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Letter of Comment No: 4161  
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**From:** Paul Schmelzer [pschmelzer@teramedica.com]  
**Sent:** Wednesday, June 16, 2004 1:08 PM  
**To:** Director - FASB  
**Cc:** jcdowling@nvca.org; Daniel J. Broderick (E-mail)  
**Subject:** LTR re File 1102-1001



Mr. Robert Herz  
Financial Accounting Standards Board

Re: File 1102-100

My name is Paul Schmelzer, Executive Vice President and General Manager of Partner Channels at TeraMEDICA, Inc. I am writing to you today in regards to the proposed "The Share-based Payment and Amendment of FASB Statements numbers 123 and 95." Though I understand FASB's intended goal of improving the transparency of a company's financial reporting, I believe the proposed methods of measurement will only lead to increased confusion and ultimately have an immediate and long-term negative effect on the financial health of all technology companies, especially young start-up companies.

As a member of the senior management team at TeraMEDICA, Inc., I am responsible for a multitude of operational and financial challenges as my team and I attempt to grow this company into a free-standing profitable operation, employing a highly skilled, fairly compensated workforce. Key to meeting these challenges is our ability to attract and retain motivated employees with a vested interest in the company's success. This motivation and ownership is made possible through the use of employee stock options.

The proposed FASB changes regarding stock option accounting will greatly diminish our ability to compensate employees through stock options due to the inherent problems of ascribing value to options that are subject to the volatile financial performance of a small start-up business and for which there is no public market. These options represent a stake in the future value of the company and not a current operating expense characterized by the rigor and precision of generally accepted accounting practice. The problems inherent in the proposed FASB change blur the distinction between balance sheet intangibles and operating results to the detriment of small companies that supply substantial energy to the job creation engine of our economic growth.

My argument against the proposed changes is three-fold:

- First, the valuation methods proposed are inaccurate and subject to potentially ambiguous variables. The Black Scholes and Binomial models for valuing stock options make a variety of disputable assumptions, including that options can be freely liquidated at any time and circumstance, and that corporate volatility can be defined in a meaningful way. This, is simply not practical in the real world
- Second, the logistical costs and efforts required to properly account for stock option plans places an unfair burden on smaller, private companies. This burden results in

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increased expenses and energies for non-core business, leaving less capital and resources for innovation and growth. If innovation slows, markets will concentrate and stagnate around established technologies.

- Finally, the proposed change will have a dramatic short-term and significant long-term negative effect on how companies are valued in private and public markets. This valuation deflation will be driven by the inadequacies in the proposed valuation methods and will make financing more difficult. As private and public financing becomes more difficult, the innovation and growth (key to technology company success) will be stifled.

In closing, I strongly urge the Financial Accounting Standards Board to reconsider altering the current stock option accounting rules. Though the ultimate goal of the changes is admirable, the proposed method falls significantly short of the intended purpose and threatens important dynamics in our nation's economy.

If I can be of further assistance, please let me know.

Sincerely,

Paul Schmelzer  
Executive Vice President  
General Manager  
Channel Partners

PS:bj