AFEP-AGREF

Paris, 3rd February 2003

Dear Sir,

The AFEP-AGREF appreciates the opportunity to offer its views on the proposals in the Exposure Draft "ED 2 Share based payment" and to set out the position expressed by its members.

We believe that there are grounds for questioning how the proposals improve the information given to users of financial statements.

We consider a grant of equity instruments to employees to result from an agreement between shareholders, which is reflected in various factors: authorisation given by shareholders, vesting conditions, link between the benefit and the enterprise's performance, risks borne by the beneficiary, etc. It should be emphasised that these *factors relate more to a sharing agreement than to a contract of employment or a contract for provision of services*. Also the IASB proposals themselves (indirect measurement method, use of the vesting period rather than the service period) reflect the difficulty in defining a concept of services rendered by employees.
In fact the grant of equity instruments compensates for the benefit to pre-existing shareholders, in particular the development of a *lasting relationship* between the enterprise and its shareholders.

Consequently, the grant of equity instruments *should not give rise to recognition of an expense in the income statement.* Booking an expense, rather than relevant information on equity instruments in the Notes to the Accounts, results from confusion between corporate governance and accounting and, by unduly burdening the enterprise's results, would have *prejudicial consequences on the salaried shareholder base.*

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***Our proposal**: The objective should be disclosing the potential or actual dilution for shareholders.* It would be better to make the information more pertinent by quantifying in the Notes to the Accounts only the potential or actual dilution effects of the exercise of options and the granting of shares.
Use of option pricing models does not make it possible to measure the dilution effect for shareholders and this leads to taking account of an instantaneous volatility of prices at grant date, which is inappropriate for long-term options. Whereas the economic impact is nil if the options arc not vested or exercised, the draft does not reconsider the value taken into account.

Our response is composed of two parts:
- our proposal for an alternative approach (below);
- our responses to the questions of the exposure draft (presented in the appendix)

For transactions with employees, the IASB project generally provides for the measurement of the fair value of equity instruments at grant date and recognition of an expense in profit or loss over the vesting period, which is considered to represent the period of consumption of goods or services (service period).

In doing this, the draft is based on the principle whereby the grant of equity instruments (shares and options) would correspond to the consideration for goods or services identified at the outset and consumed by the enterprise.

The grant of equity instruments results from an agreement between shareholders, which does not constitute an expense for the entity...

We consider a grant of equity instruments to employees (shares subscribed in relation to employee plans, such as plans d'épargne d'entreprise, options, ...) to result from an agreement made between existing shareholders and other - existing or potential shareholders and recognised by the General Meeting of Shareholders.
The previous status of the beneficiary for instance, as an employee is giving way to their status as shareholder (existing, new or future) in respect of the equity instruments granted.

Such grant of equity instruments compensates for the benefit to pre-existing shareholders, in particular the development of a stable and lasting relationship between the enterprise and its shareholders. Consequently, it should not give rise to recognition of an expense in the income statement. Booking an expense, rather than relevant information on equity instruments in the Notes to the Accounts, results from confusion between corporate governance and accounting.

… only affecting shareholders

The IASB exposure draft considers that a grant of equity instruments to employees is equivalent to remuneration or another expense and constitutes the consideration for a service consumed by the enterprise.

It disregards the nature of the instruments (equity instruments) and the terms and conditions at which they are granted, which is reflected in various factors: authorisation given by shareholders, vesting conditions, link between the benefit and the enterprise's performance, risks borne by the beneficiary, etc. However, these factors relate more to a sharing agreement than to a contract of employment or a contract for provision of services.

In France, the link between the concept of service and the grant of equity instruments is even more tenuous, since options and *plans d'epargne d'entreprise (P.E.E.)* (employee share plans) are subject to decisions taken by a reinforced majority, at an Extraordinary General Meeting of Shareholders, and the options cannot be transferred for several years.
Perhaps this situation is not as clear cut in the United States or other countries, where the shares may be available very soon after they are granted.

The IASB recognises the difficulty in defining a concept of services rendered by employees

The IASB recognises the difficulty in defining a concept of services rendered by employees, by prohibiting the direct measurement of such services and requiring instead use of the fair value of the instruments granted. Likewise, the IASB prescribes recognition of an expense over the vesting period rather than the period over which the service is provided (service period).

