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March 10, 2003

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

Dear Ms. Crook:

TIAA-CREF is writing in response to your Exposure Draft of a proposed International Financial Reporting Standard, "Share-based Payment," ED 2.

As stated in our December 2001 comment letter to you, we support changes in international accounting rules for all share-based payments. Of particular importance to the users of financial statements is that all transactions undertaken by a company, regardless of the currency (cash, stock, real property, or stock options) should be recognized in financial statements. To do otherwise has the potential to misstate corporate financial performance and results in a disservice to those who rely on the credibility of financial reports. Current reporting standards in the United States and worldwide do not require appropriate financial reporting for all share-based payments. In the U.S., one type of payment—the fixed, at-the-money stock option—can always result in zero expense in financial statements, regardless of the number of options issued. Other types of options and payments in shares, can result in recognized expenses, resulting in an unlevel playing field across all forms of compensation. We are encouraged that you are attempting to improve reporting in this area, and we are hopeful that the U.S. Financial Accounting Standards Board will reconsider its accounting rules. It would be in everyone's best interests if there were a single method of accounting required for share-based payments for all companies, regardless of their geographical location.

In Attachment 1, we respond to your specific questions. However, the most important issue to us is that stock or stock options used to attract, retain, or compensate employees should be reported as expense in income statements. Vastly different accounting for what are quite similar transactions is not a credible result. Using company resources to pay for operating expenses should be captured in financial reports. We support the Board's decision to significantly improve international financial reporting in this area.

We support the basic principles in ED 2: estimate the value of all shares and options at their fair value at the date of grant, and expense that value over the vesting or service period, without adjustment for changes in stock price after the date of grant. We have some concerns about some aspects of the proposal, none of which should detract from our support of the project or the principles. We believe that valuing stock and options at the date of grant most appropriately reflects the nature of the compensation transaction, and is consistent with other forms of equity compensation payments..

If you have questions about our views or if you would like additional information, please contact me.

Sincerely,

Peter C. Clapman
Senior Vice President, Chief Counsel-Corporate Governance

ATTACHMENT 1

Answers to the Questions Raised in the Exposure Draft, *Share-Based Payment*

Question 1
Paragraphs 1-3 of the draft IFRS set out the proposed scope of the IFRS. There are no proposed exemptions, apart from for transactions within the scope of another IFRS. Is the proposed scope appropriate? If not, which transactions should be excluded and why?

The scope is appropriate.

Question 2
Paragraphs 4-6 of the draft IFRS propose requirements for the recognition of share-based payment transactions, including the recognition of an expense when the goods or services received or acquired are consumed. Are these recognition requirements appropriate? If not, why not, or in which circumstances are the recognition requirements inappropriate?

The recognition requirements are generally appropriate. See concerns about the "unit-of-service" method in response to Question 9.

Question 3
For an equity-settled share-based payment transaction, the draft IFRS proposes that, in principle, the entity should measure the goods or services received, and the corresponding increase in equity, either directly, at the fair value of the goods or services received, or indirectly, by reference to the fair value of the equity instruments granted, whichever fair value is more readily determinable (paragraph 7). There are no exemptions to the requirement to measure share-based payment transactions at fair value. For example, there are no exemptions for unlisted entities. Is this measurement principle appropriate? If not, why not, or in which circumstances is it not appropriate?

The measurement principle is appropriate. However, we believe that measurement accommodations are acceptable for difficult situations, such as unlisted companies, discussed in our answer to Question 11.

Question 4
If the fair value of the goods or services received in an equity-settled share-based payment transaction is measured directly, the draft IFRS proposes that fair value should be measured at the date when the entity obtains the goods or receives the services (paragraph 8). Do you agree that this is the appropriate date at which to measure the fair value of the goods or services received? If not, at which date should the fair value of the goods or services received be measured? Why?

Yes, the date of receipt of goods or services is the appropriate measurement date. However, if the fair value of the goods or services received is measured directly (because it is more readily determinable), it is likely that the evidence of fair value will be a bill from the goods or services provider. In those circumstances, the measurement date will be largely irrelevant.

