NSP BUCK

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NSP Buck Submission to the IASB on ED2

IASB
International Accounting Standards Board

EXPOSURE DRAFT
ED2 SHARE-BASED PAYMENT

INVITATION TO COMMENT

The International Accounting Standards Board invites comments on any aspect of this Exposure Draft of its proposed IFRS Share-based Payment. It would particularly welcome answers to the questions set out below. Comments are most helpful if they indicate the specific paragraph or group of paragraphs to which they relate, contain a clear rationale and, where applicable, provide a suggestion for alternative wording.

Comments should be submitted in writing so as to be received no later than 7 March 2003.

This document was compiled by NSP Buck's technical staff concerned on a day to day basis with employee and executive share plans. Our comments are reserved to how the current Exposure Draft deals with employee Share-based Payments.

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 underlying spirit of the changes is generally considered to be the need to increase transparency for shareholders and to avoid hidden expenses that can affect the financial viability of a company. The main driver for the changes has been to recognise and value the grants of large numbers of options to senior employees/non-employees that use new issued capital and which do not currently register as expense in a company's account.

With this focus in mind there are two recommended exemptions:

1. Unlisted companies. The shares in unlisted companies are not open to the public to buy, they are not affected by the same fluctuations that can occur on an open market and can often be owned predominantly by a small quorum of individuals who tend to be founding members. Only very sophisticated investors will invest in these types of companies and generally only after an in depth inquiry into to the financial health of the company. Any requirement to expense Share-based Payments would be an additional expense to this type of company and for employee and executive equity based plans would add to the already complex legal and tax environment which prevents rather than promotes this type of plan.

2. Broad based employee shares plans. These types of plans are offered to the whole of the employee population on similar or equal terms and involve small quantums of shares/options. Plans of this nature are optional, not necessarily based on service criteria and not dependent on continued employment with the company. Employees are often contributing their own money to participate. The number of shares issued is usually limited because the company will be relying on an Australian Securities and Investments Commission's employee share plan class order, which limits the issued share capital to 5% over a rolling 5 year period. The additional cost and expense of accounting for the broad based employee share plan may reduce the benefits offered to employees and act as a barrier to implementing plans of this nature. Again this type of plan does not seem to fit within the initial focus and spirit of the changes. (Strict criteria will of course need to be applied if this type of plan is exempted).

<u>Question 2</u>

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?

In principle the recognition of an expense when goods or services are received is supported. However, for the purpose of employee and executive share and option plans the services are not received yearly or at the end of each year. By their very nature plans operate, especially at a senior level, such that there is a target that needs to be achieved over a certain period, the performance period, before the options can be exercised or the shares vest. The performance period is usually for three years or more.

It is artificial to say that at the end of each year the company receives a service from the participant and that the service is comparable year on year. The nature of the targets is such that an individual contributes to and focuses on a target but may not individually be able to achieve it. In a sense it is a group target. Also a participant may not make any impact at all at the end of year one or two but in year three they may exceed the target through their performance in that year. The service is not readily "received" until the end of the performance period when the target is met or not met and it is that point that the participant receives a payment or not through equity. The date of recognition of the expense should be the end of the performance period and not yearly as proposed, unless there is clear target that allows a portion of the equity to vest each year.

If this method were adopted it would also have the added benefit of eliminating the uncertainties that exist around whether the performance conditions would be met, whether employees will leave, whether equity will be forfeited etc.

<u>Question 3</u>

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 employee and executive share and option plans there is usually a recognised value for the shares/options granted for employee taxation purposes. In Australia this is fairly well defined (this is the notion of Market Value) and applies equally to unlisted and listed shares, takes into account the value paid by the employee and is based on an accepted and well recognised methodology. Where there is an existing valuation method in a country then it should apply as a default position for companies unless there is a good argument to apply a different methodology.

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?

We believe that the date of receipt is the correct date for the valuation. However, the date of receipt should be the vesting date and not yearly as suggested in the Exposure Draft. Please see our response to Question 2.

In addition it is noted that paragraph 12 of the Exposure Draft states that is not easy to measure directly the services received for particular components of the employee's pay package. This supports our argument that the receipt of services should be the date of vesting rather than what is currently proposed. At vesting there is a clear service that has been rendered or not rendered that is distinguishable from the general service provided by the employee in the normal course of business. The current methodology is based on the premise that services received by an employee for the Share-based Payment can be isolated and valued yearly and that they can be separated from the services that are generally provided in the usual course of their employment. These two comments appear conflicting.

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?

If the Share-based Payment is received and fully vested at grant then this is the appropriate time to value the equity granted. However, where the equity vests over time then it is more appropriate to value the equity at the date of receipt as recommended in our response to Question 2.

If the methodology set out in Exposure Draft is accepted then the valuation should be annually.

The value of equity changes over time, as the circumstances of a company change and as the market fluctuates. It is again artificial to take the value at one point in time and assume that it will be correct going forward. Some employee and executive share and option plans have a life of three years or over. The value at grant may not be appropriate at the end of year three.