Using option pricing models does not make it possible to measure the dilution effect for shareholders and leads to taking account of instantaneous values

According to the IASB exposure draft, options should generally be valued on the basis of their fair value at grant date by means of an option pricing model such as the Black and Scholes model or a binomial model. The model used should take account of factors such as the expected volatility of the share price, a determining parameter, and the life of the option - the expected life for non-transferable options.

Use of option pricing models does not make it possible to measure the dilution effect for shareholders and this leads to taking account of an instantaneous volatility of prices at the grant date.

The theoretical hypotheses of volatility of the pricing models do not appear to make it possible to use them for long-term options (a life of 8 to 10 years in most cases). In addition, using these models is contrary to common sense when this leads to variations in the value of options proportional to the short-term variations in the share price, while the enterprise's potential long-term value is not changed.

The objective should be only disclosing in the Notes to the Accounts the potential or actual dilution for shareholders

In fact, the IASB draft should only aim at measuring and disclosing in the Notes to the Accounts the potential or actual impact of equity instruments for shareholders.

Thus, using option pricing models is problematic and the IASB project requires the recognition of an expense which does not even reflect the dilution for shareholders. Whereas the economic impact is nil if the options are not vested or exercised, the draft does not reconsider the expense recognised.

In particular, contrary to US standard FAS 123 *Accounting for Stock-Based Compensation*, the IASB project does not, provide for modification of the value of the unit of service, and revision or corresponding reversal of the expenses recognised, if the vesting conditions (such as length of service or performance) are not satisfied or the employee departure differs from the initial projections.

According to the IASB exposure draft, the rules for attributing the value of the options or discounts are based on the value of a unit of service determined at the outset, depending on the number of expected units of service at the outset. If the vesting conditions for the rights are not satisfied *(forfeiture)* or if employee departure differs from the initial projections, not adjusting the unit of service and expenses recognised on this basis means that a value may eventually be booked to the results that is different to the value of the option at the outset.

This difference also stems from the fact that the expenses are not reversed if the options are not exercised *(lapse)* and the fact that the enterprise must continue to recognise services received over the residual term of the vesting period in the case of cancellation of the grant of a share or option (except in the case where the vesting conditions are not satisfied).

It would be better to make the information more pertinent by quantifying only in the Notes to the Accounts the potential or real dilution effects of the exercise of options and the granting of shares

There are grounds for questioning how the recent proposals improve the information given to users of financial statements.

In this respect, it is worth reiterating that standard IAS 19 *(Employee benefits)* already includes the obligation of publishing detailed information on equity instruments for employees, outstanding at the end of the period, issued and exercised (for options) during the period, and, for these, details of the exercise price. In addition, standard IAS 33 *(Earnings per share)* requires presentation on the face of the income statement of diluted earnings, taking account of the potential dilution of the options.

Rather than providing for recognising expenses that do not correspond to the dilution effect for shareholders, it would seem to be much more pertinent for shareholders and users of financial statements to include in the Notes to the Accounts only figures on the effects in respect of the period of share-based transactions, in particular the dilution effects relating to transactions that have been, or may be, settled in equity instrument.

It is necessary to avoid the prejudicial consequences on the salaried shareholder base

Whereas the IASB already provides for publication of complete information that can be used by the financial markets, it is also worthwhile drawing attention to the consequences of recognising additional expenses on the development of the shareholder base, including salaried shareholders, since share and option plans currently comprise an important means of motivation and involvement in the corporate plan.
The function of these plans is also recognised — including in France by the existence of plans d'épargne d'entreprise (P.E.E.) (employee share plans).

This is because, without giving more pertinent information, booking to expenses as provided for in the IASB exposure draft, by unduly burdening the results, is likely to lead to less take up of such plans and so needlessly worsening the relationship between the enterprise and its salaried employees.

The AFEP-AGREF would be pleased to discuss these comments further.

Yours sincerely

Patrick Rochet

2003-02-03

RESPONSE TO THE IASB EXPOSURE DRAFT
«ED 2 SHARE BASED PAYMENT»

Question 1 —Scope

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?

We consider it useful to require specific disclosures when equity instruments are granted However, this should not lead to disclosure requirements that would not take into consideration granting conditions and terms.

