

Letter of Comment No: 7
File Reference: FSP123R-A
Date Received:

July 29, 2005

Mr. Lawrence Smith
Director of Technical Application and Implementation Activities
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856-5116

RE: File Reference No. FSP FAS 123(R)-a, Classification and Measurement of Freestanding Financial Instruments Originally Issued as Employee Compensation

Dear Mr. Smith:

PricewaterhouseCoopers LLP appreciates the opportunity to respond to the Financial Accounting Standards Board (FASB or the "Board") on its proposed FASB Staff Position (the "FSP") noted above. We support the issuance of the FSP because we believe it will assist preparers by simplifying the classification requirements of instruments originally issued as employee compensation under FASB Statement No. 123 (revised 2004), *Share-Based Payment* (FAS 123(R)). We also continue to support the Board's efforts to comprehensively address identification of, and accounting for, liability and equity instruments. We do, however, have the following comments regarding the FSP as currently drafted:

- In paragraph 5 of the FSP, we recommend deleting the requirement that modifications after the rights conveyed by the instrument are no longer dependent on the holder being an employee would trigger a requirement to apply "other GAAP." We believe that all modifications should be subject to the measurement guidance of FAS 123(R) and that the balance sheet classification of an award should not be subject to other GAAP, unless the modification results in a change to the instrument's classification under the guidance of FAS 123(R).

- In Footnote 1 of paragraph 5, we suggest that the footnote be revised to clarify the applicability of the FSP to awards exchanged in business combinations as follows:

This FSP is intended to apply to those instruments issued in share-based payment transactions with employees accounted for under Statement 123(R), FASB Statement No. 123, *Accounting for Stock-Based Compensation*, or APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and to instruments exchanged issued in a business combination in exchange for share-based payment awards of the acquired business that were originally granted to ~~are held by~~ employees of that the acquired business and are outstanding as of the date of the business combination.

- In paragraph 6, we believe the reference to “substantive employee service” may cause confusion about the scope of FAS 123(R). Specifically, that term may conflict with paragraph 11 of FAS 123(R) which states that “...share-based payment transactions [are] to be accounted for under this Statement unless the transfer is clearly for a purpose other than compensation for services to the reporting entity.” FAS 123(R)’s use of the word “clearly” implies that a significant threshold must be met in order for a share-based payment transaction not to be considered employee services. Therefore, we suggest replicating the wording of paragraph 11 of FAS 123(R) in paragraph 6 of the FSP in order to avoid scope confusion.
- In paragraph 7, the FSP should address how companies that have elected to early adopt FAS 123(R) would apply the FSP (e.g., retroactively).

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If you have questions regarding our comments, please contact John Horan at (973) 236-4997.

Sincerely,

PricewaterhouseCoopers LLP