlement date)	900 100	900 (1,900)	- (2,000)
<b>Total</b>		<b>1,900</b>	<b>(100)</b>	<b>(2,000)</b>

## Example 2 – Entity has the choice of settlement (continued)

### Analysis – fair value of equity alternative at settlement exceeds fair value of cash alternative

Assume the employee satisfies the service condition. At the end of year two, the fair value of the cash and equity alternatives are CU1,900 and CU2,000 respectively.

If at the end of year two, Company C chooses to settle in cash, the following amounts are recognised:

Year	Calculation	Expense (CU)	Adjustment to Equity (CU)	Adjustment to Liability (CU)
1	Equity component: (CU1,800 × 1/2 years)	900	900	-
2	Equity component: (CU1,800 × 2/2 years) – CU900 Repurchase from equity: CU1,900 No further entries are required as the fair value of the cash alternative at settlement is less than the fair value of the equity alternative	900 -	900 (1,900)	- (1,900)
<b>Total</b>		<b>1,800</b>	<b>(100)</b>	<b>(1,900)</b>

If at the end of year two, Company C chooses to settle in equity, the following amounts are recognised:

Year	Calculation	Expense (CU)	Adjustment to Equity (CU)	Adjustment to Liability (CU)
1	Equity component: (CU1,800 × 1/2 years)	900	900	-
2	Equity component: (CU1,800 × 2/2 years) – CU900 Additional expense for excess value: CU2,000 (fair value of equity alternative at settlement) less CU1,900 (fair value of cash alternative at settlement)	900 100	900 100	- -
<b>Total</b>		<b>1,900</b>	<b>1,900</b>	<b>-</b>

### What happens if an entity changes its stated policy or intent in relation to the manner of settlement?

Subsequent to the grant date, there may be circumstances that give rise to a change in the manner of settlement and therefore, the classification of the share-based payment transaction as either equity-settled or cash-settled should be reassessed. For example, an entity may have a stated policy or history of settling in equity but now has the intent to settle in cash. IFRS 2 does not address this issue; however, in practice, changes in intent, settlement policy or settlement practice that give rise to a change in classification are accounted for as a modification, since these changes effectively represent a change to the terms and conditions of the existing arrangement. Some entities also treat changes in circumstances that are within an entity's control as modifications. Accounting for modifications is explained in our article '[Insights into IFRS 2 – Modifications and Cancellations of Share-Based Payment Arrangements with Employees](#)'.

### Practical insight – What happens when the method of settlement is contingent upon a future event?

An entity may also structure arrangements in a way that the method of settlement is contingent upon a future event, such as an initial public offering (IPO) or a change in control of the entity. IFRS 2 does not provide guidance for this situation, however, as discussed above, where the event is within the control of the entity, we believe that the change in manner of settlement should be accounted for as a modification. In contrast, where the event is outside of the entity and the counterparty's control (eg some change of control events), our view is that the entity should account for the transaction as either cash or equity-settled using one of two approaches, based on the facts and circumstances of the transaction:

- Under the first approach, the entity determines whether the award is cash-settled or equity-settled using the principles in IAS 37 'Provisions, Contingent Liabilities and Contingent Assets'. In essence, where it is possible but not probable (ie not more likely than not) for cash settlement to occur, the entity should account for the transaction as equity-settled. Whereas if cash settlement is probable, then the award should be accounted for as cash-settled. Furthermore, if the probability of one settlement alternative changes from not probable to probable, the entity assesses whether to reclassify the transaction (ie from equity-settled to cash-settled, or from cash-settled to equity-settled (using the grant date fair value)) and accounts for any differences in profit or loss.
- Under the second approach, the entity accounts for the transaction as cash-settled if it is possible for cash-settlement to occur, regardless of the probability of occurrence, since the entity cannot unilaterally avoid cash-settlement. The entity would reclassify the transaction upon settlement if necessary. This approach is similar to the guidance for contingent settlement provisions in IAS 32 'Financial Instruments: Presentation'.

Overall, the cumulative amount recognised to profit or loss between the grant date and settlement date will be equal to either the grant date fair value of the equity instrument (for the equity-settled alternative) or the fair value of the liability at settlement (for the cash-settled alternative), depending on which alternative ultimately occurs. However, by reclassifying the transaction from equity-settled to cash-settled or vice versa where necessary, volatility is introduced to profit or loss between the grant date and settlement date due to the requirement to remeasure the cash-settled alternative to its fair value at the end of each reporting period and upon settlement.

## How we can help

We hope you find the information in this article helpful in giving you insight into aspects of IFRS 2. If you would like to discuss any of the points raised, please speak to your usual Grant Thornton contact or visit [www.grantthornton.global/locations](http://www.grantthornton.global/locations) to find your local member firm.



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