We believe that the standard should not require recognition of an expense.

The standard could provide useful guidelines on disclosure.
In particular, it is relevant to identify non compensatory plans proposed to employees (which should be scoped out) and equity instruments granted to suppliers in exchange for goods or services that are clearly identified and reliably measurable.

Question 2 - Recognition requirements

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 not appropriate.
We believe that recognition of an expense should be required only in the exceptional circumstances set out below.

When equity instruments are granted to parties other than employees, recognition of an expense on the face of the balance sheet or in income, in respect of the goods or services received, can only be envisaged if those goods or services are clearly identified and meet the conditions of the IASB framework (in particular reliable measurement § 94).

Such conditions are not satisfied when equity instruments are granted to employees.

Question 3 - Measurement methods applicable to goods or services received, for equity-settled transactions

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?

For transactions with employees, the goods or services received are measured when the instrument is granted, based on its fair value (indirect method).
For transactions with parties other than employees, in principle, goods and services are measured at their fair value when received (direct method). There is a rebuttable presumption that fair value is more readily determinable for transactions (equity based transactions) with parties other than employees.

We believe that the measurement principle is not appropriate.
When goods or services that are clearly identified and reliably measurable are settled in equity instruments, the entity should in all circumstances have a choice between each of the proposed methods. As recognition of an expense implies that the goods or services are clearly identified and reliably measurable.

Questions 4 et 5 - Date for measuring the goods or services received

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?

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?

When goods or services that are clearly identified and settled in equity instruments have to be measured, we believe that they should be measured at the date when the entity obtains the goods or receives the services, under the indirect method, and at the date when the equity instruments are granted, under the direct method.
In the latter case, the vesting conditions attached to the equity instruments granted should be taken into consideration (see response to question 9).

Question 6 - Measurement method applicable to goods or services received from parties other than employees

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?

When goods or services that are clearly identified led and provided by parties other than employees are settled in equity instruments, we agree that the fair value of the goods or services received generally is more readily determinable than the fair value of the equity instruments granted.

Question 7 - Proposed measurement method for transactions with employees

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?

The IASB project assumes that the grant of equity instruments to employees constitutes a consideration for a service consumed by an entity.

We disagree with the IASB approach.
As it disregards the nature of the instruments (equity instruments) and the terms and conditions of their grant, reflected in particular by different features: approval by shareholders, vesting conditions, link between the benefit and the performance of the entity, risks borne by the beneficiary….. It should he underlined that those features relate more to a sharing agreement than to a contract of employment or a contract for provision of services.

Also, in assessing the benefit that the grant of such instruments could represent, it is necessary to take into account the terms and conditions of grant and the specific features of the equity instruments issued or to he issued, which significantly limit the dilution effect, if any:

- *As far as the terms and conditions of grant are concerned, it should be emphasized that, for the sake of transparency and shareholder protection, the commitments to issue stock-options or shares on specific terms and conditions generally are legally subject to limitations concerning their amount, disclosed to shareholders and other stockholders, controlled by auditors and market regulators, and subject to shareholders' approval.*

- *In many cases, the features of the instruments issued or to be issued —in particular long non-transferability period-, largely outweigh the apparent benefit based on the initial estimate and/or resulting from a mere comparison of prices on grant date.*

We wish to emphasize that the IASB acknowledges the difficulty in defining a notion of services received from employees by prohibiting the direct measurement and requiring instead use of the fair value of the instruments granted

When the company receives services that are clearly identified, we agree that it may be less difficult to estimate the value of the equity instruments granted

Question 8 — Expense recognition period

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?**

In addition to the elements mentioned in response to question 7, it should be underlined that the IASB acknowledges the difficulty in defining a notion of services received from employees by requiring an expense recognition over the vesting period rather than the service period.

When the company receives services that are clearly identified, we believe that it is not reasonable to assume that those services are received over the vesting period This presumption should be rebuttable.

Questions 9 et 10 - Value allocation principles under the indirect method

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?

FAS 123 *Accounting for Stock-Based Compensation* does not require an expense recognition in respect of equity instruments whose vesting conditions are not satisfied (allowing for rare exceptions). Consequently:

- When an entity recognizes expenses based on its initial vesting expectations, those estimates have to be revised based on the instruments that actually vest;
- When an entity recognizes expenses assuming that all instruments vest, the effect of actual forfeitures has to be recognized as they occur (FAS 123 § 28).

