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-----Original Message-----
From: Rick Ferri [mailto:Rick@PSinvest.com]
Sent: Thursday, November 07, 2002 10:50 PM
To: fasbcomments@fasb.org
Subject: Expensing options

I do not know who to send this to, so I am emailing in the blind.

How options are price is of critical importance to the proposal ruling. No one is talking about how options are being priced, only how to expense them. The could lead to a large error on income statements and balance sheets.

Option prices have two parts, the intrinsic value and the speculative premium. The intrinsic value is that portion of the option price that is "in the money", meaning the options strike price is below the current market price. The speculative premium is value of the option above its intrinsic value, but the speculative premium has no economic value, and is not an expense to the company. Only that portion of employee stock options that will actually affect shareholder value should be expensed. This division of pricing has MAJOR implications for a FASB ruling.

For example, if options are issued to IBM employees at a $50 exercise price, and the current stock price of IBM is $50, there is no expense to the company, so there should be no deduction in earnings. It would be inaccurate to expense the speculative premium calculated on the employee options using the Black-Sholes pricing model, or some other pricing model. The speculative premium goes to $0 when the option is exercised, so it is never an expense to the company.

I am baffled why this important fact is not being addressed.

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