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**From:** Stern, Andy [astern@datasweep.com]  
**Sent:** Friday, May 28, 2004 7:03 PM  
**To:** Director - FASB; jcdowling@nvca.org  
**Subject:** File Reference No. 1102-100--FASB Exposure Draft

**To:** FASB Directors  
**cc:** Jennifer Connell Dowling, NVCA

**From:** Andrew Stern  
Vice President & CFO  
Datasweep, Inc.

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**Comments to the FASB Exposure Draft entitled *Share-Based Payment, and Amendment of FASB Statements No. 123 and 95.***

I have been the CFO of several successful venture-backed companies, mostly software, during the past 20 years. Currently, I am the CFO of Datasweep, Inc. a leader in software solutions to assist global manufacturers drive performance, quality and value across their manufacturing processes. We are located in San Jose, California.

As a senior executive in these successful companies, I have been honored to be part of companies that grew rapidly, created many thousands of jobs, and have developed entire categories in the global economy through entrepreneurship, innovation and drive. One of the most critical elements in the model for success of these ground breaking companies has been a broad-based stock option plan that delivered equity value to the broadest possible class of employees within the organization. The new accounting rules outlined in the Exposure Draft create strong hindrances to companies like mine that utilize employee stock options as a vital part of their business models. Eliminating or reducing the use of employee stock options would do great damage to the business model which has proven, many times over, to be extremely successful. Yet, the current FASB proposal will result in exactly such a reduction or elimination.

In addition to the immeasurable impact on the economy that would result from a cutback in broad based employee stock option plans, there is also a considerable cost imposed by the proposed new rules in the form of (i) inaccuracies in financial reporting resulting from unreliable option valuation methodologies and (ii) substantial expense to prepare the new financial reports in the form of fees payable to accounting and valuation firms. These costs are an area of particular concern to private start up companies like mine who are no position to absorb these increased costs—the only result will be the hiring of far fewer people. In addition, it will be extremely difficult, if not impossible, to value shares of companies like mine using the proposed valuation methods.

Both of the proposed valuation methodologies use complex formulations that have a tendency to create inconsistent results when applied across different companies in different industries over time. The problems are compounded when these formulas are applied to private companies that do not have freely tradable stock or readily available means to evaluate critical variables in the formulas such as stock volatility. Inaccurate, unauditible and effectively misleading financial statements result when a company uses unreliable estimates to complete any calculations. The inconsistency of these estimates, especially when applied to private companies, creates confusion rather than clarity in financial statements.

As you know, in an effort to address the concerns expressed in the preceding paragraph, the FASB has proposed the use of the “intrinsic value” method when it is not possible to estimate fair value. However, this methodology does not solve the problem. Using the intrinsic value method a company would need to re-estimate its fair value each

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reporting period, resulting in inconsistency and compounding the use of unreliable estimates.

Since we all expect a company to exercise an appropriate amount of diligence and care when generating the estimates used in the formulas described above, a reasonable company would engage accountants, valuation firms and other experts to ensure that their estimates are in line with best industry practices and in compliance with the new rules. In the current regulatory environment, a company would be tempting legal fate not to engage such independent outside assistance. Although transparency is important, the time and expense required to prepare these unreliable disclosures outweighs the marginal benefits afforded by the disclosures that are the goal of the proposed new accounting rules.

Stock options, just like stock, reflect a movement in the ownership capital of a company and should not be shown as an expense in financial statements, or in a pro forma "as-if" disclosure. Stock options are not a cost of doing business, do not affect revenue or operations, and consequently should not be factored into the profit and loss of an enterprise.

If the FASB's judgment is different than mine, and it decides to implement some form of the proposed option expense regulations, then, at a minimum, it should consider providing an exemption from the new rules to private companies and to any broad based employee option pool. Employee stock options provide extraordinary economic benefits to the middle class worker, who, according to a study by Rutgers University, is the recipient of 94% of the stock options issued.

Sincerely,

Andrew Stern  
Vice President & CFO  
Datasweep, Inc.