Question 5

If the fair value of the goods or services received in an equity-settled share-based payment transaction is measured by reference to the fair value of the equity instruments granted, the draft IFRS proposes that the fair value of the equity instruments granted should be measured at grant date (paragraph 8). Do you agree that this is the appropriate date at which to measure the fair value of the equity instruments granted? If not, at which date should the fair value of the equity instruments granted be measured? Why?

We are supportive of a grant date approach for all share-based payment transactions. In the vast majority of employee transactions, the fair value of the equity instruments will be more readily determinable than the employee services. Valuing the equity at the date that the compensation contract is determined—the grant date—is most appropriate. All of the other parts of the compensation arrangement are determined at the beginning of the contract period. The number of equity instruments included in the compensation arrangement is based on the stock price (and all other known factors that might affect the value of other equity, such as options) at the beginning of the contract period. The employer and employee understand the terms of the agreement at the date of grant. We believe that entities must be able to reasonably estimate the value of share-based awards at the date of grant in order to determine the details of the award, including the number of shares or share options to grant.

Question 6

For equity-settled transactions with parties other than employees, the draft IFRS proposes a rebuttable presumption that the fair value of the goods or services received is more readily determinable than the fair value of the equity instruments granted (paragraphs 9 and 10). Do you agree that the fair value of the goods or services received is usually more readily determinable than the fair value of the equity instruments granted? In what circumstances is this not so?

Yes, we agree that transactions with non employees will generally provide a more readily determinable fair value of the goods or services than the equity instruments, and a rebuttable presumption is appropriate. However, we would like to be assured that similar transactions will be accounted for in a similar manner. For example, share options given to a consultant or contract "employee" with the same terms as those given to employees should be recognized in the same manner as employee share options. We propose that, even with a rebuttable presumption for non employees, the fair value of the equity instruments granted be estimated and compared to the fair value of the goods or services to ensure reasonableness of the amount recognized.

Question 7

For equity-settled transactions with employees, the draft IFRS proposes that the entity should measure the fair value of the employee services received by reference to the fair value of the equity instruments granted, because the latter fair value is more readily determinable (paragraphs 11 and 12). Do you agree that the fair value of the equity

instruments granted is more readily determinable than the fair value of the employee services received? Are there any circumstances in which this is not so?

In almost all circumstances, it is impossible to directly measure the value of employee services. Like all other employee benefit transactions, including pensions, IFRS should recognize the value of the instrument transferred to the employee as the cost of those employee services. Therefore, we agree that the fair value of the equity instruments granted is more readily determinable than the fair value of the employee services and should be considered the cost of the employee services.

Question 8

Paragraphs 13 and 14 of the draft IFRS propose requirements for determining when the counterparty renders service for the equity instruments granted, based on whether the counterparty is required to complete a specified period of service before the equity instruments vest. Do you agree that it is reasonable to presume that the services rendered by the counterparty as consideration for the equity instruments are received during the vesting period? If not, when are the services received, in your view?

If there is a stated vesting period, that should be presumed to be the period during which services are received.

Question 9

If the services received are measured by using the fair value of the equity instruments granted as a surrogate measure, the draft IFRS proposes that the entity should determine the amount to attribute to each unit of service received, by dividing the fair value of the equity instruments granted by the number of units of service expected to be received during the vesting period (paragraph 15). Do you agree that if the fair value of the equity instruments granted is used as a surrogate measure of the fair value of the services received, it is necessary to determine the amount to attribute to each unit of service received? If not, what alternative approach do you propose? If an entity is required to determine the amount to attribute to each unit of service received, do you agree that this should be calculated by dividing the fair value of the equity instruments granted by the number of units of services expected to be received during the vesting period? If not, what alternative method do you propose?

We do not agree that it is necessary to determine the amount attributable to each unit of service received. First, the method is complicated and difficult to explain in all circumstances. More importantly, entities should be required to recognize the value only of the amount actually transferred in exchange for the employee services. In employee transactions, the value of the equity transferred is being used as a surrogate measure for the value of the employee services received because it is not possible to directly value the employee services. That approach is the one used for all employee service transactions, regardless of the form of payment: measure the value of what is transferred in exchange for the receipt of employee services.

