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Date 7 March 2003
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Dear Sirs

FRED 31

We have read with interest the Financial Reporting Exposure Draft 31 on share based payment.

You will be aware of the general disquiet that the proposals have caused amongst those who are convinced that equity based incentives provide a useful tool for industry to provide targeted incentives to directors and employees. These arguments have been well rehearsed and we do not feel we have any new comments to add to that debate. However, please do not take the comments set out below on the method of implementation of the new standard as any comment or endorsement of the overall principle.

In terms of implementation, we are concerned that the new standard places very onerous obligations on companies in terms of calculating the profit and loss account implications.

This may cause companies to be reluctant to offer equity based incentives even though this is in the best interests of employees and shareholders, even taking into account the profit and loss account implications. Indeed, for many companies the costs of complying with the proposals for many companies will be disproportionate when compared to any benefit that may be derived from the appearance of the extra information in the accounts. We assume that the Accounting Standards Board do not have an agenda of discouraging share based incentive arrangements and therefore that it is incumbent on you to look again at your proposals if in fact their implementation would impose such onerous compliance costs that this useful motivational tool would be abandoned by many companies.

The main reason for our concern is the extremely detailed process which a company must go through in order to construct a valuation model suitable to their circumstances and to assess the variables involved in calculating the value of the share based incentives. Companies would have to assess such factors as the likelihood of employees leaving and when they are likely to exercise the option. At its worse this could come down to assessing the future intentions of individual directors and senior employees and publishing this information. We do not consider this to be a useful process.

We would suggest that you consider including in the Financial Reporting Standard an acceptance that companies may wish to use published information on the industry norms for some/most of the relevant factors, although they may wish to depart from these in particular circumstances, but they should not be obliged to do so merely because their historical data differs from industry average or that the intentions of a particular employee may differ from the norm.

We believe that this approach would not only help companies, particularly smaller quoted companies, to comply with the new requirements, but potentially would also increase transparency if the same variables were to be used by most companies in these circumstances.

Whilst we appreciate that the Accounting Standards Board would not consider it part of its role to publish such information, it is quite possible that certain commercial providers would be prepared to do so or that other bodies whose object is to encourage employee share ownership (such as Proshare) would be prepared to do so, particularly if there was encouragement to do so in the Financial Reporting Standard itself.

If given sufficient time, organisations such as Proshare may also be prepared to investigate publishing option pricing models for the most common situations, which would further help to reduce the burden of complying with the new requirements.

In the light of the above comments and the need to properly assess the benefits of the new standard for most companies when compared to the potentially damaging compliance cost implications, we would also suggest that the proposed implementation date of 1st January 2004 be postponed by one year as advocated by the UK Share scheme Lawyers Group in their submission to you.

If you have any views on this suggestion or would like further details please call Lawrence Green on 0121 232 1042.

Yours faithfully

Eversheds