

Gary R. Kabureck Vice President and Chief Accounting Officer Letter of Comment No:
File Reference: FSP123R-D

January 31, 2006

Director, TA&I—FSP Financial Accounting Standards Board 401 Merritt 7 P.O. Box 5116 Norwalk, CT 06856-5116

Subject: Comments on Proposed FSP

FSP FAS 123(R)-d

Dear Sir/Madam:

We appreciate the opportunity to express our views on the proposed FASB Staff Position on Statement 123(R) (FSP FAS 123(R)-d), "Classification of Options and Similar Instruments Issued as Employee Compensation That Allow for Cash Settlement upon the Occurrence of a Contingent Event". We fully agree with the guidance in the proposed FSP as we believe it eliminates a significant source of confusion in FASB Statement No. 123(R), Share-Based Payment (FAS 123R), with respect to contingent repurchase provisions. We also believe that the current guidance included in FAS 123R, if literally applied in practice, would potentially result in companies recording significant liabilities that likely would never require settlement in either cash or other assets of the company.

The following are our specific responses to the questions raised in the FSP:

Issue 1: We do not believe the Board should restrict the guidance in this FSP only to specific types of contingent events. First, the proposed guidance is consistent with footnote 16 of FAS 123R regarding contingent share repurchase rights which is not restrictive to specific types of contingent events other than for the repurchase event to be outside the employee's control. We believe it is important to have consistent guidance with respect to share and option repurchase provisions since we fail to see the economic difference between the two provisions. We do not believe a different accounting answer is warranted between an award with a repurchase right on a share issued upon exercise of an option that became fully vested and exercisable upon a contingent event and an award with a repurchase right on an option that became fully vested and exercisable upon a contingent event. In either case both the company and the employee are in the same economic position both before and after the repurchase. Accordingly, we believe maintaining consistent guidance for puttable shares and puttable options should be the primary focus of the proposed guidance and for the reasons

Xerox Corporation 800 Long Ridge Road Stamford, Connecticut 06904

Telephone 203-968-3684 Facsimile 203-968-3918 expressed in this letter, we believe the "probable" guidance expressed in footnote 16 of FAS 123R represents the preferred approach to reconcile the current inconsistency.

Secondly, as the Board noted in its background material, under existing guidance on accounting for repurchase rights included in APB Opinion No. 25, "Accounting for Stock Issued to Employees" and continued under FASB Statement No. 123, "Accounting for Stock-Based Compensation" (FAS123), an entity would have assessed the probability of the contingent repurchase feature occurring. The existing guidance was not restrictive to specific types of contingent events. Accordingly, we believe there is enough of a basis in existing practice to assess contingent repurchase events based on probability consistent with the proposed FSP guidance. Restricting the guidance to specific events would likely just complicate the implementation of FAS 123R. We also believe that the assessment of probability in determining the existence of a liability is likewise well founded in practice such that its application should not be overly complicated. Accordingly, the proposed FSP guidance would effectively be an extension of an existing well understood practice followed under FAS 123 and consistent with the objective of FAS 123R to maintain existing practice to the extent possible (paragraph B134 of FAS 123R).

In addition, we believe that use of the probability standard is the correct guidance to apply since it is consistent with the definition of a liability as included in FASB Concepts Statement No. 6 "Elements of Financial Statements" (CON 6). Per CON 6, liabilities are generally defined as probable future sacrifices of cash or other assets. The current guidance included in FAS 123R appears to be at variance with this definition since, as noted previously, it would potentially require the recognition of significant liabilities that are remote from ever being settled in cash. We believe that such recognition would not be relevant and would be representationally unfaithful to the reporting of a Company's results of operations or statement of position.

Lastly, although the Board has noted the proposed FSP guidance will be inconsistent with the classification guidance for put options included in FASB Statement No. 150 "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity" (FAS 150), we believe it will be consistent with the guidance included in paragraph 10 and A7 through A9 of FAS 150 regarding the accounting for conditional redeemable securities. That guidance effectively requires a probability assessment to be made by not requiring liability classification for these securities until "...the event has occurred, the condition is resolved, or the event has become certain to occur, the financial instrument is reclassified as a liability". In addition, FAS 150 does not provide any restriction with respect to the type of conditional event that would be considered under this guidance. Accordingly, we believe the proposed FSP guidance would be consistent with FAS 150 with respect to the classification of conditional redeemable securities.

<u>Issue 2</u>: We do not believe the grandfathering approach would appropriately address the issue. As enumerated above, we believe consistency in application between share and option repurchase rights as well as existing practice under FAS 123 is a more important objective to

address and would not be adequately addressed under the grandfathering approach. In addition, we believe the grandfathering approach will likely lead to additional complexities in the implementation of FAS 123R. Specifically, there would be issues in determining to what extent modifications of an award would no longer make them subject to grandfathering; and likewise there would be issues regarding whether grandfathering would apply at the plan or grant level. Accordingly, we believe grandfathering would further complicate the implementation of FAS 123R and would not resolve the current inconsistency that exists in the guidance with respect to share and option repurchase rights but rather add to it by having inconsistent guidance for similar awards.

In summary, we fully support the proposed FSP guidance as it will eliminate the current inconsistent guidance in FAS 123R and will effectively maintain existing practice. We appreciate this opportunity to present our views to the Board on this very important matter, and are available to discuss any of our comments with you.

Sincerely,

Gary R. Kabureck

Vice President and Chief Accounting Officer

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