We understand the principle of recognizing that some employee services were received. However, consistent with the measurement of other employee benefit contracts, if the conditions of the agreement (vesting period) are not fulfilled, the entity has no obligation to transfer benefits. That principle is appropriate whether the payment is cash or shares or share options. The objective is to account for the cost of employee services and if the instrument is not earned and does not vest, it seems reasonable to us that no expense should be recognized. In recognizing the value of the equity instrument as the cost of the employee services, it is appropriate to show expense only for those equity instruments actually transferred to employees. Recognizing expense for the amount transferred is consistent with all other forms of employee benefits, including salaries, bonuses, and pensions, among others.

If the attribution method proposed in ED 2 were applied to all other employee benefit transactions, it would seem to us that pension costs other compensation arrangements would be significantly changed. Some cost would need to be recognized for services rendered during part of the vesting period, even though no payment in cash would be required. Just because they are liability transactions, the company would be able to reverse the liability, but cost recognition for the receipt of employee services would seem appropriate under the model proposed in ED 2. We do not agree with that approach to attribution for employee benefit transactions, regardless of whether the payment is shares or cash.

Question 10

In an equity-settled share -based payment transaction, the draft IFRS proposes that having recognized the services received, and a corresponding increase in the equity, the entity should make no subsequent adjustment to total equity, even if the equity instruments granted do not vest or, in the case of options, the options are not exercised (paragraph 16). However, this requirement does not preclude the entity from recognising a transfer within equity, i.e. a transfer from one component of equity to another. Do you agree with this proposed requirement? If not, in what circumstances should an adjustment be made to total equity and why?

We believe that if an equity instrument is not issued because of failure to vest, no transfer takes place and no expense or change in equity should be recognized.

If vested shares or options are not exercised for any reason, a transfer within equity should be permitted.

Question 11

The draft IFRS proposes that the entity should measure the fair value of equity instruments granted, based on market prices if available, taking into account the terms and conditions of the grant (paragraph 17). In the absence of a market price, the draft IFRS proposes that the entity should estimate the fair value of options granted, by applying an option pricing model that takes into account various factors, namely the exercise price of the option, the life of the option, the current price of the underlying shares, the expected volatility of the share price, the dividends expected on the shares (where appropriate) and the risk-free interest rate for the life of the option (paragraph 20). Paragraph 23 of the proposed IFRS explains when it is appropriate to take into account expected dividends. Do you agree that an option-pricing model should be applied to estimate the fair value of options granted? If not, by what other means should the fair value of the options be

estimated? Are there circumstances in which it would be inappropriate or impracticable to take into account any of the factors listed above in applying an option-pricing model?

We agree that estimating the fair value of shares and options at the grant date based on market prices, if available, is appropriate for public companies. We also agree that an estimate of the fair value at the date of grant using option-pricing models for employee options is appropriate because there is no observable market price.

Because of uncertainties about measurement, we would allow nonpublic companies the choice of estimating expected share price volatility or using a zero input (FASB Statement 123's so called "minimum value.") for that assumption. Some nonpublic companies may want to use peer company volatility or other information to estimate a fair value for their options. Allowing a choice of measurement methods is clearly an exception to the basic approach of fair value for all companies. We are concerned, however, that many nonpublic companies might have little basis for estimating stock price volatility. There likely are some large, established private companies with clear peer groups. in principle, this same exception could be provided for newly public companies as well, particularly given the risks of long-term public success. However, besides some arbitrary period of time, we are unable to support that approach. Therefore, the public/nonpublic measurement differences seem a practical alternative that should be permitted.

Question 12

If an option is non-transferable, the draft IFRS proposes that the expected life of an option rather than its contracted life should be used in applying an option pricing model (paragraph 21). The draft IFRS also proposes requirements for options that are subject to vesting conditions and therefore cannot be exercised during the vesting period (paragraph 22). Do you agree that replacing an option's contracted life with its expected life when applying an option pricing model is an appropriate means of adjusting the option's fair value for the effects of non-transferability? If not, do you have an alternative suggestion? Is the proposed requirement for taking into account the inability to exercise an option during the vesting period appropriate?

