



WACHOVIA

Letter of Comment No: 2  
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August 6, 2002

Financial Accounting Standards Board  
401 Merritt 7  
P.O. Box 5116  
Norwalk, Connecticut 06856-5116

Subject: Transition provisions of Statement of Financial Accounting Standards No. 123,  
*Accounting for Stock-Based Compensation*

Dear Board Members:

In July, Wachovia Corporation announced the adoption of the fair value method of accounting for stock options under the provisions of Statement of Financial Accounting Standards No. 123, *Accounting for Stock-Based Compensation* ("Statement 123"). We made the decision to adopt Statement 123 in view of our belief that expense recognition is the preferable method of accounting for stock options and represents a best practice in corporate governance. Further, it is consistent with the direction that the International Accounting Standards Board is taking on this same issue, and we believe that it is in the best interests of the United States and the global capital markets to harmonize accounting standards as soon as possible.

In accordance with the transition provisions in paragraph 52 of Statement 123, we will adopt the expense recognition provisions retroactive to January 1, 2002, and will only include awards granted after that date. Accordingly, since our stock option awards generally vest over three years, the expense we recognize in 2002 (approximately one-third of the fair value of the 2002 award) will not necessarily be representative of the typical run rate assuming that we continue to award stock options as has been our practice in the past. Our expected run rate would include the expense related to the current year award as well as the prior two years. We will address this issue with the appropriate disclosures in our Form 10-Q. Statement 123, paragraphs 269-270, refers to this anomaly as the "ramp-up" effect.

It is our understanding that the FASB plans to consider adding to its agenda a limited scope project on the Statement 123 transition provisions in response to the number of companies that have recently announced the adoption of the fair value method. Further, we understand that at least part of the motivation for undertaking such a project is the perceived problems associated with the "ramp up" effect.

While there were many complex issues surrounding the original deliberations on Statement 123, not the least of which was significant pressure from various constituencies who were against

expense recognition, it is clear that the FASB addressed the issue of transition and weighed the feasibility of retroactive application versus the potential for “misleading implications” of the “ramp-up” effect.

We are convinced that the fair value method of accounting should be a requirement under United States GAAP because it is very clear that stock options are a form of compensation, and there is no basis to argue that compensation arrangements are anything other than an expense to a company. With that said, however, we support the current transition provisions of Statement 123. We do not think that it is appropriate for the FASB to reconsider these provisions mainly because it may discourage other companies from adopting this preferential method of accounting. The transition provisions have been in effect since the issuance of Statement 123 in 1995, and to the best of our knowledge, have until now not been the subject of any debate. As the FASB is well aware, there are always compromises in developing a comprehensive accounting model and the FASB adequately weighed the alternatives during the deliberations on the exposure draft that lead to the issuance of Statement 123.

Even with a fast-track, limited-scope project, it is difficult to envision that an amendment to Statement 123 could be issued until late in the year meaning that calendar year-end companies may be faced with recording the adoption of the fair value method in one quarter and an amendment to Statement 123 in a subsequent quarter. That could be confusing for investors and other users of financial statements. The issues that apparently are leading the FASB to consider a project on the transition provisions of Statement 123 can be very adequately addressed with the appropriate disclosures in the notes to the financial statements and in Management’s Discussion and Analysis (MD&A).

Further, some companies may have issues with respect to debt covenants if Statement 123 is amended such that additional expense (eliminating the “ramp-up” effect) is required to be recognized in 2002. We would expect that a fourth quarter amendment to Statement 123 could leave such companies with little time to negotiate the appropriate changes to debt agreements.

**In conclusion, we strongly recommend that, rather than address the transition provisions of Statement 123, the FASB undertake a fast-track project to amend the recognition provisions of Statement 123 and require that all companies adopt the fair value method by the end of 2002. Any issues with the transition provisions can be solved with more robust MD&A disclosures.**

Should you have any questions regarding the views expressed in this letter, please feel free to call me at 704-383-2555, or David Julian, our controller, at 704-383-6101.

Sincerely,

Robert P. Kelly  
Senior Executive Vice President and  
Chief Financial Officer

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cc: David M. Julian, Senior Vice President and Controller