Stacey Sutay

Subject: FW: FASB 123 (Stock Option abuse)

----Original Message----

From: R.W. Glenn [mailto:rwglenn@netzero.com]
Sent: Wednesday, October 15, 2003 11:54 AM

To: Michael Tovey

Cc: chairmanoffice@sec.gov; lasb@lasb.org.uk **Subject:** Re: FASB 123 (Stock Option abuse)

October 15, 2003

Mr. Michael W. Tovey Financial Accounting Standards Board Abuse P.O. Box 5116 Norwalk, Connecticut 06856-5116

Dear Mr. Tovey.

Letter of Comment No: 1/2 A
File Reference: 1101-SCU
Date Received: 10/15/03

RE: FASB 123 Stock Option

Thank you for your response to my October 9 email expressing concern that the Board had not fully grasped the "GRAND THEFT" where the <u>investing public is being scammed by corporate management to the tune of billions and billions of dollars</u>. Before reviewing the April and May decisions "with respect to measurement date" and the August 13 "meaning of cash settlement" as you suggested, I wanted to reiterate my concerns to be sure everyone understands exactly how Corporate Management is shifting these billions from their Corporate Coffers into there own pockets,

For 2002, the S&P TOP 10(1991) shifted almost \$29.7 billion dollars into their pockets, up 28% from the prior year! As noted in the one example below, Pfizer's Management pocketed \$9.6 billion over the three years 2000-2002 and Pfizer's \$25.6 billion net income was overstated by \$7.4 billion or 29% over the four years 1999-2002. All of this is "in conformity with accounting principles generally accepted in the United States of America". The Board must acknowledge this rip-off and take the necessary action to correct this injustice.

Your efforts and those of the Board and other senior staff members on FASB 123 are of critical importance. The billions of dollars that are being shifted to corporate management at the expense of individual shareholders are affecting the very pillars of our capitalistic society; investor confidence is being destroyed by this "infectious greed". In the Board's efforts to date, I hope it is not missing the "forest for the trees". Anticipating every scenario is important, but to miss the Grand Theft that results from the lethal combination of an INDEPENDENT stock option plan and an INDEPENDENT stock buyback program, neither established in conjunction with the other, would be to render all of the Boards' time a meaningless effort. This analogous relationship between stock options and stock buy-back programs and how management is using these programs to bilk billions from the investing public must be addressed. Not addressing this is to become an accomplice.

In my review of major corporate financials, I have not found a hint of any policy or program *linking* the buying of shares in the market to offset the options exercised! I have never seen a corporate stock buyback announcement say "We're buying back shares to offset the shares issued to ourselves under our stock option program" but rather something like, "shares will be used for general corporate purposes". To make this connection would bring the **deadly** <u>combination</u> to light, the last thing corporate management wants. Management wants shareholders to believe stock buyback programs reduce the shares outstanding. Management wants shareholders to believe that stock option programs provide incentives to management to increase profits. But Management does not want shareholders to know stock buyback programs are being used to offset or fund the shares exercised under the stock option programs and at only a fraction of their true expense. They

do not want their shareholders to know the earnings per share they are reporting are grossly overstated and their own compensation grossly understated.

A stock option program in and of itself is fine. A stock buyback program in and of itself is fine. But when a company that has a stock option plan "buys back" its stock for whatever the reason and the number of outstanding shares does not decline because the amount of shares bought back is equal to or less than the shares exercised under the company's stock option plan, those cash funds used to buy back the shares should represent a compensation expense to the company. Any shares bought back which exceed the number of shares exercised under the stock option program need not be expensed, because those shares will properly reduce the number of shares outstanding, increasing earnings per share.

To illustrate specifically how the deadly combination works, lets look at Pfizer for the four years 1999-2002. Over this period, Pfizer spent \$12.2 billion (48% of its \$25.6 billion income) to buy back 31 million shares. According to the Consolidated Statement of Shareholders' Equity shares outstanding should have decreased 331 million shares because of the buybacks, but instead only decreased a token 25 million shares (6.129 billion shares to 6.104 billion as of December 31, 2002).

What accounts for the 306 million share difference?

Of the 306 million shares, 262 million shares were issued under the company's stock options' programs with the remaining 44 million shares (net) going to Pfizer's employee benefit trust and "Other". (This is noted as the increase in "common")

stock/shares", "Stock option transactions" on Pfizer's 1999-2002 Consolidated Statement of Shareholders' Equity.)

If the 44 million employee benefit trust and "Other" shares issued that were bought back were properly expensed, where did the other 262 million shares that were bought back go which did not reduce the number of shares outstanding?

Of the 331 million shares bought back, 262 million were issued to Management as compensation under the company's stock option program with **no drop** or decrease in the number of shares outstanding (and with minimal to no effect on earnings per share).

What is the value of the 262 million shares issued to management under the stock option program which did not reduce the number of shares outstanding?

Pfizer bought back 331 million shares for \$12.2 billion or \$36.75 per share. 262 million shares times \$36.75 is **\$9.6 billion**. Thus **\$9.6 billion** in cash was used to buy back the 262 million shares issued under Pfizer's stock option programs with **no reduction in outstanding shares**.

How much did Pfizer expense against earnings per share during this period 1999-2002?

Absolutely nothing! \$9.6 billion went into the pockets of management with no expense recorded against income, all in

accordance with generally accepted accounting guidelines. Amazing!

