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4 November, 2002

**RE: Amendments SFAS 123, Accounting for Stock-Based Compensation**

Dear Mr. Lucas:

UBS AG is pleased to have the opportunity to comment on the Exposure Draft of the Proposed Statement of Financial Accounting Standards, *Accounting for Stock-Based Compensation – Transition and Disclosures*. UBS AG listed its global registered shares on the New York Stock Exchange in May 2000. Although UBS AG utilizes International Accounting Standards ("IAS") as its primary reporting framework, we provide a reconciliation to US GAAP. We are thus keenly interested in the work of the FASB and cognizant of the need for high quality accounting standards, which facilitate the international comparability of financial statements. Through our Warburg Business Group we are one of the leading investment banks in the world and have extensive knowledge of the derivatives markets, including employee stock and options. The comments provided below represent a view held by the Bank. The UBS Equities Research Department has submitted a separate letter expressing their view from an equity analysis perspective. The views submitted by the UBS Warburg Equity Research Department may differ from those expressed in this letter. We hope you find our comments useful.

We agree with the Board's concerns over the "ramp-up" effect, which would likely result from application of the existing transition provisions of SFAS 123. Although, we acknowledge the appropriateness of the decision to allow for prospective adoption in 1995, the arguments supporting it are no longer valid. We believe that, having complied with the disclosure requirements of SFAS 123 since its effective date in 1995, entities can no longer justify a view that "retrospective application" is an overly burdensome and costly chore. Conceptually, retrospective application will provide the greatest utility to financial statement users as it promotes consistency within and comparability among financial statements. As such, we recommend that the FASB consider elimination of the other two transitional alternatives, as they will only hinder financial statement users, provide an opportunity for arbitrary manipulation of results, and reduce comparability among enterprises.

If it is concluded that alternative transitions are, indeed necessary, we would recommend that the Board consider rating the alternatives from most to least preferable, and developing conditions which must be met to apply the less preferable alternatives; e.g., insufficient data for segment reporting.

In light of the FASB's intent to issue an invitation to comment on the IASB's impending share-based compensation exposure draft, we would like to mention in advance some notable discrepancies between the FASB's pricing model guidance, as described under SFAS 123, and what we observe to be standard market pricing practice.

Interest rate

Global market practice uses a LIBOR-based rate as the risk-neutral discount rate variable input in option pricing models. As currently written, the standard (paragraph 19) requires US entities to use the implied yield currently available on zero coupon US government issues with a remaining term equal to the expected life of the option (the treasury rate). We believe it is more appropriate to use the same rate as the market in order to get an accurate fair market valuation for options. As such, we recommend that the FASB amend the standard to require entities to use the interest rate curve that is used by market convention.

Stock price

In practice, traders consider the impact of option issuance on the overall market capitalization of the issuer when developing pricing inputs. Typically, a trader would anticipate that the dilutive impact of newly issued options would result in a dampening of share prices. This impact would be incorporated into the trader's pricing model via a discount against the share price variable input. As employee options awards are often significant with respect to the normal daily volumes of share trading, omission of such a discount could result in a material over-pricing. As currently written, the standard does not permit any share price discount. We recommend that the FASB allow for such discounting as it is reflective of true market pricing.

Restriction period

We further recommend that the Board re-evaluate its previous decision to prohibit issuers from reducing the value of non-vested options for transferability restrictions (as expressed in paragraphs 155-160). We believe that companies and employees consider options to be one of many available alternative compensation tools. Increasingly, as companies have moved toward a variable compensation framework, options are used as a significant portion of compensation. Restricted option awards (or any restricted awards, for that matter) are simply less valuable than an equivalent award without restrictions. We therefore believe that there is a growing disconnect between the amount reported as compensation expense under SFAS 123 and the actual grant-date economic value.

In summary, we would encourage the Board to reconsider the existing pricing constraints in the standard in light of the significant technical advances in the market place since its issuance.

We very much appreciate the opportunity to comment. If you would like to discuss any comments that we have made, please contact us at your convenience. Your contacts on the subject are Ralph Odermatt, Managing Director (+41-1- 236-8410) and John Gallagher, Executive Director (+1-203-719-4212).

Yours sincerely,

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