AIR PRODUCTS

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Letter of Comment No: 1
File Reference: FSP123RDU

4 January 2006

Mr. Robert H. Herz, Chairman
Financial Accounting Standards Board
401 Merritt 7, P.O. Box 5116
Norwalk, Connecticut 06856

Re: Employee Share Options as Liabilities

Dear Mr. Herz:

We have just been advised by our auditors (KPMG) of a change in a generally accepted interpretation regarding the classification of employee share options as liabilities versus equity when adopting SFAS No. 123R, "Share-Based Payment." Specifically, the interpretation that employee share option awards which permit the employee to elect a cash settlement on the occurrence of a change in control require liability classification and mark-to-market accounting. We disagree with the conclusion reached on a theoretical basis. We also find it unreasonable to be required to implement this guidance immediately, given our 30 September 2005 fiscal year end.

Air Products is a multinational major supplier of chemicals, industrial gases and related equipment with annual sales exceeding $8 billion, assets of $10 billion, and a worldwide workforce of 20,000 employees. Air Products adopted SFAS No. 123R effective 1 October 2005, on a prospective basis, and had been estimating the impact in 2006 to reduce diluted earnings per share by approximately $.13. The company had approximately 24 million share options outstanding at 30 September 2005.

We urge the FASB to review the issue of liability versus equity classification of employee share options, clarify its position, and at a minimum support extending the time to implement if the resulting guidance is a change from current practice. Summarized below are items we believe should be considered in review of this matter.

SFAS No. 5 is Fundamental
The liability classification of employee share option plans with an elective contingent cash-settlement provision should be consistent with the fundamental generally accepted accounting principle underlying the accounting for contingencies. Under SFAS No. 5, a liability is recognized when it is probable that a liability has been occurred and the amount can be reasonably estimated. Consistent with this well-established and guiding principle, an elective cash-settlement provision in an employee share based plan which is deemed remote to ever be triggered by a change in control, should not result in liability classification.

Inconsistency within SFAS No. 123R
Based on paragraph 31 of SFAS No. 123R, probability is a consideration in the determination of liability classification for share-based compensation other than stock options (such as restricted stock units, restricted shares, etc.). Based on paragraph 32 of SFAS No. 123R, probability is not a consideration in the determination of liability classification for employee share options. We do not understand the basis for different treatment for different types of share-based compensation. We believe probability is a key criteria in either case and the standard must be consistent within itself and also in comparison to other existing accounting literature such as SFAS No. 5.

Allow For Remedy
Earlier in 2005, based on our review of SFAS No. 123R, we identified the potential issue of liability classification for our stock option programs which included a change in control provision. We discussed this matter with our auditors, who after review with their national office, concurred that equity classification was appropriate. It is our understanding that the other major public accounting firms took a similar position. We proceeded accordingly. Otherwise, we may have taken steps at that time to modify our plans to avoid liability classification and mark-to-market accounting.

Given the generally accepted interpretation has been overturned, we believe at a minimum it is appropriate to allow companies a reasonable period of time (e.g., 1 year) to implement this new interpretation of the standard. Based on this provision, we would amend our employee share option plans. It is our understanding that a number of other Fortune 500 companies are currently in the process of amending their share option plans. While our company is clearly at a disadvantage given its fiscal year ends 30 September, we imagine even calendar year companies will also find themselves without adequate notice given the communication of this guidance over the holiday season and just prior to their year-end.

Time to Implement
Air Products adopted SFAS No. 123R effective 1 October 2005, on a prospective basis, and is in the process of preparing its first quarter earnings release and 10Q filing. Liability classification will require a significant administrative effort to calculate the initial cumulative effect, remeasure quarterly, and then establish a process to track details of the awards granted over the past 10 years going forward. We believe if this guidance must be implemented, a reasonable timetable for implementation must be provided.

The FASB's recent approach in the FSP regarding the transition election related to accounting for tax effects is a noteworthy example of responding to the complexity and implementation issues associated with SFAS No. 123R. We commend the FASB for reacting to feedback from constituents who did not have information readily available to implement the original requirement of SFAS No. 123R and accordingly provided an elective alternative transition method, allowing entities one year to evaluate the transition method. If the FASB disagrees with our theoretical arguments, we would encourage a similar approach.

Credibility to the Public
We have not prepared the calculations required by this new guidance and therefore have not communicated the expected impact of it externally to the users of our financial statements. We are concerned about the impact of such as surprise on the credibility of financial reporting and the users understanding of our financial results. The impact of this revised interpretation will have a significant impact on our reported results. We believe rushed implementation of this guidance will be perceived negatively and potentially impact our ability to deliver the highest quality of communication and disclosure for which we constantly strive.

We appreciate your consideration of our comments and we are available to discuss at any time. We expect the FASB will receive feedback from constituents on the impact of this guidance on liability classification but do have concerns on the timeliness in which this feedback might be received e.g., considering the holiday season and year-end of calendar year companies. We urge the FASB to review this issue and clarify its position promptly given the significant impact to companies currently in the process of preparing their financial statements.

Sincerely,

Paul E. Huck
Vice President and
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