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Letter of Comment No: 2753
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From: Peters, Greg [greg.peters@zilliant.com]
Sent: Tuesday, May 25, 2004 3:48 PM
To: Director - FASB
Cc: jcdowling@nvca.org; kpaschall@austinventures.com; Peters, Greg
Subject: Expensing of Employee Stock Options (File Reference No. 1102-100)

To the Director@fasb.org (File Reference No. 1102-100):

I am the CEO of a privately held software company, Zilliant, Inc., based in Austin, Texas. Previously I have been the CEO of two public companies listed on the NASDAQ exchange. I am writing to voice my concern and opposition to the potential passage of the proposed FASB Statement 123, regarding the expensing of employee stock options.

In my opinion, the passage of this accounting standard will:

- o **Substantially reduce the value of financial statements** – The passage of this standard will continue a trend of making financial statements meaningless. The usage of pro forma results by companies to eliminate one-time and non-cash charges will only intensify with this release.

In addition, the use of the fair value methodology for calculating the compensation cost for stock options creates less rather than more clarity and transparency to a company's financial reports. Given the degree of subjectivity associated with several of the fair value calculation inputs (i.e. volatility, employee behavior, ...), the results are less comparable across time for a given company or across companies at a given time.

In addition, given that many investors care more about the after-tax cash flows in the process of valuing companies, the proposed reporting requirements make that job harder, not easier for those investors.

Specifically with respect to private companies, investors and creditors pay minimal attention to earnings per share performance. Their collective focus is on cash – cash balance, cash generation, cash consumption and the cash required for the company to reach self-sufficiency. Consequently, I do not believe the expensing of stock options will provide any value to the capital and resource allocation decision processes of private companies, their investors or creditors. In fact, the reporting requirements will only make the financial statements less helpful in assessing company performance since it will be more difficult to model cash.

- o **Increase administrative costs** - The administrative effort and expense associated with the proposed standard compliance is meaningful. The proposed methods for stock option expensing will require significant effort and cost to perform and audit and will undoubtedly consume management time ensuring the methodologies are applied correctly and the results are interpreted appropriately.

The success of a company, whether public and private, is predicated on its ability to leverage a dollar spent into multiple dollars of return through the application of time and talent. The administrative effort and costs of the proposed standard in terms of company dollars and time create no positive return, more likely, negative returns for the reasons outlined above.

- o **Reduce competitiveness** – Today's markets are global. Companies in other parts of the world do not have to deal with the confusion and cost associated with expensing stock options. This gives those companies a decided advantage both in the allocation of resources and when it comes to hiring the best people.
- o **Double the cost impact from employee stock option programs** – The cost of employee stock options is

- already reflected in the earnings per share calculation on companies' income statements through their inclusion in the number of shares outstanding. Additional expensing is overly burdensome to companies.
- o **Possibly result in the termination of employee stock option programs** - While it is doubtful that private companies will curtail the use of employee stock option plans, it is probable that pressure from institutional investors on public companies will significantly reduce the use of employee stock options to reduce the associated expense. In addition it will lead to their use solely in the executive suites of these corporations, something that dilutes the American entrepreneurial spirit. The ultimate result could be a general reduction in innovation within the technology sector and thus a drain on the U.S. economy.

I am hopeful that there is still the opportunity to change if not totally eliminate the proposed accounting standard. I have included my contact information below if you would like to discuss further.

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