

## Karen Salmansohn

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**From:** Director - FASB  
**Sent:** Saturday, February 01  
**To:** Karen Salmansohn  
**Subject:** FW: File Reference N

Letter of Comment No: 242  
File Reference: 1102-001  
Date Received: 1-31-03



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-----Original Message-----

From: Tom McCullough [mailto:TMcCullough@firstregional.com]  
Sent: Friday, January 31, 2003 5:31 PM  
To: Director - FASB  
Cc: ccg@mail@nasdaq.com  
Subject: File Reference No. 1102-001

Gentlemen:

Thank you for allowing me the opportunity to comment on the proposal to require companies to record expenses relating to stock options. By way of background, I am the Chief Executive Officer of First Regional Bancorp, a bank holding company headquartered in Los Angeles, California. Our common stock is listed on The Nasdaq Stock Market, and currently has a market capitalization of approximately \$41 million.

I believe that this proposal is ill-advised in the extreme. Not only will the proposal do little to combat corporate abuses as its proponents claim, but I believe the proposal will also have harmful if unintended impacts on the success and competitiveness of American business.

Proponents of option expensing claim that stock options enrich managers at the expense of shareholders. This view betrays a fundamental misunderstanding of how options work and how they come to have value. Options only have value if the underlying stock increases in price. If that stock increases in price, giving value to the option, it also enhances the value of all the shares held by stockholders. Rather than rewarding managers at the expense of shareholders, stock options precisely align the interests of managers and shareholders. By allowing a manager to share in the value which his or her efforts help create, that manager has a powerful incentive to improve performance for the benefit of all shareholders, and the manager will only benefit if the shareholders do.

Proponents claim that the expensing of stock options will make corporate financial statements more informative. This view ignores the fact that existing financial reporting standards already require extensive disclosure of stock option activity. Interested parties already have abundant information available to enable them to analyze potential dilution and other possible impacts of a company's stock option program. Thanks to the efficiency of our capital markets, the market prices of securities already reflect these factors.

Proponents claim that option expensing is required to reflect the "true costs" of stock options. But what exactly are those costs? The issuer of stock options incurs no actual expense, nor is it harmed in any way, when stock options are issued or exercised. The fact that the proposed offset to "stock option expense" is a credit to a capital account demonstrates that there is no real expense incurred. Indeed, companies benefit from an influx of capital when options are exercised and the option holder pays the exercise price to the issuer. I suppose one could argue that the company suffers an "opportunity cost" when a security is sold for less than its fair market value, but to the best of my knowledge "what might have been" has yet to work its way into financial statements. No, the "costs" that proponents propose to include in company financial statements are nothing more than a formulaic estimate of a theoretical concept that cannot be perceived, let alone measured, in the real world.

And therein lies a significant problem. By injecting a theoretical estimate into corporate financial statements, we do not make those statements more accurate, we make them less so. If proponents feel that users of financial statements have lost confidence in the accuracy of financial reporting, substituting theory for reality will certainly do nothing to restore that confidence.

Clearly, the proposal to require the expensing of stock options is a very bad idea, and it should not be incorporated into financial reporting standards. Maintaining the existing system of extensive disclosure of stock option activity will provide ample information for a thorough analysis of securities value without eroding the accuracy of corporate financial statements.

Thank you for considering my views on this important issue.

Sincerely,

Jack A. Sweeney  
Chairman and Chief Executive Officer  
First Regional Bancorp