The dangers associated with valuing at one point in time are increased if the initial valuation is based on, for example, the listed share price of the shares at the date of grant (rather than an average share price). The value is subject to change over time and also runs of the risk of not being an indicative price because of the timing of the grant or because of the market conditions on a particular day.

Question 6

For equity-settled transactions with parties other than employees, the draft IFRS proposes a rebuttable resumption 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?

We have no submissions to make on this point.

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?

Agree that this is generally the case, provided fair value concept is based on a sound basis and provided that comments on timing in replies to Q2 and 5 are observed above.

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?

We agree that services are received over time where the Share-based Payment does not vest in the employee until the service criteria are met. However, this service criteria are similar to a performance condition and our suggested approach in Question 2 should equally apply to this type of plan. The expense should be accounted for only when the equity vests.

The current approach set out in the Exposure Draft may not be easy to apply for Share-based Payments that vest according to service criteria. The employees who receive the equity are likely to have different contractual hours, likely to work different hours each day and may have worked for a company for different periods of time and it would be artificial and incorrect to allocate the same time to each employee for calculation of the service units provided each year.

Where the equity is fully vested at the date of grant but is:

- restricted (ie can not be sold) until an employee has served a certain period of service; or
- may be forfeited in certain limited circumstances (fraud/dismissal); or
- has been granted only after a certain period of service has already been met; then

The expense should be recognised at grant as suggested in paragraph 13. It is important that the idea of service criteria is not confused with the position above where there are restrictions or time vesting on the equity.

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?

Our concerns with attributing the value to each unit of service are as follows:

- as noted in Question 8 above employees work different hours and have a different impact on the business, so the wider the group of employees the more artificial it becomes to use this methodology;
- the current method is very subjective and requires a company to estimate upfront the likely employee turnover for the period. This will increase the likelihood for variance between companies, inaccuracies and complexity; and
- there is no real distinction between the work that an employee would normally undertake as part of their normal job description and the work that they undertake to achieve the performance target for instance.

The methodology referred to in Question 2 is again preferred as the simplest and most accurate means to account for the expense.

As an alternative and to make the process more transparent, if our preferred method is not accepted, would be to divide the fair value of the total equity granted equally over the performance period or service criteria period. Adjustments could occur yearly to take into account change to the value of the equity and changes to value because of employee turnover.

Question 10

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?

The fact that the current methodology is likely to expense more or less than is the actual realised amount highlights the potential variations and inaccuracies inherent in it. However, if the current approach is accepted then we would support the current position in paragraph 16.

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?

As noted above in Question 3 there is already a recognised method used in Australia both to value options (both for tax purposes and otherwise). This methodology (commonly referred to as the Black Scholes Model) is widely accepted and used internationally and takes into account the six variables set out in Paragraph 16. The alternative suggested in paragraph 20, the binomial method also has merits and is preferred by some companies. Both methods if specified and used universally by companies would be an accepted means to value options.

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?

The approach suggested in paragraph 21is that for non-transferable options (which most options issued under an employee option plan are) is the expected life rather than the contractual life of the options should be used for measurement purposes. We disagree with this method. This approach again leaves for subjectivity and is at odds with the way that companies in Australia currently value their options. Generally companies calculate options based on the contractual life. The contractual life takes into account the full value of the option to the employee, so that whilst they may exercise the option before the end of the contractual life the full value of the option is that they have the ability to exercise for a fixed period. If the option is out of the money at one point in time or where an employee wishes to speculate on the likely increase in the share price they can do so for the full fixed period. The expected life is subject to many variations and can change over time, therefore, its accuracy must be questionable. The preferred approach then is to base the measurement on the contractual life rather than the expected life.

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?

Traditionally any option or share valuation models do not take into account vesting conditions. This is principally because it is hard to determine the reduction that should be given for any one vesting condition. Vesting conditions traditionally vary from company to company and even where they are consistent year on year for an individual company the reduction can vary because of many different factors which can affect whether the condition is met, including market conditions.

If the equity is not expensed until the shares/options are vested then the valuation methodology is not required to take into account vesting conditions or vary the value expensed to estimate this factor. Again this is the preferred model because it does not rely on subjective factors and "guesstimates".

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?

In Australia reload features and reloading of options are specifically excluded by the Australian Stock Exchange's Listing Rules.

However, in principle we agree that if a plan includes a reload feature this should be considered when the equity is accounted for. Preferably companies should deal with this additional expense at the time when the reload feature is triggered rather than at the time of grant, when fair value is calculated. Again this is to minimise the potential for inaccuracy and to ensure consistency in the approaches of companies.

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 21-25).

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

While we do not support some of the proposed valuation methods set out above, we believe that there are features common to employee share and option plans that should be addressed in the proposed IFRS to ensure that the standard is clear, unambiguous and applied consistently. Some of these features are noted above. The additional features that we consider should be addressed are as follows:

- vesting based on performance criteria alone;
- vesting based on share price increase;
- plans that have staggered vesting – so that vesting happens over a fixed period but tranches of the shares/options vest at different points over that period;
- deferred share plans that have restrictions and forfeiture conditions on the shares but are fully vested from the date of grant;
- non-recourse employee loan plans; and
- salary sacrifice plans.

