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From: Debbie Nightingale [Debbie.Nightingale@Sun.COM]

Sent: Monday, June 07, 2004 7:42 PM

To: Director - FASB Cc: Len Tatore

Subject: Comments regarding File Reference No. 1102-110

Dear Sir,

I write in regard to file reference number 1102-100, to express my strong opposition to the mandatory expensing of employee stock options proposed therein.

Letter of Comment No: 3094 File Reference: 1102-100

I am not a corporate executive. I am not an accountant or even an MBA graduate. I therefore do not possess the expertise to engage in debates on accounting theory. I am however an employee of a high tech company and like 85% of my fellow employees I am a part owner in my company because of the stock options I have been given. This does qualify me to speak with more authority on the value and impacts of a stock option than someone who does not have any stock options. Furthermore because I have been employed by companies who did not use broad-based stock options, I am even more qualified to articulate the value and impacts of broad-based stock options from an employee perspective because I have worked for companies with and without broad-based stock options. I am also a shareholder of other companies. I feel this entitles me to at least express my opinion on what I feel is in the best interests of shareholders. Finally, I am a U.S. Citizen and as a result, I have a vested interest and responsibility in ensuring the United States remains the world leader in high technology development so that we retain our number one position in the global economy as well as our position as the only remaining superpower.

Issue #1

If my company were simply to calculate the fair market value of my stock options using the methods proposed by the FASB and increase my salary by that amount over the period in which my stock options would vest, I believe in accounting terms this would be considered an identical transaction as to the one the FASB is proposing. Yet, I can absolutely assure you, the "services" I would provide would not be the same. Yes, I would work hard and do my job in both scenarios. However, when my company gives me stock options, I think and behave differently. The differences in my thoughts and actions directly align to the best interests of the shareholders and in my opinion cannot be considered part of "services" provided by employees.

When I worked for companies and didn't have stock options, I never paid attention to the company's stock price. It had no impact on me, so why should I care. Now I always know what the company stock price is. Furthermore, my actions are different as a result of my desire to help increase the stock price. If there is a meeting or event that needs to occur, but we don't have budget for it, I am willing to contribute my own money to help cover expenses. I have paid for business lunches and snacks for day long meetings without being reimbursed. I have not claimed legitimate travel expenses in order to keep the overall travel bills low enough to be approved. Other employees I work with have had team members stay at in their homes to avoid the expenses of hotel bills. I never would have even considered these things if I didn't have stock options. My attitude prior to having stock options was that if the company didn't cover the expenses, then it must not be worth doing. Now my attitude is that if I believe it is important and it might drive up the stock price, I need to get creative to find a solution to cover the expenses and get the job done. Furthermore, although I have worked at

several companies who were struggling financially and under severe budgetary restrictions, the only company where I have seen employees taking this type of action is where the majority of employees have been given stock options. In my opinion, this is not a "service" that we as employees provide, it is the action of someone who "owns" part of the company.

Because I now care about the stock price, I take a much broader interest in everything that happens within my company. Prior to having stock options, I focused only on my own job responsibilities. If there was an opportunity that came up outside of my responsibilities that I thought could lead to a promotion, then I would engage and support that as well. My focus is entirely different as a result of having stock options. I am always looking at what other parts of the company are doing. If I think I can help or have a better idea, I don't hesitate to get involved. In addition to doing my own job, I am willing to do whatever it takes to help the stock price climb. If it means extra hours in an area completely outside of my responsibilities, that's just fine by me. I will offer my services without out being asked. Again, I see this as very typical behavior of other employees at my current company and saw this as very unusual behavior at companies I worked at previously that didn't have broad based stock options. In fact at these companies, other employees would have considered this type of behavior as suspicious, unusual or even unwelcome. Again, in my opinion, the willingness of employees with stock options to go far beyond the scope and responsibilities of their own job is not part of a typical "service" provided by employees, but is aligned to the best interests of the shareholders.

Finally, while I agree there is a cost, I don't believe the employee stock options meet the definition of a corporate expense under Statement of Financial Accounting Concepts No. 6. There is no "outflow or other using up of assets or incurrences of liabilities (or a combination of both) from delivering or producing goods, rendering services, or carrying out other activities that constitute the entity's ongoing major or cental operations." The issuance of an employee stock option does not reduce or encumber corporate assets and, under the Exposure Draft, in most instances does not cause the company to incur a liability. Rather the cost is to the shareholders. It is that cost - the potential dilution to existing shareholders -- that should be notified accurately and transparently to existing shareholders and potential investors. As previously outlined, it is the shareholders who receive the benefit from broad based stock options and so I believe it is the appropriate that the shareholders bear the cost through the dilution of shareholder value. This seems very logical to me particularly since there is only a cost if the stock price increases and the shareholders benefit will always exceed the cost associated with the dilution of shareholder value.

Issue #4

As a shareholder of a variety of companies including several high tech companies who grant broad based employee stock options, I am unclear how FASB has concluded that the lattice or binomial model will produce a value that is reliable enough to be recorded in the income statement. The assumptions underlying current option pricing models do not mesh with the unique characteristics of employee stock options, such as the lack of a market; vesting requirements; forfeiture possibilities; inability to transfer or hedge; and long life. While FASB has apparently concluded that the flexibility inherent in a lattice model will allow companies to adjust the model for all of these differences and restrictions, there has been no evidence or proof presented that this is, in fact, the case. Nearly every public company in the US has been using the Black-Scholes model in its footnote disclosures for the past 10 years. Hardly anyone has been using a binomial method. Despite the lack of testing, data or other information indicating that the binomial method produces accurate numbers when it comes to valuing employee stock options, FASB now strongly recommends in the Exposure Draft that most

companies use that method. Put differently, FASB is proposing that companies use an untested and unproven model that will cut billions and billions of dollars from earnings. All without any - absolutely zero -- field testing.

