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From: Peter Fisher [peter@shepherdventures.com]
Sent: Tuesday, June 22, 2004 3:43 PM
To: Director - FASB
Cc: jcdowling@nvca.org
Subject: File reference No. 1102-100

Letter of Comment No: 4783
File Reference: 1102-100

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

Dear Chairman Herz:

I am writing to express my concerns with FASB 123 (Share-Based Payment, and Amendment of FASB Statements No.123 and 95).

By way of introduction, I am a former Chartered Accountant, having been admitted to the The South African Institute of Chartered Accountants and the Ontario (Canada) Society of Chartered Accountants. I have been in the financial sector for the past 25 years, and am currently a founding partner and Managing Director of Shepherd Ventures, based in San Diego.

Here are my comments on the FASB's proposed amendments to Statement No. 123:

1. I am of the opinion that basic accounting principles have been infringed by the proposed amendments.

It is proposed that the estimated value of the options be debited or treated as an expense in the Profit and Loss Statement. However, it is also proposed that a corporation's equity be credited with the amount of the estimated value of the options. This, I suggest, breaches basic accounting principles. The corresponding credit to any expense (a debit) can either be to the corporation's bank account (if the amount is paid), or raised as a liability on the Balance Sheet if the expense is accrued, to be paid in a subsequent year. An expense **decreases** the net assets of a corporation; it is therefore factually incorrect to **increase** a corporation's net wealth or net assets by crediting its equity account.

I believe that the problem stems from the fact that the option grant may never be an expense in the first place. The estimated value of the option grant is never paid (in cash) or accrued as a liability. It is somehow an 'expense' that is not owed to another entity. If it is a true expense (a debit), the corporation must ultimately pay this amount, or accrue it to be paid in another accounting period. The proposed accounting treatment never anticipates payment, and therefore the basic assumption of the option grant being an **expense** must of necessity be challenged. Given that every debit must have a corresponding credit, in this case there is no alternative but to credit the corporation's equity account. This, in my opinion, is flawed accounting logic. It is tantamount to taking money from one pocket, realising the error, and then putting the money back into another pocket!

2. Furthermore, it is suggested that the proposed accounting treatment will not result in a better depiction of a company's economic health, or make for more transparent financial statements. In contrast, it is likely to confuse a reasonable and logical investor: why, one may ask, does this expense not impact the net assets of the corporation, as **all** other expenses do? Is it really an expense? If there is doubt, possibly one should add it back and not treat it as an expense? What will other analysts do? How will one ever be able to know for sure if one is comparing 'apples with apples'?

3. On a macroeconmic level, I do not believe that FASB has given due consideration to the potential impact that this expensing rule will have on the nation's economy. I am a venture capitalist, and invest in early stage, high risk companies. This is an investment, incidently, that most other financial institititions, such banks, are not prepared to take. It is well known that encouraging the formation of early stage companies is the way most jobs in this nation are created.

One way that the risk of early stage companies is mitigated is by hiring, and retaining, the best employees in a particular sector. Employee retention is critical to the success of an emerging company. There is no better way of providing for employee loyalty, and hence retention, than by the granting of stock options. If this process is complicated the the large and unnecessary cost of valuing stock options by either the Black-Scholes or binomial models, companies may opt to 'take the path of least resistance' and not issue stock options. This, I believe, will unnecessarily increase the risk of investing in early stage companies, thereby jeopardizing the entire venture capital process. I believe that FASB's proposal, if enacted, will ultimately undermine stock options as a tool that has successfully aligned the interests of shareholders with employees and which has been critical in our ability to foster the companies that have driven the nation's economic growth engine.

My request, therefore, is that FASB support and encourage legislation that will protect broad-based employee stock option plans, while addressing executive compensation for senior corporate executives. This is the appropriate action that is needed at this time.

Yours truly,

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