This approach differs from the IASB approach, which requires recognition of expenses from the grant date onwards and does not allow their revision or reversal, when the vesting conditions are not met.

We disagree with the proposal that the fair value of equity instruments granted is used as a surrogate measure of the fair value of goods or services.
As, under the L4SB project, this leads to take into consideration only the goods or services that would be received and to disregard the vesting conditions of the options and, when appropriate, their forfeiture. Or, in other words, to recognize an expense, although there is no value loss for the entity or its shareholders.

It is difficult to understand why the project so much focuses on expense recognition, although this treatment is contrary to the framework and ignores both the substance of the transactions and the terms and conditions of the contracts.
Although the project requires using the fair value of the equity instruments as a surrogate measure of the fair value of goods or services, it fails to take into consideration the revisions of this fair value measurement.

Recognition of an expense should be envisaged only for goods or services that are clearly identified and reliably measurable.
If in that case, the entity chooses the indirect method, we agree that it is necessary to determine the amount to allocate to each unit of service and to calculate that amount by dividing the value of equity instruments by the number of units of services expected However, when the recognition of an expense is followed by a forfeiture, we believe that it is necessary to reflect the terms and conditions of the contracts and to adopt principles similar to those defined in FAS 123, i.e. revision of the initial estimates or reversal of previously recognized expenses.

Question 10 – Proposed prohibition of adjustments relating to amounts previously recognised as expenses

In an equity-settled share -based payment transaction, the draft IFRS proposes that having recognised the services received, and a corresponding increase in 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, ie 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 disagree with the proposed approach, which does not allow adjustments of amounts previously recognized as expenses when vesting requirements are not satisfied The bases for that position and our proposal are set out in the response to question 9.

Question 11 — Measurement of options

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 disagree that an option pricing model should be applied in all circumstances to estimate the fur value of options granted

The use of such models is not suited for estimating options whose underlying instrument is not listed In particular, it proves difficult to take into consideration the volatility of that instrument and the life of the option.

For the purpose of estimating the fair value of such options, contractual formula should be taken into consideration in the first place. The initial estimate of the option 's fair value often is difficult, if not impossible.

Also, for other options, the theoretical hypotheses of volatility of the pricing models do not appear to make it possible to use them for long-term options (a life of 8 to 10 years in most cases). In addition, using these models is contrary to common sense when this leads to variations in the value of options proportional to the short-term variations in the share price, while the enterprise 's potential long-term value is not changed

Question 12 — When measuring options, taking into account the non-transferability feature and the impossibility to exercise during the vesting period

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?

If an option is non-transferable (general case), the IASB proposes to use the expected life of the option rather than its contracted life. By contrast, the contracted life is used for a transferable option.

That proposal does not call for specific comments.

For options that are subject to vesting conditions, the impossibility to exercise them during the vesting period should be taken into consideration when applying a model valuing options that can be exercised at any time during the option's life (such as a binomial model applicable to US type options), Such an adjustment is not necessary when applying a Black and Scholes model, which values options that can be exercised only at the end of the option's life (European type options).

That proposal does not call for specific comments.

However, when the recognition of an expense is followed by a forfeiture, we wish to emphasize that we believe it necessary to reflect the terms and conditions of the contracts and to adopt principles similar to those defined in FAS 123, i.e. revision of initial estimates or reversal of previously recognized expenses.

Question 13 Taking into account the vesting conditions when measuring options or shares granted

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?

We agree, with the following reservation, that vesting conditions should be taken into consideration when estimating the value of the options or shares granted

In the case of an expense recognition followed by a forfeiture, we believe it necessary to reflect the terms and conditions of the contracts and to adopt principles similar to those defined in FAS 123, i.e. revision of initial estimates or reversal of previously recognized expenses.

Question 14 —Reload feature

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?

According to the project, the reload feature, where possible, should be taken into consideration when an entity measures the fair value of the option granted or, failing that, should be regarded as a new option grant.

That proposal does not call for specific comments.

Question 15 — Taking into account the characteristics of options granted to employees

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 21-25).

