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International Accounting Standards Board
30 Cannon Street
London EC4M 6XH
United Kingdom

Re: Expensing of Employee Stock Options

Dear Sirs,

After reviewing the IASB's recent discussion on the expensing of employee stock options, I would like to voice my concern as a practitioner over the "reliable measurement" methodology suggested. I believe that simply relying on existing fair value models is not sufficient to value the complexities present in employee stock options.

My understanding of the current proposal is that those preparing financial statements will have the leeway to value employee stock options in several ways. Initially they must use an option pricing model and then make adjustments to reflect vesting, repricing and perhaps other complications.

My concern with this conclusion is that it relies on current methodologies and has enormous potential for variance. Current models were created to value very different securities. They rely on very accurate measures of input values, values that are confirmed through the Market's trading mechanisms. Employee stock options are securities that have some similar features to traded options but also many additional complexities that our current models did not originally envision. For example, vesting is one time issue that can be incorporated in pricing but the effect of blackout periods is another time issue that cannot be adjusted so easily. Blackout periods have an effect on the volatility input as well as the time input. Liquidity constraints, in particular the inability to sell time value, have another significant impact on option prices. Even small errors in input values can have a significant effect on option prices. Without a trading environment to check the option values, the potential for those preparing financial statements to choose input values that result in an option expense to their liking, is too high.

The Generally Accepted Accounting Principles on expense recognition state that an item must be both likely to occur and be reasonable estimable. My concern with being able to 'adapt' current option pricing models is that the adapted figure can come from such a wide dispersion of values that we cannot claim the figure is reasonably estimated. We have the potential to create such confusion in financial statements that instead of providing no recognition (only disclosure) we likely will provide misleading recognition. As a user of financial statements I would rather have the onus placed on me to evaluate disclosures (understanding the dilution effect) than to be given misleading information by a corporation.

Sincerely,
Derek Strocher, CGA, MSc