

International Accounting Standard IAS 33

Earnings per Share

January 2022

BASIS FOR CONCLUSIONS

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Basis for Conclusions on IAS 33 *Earnings per Share*

This Basis for Conclusions accompanies, but is not part of, IAS 33.

Introduction

- BC1 This Basis for Conclusions summarises the International Accounting Standards Board's considerations in reaching its conclusions on revising IAS 33 *Earnings Per Share* in 2003. Individual Board members gave greater weight to some factors than to others.
- BC2 In July 2001 the Board announced that, as part of its initial agenda of technical projects, it would undertake a project to improve a number of Standards, including IAS 33. The project was undertaken in the light of queries and criticisms raised in relation to the Standards by securities regulators, professional accountants and other interested parties. The objectives of the Improvements project were to reduce or eliminate alternatives, redundancies and conflicts within Standards, to deal with some convergence issues and to make other improvements. In May 2002 the Board published its proposals in an Exposure Draft of *Improvements to International Accounting Standards*, with a comment deadline of 16 September 2002. The Board received over 160 comment letters on the Exposure Draft.
- BC3 Because the Board's intention was not to reconsider the fundamental approach to the determination and presentation of earnings per share established by IAS 33, this Basis for Conclusions does not discuss requirements in IAS 33 that the Board has not reconsidered.

Presentation of parent's separate earnings per share

- BC4 The Exposure Draft published in May 2002 proposed deleting paragraphs 2 and 3 of the previous version of IAS 33, which stated that when the parent's separate financial statements and consolidated financial statements are presented, earnings per share need be presented only on the basis of consolidated information.
- BC5 Some respondents expressed concern that the presentation of two earnings per share figures (one for the parent's separate financial statements and one for the consolidated financial statements) might be misleading.
- BC6 The Board noted that disclosing the parent's separate earnings per share amount is useful in limited situations, and therefore decided to retain the option. However, the Board decided that the Standard should prohibit presentation of the parent's separate earnings per share amounts in the consolidated financial statements (either on the face of the financial statements or in the notes).

Contracts that may be settled in ordinary shares or cash

- BC7 The Exposure Draft proposed that an entity should include in the calculation of the number of potential ordinary shares in the diluted earnings per share calculation contracts that may be settled in ordinary shares or cash, at the issuer's option, based on a rebuttable presumption that the contracts will be settled in shares. This proposed presumption could be rebutted if the issuer had acted through an established pattern of past practice, published policies, or by having made a sufficiently specific current statement indicating to other parties the manner in which it expected to settle, and, as a result, the issuer had created a valid expectation on the part of those other parties that it would settle in a manner other than by issuing shares.
- BC8 The majority of the respondents on the Exposure Draft agreed with the proposed treatment of contracts that may be settled in ordinary shares or cash at the issuer's option. However, the Board decided to withdraw the notion of a rebuttable presumption and to incorporate into the Standard the requirements of SIC-24 *Earnings Per Share—Financial Instruments and Other Contracts that May Be Settled in Shares*. SIC-24 requires financial instruments or other contracts that may result in the issue of ordinary shares of the entity to be considered potential ordinary shares of the entity.
- BC9 Although the proposed treatment would have converged with that required by several liaison standard-setters, for example, in US SFAS 128 *Earnings per Share*, the Board concluded that the notion of a rebuttable presumption is inconsistent with the stated objective of diluted earnings per share. The US Financial Accounting Standards Board has agreed to consider this difference as part of the joint short-term convergence project with the IASB.

Calculation of year-to-date diluted earnings per share

- BC10 The Exposure Draft proposed the following approach to the year-to-date calculation of diluted earnings per share:
- (a) The number of potential ordinary shares is a year-to-date weighted average of the number of potential ordinary shares included in each interim diluted earnings per share calculation, rather than a year-to-date weighted average of the number of potential ordinary shares weighted for the period they were outstanding (ie without regard for the diluted earnings per share information reported during the interim periods).
 - (b) The number of potential ordinary shares is computed using the average market price during the interim periods, rather than using the average market price during the year-to-date period.
 - (c) Contingently issuable shares are weighted for the interim periods in which they were included in the computation of diluted earnings per share, rather than being included in the computation of diluted earnings per share (if the conditions are satisfied) from the beginning of the year-to-date reporting period (or from the date of the contingent share agreement, if later).

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- BC11 The majority of the respondents on the Exposure Draft disagreed with the proposed approach to the year-to-date calculation of diluted earnings per share. The most significant argument against the proposed approach was that the proposed calculation of diluted earnings per share could result in an amount for year-to-date diluted earnings per share that was different for entities that report more frequently, for example, on a quarterly or half-yearly basis, and for entities that report only annually. It was also noted that this problem would be exacerbated for entities with seasonal businesses.
- BC12 The Board considered whether to accept that differences in the frequency of interim reporting would result in different earnings per share amounts being reported. However, IAS 34 *Interim Financial Reporting* states 'the frequency of an entity's reporting (annual, half-yearly, or quarterly) should not affect the measurement of its annual results. To achieve that objective, measurements for interim reporting purposes should be made on a year-to-date basis.'
- BC13 The Board also considered whether it could mandate the frequency of interim reporting to ensure consistency between all entities preparing financial statements in accordance with IFRSs, ie those that are brought within the scope of IAS 33 by virtue of issuing publicly traded instruments or because they elect to present earnings per share. However, IAS 34 states that, 'This Standard does not mandate which entities should be required to publish interim financial reports, how frequently, or how soon after the end of an interim period.' The frequency of interim reporting is mandated by securities regulators, stock exchanges, governments, and accountancy bodies, and varies by jurisdiction.
- BC14 Although the proposed approach for the calculation of year-to-date diluted earnings per share would have converged with US SFAS 128, the Board concluded that the approach was inconsistent with IAS 34 and that it could not mandate the frequency of interim reporting. The US Financial Accounting Standards Board has agreed to consider this difference as part of the joint short-term convergence project with the IASB as well as the issue noted in paragraph BC9.

Other changes

- BC15 Implementation questions have arisen since the previous version of IAS 33 was issued, typically concerning the application of the Standard to complex capital structures and arrangements. In response, the Board decided to provide additional application guidance in the Appendix as well as illustrative examples on more complex matters that were not addressed in the previous version of IAS 33. These matters include the effects of contingently issuable shares, potential ordinary shares of subsidiaries, joint ventures or associates, participating equity instruments, written put options, and purchased put and call options.