Are there other common features of employee share options for which the IFRS should specify requirements?

We believe that the project should address the situation where the underlying instrument of the options granted to employees are not listed

Question 16 Absence of prescriptive guidance on the estimation of the value of options

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 that the draft standard does not contain prescriptive guidance on the estimation of the value of options.

Question 17 - Repricing

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, ie 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?

As mentioned in response to question 2, we believe that recognition of an expense should be required only in exceptional cases.

When an entity modifies the granting terms and conditions; we believe that the incremental value should be taken into account when measuring the equity instruments granted or the services rendered, resulting in the adjustment of the amounts previously taken into account.

Question 18 Cancellation of a share or option grant (other than by forfeiture)

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.

As mentioned in response to question 2, we believe that recognition of an expense should be required only in exceptional cases.
The cancellation of rights should be taken into account when measuring the equity instruments granted or the services received, resulting in the adjustment of the amounts to be disclosed and, where applicable, in the reversal of the expenses previously recognised

Question 19 — Cash-settled share -based payment transactions

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

Although the objective of the project is to recognise the services rendered over the vesting period, we note that the measurement of services differs depending on whether the equity-based transactions are settled in equity instruments or in cash:

- *for cash-settled transactions, the value of the rights is measured and an adjustment taken into account at the end of each reporting period until the liability is settled;*
- *for equity-settled transactions, there are no such re-measurement and adjustment.*

In our response to question 3, we have mentioned that an entity should in all circumstances have a choice between each of the proposed methods (measurement of the goods or services received or measurement of the equity instruments granted), when goods or services that are clearly identified and reliably measurable are settled in equity instruments.

By analogy, we believe that an entity should have a choice between the measurement of the goods or services that would be received and the measurement of the consideration given.

Question 20 Choice of settlement in cash or equity instruments

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.

On the assumption that there are different treatments, and more specifically in respect of 41 (choice lying with the counterparty), we believe, by analogy with our response to question 9, that the choice of a cash settlement is not equivalent to a forfeiture.
According to § 41, if an entity pays cash rather than issuing equity instruments, the equity component previously recognised shall remain within equity the cash payment shall be applied to settle the liability in full. As, among other things, the equity component is not taken into account, the cash payment can be higher than the amount of the liability. That would imply that the entity should recognise an additional expense, although an expense would already have been recognised in respect of the equity component.
We acknowledge that this approach reflects the JASB proposal, mentioned in § 41 (<<By electing to receive equity instruments, the counterparty forfeited the right to receive equity instruments>>), that a forfeiture does not imply an expense reversal.
However we note that the § 41 proposal results in double counting of an expense, which is inappropriate.

Question 21 - Disclosures

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)?

As mentioned in our response to question 2, we believe that an expense recognition should be required only in exceptional cases. Consequently, the disclosures proposed under § 52 are not appropriate.
Furthermore, as the objective of the project is to recognise the services rendered over the vesting period, we believe it inappropriate to require the disclosure in § 52 (b) i.e., for cash-settled transactions, the portion of the expense recognised for the period that is attributable to the transaction having been measured as a cash-settled transaction rather than as an equity-settled transaction.

Question 22 — Transitional provisions

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 believe that the proposed transitional provisions are not appropriate.

The possible changes introduced by the standard should be applied prospectively and should be applicable only to the equity instruments granted from the effective date of the final standard onwards.

It should be underlined that any change implies the adaptation of reporting systems. Such changes are costly and can be done only based on final provisions.
In setting dates the Board should take into consideration the time necessary for adopting and implementing standards.

Question 23 – Recognition of tax effects in the income statement

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 recognised in the income statement.**

Are the proposed requirements appropriate?

As mentioned in our response to question 2, we believe that an expense recognition should be required only in exceptional cases.

consequently, we believe that the project proposals are appropriate only in those exceptional cases.

Question 24 — Differences with US standard

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 employess: 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 BC70-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).**

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.

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 recognised 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.

d) SEAS 123 does not specify a measurement date for transactions with parties other than employees that are measured at the fair value of the equity 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 date. Under the draft IFRS, the fair value of the equity instruments granted is measured at grant date in all cases.

