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To: Director - FASB
Subject: Comments on the Exposure Draft - SBP FAS 123

Comments on the Exposure Draft - Share Based Payment, an amendment of FASB Statement No. 123 and 95

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Issue 4 (c):

The Board should require a specific method of estimating expected volatility, however the Board should not default to historical volatility as the estimate of expected volatility without taking into consideration other available information. Based on my research, I think that if there is a specific method of estimating expected volatility, historical volatility should be one to be used unless there are other significant information available.

1. The scope of my research: to find out how firms estimated their expected volatility in 1999, and then compare them to the 5-year historical volatility from 1995-1999 and the 5-year historical volatility from 1999-2004. For simplicity I assumed that the expected life of options was 5 years for all companies.

2. Method I used. From a list of over 7,000 public companies, 200 companies were randomly selected. Then I went to SEC's web-site to look for their 1999's 10K. The information I needed is the total shares of stock option, the expected volatility and the fair value calculated. 35 companies that had all the required information were finally selected. (see attached list)

3. Results of my research:

Total number of companies:	35	
Total shares of options:		
365,599,399		
Weighted fair value as report:		\$12.83
Weighted expected volatility as reported:	47%	
Weighted 5 year historical volatility in 1999 ("1999 Volatility"):		51%
Weighted 5 year historical volatility in 2004 ("2004 Volatility"):		59%
Number of firms whose reported volatility < 1999 Volatility:	26	
lower 5% or more:	22	
Number of firms whose reported volatility < 2004 Volatility:	29	
lower 5% or more:	28	
Number of firms elected to expense options in 1999:	None	

4. Analysis

As indicated in Item 3, most companies reported lower than historical volatilities. 63% of them used the expected volatilities lower by 5% or more than historical volatilities. As the expected volatilities are so subjective, the estimates tend to be far from close to the actuals. The weighted expected volatility was 47% compared to the 59% of actual 5 year historical volatility. Assuming all options granted at the market value with a 5-year life, everything equals, this variance of 12% would increase fair value by 15%, which in turn would increase the expense or reduce the net income by 15%! Also because the estimated expected is subjective, there is yet a way to prove/overturn anybody's estimate, how can investor compare the performance among companies?

5. Suggestion:

Before inventing a way to justify the estimated volatility, I believe that historical volatility is the best estimate of the expected volatility and thus historical volatility should be used unless there are significant evidences to justify the historical volatility is not a better indicator. It's easy to obtain and it will improve the comparability of reported financial information since all firms are using one single standard.

Name List of my Research

Interpublic Group
Johnson Controls
Sportsmans Guide Inc
Cintas Corp.
Sears Roebuck
Commerce Group
Andersons Inc
Bassett Furniture
Regent Communications Inc
LandAmerica Finl Group
Ford Motor
BioMarin Pharmaceutical Inc
Tower Automotive
NuCo2 Inc
Allmerica Financial
Amer. Greetings
Graco Inc.
KEMET Corp.
Nocopi Technologies Inc/MD/
Cheesecake Factory
Persistence Software Inc
Embrex Inc.
America Service Group
CPC Of America Inc
Printronic Inc.
Home Depot
CDW Computer Ctrs
Charles River Associates
Scientific Games Corp.
Corinthian Colleges
Manugistics Group
Twinlab Corp
NeoMagic Corp
Ista Pharmaceuticals
Verisity Ltd
MatrixOne Inc
NetGuru Inc
CoStar Group
Turnstone Systems Inc
Superior Energy Svcs
CTI Group Holdings Inc
MFIC Corp
Ask Jeeves Inc
NovaStar Financial