We agree that a "discount" for nontransferability from option-pricing model values is appropriate at this time for employee options. Nontransferability is an attribute of employee options that is significantly different from traded options, and adjustment for it is necessary. It is possible that some other methodology might be developed to recognize the nontransferability of employee options. For that possibility and others, it is important that the final IFRS be drafted in a principles-based, flexible manner to accommodate technological innovations in option valuation.

We question the guidance in paragraph 22 (b) that is supposed to take into account the inability to exercise an option during the vesting period. If the expected life is used as an input in the model, and the model assumes that the option can only be exercised at the end of the term, we do not follow how that addresses the vesting period restriction.

Question 13

If a grant of shares or options is conditional upon satisfying specified vesting conditions, the draft IFRS proposes that these conditions should be taken into account when an entity

measures the fair value of the shares or options granted. In the case of options, vesting conditions should be taken into account either by incorporating them into the application of an option pricing model or by making an appropriate adjustment to the value produced by such a model (paragraph 24). Do you agree that vesting conditions should be taken into account when estimating the fair value of options or shares granted? If not, why not? Do you have any suggestions for how vesting conditions should be taken into account when estimating the fair value of shares or options granted?

Yes, vesting conditions must be taken into account in valuing employee options. The method illustrated in the example in Appendix B seems a reasonable way to discount for vesting conditions. Again, we encourage the IASB to incorporate flexibility into the final IFRS to allow for developments in option valuation methodologies.

Question 14
For options with a reload feature, the draft IFRS proposes that the reload feature should be taken into account, where practicable, when an entity measures the fair value of the options granted. However, if the reload feature is not taken into account in the measurement of the fair value of the options granted, then the reload option granted should be accounted for as a new option grant (paragraph 25). Is this proposed requirement appropriate? If not, why not? Do you have an alternative proposal for dealing with options with reload features?

If it is possible to properly measure the value of a reload feature at the date of grant, that approach should be taken. We are unaware of any reliable methodology to do so. In the absence of a reliable reload measurement at the date of grant, we support requiring each reload to be accounted for as a new grant.

Question 15
The draft IFRS proposes requirements for taking into account various features common to employee share options, such as non-transferability, inability to exercise the option during the vesting period, and vesting conditions (paragraphs 2 1-25). Are there other common features of employee share options for which the IFRS should specify requirements?

Some employee option plans have other features, including black-out periods or exercise restrictions beyond vesting date. It is possible that more elaborate employee option plans will be developed in future years. If there is a reasonable way to account for those features, they should be incorporated into the option valuation process. This is another reason to be less prescriptive about particular discounts for particular features in employee options.

Question 16
The draft IFRS does not contain prescriptive guidance on the estimation of the fair value of options, consistently with the Board's objective of setting principles-based standards and to allow for future developments in valuation methodologies. Do you agree with this

approach? Are there specific aspects of valuing options for which such guidance should be given? .

We agree with the Board's objective of setting principles-based standards to allow for future developments in valuation. However, it seems to us that there is some quite prescriptive guidance in the draft IFRS on option valuation, particularly paragraph 21 regarding the treatment for nontransferability (use expected life). See our response to Question 12.

Question 17
If an entity reprices a share option, or otherwise modifies the terms or conditions on which equity instruments were granted, the draft IFRS proposes that the entity should measure the incremental value granted upon repricing, and include that incremental value when measuring the services received. This means that the entity is required to recognise additional amounts for services received during the remainder of the vesting period, i.e. additional to the amounts recognised in respect of the original option grant. Example 3 in Appendix B illustrates this requirement. As shown in that example, the incremental value granted on repricing is treated as a new option grant, in addition to the original option grant. An alternative approach is also illustrated, whereby the two grants are averaged and spread over the remainder of the vesting period.

Do you agree that the incremental value granted should be taken into account when measuring the services received, resulting in the recognition of additional amounts in the remainder of the vesting period? If not, how do you suggest repricing should be dealt with? Of the two methods illustrated in Example 3, which is more appropriate? Why?

