

**Karen Salmansohn**

---

**From:** Director - FASB  
**Sent:** Saturday, February 01  
**To:** Karen Salmansohn  
**Subject:** FW: File Reference No.

**Letter of Comment No:** 240  
**File Reference:** 1102-001  
**Date Received:** 1-31-03

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

**From:** Sommer, Regina [mailto:RSommer@netegrity.com]  
**Sent:** Friday, January 31, 2003 5:42 PM  
**To:** Director - FASB  
**Cc:** Sommer, Regina  
**Subject:** File Reference No. 1102-001

January 31, 2003

To Whom It May Concern:

As the Chief Financial Officer of Netegrity, a publicly held, leading provider of security software solutions, and veteran CPA, I strongly support corporate governance reforms, greater enforcement against corporate fraud and enhanced disclosure to shareholders. However, I strongly oppose the mandatory expensing of employee stock options. I firmly believe that expensing stock options would not produce more accurate financial statements or curb corporate abuses. In contrast I feel as though mandating the expensing of stock options is a poor decision because of the following factors: (1) the inability to properly value the options and the resulting inaccuracy of the financial statements (2) the impact on market and more importantly the fragile high technology industry, (3) the impact on non-executive employees.

First, FASB should not mandate the expensing of stock options until it determines a more accurate method for valuing stock options. Currently, there is no standardized method that measures the true "cost" of an option with reasonable precision. The most frequently used method for valuing stock options, the Black-Scholes formula, produces highly misleading results that often significantly overstate the value of employee stock options. The use of this model is particularly problematic for companies with volatile stock prices, such as Netegrity and our other high-tech peers and emerging growth companies.

Nevertheless the flaws are not with the model, but how it is applied. The Black-Scholes formula was designed for the short-term trading of liquid, market listed options. The method was not intended to value employee stock options, which have relatively long vesting periods, cannot be freely exchanged and contain restrictions on exercises. Additionally, the inputs of this model (dividend yield, volatility, risk-free rate) can be easily manipulated to significantly alter the end result. The values that result from the model are speculative and in most instances overstate the value of employee stock options. This produces highly distorted financial statements that will mislead the investor community that will ultimately have a negative impact on companies' stock prices.

Second, the overall market and investor community will be negatively impacted if companies are required to expense stock options. Currently, the global economy is struggling. High-tech companies in particular are bearing the brunt of the struggling economy and as a result have undervalued stock prices. Mandating the expensing of stock options will further increase companies' operating expenses making it more difficult for companies to sustain or in many cases achieve profitability. This will result

in stock prices being further depressed. There is no logical reason to let this happen. There is no "cost" to a company for issuing a stock option. Although it dilutes the ownership of existing investors, it does not take cash out of the company. Requiring companies to expense their stock options is requiring them to erroneously depress their earnings. The resulting distorted earnings will cause investors to see increased volatility as option expensing multiplies the movement of various key metrics such as earnings per share and price-to-earnings ratio. This inaccurate information will mislead investors causing them to make poor decisions. The result will be depressed stock prices and a reduction in the already slow economic growth rates.

Finally, I feel that expensing stock options will have a severe impact on non-executive employees. Stock options are widely granted to all employees, not just top executives. Often times what is lost in the debate over whether to expense stock options is the fact that, on the whole, broad-based stock option plans have been good for employees. They have and continue to provide powerful incentives for companies to recruit and retain talented employees, especially during crucial start-up periods, particularly in the high-tech industry. Stock option incentives increase productivity by encouraging employees to act like owners. Additionally, they are a driving force behind creativity and thought leadership. Mandating the expensing of options would likely reverse this effect. The mandatory expensing of stock options would most likely result in the elimination of stock option programs for middle management and rank and file employees, as many companies that widely distribute options will be deterred by the prospect of a significant and distorted impact to earnings. In short, it would undermine a tool that has fueled innovation and growth in the economy, most prominently in the high-tech arena.

There is no question that I will continue to support efforts by FASB and Congress to craft thoughtful and reasoned responses to issues of corporate accountability. Nevertheless, I do not feel that requiring companies to expense stock options is a sound decision. Mandatory expensing of stock options will put accounting policy on a collision course with innovation, entrepreneurship, competition and new business growth. Furthermore, requiring companies to account for stock options as expenses will not give investors the information they need; rather it would be a misguided accounting policy that does very little to preserve the important reforms that protect investors, employees and economic growth. It is important that policymakers focus not on stock option accounting, but on a package of real reforms that will directly address the issues that contribute to corporate abuse.

Regards,

Regina O. Sommer

\*\*\*\*\*

**Regina O. Sommer**  
**Chief Financial Officer**

Netegrity, Inc.  
 52 Second Avenue  
 Waltham, MA 02451  
 Email: [rsommer@netegrity.com](mailto:rsommer@netegrity.com)  
 Direct: (781) 697-2696  
 Fax: (781) 697-0025