



Letter of Comment No: 5534
File Reference: 1102-100

June 30, 2004

Director of Major Projects
Financial Accounting Standards Board
401 Merritt 7
Norwalk, CT 06856-5116

VIA email to director@fasb.org

Re: File Reference No. 1102-100 – Proposed Statement of Financial Accounting Standards – Share-Based Payment, an amendment of FASB Statements No. 123 and 95

Dear Director of Major Projects:

On behalf of Science Applications International Corporation, (“SAIC”), we appreciate the opportunity to comment on the FASB’s March 31, 2004 exposure draft of a Proposed Statement of Financial Accounting Standards, *Share-Based Payment – an amendment of FASB Statements No. 123 and 95* (the “ED” or the “Proposed Standard”).

SAIC is the largest employee-owned research and engineering company in the United States, providing information technology, systems integration and eSolutions to government and commercial customers. With annual revenues of \$6.7 billion, SAIC and its subsidiaries, including Telcordia Technologies, have more than 43,000 employees at offices in more than 150 cities worldwide. We extensively use broad-based employee share and option award programs. SAIC is an SEC registrant, but as an employee-owned company, our stock does not trade on a public exchange; we also have registered debt securities held by the public.

Although there has never been a general public market for our common stock, we have maintained a limited market through our wholly-owned broker-dealer subsidiary. Quarterly determinations of the price of our common stock are made by the Board of Directors pursuant to a valuation process that includes valuation input from an independent appraisal firm.

SAIC currently accounts for employee stock-based compensation using the intrinsic value method under the recognition and measurement principles of APB Opinion No. 25, “Accounting for Stock Issued to Employees.” For disclosure purposes, we meet the definition of a “nonpublic entity” in SFAS No. 123 and use the minimum value method for option valuation in applying the fair value recognition provisions of SFAS No. 123 to employee stock options and the employee stock purchase plan.

We have three areas of the proposed standard that we would like the FASB to reconsider as discussed below.

Issue 9 and Attribution of Compensation Cost for Awards with Graded Vesting

For the reasons described in paragraphs C89–C91, the Board concluded that this proposed Statement would require a single method of accruing compensation cost for awards with a graded vesting schedule. This proposed Statement considers an award with a graded vesting schedule to be in substance separate awards,

each with a different fair value measurement and requisite service period, and would require that they be accounted for separately. That treatment results in a recognition pattern that attributes more compensation cost to early portions of the combined vesting period of an award and less compensation cost to later portions. Do you agree with that accounting treatment? If not, why not?

We do not agree with Board's decision to require share-based payment awards with graded vesting to be accounted for as separate awards similar to the accounting under FASB Interpretation No. 28, *Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans*. We do not believe that recognizing expense based on graded vesting best reflects the benefits received by the Company or earned by the employee. In particular, we do not believe a disproportionate allocation of compensation cost, which is heavily weighted in the earlier periods, typically would reflect the service the Company is receiving from the employee as an employee provides service evenly throughout the service period. We believe the final standard should call for an approach that recognizes compensation cost on a systematic and rational basis that reflects how the service is provided and earned.

Issue 11 and Income Tax Accounting

*This proposed Statement changes the method of accounting for income tax effects established in Statement 123 as originally issued. Paragraphs 41–44 of Appendix A describe the proposed method of accounting for income tax effects and paragraphs C128–C138 describe the Board's rationale. That method also differs from the one required in International Financial Reporting Standard (IFRS) 2, *Share-based Payment*. Do you agree with the method of accounting for income taxes established by this proposed Statement? If not, what method (including the method established in IFRS 2) do you prefer, and why?*

We do not agree with the proposed standard's treatment of insufficient tax benefits or tax shortfalls. We consider the grant of a share award to be compensation. We believe that subsequent actions or events should be viewed as equity transactions. Consequently, we believe that both excess and insufficient tax benefits should be consistently recorded in equity.

Issue 14(b) and Transition Provisions

Consistent with its mission, when the Board developed this proposed Statement it evaluated whether it would fill a significant need and whether the costs imposed to apply this proposed Statement, as compared to other alternatives, would be justified in relation to the overall benefits of the resulting information. As part of that evaluation, the Board carefully considered the impact of this proposed Statement on nonpublic entities and made several decisions to mitigate the incremental costs those entities would incur in complying with its provisions. For example, the Board decided to permit those entities to elect to use either the fair-value-based method or the intrinsic value method (with final measurement of compensation cost at settlement date) of accounting for share-based compensation arrangements. Additionally, the Board selected transition provisions that it believes will minimize costs of transition (most nonpublic entities would use a prospective method of transition rather than the modified prospective method required for public entities). Moreover, the Board decided to extend the effective date of this proposed Statement for nonpublic entities to provide them additional time to study its requirements and plan for transition. Do you believe those decisions are appropriate? If not, why not? Should other modifications of this proposed Statement's provisions be made for those entities?

We do not agree with the alternate transition provisions for nonpublic entities that use the minimum value method of measuring options for pro forma disclosure purposes as discussed in paragraph 22. While we appreciate the Board's sensitivity to minimizing costs of transition and making the transition less cumbersome for nonpublic entities, we believe these provisions run counter to one of the primary objectives of the proposed standard - comparability of financial statements across all entities. As described earlier, SAIC is considered a nonpublic entity based on the definition in SFAS No. 123. However, we find that the users of our financial

statements (employee owners, public debt holders, rating agencies, and our independent appraiser) all wish to compare them to those of similar public companies as a means of better understanding relative performance. The proposed standard would not provide this direct comparability for several years.

The proposed standard would allow SAIC to early adopt at the same time public companies are required to adopt, thus making us comparable from a timing of adoption perspective. However, paragraph 22 would require us to use a prospective method of transition and, therefore, would not put us on a comparable basis with public companies that are required to use the modified prospective method based on paragraph 21. Paragraph 21 transition requires expense recognition for awards granted or modified after December 15, 1994 that are unvested at adoption date. We recommend that a nonpublic entity be allowed to elect the modified prospective method transition rules as discussed in paragraph 21 of the ED. We would further recommend that if a nonpublic entity elects this method of transition, the entity would remeasure the unvested awards previously granted, and not be required to use the expense previously disclosed under the minimum value method.

We welcome any questions regarding our response and appreciate the opportunity to respond. Please feel free to contact Peter Pavlics at (858) 826-6690 or Anne Liu at (858) 826-4624.

Sincerely,

/s/ Thomas E. Darcy
Executive Vice President and
Chief Financial Officer