An incremental approach should be taken to repricings, or other modifications of option grants. That incremental value given, based on the fair values at the date of modification, should be recognized over the remaining or new vesting period, if there is one in the new grant. However, it does not seem to make sense to continue to recognize the original expense from the unvested portion of the original grant over what would have been the original vesting period. No reversal of recognized expense should be allowed for the original grant, but we don't understand why it is appropriate to require continued expensing for a grant that no longer exists after repricing or modification. See our answer to Question 18.

Question 18
If an entity cancels a share or option grant during the vesting period (other than a grant cancelled by forfeiture when the vesting conditions are not satisfied), the draft IFRS proposes that the entity should continue to recognise the services rendered by the counterparty in the remainder of the vesting period, as if that grant had not been cancelled. The draft IFRS also proposes requirements for dealing with any payment made on cancellation and/or a grant of replacement options, and for the repurchase of vested equity instruments. Are the proposed requirements appropriate? If not, please explain why not and provide details of your suggested alternative approach.

For reasons similar to those in Question 17, we believe it is inappropriate to continue recognizing expense for a share or option grant that no longer exists. In mergers and acquisitions, it is common for the acquired entity's options to be cancelled and replaced. In those situations, the acquired entity no longer exists, and it is inconceivable to us that the value of options based on that nonexistent entity should continue to be recognized as expense over what would have been the original vesting period.

Question 19

For cash-settled share-based payment transactions, the draft IFRS proposes that the entity should measure the goods or services acquired and the liability incurred at the fair value of the liability. Until the liability is settled, the entity should remeasure the fair value of the liability at each reporting date, with any changes in value recognised in the income statement. Are the proposed requirements appropriate? If not, please provide details of your suggested alternative approach.

Yes, we agree that share-based liabilities should be initially measured and remeasured based on the fair value of the liabilities at each reporting date, with fair value changes recognized in the income statement. We acknowledge that there will be different accounting recognition depending on the form of payment, a result that exists under current accounting in the U.S. and elsewhere. Cash payments, based on share prices, must be shown as liabilities, resulting in what amounts to as "exercise date" measurement. The only way to achieve symmetry between cash-settled and equity-settled payments is to use an exercise date measurement for equity instruments. In our December 2001 letter to you, we described the benefits of using exercise date as the final measurement date for shares and options. We read ED 2's basis for conclusions that describes the reasons the IASB rejected exercise date measurement for equity transactions. For a variety of reasons, including symmetry between cash and equity payments, exercise date is an appealing approach, if only for practical purposes. However, on balance, for the reasons stated earlier in this response, we are supportive of a grant date approach for equity payments.

Question 20

For share-based payment transactions in which either the entity or the supplier of goods or services may choose whether the entity settles the transaction in cash or by issuing equity instruments, the draft IFRS proposes that the entity should account for the transaction, or the components of that transaction, as a cash-settled share-based payment transaction if the entity has incurred a liability to settle in cash, or as an equity-settled share-based payment transaction if no such liability has been incurred. The draft IFRS proposes various requirements to apply this principle. Are the proposed requirements appropriate? If not, please provide details of your suggested alternative approach.

Calling for separate identification and recognition of debt and equity components of share-based payments with optional settlement forms, is complicated. We question the number of circumstances in which optional settlement is a condition, and whether detailed guidance in an IFRS on share-based payments is necessary. We assume that the majority of transactions offer equivalent value at the date of grant, calling into question some of the proposed guidance, particularly that in paragraph 38. If the award calls for a choice of 2 settlement alternatives with equivalent value at the date of grant (share options or cash-settled share appreciation rights), why would that be considered a compound instrument in which the value of the equity component is zero? If the value of the entire award can be estimated directly at the date of grant, there should be no need to bifurcate the components and value each separately. Perhaps it is possible to refer to the IASB standards on financial instruments in those unusual circumstances in which compound financial instruments for share-based payments are granted.

