Accounting Standards Board
AcSB
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Conseil des normes comptables

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CL 155

March 11, 2003

Ms. Kimberley Crook
Project Manager
International Accounting Standards Board
30 Cannon Street
London
EC4M 6XH
United Kingdom

Dear Ms. Crook:

Exposure Draft – ED 2 Share-Based Payment

Introduction

The Accounting Standards Board (AcSB) is extremely supportive of the IASB's initiative in accounting for share-based payments. We strongly agree that all share-based payment transactions should be recognized in the financial statements and that they should be measured at fair value.

The AcSB issued STOCK-BASED COMPENSATION AND OTHER STOCK-BASED PAYMENTS, Section 3870 in December 2001, effective (for most enterprises) for fiscal years beginning on or after January 1, 2002. Section 3870 is based on Financial Accounting Standards Board (FASB) Statement No. 123, *Accounting for Stock-Based Compensation*.

As you may be aware, the AcSB has a policy of converging its standards with the best quality international or FASB standards unless there is a compelling reason not to do so. Prior to the issue of Section 3870, the AcSB took the decision to harmonize that standard with those of the United States. Similar to US standards, Section 3870 encourages but does not force enterprises to recognize compensation expense for so called "plain vanilla" stock options. Enterprises issuing these instruments have the option of disclosing pro forma net income and pro forma earnings per share as if the fair value based accounting method had been used. Although not persuaded that the disclosure option was conceptually sound, the AcSB accepted it as a short- term expedient to avoid what many viewed as a serious potential competitive disadvantage relative to US enterprises while the AcSB continued to work with the IASB and the FASB to eliminate the disclosure option.

Events post-Enron have caused many in Canada to believe that the “competitive disadvantage” card has been overplayed. Recent financial reporting scandals and a growing amount of academic research indicate that the market rewards good accounting and punishes bad. In September, 2002, the AcSB’s oversight body, the Accounting Standards Oversight Council, unanimously recommended that the AcSB reconsider the desirability of the disclosure option. In December 2002 the AcSB issued an exposure draft, proposing mandatory expense recognition (with some minor exceptions) for all stock-based compensation transactions. That exposure draft also identified the significant differences between Section 3870 and ED 2 *Share-Based Payment*. The AcSB indicated that if its respondents believe ED 2 to be demonstrably superior to Section 3870, the AcSB would be prepared to converge Section 3870 with ED 2. The exposure draft’s comment period ends on March 31, 2003, and the proposed implementation date is for fiscal years beginning on or after January 1, 2004.

Plea for convergence

The AcSB is strongly of the view that the major national standard setters and the IASB should make a concerted effort to resolve and remove the differences identified in Question 24, so that the end result is full harmonization on fair value measurement and recognition principles, as well as all significant aspects of implementation. The AcSB is of the opinion that the demonstration of a united front among standard setters would demolish the arguments of those who worry about potential competitive harm in the international capital markets if the recognition and measurement of stock-based compensation can vary significantly depending on the accounting standards being applied.

The AcSB strongly suggests that the IASB and its partner national standard setters co-ordinate their timetables so that, if possible, these bodies discuss the different philosophies underlying the proposed IFRS and SFAS 123, and thereafter issue a single converged standard simultaneously.

The AcSB believes that the ultimate objective should be the best possible measurement of fair value in a way that faithfully represents the economic substance of the transaction. The interpretation and application of the fair value measurement objective raises issues that, while clearly important, are secondary to the fundamental objective.

The AcSB has not yet deliberated on whether the approach taken in the proposed IFRS is an improvement to the fair value measurement approach previously adopted by the FASB in SFAS 123. It will do so when it has heard from its constituency. The AcSB did, however, request its respondents to respond directly to the IASB on the proposed IFRS.

Please get back to me or Harry Klompas [harry.klompas@cica.ca] if you need any additional information.

Yours truly,

Paul Cherry
Chair
Accounting Standards Board