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 value of the SARs, in the same way that options have time value (refer to paragraphs BC70-BC81 of the Basis for Conclusions for a discussion of intrinsic value, time value and fair value).

f) For a share-based payment transaction in which equity instruments are granted, SFAS 123 requires realised 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 recognised in respect of that grant of equity instruments. The draft IFRS, in a consequential amendment to IAS 12 (revised 2000) *Income Taxes*, proposes that all tax effects of share-based payment transactions should be recognised in profit or loss, as part of tax expense.

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.

(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.)

For the reasons mentioned in our response to question 7, we disagree with the IASB assumption that the grant of equity instruments' constitutes the compensation of a service consumed by the entity.

General principles

The treatment preferred is set out in our responses to questions 1, 2 and 7.

Equity instruments granted to employees

We note that the US standard contains exemptions for the employee share purchase plans. We believe that the characteristics of the grants of equity instruments to employees should be taken into account (see our response to question 25).

Forfeiture

In the case of' an expense recognition followed by a forfeiture, we believe it necessary to reflect the terms and conditions of the contracts and to adopt principles similar to those defined in FAS 123, i.e. revision of initial estimates or reversal of previously recognised expenses.

Question 25— Other comments

Do you have any other comments on the Exposure Draft?

Employee plans

We consider it essential to take into account the characteristics of equity instruments granted to employees (shares issued at a discount to their cost or stock-options,), which relate more to a sharing agreement than to a contract of employment or a contract for provision of services:
granting conditions (length of service, ...), link between the benefit and the entity 's performance, risks borne by the beneficiary.

Furthermore we wish to emphasize that in France, the link between the concept of service and the grant of equity instruments is even more tenuous, since options and plans d'épargne d'entreprise (P.E.E.) (employee share plans) are subject to decisions taken by a reinforced majority, at an Extraordinary General Meeting of Shareholders, and the options cannot be transferred for several years.
Perhaps this situation is not as clear cut in the United States or other countries, where the shares may be available very soon after they are granted

We believe that the JASB approach should under no circumstances apply to Employee Share Purchase Plans, such as plans d'épargne d'entreprise (P.E.E.). For those plans, it should be underlined that conditions are often minimal in terms of length of service, vesting period and *performance and that the instruments, proposed to all employees, generally are granted regardless of the salary. The case of Employee Share Purchase Plans granted under French law is more specifically addressed below.*

Employee Share Purchase Plans

The exposure draft proposes to apply to Employee Share Purchase Plans the same accounting treatment as stock options plans (see BC 8 to BC 15).

We do not agree with this proposal and believe that those plans are not properly addressed. Employee Share Purchase Plans developed under French law generally present the following features, most of which differ from those of stock options plans:

1. *Employees subscribing to Employee Share Purchase Plans pay cash at the purchase date. The risks and rewards linked to share ownership are immediately transferred to the buyer. By contrast, for stock options plans, the payment occurs only if the option is exercised, limiting the risks borne by the beneficiaries.*

2. *Share ownership is transferred to employees as soon as they subscribe to the Employee Share Purchase Plan. Even if they leave the enterprise, they remain the owners. Due to tax incentives for individuals, employees cannot withdraw from the plan for a 5 year period, unless there are exceptional changes in their individual situation (such as wedding, birth of a child, ...). This 5 year period does not represent a vesting period, as the beneficiary has no obligation to stay with the enterprise.*

3. *It is up to the employees to decide whether or not they subscribe to the plan.*
   The attribution of shares is not conditional on the employee meeting performance criteria or staying with the enterprise.

For the reasons mentioned above, we consider that Employee Share Purchase Plan should be scoped out of the future standard.
The benefits granted in relation to such plans do not compensate for services. The related dilution effect, if any, should be accounted as for other capital increases, since their features are similar:

a. *Immediate cash payment and immediate share ownership, as in any capital increase.*
   Likewise:

   - *The employees bear the price risk after the purchase date (when hedging mechanisms are in place, they are managed and paid by the employees as a community, and do not benefit from the enterprise 's guarantee)*
   - *Share ownership is not subject to vesting conditions determined by the enterprise.*

b. *The discounted price of shares issued in relation to an Employee Share Purchase Plan may be similar to the discounted price offered to other shareholders, whether or not they are employees of/he enterprise.*