Question 21
The draft IFRS proposes that an entity should disclose information to enable users of financial statements to understand:

(a) the nature and extent of share-based payment arrangements that existed during the period,
(b) how the fair value of the goods or services received, or the fair value of the equity instruments granted, during the period was determined, and
(c) the effect of expenses arising from share-based payment transactions on the entity's profit or loss.

Are these disclosure requirements appropriate? If not, which disclosure requirements do you suggest should be added, deleted or amended (and how)?

The disclosures are appropriate.

Question 22
The draft IFRS proposes that an entity should apply the requirements of the IFRS to grants of equity instruments that were granted after the publication date of this Exposure Draft and had not vested at the effective date of the IFRS. It also proposes that an entity should apply retrospectively the requirements of the IFRS to liabilities existing at the effective date of the IFRS, except that the entity is not required to measure vested share appreciation rights (and similar liabilities) at fair value, but instead should measure such liabilities at their settlement amount (ie the amount that would have been paid on settlement of the liability had the counterparty demanded settlement at the date the liability is measured). Are the proposed requirements appropriate? If not, please provide details of your suggestions for the IFRS's transitional provisions.

We suggest that the final IFRS apply to new grants after publication of the final IFRS. Requiring entities to retroactively apply the fair value approach to the date of the Exposure Draft, particularly to option valuation, seems quite onerous and not necessary. We also believe that entities should have the ability to redesign share-based compensation schemes with the understanding of the new financial reporting requirements.

Question 23
The draft IFRS proposes a consequential amendment to IAS 12 (revised 2000) Income Taxes to add an example to that standard illustrating how to account for the tax effects of share-based payment transactions. As shown in that example, it is proposed that all tax

effects of share-based payment transactions should be recognized in the income statement. Are the proposed requirements appropriate?

The IASB approach of having all of the tax effects of share-based payments go through the income statement is appealing, particularly in its simplicity. The tax effects, generally obtained in the U.S. from the cash flow statement, are a critical measure for financial statement analysis. However, recognizing the full amount in the income statement is a significant difference from FASB Statement 123, presumably due to differing tax accounting rules prescribed in IASB and FASB literature. We urge the FASB and IASB to consider the alternatives and converge upon one or the other. Both approaches are acceptable to us and easily explained to financial statement readers. In addition, if there is international harmonization on an improved and more detailed performance reporting statement, the accounting difference may be less critical.

Question 24

In developing the Exposure Draft, the Board considered how various issues are dealt with under the US standard SFAS 123 *Accounting for Stock-Based Compensation*, as explained further in the Basis for Conclusions. Although the draft IFRS is similar to SFAS 123 in many respects, there are some differences. The main differences include the following.

(a) Apart from transactions within the scope of another IFRS, the draft IFRS does not propose any exemptions, either from the requirement to apply the IFRS or from the requirement to measure share-based payment transactions at fair value. SFAS 123 contains the following exemptions, none of which are included in the draft IFRS:

- **employee share purchase plans are excluded from SFAS 123, provided specified criteria are met, such as the discount given to employees is relatively small;**
- **SFAS 123 encourages, but does not require, entities to apply its fair value measurement method to recognise transactions with employees; entities are permitted to apply instead the intrinsic value measurement method in Accounting Principles Board Opinion No. 25 *Accounting for Stock Issued to Employees* (paragraphs BC7O-BC74 in the Basis for Conclusions give an explanation of intrinsic value); and**
- **unlisted (non-public) entities are permitted to apply the minimum value method when estimating the value of share options, which excludes from the valuation the effects of expected share price volatility (paragraphs BC75-BC78 in the Basis for Conclusions give an explanation of minimum value).**

We assume that a general notion of materiality would exempt the same employee share purchase plans as FASB Statement 123—those purchase plans with a discount equivalent to the savings from selling shares directly rather than through intermediaries. We agree that plans such as U.S. Section 423 plans, which typically offer a *15%* discount and a look-back option, are compensatory plans that should not be exempted under accounting rules.

We strongly support the IASB approach that all forms of compensation must be recognized in income statements, not simply disclosed as permitted under FASB Statement 123. We are hopeful that the FASB will be reconsidering its "optional" requirements later this year.

