

----- Original Message -----

From: Karen Kay Malmstrom
To: 'Jeff Mahoney'
Sent: Friday, December 19, 2003 10:32 AM
Subject: RE:

Dear Mr. Mahoney,

Thank you for your prompt and detailed reply.

I'm not questioning whether "fixed plan" call options (issued with a strike price at or above the stock's current market price) have any value - - I'm contending that they have no cost - - other than an opportunity cost, as discussed in my original e-mail. (As we would both agree, their value - - i.e, their opportunity cost - - is approximately equal to their "speculative value" as determined by stock option models like Black-Scholes, etc.).

However, even the Harvard Business Review admits that these stock options have no impact on cash flow, and that they are just an opportunity cost to the company.

Perhaps another example will illustrate my point about opportunity costs:

Suppose a retail store puts some of its merchandise "on sale" at a 25% discount to its normal price. Clearly, its P&L will reflect the "lower" revenue due to the lower sales prices, and it will also reflect whatever the "real costs" of providing those products were - - but the FASB certainly would not contend that the P&L should ALSO be charged an "additional expense" for the (missed) opportunity cost of not selling the products at their normal prices!! (Yes, the products sold did transfer additional value to the purchaser. However, there was no additional cost incurred by the company - - other than the opportunity cost of not selling the products at their normal prices).

There is no essential difference between that type of opportunity cost and the opportunity cost of the aforementioned stock options - - yet the FASB is shortly going to require that they be handled differently in GAAP accounting statements!!

I believe the FASB is really trying to solve the (very urgent) problem of "excessive executive compensation" by violating its own accounting principles . . . Whatever happened to recording assets - (and hence, subsequent corresponding P&L expenses) - at the lower of cost or market??

I applaud the FASB's well intentioned effort to try and attack the excessive executive compensation problem, but I'm not in favor of doing it via the (soon to be mandatory) "stock option expensing" manner.

In my opinion, you are risking significant adverse impacts on small-cap company market valuations by selectively imposing the mandatory inclusion of (non-cash) opportunity costs in their P&L's. You need to find another way to attack the excessive pay problem.

Please forward this e-mail to all members of the FASB so I don't have to repeat it to each one separately.

I respectfully look forward to your response.

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