This makes a farce of KPMG's Independent Auditor's opinion which states, "...(Pfizer's financial statements) present fairly, in all material respects, the financial position of Pfizer Inc...in conformity with accounting principles generally accepted in the United States of America", and Dr. McKinnell's and Mr. Shedlarz's statements filed under Investor Protection Act of 2002 of questionable value. Both signed statements saying (item 2.) "Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;" and (item 3.) "...the financial statements...fairly present in all material respects the financial condition, results of operations and cash flows...for the

period presented in this annual report." NO WAY!

How much did Pfizer expense against earnings per share during this period 1999-2002 on a pro forma basis as if they had recorded stock option compensation expense?

According to the footnotes (Footnote J, Pfizer's 2002 Annual Report), Pfizer recorded the following compensation amounts on a pro forma basis using the Black-Scholes option-pricing model as required under accounting principles generally accepted in America (GAAP):

1999 \$519 million 2000 \$807 million 2001 \$560 million 2002 \$518 million Total \$2,404 billion

How much, approximately, were Pfizer earnings overstated?

If the 44 million employee benefit trust and "Other" shares issued were properly expensed,
Pfizer's \$25.6 billion net income was overstated by the \$9.6 billion of pretax of stock option compensation expense on the 262 million shares that went into

Management's pocket which did not reduce outstanding shares. On this basis using a 22.975% as the average tax, etc. provision over the four years, **Pfizer's \$25.6 billion net income was overstated by \$7.4 billion or 28.9%** \$25.6 billion - ((\$9.6 billion - (\$9.6 billion x 22.975%)).

Is this large (\$7.4 billion or 28.9% net income) overstatement unique to Pfizer?

No, as noted below, companies such as Microsoft, Johnson & Johnson, and Citigroup, exhibit similar patterns (large common stock purchases as a percent of net income 69%, 59%, and 29%, respectively, with minimal to token decreases in outstanding shares +0.99%, -1.48%, and 0.74%, respectively) over the 3 year period 2000 to 2002. IBM is similar (66% and a -7.53%) but has decreased its common stock purchases over the last two years compared to the prior two with a 4% decrease in outstanding shares. Based on 2002, WalMart is exhibiting similar negative patterns with common stock purchases at 2 1/2 times the prior year with less than a 1% decrease in outstanding shares. AIG, but especially General Electric and Coca-Cola, are showing less abuse in their stock option/stock buyback programs.

	2000 to 2002 Common stk purchases as % Net Income	2000 to 2002 % Change in Outstanding shares
Microsoft	69%	+0.99%
IBM	66%	-7.53%
Johnson & Johnson	59%	-1.48%
Pfizer	47%	-1.20%
Exxon Mobil	29%	-3.68%
Citigroup	29%	-0.74%
WalMart	22%	-0.63%
AIG	18%	-0.60%
General Electric	13%	-0.04%
Coca Cola	12%	-0.16%

How can this gross abuse of stock options/stock buyback programs be curtailed?

By integrating wording into the proposed standards such as "stock option compensation expense will be the *greater of.* (a) that determined under Black-Scholes, etal., <u>or</u> (b) the value of any shares bought back which are equal to or less than the shares

exercised (issued) under the company's stock option plan(s). (Any shares bought back which

exceed the number of shares

exercised under the stock option program need not be expensed because those shares will properly reduce the number of shares outstanding, increasing earnings per share).

IN SUMMARY

Proper accounting for stock-based compensation must recognize the direct connection between stock options exercised and "share-purchase" or stock buy-back programs. Ignoring this relationship passes over the reality of what corporations are doing with substantial amounts of their cash. They are using this cash with no significant effect on earnings to offset the dilutive effect of the increase in the number of shares outstanding resulting from the number of shares exercised under their stock option programs. It is truly a license to drain the corporate coffers into management pockets with minimal effect on earnings. Uncontrolled as it is, this infectious greed completely destroys the incentive for investors to invest because significant amounts of cash are being siphoned to management with minimal to no effect on earnings per share.

The investing public is being scammed by stock options. Enron, WorldCom, et al is peanuts when compared to the billions the corporate elite are robbing from their shareholders through stock options. This grand theft is legal and complies with accounting guidelines. In addition to the billions going from corporate coffers into the pockets of their management, corporate earnings are being grossly overstated making financial statements meaningless.

This scam, the quintessence of infectious greed, is systemically destroying the incentive to own stock. Not only do shareholders lose but management, board members, employees, and even customers lose. It's a lose-lose situation for all concerned. The accounting standards must change to stop this scam. Compensation expense must be properly recognized in order to restore credibility and investor confidence. As Mr. Robert H. Herz, Chairman of the Financial Accounting Standards Board" most aptly stated in his opening statement to the roundtable participants on May 8, 2003, "Our capital markets, and the investors who participate in those markets, are demanding and deserve sound, transparent, and unbiased financial information."

Thank you and may God bless you in your efforts to resolve this Grand Theft from the American public. Please let me know if any additional information is needed. I sincerely believe that your efforts and those of the board regarding this matter are of the greatest significance to America.

Sincerely,

R. W. Glenn, 6 Woodstock Court, Greensboro, NC 27408; (336) 288-8429

Copies to William H. Donaldson (SEC), Kimberley Crook (IASB), Sir David Tweety (IASB), Pfizer Board of Directors