<u>Question 16</u>

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 standards should not be prescriptive and should allow for flexibility and change over time. However, it is important that the standard is applied consistently between organisations and that the ambiguities do not allow for manipulation of the accounting process. We believe that more guidance is needed on how to calculate fair value in specific circumstances and if there is to be adjustment to value then guidelines should exist around the adjustments to limit subjectivity.

<u>Question 17</u>

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?

In principle we agree with the incremental value method used when a company reprices equity (shares or options) prior to vesting. As noted in Question 14 above there are only very limited circumstances in which this would apply in Australia.

In relation to the two methods used in Example 3 it may be appropriate for either method to be used depending on the particular circumstances of a company. There is insufficient information to comment on the methods set out in that example.

<u>Question 18</u>

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.

It is suggested that upon cancellation of an option prior to vesting that the entire amount outstanding be expensed in that year so that cancellation completes the expense item. Whilst past practice on option repricing in some companies and in some countries has been extensive and there is a recognised need for a deterrent factor in any accounting method, it seems inaccurate for there to be continued accounting for the initial option grant beyond the year of cancellation. The services that are received after that date are in relation to the repriced option only.

There appears to be no treatment of repricing of vested options.

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.

We support the valuing of the liability for cash-settled share-based payments as at the end of each reporting period. We have no objections to using the fair value of the liability as the means to measure the liability.

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.

NSP Buck does not substantially disagree with the proposals for these types of transactions.

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)?

As a general principle we support any disclosure requirements which increase the transparency and understanding of shareholders as to how a company operates its employee and executive share or option plans. At an executive level this of particular importance where the quantums are large.

In respect of the disclosure requirements we make the following comments:
- Paragraph 46 (b) would suggest rather than the weighted average prices that the disclosure sets out the different grants with the actual exercise prices. Generally each annual grant will only have one exercise price and the disclosure should distinguish between different grants and detail how many of the options granted are exercisable and have been exercised. The categories set out in paragraph 46(b) (I) – (vii) should be adhered to for each of those grants.
- Paragraph 52. More clarification should be given about Share-based Payments are disclosed so ensure that it is transparent to shareholders and it is clear what the expenses relate to and what expenses relate to non-employees and employees.

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.

The transitional arrangements are supported as they ensure companies are considering and focusing on how to expense their employee and executive share and option plans prior to standard coming into force. This transitional reporting will also highlight issues and concerns prior to the standard taking effect. However, for the first reporting period there should be some recognition of the fact that companies are implementing the standards for the first time and that there undoubtedly be initial "teething problems".

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 recognised in the income statement.

Are the proposed requirements appropriate?

We have no submissions to make on this point.

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.

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;***

This exemption as noted in our reply to Question 1 is supported. In Australia where the level of employee grants are generally limited it seems inappropriate and detrimental to include these items in the accounting standard. Not only is it likely to impact companies offering these types of plans, but the plans themselves are not the primary focus of the changes because of the low level quantums generally used. As noted in our reply to Question 1 it is imperative that the parameters of the exemption are clearly defined to ensure an exemption of this nature is not abused.

- ***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 BC70-BC74 in the Basis for Conclusions give an explanation of intrinsic value); and***

The notion of fair value is generally supported as the best method of valuing Share-based Payments. However, we do not support the suggested subjective adjustments to fair value to take into account vesting conditions, employee turnover levels and forfeiture conditions.

- ***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).***

In our reply to Question 1 we would suggest that unlisted companies are exempted from the standards or at the least a different methodology is applied to them. More consideration should taken to decide which if any is the best methodology for unlisted companies.

(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.

As noted above we do not support adjustment of the fair value for forfeiture conditions. Our general argument is that this kind of adjustment can be subjective and can be open to ambiguity and applied inconsistently. We support expensing at the date of vesting which would avoid the necessity to guesstimate the various uncertainties that executive share and option plans generally contain because of the performance and other vesting criteria.

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.

As noted in our response to the section above SFAS 123 is fully supported in its approach for the reasons stated 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 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.

We have no submissions to make on this point.

(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 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, 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.

As noted in our response to Question 18 we support the approach of SFAS 123.

(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).

We have no submissions to make on this point.

(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.

We have no submissions to make on this point.

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.)

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

Effect of Taxation in each jurisdiction

We understand the charter of the IASB and its role in the development of international accounting standards. However, we believe the IASB should recognise the potential effect of adoption of those standards by participating countries.

Value of options issued in respect of Share-based Payments. In addition, a company may also loose significant tax advantages because of the indicated accounting treatment, namely the crediting of amounts to a "option share reserve". It is believed that by crediting amounts to such a reserve the amounts are included for tax purposes in a company's share capital account. The tax law then considers the share capital account to be tainted and the shareholders loose the advantages of tax rebates.