Didn't FASB reach the same conclusion 10 years ago about the Black-Scholes model? Didn't FASB urge companies to use that model on the assumption that it would produce accurate estimates of the value of employee stock options. In the current Exposure Draft, FASB is now discouraging companies from using the Black-Scholes model. Indeed, I've been told FASB last fall considered prohibiting the use of Black-Scholes. I fear that once the jury is in on the use of binomial models the same conclusion will be reached — it, too, will be proven simply not to work for valuing employee stock options. If the FASB standard will require companies to estimate the future value of a stock option, it is essential for stockholder clarity that there be a proven method for accurately predicting the value of a stock option after vesting.

Paragraph 26B

As a small investor, I am absolutely at a loss to understand how an option that expires as worthless is permanently considered as having been an expense to the company. If no money has been spent, no dilution to shareholder value has occurred, how can this possibly be considered an expense. I have read paragraph C20 several times. While I think I understand the accounting theory the FASB feels supports paragraph 26B, the result in my opinion is the potential for a completely inaccurate financial statement with no hope of a small investor such as myself ever knowing the degree of inaccuracy.

Overall Economic Impact

In my opinion, every US citizen has a responsibility to consider the impacts of their actions not only in regards to themselves, their families and their employers, but also to this country as a whole. Therefore, it disturbs me greatly that Chairman Herz in congressional testimony has said that it is not his job to be concerned with macro issues such as innovation, competitiveness and US economic health. Congress represents us, they aren't employees with the sole burden of managing and running the country. It is our country and I believe it is a responsibility of every citizen to consider the impact to our nation of all of our individual actions.

The United States' high tech industry is a valuable asset that we need to protect. It has been a major source of economic power. It contributes to our national security because of the economic strength it continues to create as well as the fact that our homeland security and defense departments have a decisive advantage over other nations because of the leading edge technology available to them as a result of our leadership in high tech. For these reasons, the health of this industry should be of concern to all citizens of this country.

I have to assume that high tech industry (companies, executives and average employees) have been more vocal than any other group in expressing concern and opposition to the proposal to expense stock options. There is good reason for the concerns. Mr. Kip Hagopian on page 29 of his comment letter to the Exposure Draft (posted on the FASB site as comment letter number 8) did an excellent job in summing up the difficulties high tech companies will have in estimating the value of stock options, the likely higher charges to net income and resulting devaluation of the high tech companies. In my opinion, the current Exposure Draft will force high tech companies to take one of two actions. Deal with the impacts of an inaccurate and undervalued earnings report or dramatically reduce/eliminate broad based employee stock options. I believe that most companies will be forced to do the later since they can't afford the near term impacts of the former. In fact there is already precedence to this trend with Microsoft moving away

from the standard broad based stock options in response to the current proposal to begin expensing broad based stock options.

Broad based stock options are in integral part of the high tech industry and have been for years. They have been the key to the small start-ups that have grown into industry giants. Employees of these start-ups have often left higher paying jobs for the stock options offered by these start-ups. Stock options are the number one retention tool for all companies in the industry. Regardless of the size of the company, this continues to be a volatile, demanding and unsecure industry for employees. A prime reason many of us stay is the belief that risks we take could be worth it for the potential growth in our stock options. If it were not for my stock options, I would have absolutely left my company within the last two years for something more secure and less demanding. The hours have been long. There have been no increases. Many of my fellow co-workers have been laid off. Yet, I haven't even explored other options because I don't want to even consider having to make a choice that would force me to give up my stock options, even though my stock options are significantly underwater. The owners and executives of high tech companies all know just how powerful a retention tool stock options are in retaining the talent they need to help them lead each of the companies to increased growth and value. These companies must retain the knowledge and talent of their employees in order to grow the industry. Growing this industry is not only vital to the industry, but it is vital to this nation.

I believe that as United States citizens, members of the FASB must not only consider the accounting considerations but also the ramifications of any changes to the economic strength and security of this nation. The FASB has indicated that Congress should not get involved with setting accounting standards. I can easily support this position, but only if FASB takes responsibility for the full ramifications of their actions to our national economy. If FASB will not embrace this responsibility and assess national economic impacts, then Congress must assume this responsibility and take appropriate action even if it means interfering with the setting of accounting standards.

Summary

While I absolutely support anything the FASB can do to limit corporate corruption by those executives who do not possess the personal integrity level needed to hold a position of such responsibility, I do not support the current FASB proposal for expensing broad based employee stock options. I do not believe this proposal will have any positive impact on reducing corporate corruption. Furthermore, I am opposed to FASB's current proposal for the following reasons:

- 1. I strongly believe that broad based stock options cause employees to think and act like shareholders. They do not cause employees to increase the level of "services" they provide to the company. Therefore the "cost" of stock options are more appropriately born by the shareholders as opposed to considering them to be an "expense" to the company.
- 2. There is no evidence that the valuations models proposed will result in an accurate valuation of broad based stock options. Rigorous testing must be done before a change to the standard can be made.
- 3. Even after it has been proven that an accurate valuation methodology exists, there will be instances when this methodology will fail to accurately predict the future. There must be some method of "truing-up" company earnings statements in order to provide transparency for all investors.
- 4. As citizens of the United States, the FASB must assume full responsibility for their actions and consider ramifications to our national economy and national security in addition to fulfilling their responsibilities as an accountant standards board.

I look forward to further discussion of this important issue during the roundtable in Palo Alto, CA on June 24th.

Sincerely, Deborah A. Nightingale Program Manager, Sun Microsystems 510-315-9597