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Sent: Tuesday, May 25, 2004 4:16 PM
To: Director - FASB
Cc: JC Dowling (E-mail); Gina Kenney (E-mail); Joe Aragona (E-mail)
Subject: Expensing of Employee Stock Options

May 25, 2004

Director Financial Accounting Standards Board
Re: File 1102-100
Expensing of Employee Stock Options

I would like to offer some comments on the topic of expensing employee stock options. My comments touch on both the theory behind the move to expense options and also on the practical application of the theory as outlined in the Board's Exposure Draft dated March 31, 2004. I will also provide my thoughts on how this proposed standard might affect Staktek Holdings as a company.

On the theory side, I understand the FASB's desire to include costs considered compensation in the financial statements. I also understand the goal of increasing the level of transparency and comparability in and between companies in these financial statements. However, I would argue that the impact of employee stock options is already considered in our financial results through the calculation of diluted earnings per share. To also include some additional number in total costs and expenses would be to double-count this item. Even more concerning is the impact on the goals of transparency and comparability. I don't think either of these is accomplished through this and in fact, I believe both are weakened. The calculation methodology requires several inputs that are very subjective in nature. Different decisions on these inputs can create wild swings in the compensation cost numbers ultimately recorded. This will make it even more difficult for financial statement readers to compare our results with those of our competitors.

The application of this standard will be very complicated. The inputs required are numerous and are subjective. Estimating future volatility and predicting future exercise behavior are just two examples of inputs that are very imprecise yet will have a significant impact on the ultimate calculation of compensation costs. Being a relatively new public company, we would have little historical data to use as a basis for either of these, even further increasing the variability in results. Looking forward, I can't imagine how much effort will be required to explain fluctuations in financial results from one period to another created by the inputs required in this calculation and by the transition methodology. Even with all these inputs, the ultimate calculation still does not truly recognize some of the restrictions inherent in employee options that make them less valuable than open-market options.

Let me close with some thoughts on how this exposure draft might impact Staktek. First is the increase in administrative costs. We are a small company and have always taken great pride in our ability to control costs by focusing on those things that create value. The effort and manpower required to comply with this new standard will be significant. It requires that each vesting period for each employee class be treated as a separate option valuation point. That greatly increases the level of effort versus today's requirements. The costs of the audit will also increase as these subjective inputs will require more time and effort on the part of our external accountants as well.

Using the standard we use for our internally driven costs, it is unclear what value is ultimately created by this increase in costs. First, it will make it more difficult for readers of financial statements to understand our results and even more important, to interpret how they compare with other companies. It seems that, because of the lack of consistency, most readers will simply ignore this cost component when doing any comparisons. If that is the case, we have put a lot of time and effort into an exercise that provides very little value.

A second potential outcome is the decline in competitive position versus companies in

countries where stock option expensing is not required. Again, there is the appearance of weakened financial results versus those companies that are not required to expense options due to the inclusion of the fair value as an expense. In addition, there is the real incremental administrative cost associated with the calculation and audit fees that only exacerbate this problem.

All of this could drive companies like Staktek to discontinue employee stock option plans. The incremental cost, both in real terms for the calculation and audit, and in financial statement terms for the fair value, could put us in a competitively disadvantaged position. If this happens, we would have no choice but to reduce or even discontinue the practice of granting stock options.

Of course that creates another major problem for technology companies like Staktek. What would happen if we decided to significantly reduce options? I think it's clear that over the long term our ability to attract talented people would be significantly adversely impacted, which would directly impact our ability to succeed in the market. Spreading this impact to all the other young technology companies trying to make a business work could be very widespread.

The spirit of entrepreneurs in this country provides immense benefit and is not something that we should jeopardize by creating accounting standards that add little value to ultimate financial statement users.

Sincerely,

James W. Cady
President and CEO
Staktek Holdings, Inc.