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Susan Cheng [susan_cheng@idgventures.com]

From: Sent:

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To:

Director - FASB

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I am writing to express my opposition to FASB's proposed stance on option valuation, particularly as it applies to small business. While I can contribute to the debate about whether options are really an expense, I would rather take this time to detail the practical issues around the proposal because I believe it is the practical application of these proposals that will cause the greatest distress amongst small companies.

As a venture capital professional, I have great concern for my small portfolio companies who will have to grapple with the difficulties of implementing the valuation procedures. Most of these small companies do not have large financial staffs; in fact, many of them survive with only a controller and two or three staff members and are stretched as thin as possible. These staff have neither the time nor the educational training to be able to implement a proper valuation process. They will have to hire consultants, accountants and experts to help them with this process. The additional expense and time will mean resources will be diverted from helping these companies grow. The ultimate result could very well be that options will cease to be granted by small companies, but this will lead to an increase in pressure on wages. The result of this will again be less resources available to help the companies grow. If one follows this premise through, this will mean that it will cost more to start and grow young companies and ultimately fewer new companies will be funded by investors. Investors will look to other asset groups or move overseas to countries where options are being embraced, such as China. Given that a disproportionate percentage of the growth in the US economy is fueled by small companies, the move to expense options could have a potentially deleterious effect on the longterm economic health of the country.

As a former professor of finance whose research specialty was the pricing of complex derivative assets, I am also very concerned with how these companies are going to apply the valuation models that are being proposed. In particular, it is very very difficult to estimate stock price volatility for small companies, some of whose capital structures are heavy in preferred stock (whose trading is restricted) as opposed to common stock. There is a fairly large body of literature which addresses the practical issues of determining volatility in highly liquid publicly traded common stock and, even there, there are questions of how to model the variable. In privately held companies, it is not even clear that volatility can be reliably or accurately measured. In fact, it is not even clear under that the models for pricing options actually hold true for such stock. I simply do not see how any of these small companies are going to be able to price their options with any certainty.

Given my concerns as outlined above, I would urge the FASB to consider again whether small closely held private companies should be included in their proposals to expense options. I believe that forcing these companies to do so imposes an undue burden on their staff and is, from a valuation standpoint, impractical and impossible.

Susan Cheng, PhD General Partner IDG Ventures 650 California St., 24th Floor, San Francisco, CA 94108 susan_cheng@idgventures.com 415.439.4420