(b) For transactions in which equity instruments are granted to employees, both SFAS 123 and the draft IFRS have a measurement method that is based on the fair value of those equity instruments at grant date. However:

- **under SFAS 123, the estimate of the fair value of an equity instrument at grant date is not reduced for the possibility of forfeiture due to failure to satisfy the vesting conditions, whereas the draft IFRS proposes that the possibility of forfeiture should be taken into account in making such an estimate.**

- **under SFAS 123, the transaction is measured at the fair value of the equity instruments issued. Because equity instruments are not regarded as issued until any specified vesting conditions have been satisfied, the transaction amount is ultimately measured at the number of vested equity instruments multiplied by the fair value of those equity instruments at grant date. Hence, any amounts recognised for employee services received during the vesting period will be subsequently reversed if the equity instruments granted are forfeited. Under the draft IFRS, the transaction is measured at the deemed fair value of the employee services received. The fair value of the equity instruments granted is used as a surrogate measure, to determine the deemed fair value of each unit of employee service received. The transaction amount is ultimately measured at the number of units of service received during the vesting period multiplied by the deemed fair value per unit of service. Hence, any amounts recognised for employee services received are not subsequently reversed, even if the equity instruments granted are forfeited.**

We are supportive of allowing a specific discount for vesting conditions of employee options. In addition, we prefer the SFAS 123 approach to attribution of the compensation cost, whereby expense is recognized only for options or shares that actually vest, as discussed in our answers above.

(c) If, during the vesting period, an entity settles in cash a grant of equity instruments, under SFAS 123 those equity instruments are regarded as having immediately vested, and therefore the amount of compensation expense measured at grant date but not yet recognised is recognized immediately at the date of settlement. The draft IFRS does not require immediate recognition of an expense but instead proposes that the entity should continue to recognise the services received (and hence the resulting expense) over the remainder of the vesting period, as if that grant of equity instruments had not been cancelled.

We prefer the SFAS 123 approach, with immediate recognition if payment is made in cash.

(d) SFAS 123 does not specify a measurement date for transactions with parties other than employees that are measured at the fair value of the e quity instruments issued. Emerging Issues Task Force Issue 96-18 *Accounting for Equity Instruments That Are Issued to Other Than Employees for Acquiring, or in Conjunction with Selling, Goods or Services* requires the fair value of the equity instruments issued to be measured at the earlier of (i) the date a performance commitment is reached or (ii) the date performance is complete. This date might be later than grant, for example, if there is no performance commitment at grant date. Under the draft IFRS, the fair value of the equity instruments granted is measured at grant date in all cases.

We are supportive of the L&SB approach in which employee and nonemployee transactions are measured at the date of grant.

(e) SFAS 123 requires liabilities for cash-settled share appreciation rights (SARs) to be measured using an intrinsic value measurement method. The draft IFRS proposes that such liabilities should be measured using a fair value measurement method, which includes the time of the SARS, in the same way that options have time value (refer to paragraphs BC7O-BC81 of the Basis for Conclusions for a discussion of intrinsic value, time value and fair value).

Although both standards would result in the same amount of expense by the time of settlement, we prefer the IASB approach that would require fair value accruals until the time of settlement.

(f) For a share-based payment transaction in which equity instruments are granted, SFAS 123 requires realized, tax benefits to be credited direct to equity as additional paid-in capital, to the extent that those tax benefits exceed the tax benefits on the total amount of compensation expense recognized in respect of that grant of equity instruments. The draft IFRS, in a consequential amendment to lAS 12 (revised 2000) *Income Taxes*, proposes that all tax effects of share-based payment transactions should be recognized in profit or loss, as part of tax expense.

See our answer to Question 23.

For each of the above differences, which treatment is the most appropriate? Why? If you regard neither treatment as appropriate, please provide details of your preferred treatment.

See above.

(Respondents may wish to note that further details of the differences between the draft IFRS and SFAS 123 are given in the FASB's Invitation to Comment.)

Question 25
Do you have any other comments on the Exposure Draft?

No.