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Kimberley Crook
Project Manager
International Accounting Standards Board
30 Cannon Street, London EC4M 6XH
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Re: Draft International Financial Reporting Standard
ED 2 - Share-based Payment

Johnson & Johnson is pleased to comment on the Board's proposed IFRS, Shared Based Payment.

Johnson & Johnson is the world's most comprehensive and broadly based manufacturer of health care products, as well as a provider of related services, for the consumer, pharmaceutical, and medical devices and diagnostics markets. We have over 100,000 employees and sell products in more than 175 countries.

We believe the discussions and deliberations on Stock based Compensation and Share based Payment are important and understand many constituents hold strong and differing views on this topic.

At a very high level, we believe three important factors need to be considered: (1) the need for meaningful and accurate information; (2) international convergence; and (3) principles based accounting standards.

Meaningful and accurate information would include the notion that transactions, assets and liabilities, revenues and costs are accounted for taking into account their (sometimes unique) economic characteristics, and that the information would be understandable and meaningful to the users of financial statements. We believe the proposed IFRS does not take into account some of the unique characteristics of employee stock options. Some of these are discussed further in the latter part of our comment letter

International convergence of accounting standards is important and necessary, as it will enhance investor confidence in global capital markets. Stock based compensation and Share based Payment is a high profile example of an area where convergence is desirable. In that respect, we are pleased to note that the Board and the FASB in the United States are working on international convergence projects, including this particular topic.

We strongly support a principles based approach to accounting standards setting. A rules based approach can lead to accounting standards that are too complex, too detailed or too prescriptive and may not allow for sufficient, reasonable judgment. Fair value measurement, in our opinion, is an example of such an area. Stock based compensation and Share based Payment is a topic with very specific and unique complexities. As you are aware, a number of valuation methods have been (and are being) developed to determine the (fair) value of employee stock options. Application of these methods can lead to very different results. We believe that, while the proposed IFRS is rooted in principles, it still represents a rule based standard. We believe the proposal needs to be challenged from a principles versus rules based standpoint.

The following are some specific comments and observations.

Employee stock options typically have unique characteristics that differentiate them from other equity instruments: they would typically vest only after a certain period (either via cliff vesting or graded vesting); and they may not vest because of forfeitures. Equity instruments are typically issued when consideration is exchanged. It appears to us that, in the case of employee stock options, consideration is not exchanged prior to vesting. Therefore, we believe employee stock options are issued when vested.

The proposed IFRS uses a units-of-service attribution model to record compensation expense. This method may lead to recognizing expense for options that will not vest. This, in our opinion is flawed.

A unique aspect of employee stock options is that they typically cannot be traded. Thus, valuation methods should carefully consider the difference between instruments (options in this case) that can be traded and those that cannot. The use of any pricing models that do not take into account that difference will lead to overstatements of the value of those instruments that are not traded. Replacing the contracted life with its expected life does not achieve this objective. More importantly, we believe that any method that does not recognize the change in value over time (true-up) is flawed.

We believe that reporting the effect of employee stock options via the calculation of fully diluted Earnings per Share (EPS) is the best reporting method. However, a fully diluted EPS calculation, in our opinion, is not compatible with expensing options following an options pricing model. The fair value of stock options, which would be recorded as an expense, is determined or influenced in a significant way by future considerations that occur over a period of time. Calculating EPS on a fully diluted basis assumes potential shares exercisable under stock options plans are exercised as of Statement date. The effect will generally be that diluted EPS will be understated if stock options are expensed. Therefore, we believe that reporting the effect via diluted EPS, rather than expensing stock options, is the best reporting method.

We thank you for taking our comments into consideration and will be pleased to discuss these with you.

Sincerely,

Stephen Cosgrove

S.J. Cosgrove
Vice President, Corporate Controller