Commission Regulation (EC) No 211/2005 of 4 February 2005 amending Regulation (EC) No 1725/2003 adopting certain international accounting standards in accordance with Regulation (EC) No 1606/2002 of the European Parliament and of the Council as regards International Financial Reporting Standards (IFRS) 1 and 2 and International Accounting Standards (IASs) No 12, 16, 19, 32, 33, 38 and 39 (Text with EEA relevance)

COMMISSION REGULATION (EC) No 211/2005

of 4 February 2005

amending Regulation (EC) No 1725/2003 adopting certain international accounting standards in accordance with Regulation (EC) No 1606/2002 of the European Parliament and of the Council as regards International Financial Reporting Standards (IFRS) 1 and 2 and International Accounting Standards (IASs) No 12, 16, 19, 32, 33, 38 and 39

(Text with EEA relevance)

THE COMMISSION OF THE EUROPEAN COMMUNITIES,

Having regard to the Treaty establishing the European Community.

Having regard to Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards[(1)], and in particular Article 3(1) thereof,

Whereas:

(1) By Commission Regulation (EC) No 1725/2003[(2)], certain international standards and interpretations that were extant at 1 September 2002 were adopted.

(2) On 19 February 2004, the International Accounting Standards Board (IASB) published International Financial Reporting Standard (IFRS) 2 *Share-based Payment*. IFRS 2 requires for the first time that companies reflect in their income statements the effects of share-based payment transactions, including expenses associated with transactions in which share options are granted to management and employees. In the past, transactions in which share options were granted to employees were not recognized in the company's income statements but were disclosed in the notes not affecting reporting of earnings to capital markets.

(3) The consultation with technical experts in the field confirms that IFRS 2 meet the technical criteria for adoption set out in Article 3 of Regulation (EC) No 1606/2002, and in particular the requirement of being conducive to the European public good.

(4) IFRS 2 does not specify which valuation models should be used. Instead, it only describes the factors that should be at least taken into account when estimating the *fair value* of share based payments. This was done on purpose in order not to prevent the development of appropriate measurement techniques which hitherto do not exist for all forms of share based payments (e.g. non tradable long term employee stock options).

New alternative methods might be developed in the future to accommodate the needs of companies, auditors and investors. In particular, newly listed companies or companies without a sufficient track record might have difficulties to estimate future share prices.

(5) The Commission took note of the criticism about the complexity of *IFRS 2 Share-based Payment* that were advanced from several concerned parties during the consultation process. The Commission is aware of the remaining technical issues of this standard and the related concerns regarding their economic impact. The Commission recognizes that, in view of the potential impact, such as on employee stock option schemes, and the possible implications for the competitiveness of EU companies, the application should be regularly monitored. However, endorsement is in the interest of European capital markets and European investors. The Commission will therefore monitor the future effects of IFRS 2 on European companies and review the applicability of the standard by July 2007 at the latest.

(6) The Commission recalls that Regulation (EC) No 1606/2002 (the IAS Regulation) of 19 July 2002 requires that for each financial year starting on or after 1 January 2005, companies governed by the law of a Member State shall prepare their consolidated accounts in conformity with the international accounting standards adopted in accordance with the procedure laid down in Article 6(2) if, at their balance sheet date, their securities are admitted to trading on a regulated market of any Member State within the meaning of Article 1(13) of Council Directive 93/22/EEC of 10 May 1993 on investment services in the securities field[(3)].

(7) The adoption of IFRS 2 implies, by way of consequence, amendments to other international accounting standards in order to ensure consistency between international accounting standards. Those consequential amendments are affecting International Financial Reporting Standard (IFRS) No 1, International Accounting Standards (IASs) Nos 12, 16, 19, 32, 33, 38 and 39.

(8) Regulation (EC) No 1725/2003 should therefore be amended accordingly.

(9) The measures provided for in this Regulation are in accordance with the opinion of the Accounting Regulatory Committee,

HAS ADOPTED THIS REGULATION:

Article 1

The Annex to Regulation (EC) No 1725/2003 is amended as follows:

1. International Financial Reporting Standard (IFRS) 2 *Share-based Payment* is inserted in the Annex to Regulation (EC) No 1725/2003;

2. the adoption of IFRS 2 implies, by way of consequence, amendments to IFRS 1, to International Accounting Standards (IASs) No 12, 16, 19, 32, 33, 38 and 39 in order to ensure consistency between international accounting standards;

3. the text for insertion is set out in the Annex to this Regulation

Article 2

This Regulation shall enter into force on the third day following its publication in the *Official Journal of the European Union*.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels, 4 February 2005.

