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Accounting Services

November 1, 2002

Financial Accounting Standards Board
410 Merrit 76
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MP&T Director – File Reference 1101-001
FASB Exposure Draft: Accounting for Stock-Based Compensation - Transition and Disclosure – An amendment to FASB Statement No. 123 *Accounting for Stock-Based Compensation*

Dear Ms. Bielstein:

Pfizer has a long history of involvement with the issue of stock option accounting and disclosure. We commented frequently during the initial development of the SFAS 123 standard, participated in the FASB Field Test and have provided input to members of the International Accounting Standards Board. Further, as a large multi-national company, we have been exposed to a wide variety of stock option accounting issues. We welcome the opportunity to continue to participate in the process and commend the FASB for working so quickly to respond to the needs in the investor community.

Pfizer is a research-based health care company with global operations in over 140 countries. The Company's 2001 sales were approximately $32 billion and assets are approximately $39 billion.

As we have conveyed in numerous forums, we continue to believe that of expensing employee stock options does not address the true investor issue of corporate governance nor do we believe that it is appropriate given existing fair value models. We do not believe that such an approach makes the financial statements more understandable, more transparent or more "correct."

- It is well accepted that there are no existing fair valuation models that adequately account for the restrictions inherent in employee stock options. The use of these potentially (and probably) unreliable estimates is a concern - - even for disclosure only purposes. But, to include such estimates in the primary financial statements simply serves to elevate the consequences of the problem, which is, in our opinion, an undesirable outcome.

- We observe that the EPS accounting model (treasury stock method) already accounts for the impact of stock options. As "in-the-money" stock options are reflected as increased outstanding stock for EPS purposes, we believe that expensing stock options in the income statement will only serve to magnify this impact.

- We are concerned about the "permanent" volatility that is introduced into the income statement by the use of the expense method. Although the book income charge is based on an uncertain estimate at a fixed point in time, the income statement impact is never "trued-up" to actual. (But, the tax impact of stock options can be eventually trued-up via a valuation reserve). Further, the expense method does not permit adjustment for subsequent economic events, such as changes in forfeiture rates.

With regard to the exposure draft, we are concerned that the proposed standard will continue to elevate the importance of expensing employee stock options in the mind of the investing public. The true issue around stock options is one of corporate governance as the current footnote disclosures required are readily transparent and address the issue of the possible expense of stock options. We understand the motivation of the FASB in issuing this exposure draft, but, because of our concerns about the appropriateness of the expense method, we do not believe that it will serve the public well.

Our comments to the exposure draft, which are expressed more fully in the attachment, primarily relate to the following:

- Concern about the prescribed placement and format
- Concern about permitting three implementation choices, which in our opinion will only provide more confusion to investors due to lack of consistency amongst companies.

We would be happy to discuss our views with your staff.

Very truly yours,

Loretta V. Cangialosi

Loretta V. Cangialosi
Vice President and Controller

Attachment

cc: Mr. D.L. Shedlarz, Executive Vice President and Chief Financial Officer
Mr. A. G. Levin, Vice President - Finance

As expressed in our cover letter, we continue to object to the appropriateness of expensing employee stock options in the income statement. As such, we are disappointed to see that the FASB seeks to issue a standard that serves to elevate the importance of the expense method contained in SFAS 123.

Furthermore, we have seen little evidence that stock analysts for Pfizer or other companies use such value. We have also seen no evidence that the fair value methods assist in promoting consistency or comparability of companies' financial statements.

Amendments to the Transition Provisions

We recommend that the FASB mandate option "b." That is, adopting companies should "recognize stock-based employee compensation cost from the beginning of the fiscal year in which the recognition provisions are first applied as if the fair value based accounting method in this Statement had been used to account for all employee awards granted, modified, or settled in fiscal years beginning after December 15, 1994."

Specifically, we are unclear as to the value of offering three choices while disallowing a cumulative effect approach:

- The profusion of choices does not promote comparability and will further serve to confuse investors.

- In A7, the FASB states that a cumulative effect would not represent a meaningful amount since it would relate to the time from the original issuance of SFAS 123. But we note that full restatement back to the original issuance of SFAS 123 is permitted. Also, the FASB could dictate the cumulative effect "period" that it deems appropriate.

- In A7, the FASB noted concern about user confusion created by the cumulative effect approach. We are concerned that this may be a reflection of a new FASB "policy" that will reject the use of the cumulative effect approach in the future. If investors are confused, it generally should not result in abandonment of a principle, but rather should result in educating investors.

- In A7, the FASB states that a cumulative effect would result in an increase in additional paid in capital that is offset by a reduction in retained earnings. This statement is presented as a reason for not permitting a cumulative effect approach. However, we observe that this impact is similar to what happens with SFAS 123 income statement recognition. That is, there is an initial credit to paid-in capital for the SFAS 123-based fair value and an expensing of the SFAS 123-based value, which then serves as a reduction in retained earnings.

- In A11, the FASB did not want to preclude the existing SFAS 123 transition method out of concern for early adopters. However, we note that adding options that were previously unavailable to early adopters already sets up an "unfairness" to early adopters.

Amendments to the Disclosure Provisions

We recommend that the FASB not mandate the placement of these disclosures. Given the unreliable nature of the estimates underlying these disclosures, we believe that the ED approach inappropriately emphasizes the importance of the disclosures. Further, as we believe that all financial disclosures are an integral part of the financial statements, we disagree with a mandated positioning of any disclosure elements. As management is responsible for the fair presentation of financial results, management should determine the appropriate location of its disclosures.

We have the following specific comments:

- Technically, the requirement to disclose the use of APB 25 versus SFAS 123 income statement recognition already exists under APB 22 (*Disclosure of Accounting Policies* (12. a)). Moreover, our casual review of other company financial statements suggests this has also been the practice.

- We note that the ED requires a company to move the pro forma and actual amounts into the narrative discussion of the accounting policy. We are puzzled as to the rationale for placing the pro forma and actual stock option information in a location that will likely be several pages away from the traditional stock option footnote location. We are unclear as to how a user of the financial statements will be served.

  The FASB appears to want to elevate the placement of this information in the footnotes. However, we argue, in the words of the FASB itself, that "**all** [emphasis added] financial disclosures required under generally accepted accounting principles are integral to the financial statements." (ED A16)

  Moreover, we are concerned about the disclosure of fair values without concurrently disclosing, in context, the assumptions used to determine those values. Again, as noted above, those assumptions will likely appear several pages later.

- Technically, the requirements to disclose APB 25 –stock based compensation already exists (SFAS 123 (47 e)). Only the format is different.

Additional Comment

The FASB has asked whether it is appropriate to report the SFAS 123-based fair value by income statement line classification (Notice for Recipients). We do not think it is appropriate because we do not think the aggregate valuation is relevant. In addition, we doubt that many companies collect information in this manner. As such, as a practical matter, we are concerned about such a request, particularly for the current yearend reporting requirements. Finally, we are unclear as to the value of this information to the users of the financial statements.