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From: Steve Dow [sdow@srfunds.com]
Sent: Monday, May 03, 2004 4:28 PM
To: Director - FASB
Cc: jcdowling@nvca.org
Subject: Stock Option Expensing File Reference No. 1102-100



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To whom it may concern:

I'm writing to express a major concern with the current debate on the expensing of stock options that has not been in any writings I have seen. The focus of the press and articles surrounding this issue have, in my opinion, completely missed the issue.

The purpose of accounting, among others, is to provide clarity into the finances of an organization, to do so with standard rules that create repeatable results from following those rules and to allow for "apples to apples" comparisons across companies. Moreover, accounting is supposed to increase certainty, not increase confusion.

The current proposal to expense options will not accomplish this and is I fear, a politically driven (not accounting) decision that will confuse and obfuscate financial results. It will do nothing to stop any 'abuse' of options -- there are other mechanisms for that within the realm of corporate governance. But the FASB should not lower its standards of accounting to try to step into this other realm.

My main problem with expensing options is that it is NOT an expense to the corporation. Stock options are a contingent liability to the shareholders of a corporation in the form of potential future dilution of earnings per share. It is the shareholders who should care -- not the accountants. So my argument is not that options have no cost. My argument is that running that cost through the P&L is incorrect accounting.

That is why full disclosure of the options granted by date and by exercise price will allow shareholders to provide their own assessment of future dilution based on their own assessment of future stock movements in the timeframes that matter to them (whether they have short or long term views).

If you force companies to expense options, then to be consistent you must have those expenses on the balance sheet as some form of non-cash entry that must be adjusted quarterly as the stock price moves - just as you would a bond, for example, when interest rates move. If you do not, you violate standard accounting approaches. To give an example: if 3 months after a grant of a four year option at an exercise price of 10, the stock drops to 5 -- what is the value? If the employ leaves at the end of 6 months and does not exercise -- do you reverse the expense? If the stock goes to 20 and the employee does not exercise, has the option increased in value? Should you write-up the expense because the value is now higher than, say, a Black Scholes model calculated? If the price of the stock is at 7 when the option expires in 4 years, what accounting should apply? Can you imagine each and every company trying to decided how to answer all these questions. IF you only have it apply to public companies and not private companies you defy all the logic of accounting by having similar companies (say 2 software companies) playing by a different set of rule. -- and giving a great advantage to private companies.

While I may view that options are a great engine for stimulating new company formation, that is not the point. Expensing stock options is just bad accounting treatment.

Sincerely,
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