For the Commission

Charlie McCREEVY

Member of the Commission

Changes to legislation: *There are currently no known outstanding effects for the Commission Regulation (EC) No 211/2005. (See end of Document for details)*

ANNEX

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INTERNATIONAL FINANCIAL REPORTING STANDARD 2

Share-based Payment

OBJECTIVE

1. The objective of this IFRS is to specify the financial reporting by an entity when it undertakes a *share-based payment transaction*. In particular, it requires an entity to reflect in its profit or loss and financial position the effects of share-based payment transactions, including expenses associated with transactions in which *share options* are granted to employees.

SCOPE

2. An entity shall apply this IFRS in accounting for all share-based payment transactions including:

   (a) *equity-settled share-based payment transactions*, in which the entity receives goods or services as consideration for *equity instruments* of the entity (including shares or share options),

   (b) *cash-settled share-based payment transactions*, in which the entity acquires goods or services by incurring liabilities to the supplier of those goods or services for amounts that are based on the price (or value) of the entity's shares or other equity instruments of the entity,

   and

   (c) transactions in which the entity receives or acquires goods or services and the terms of the arrangement provide either the entity or the supplier of those goods or services with a choice of whether the entity settles the transaction in cash (or other assets) or by issuing equity instruments,

   except as noted in paragraphs 5 and 6.

3. For the purposes of this IFRS, transfers of an entity's equity instruments by its shareholders to parties that have supplied goods or services to the entity (including employees) are share-based payment transactions, unless the transfer is clearly for a purpose other than payment for goods or services supplied to the entity. This also applies to transfers of equity instruments of the entity's parent, or equity instruments of another entity in the same group as the entity, to parties that have supplied goods or services to the entity.

4. For the purposes of this IFRS, a transaction with an employee (or other party) in his/her capacity as a holder of equity instruments of the entity is not a share-based payment transaction. For example, if an entity grants all holders of a particular class of its equity instruments the right to acquire additional equity instruments of the entity at a price that is less than the fair value of those equity instruments, and an employee receives such a right because he/she is a holder of equity instruments of that particular class, the granting or exercise of that right is not subject to the requirements of this IFRS.

***Changes to legislation:** There are currently no known outstanding effects for the Commission Regulation (EC) No 211/2005. (See end of Document for details)*

5. As noted in paragraph 2, this IFRS applies to share-based payment transactions in which an entity acquires or receives goods or services. Goods includes inventories, consumables, property, plant and equipment, intangible assets and other non-financial assets. However, an entity shall not apply this IFRS to transactions in which the entity acquires goods as part of the net assets acquired in a business combination to which IAS 22 *Business Combinations* applies. Hence, equity instruments issued in a business combination in exchange for control of the acquiree are not within the scope of this IFRS. However, equity instruments granted to employees of the acquiree in their capacity as employees (eg in return for continued service) are within the scope of this IFRS. Similarly, the cancellation, replacement or other modification of *share-based payment arrangements* because of a business combination or other equity restructuring shall be accounted for in accordance with this IFRS.

6. This IFRS does not apply to share-based payment transactions in which the entity receives or acquires goods or services under a contract within the scope of paragraphs 8-10 of IAS 32 *Financial Instruments: Disclosure and Presentation* (as revised in 2003) or paragraphs 5-7 of IAS 39 *Financial Instruments: Recognition and Measurement* (as revised in 2003).

RECOGNITION

7. **An entity shall recognise the goods or services received or acquired in a share-based payment transaction when it obtains the goods or as the services are received. The entity shall recognise a corresponding increase in equity if the goods or services were received in an equity-settled share-based payment transaction, or a liability if the goods or services were acquired in a cash-settled share-based payment transaction.**

8. **When the goods or services received or acquired in a share-based payment transaction do not qualify for recognition as assets, they shall be recognised as expenses.**

IFRS 29. Typically, an expense arises from the consumption of goods or services. For example, services are typically consumed immediately, in which case an expense is recognised as the counterparty renders service. Goods might be consumed over a period of time or, in the case of inventories, sold at a later date, in which case an expense is recognised when the goods are consumed or sold. However, sometimes it is necessary to recognise an expense before the goods or services are consumed or sold, because they do not qualify for recognition as assets. For example, an entity might acquire goods as part of the research phase of a project to develop a new product. Although those goods have not been consumed, they might not qualify for recognition as assets under the applicable IFRS.

EQUITY-SETTLED SHARE-BASED PAYMENT TRANSACTIONS

Overview

10. **For equity-settled share-based payment transactions, the entity shall measure the goods or services received, and the corresponding increase in equity, directly, at the *fair value* of the goods or services received, unless that fair value cannot be estimated reliably. If the entity cannot estimate reliably the fair value of the goods or services received, the entity shall measure their value, and the corresponding increase in equity, indirectly, by reference to the fair value of the[(4)] *equity instruments granted*.**

11. To apply the requirements of paragraph 10 to transactions with *employees and others providing similar services*[(5)], the entity shall measure the fair value of the services received by reference to the fair value of the equity instruments granted, because