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

Letter of Comment No: 5096 File Reference: 1102-100

RE: Comments on FASB Major Project 1102-100

## Dear Sirs:

I am the Controller of a small development stage company that has 180 shareholders and is in the process of obtaining additional financing. The company is 5 years old and has not generated significant revenue and has not been profitable during any year of its' existence. There would not be a market for its' stock even if the stock was registered with the SEC.

The senior team for this company is being compensated below current market rates. One factor in deciding to accept the lower compensation is for the stock options and the potential gains possible from the options. There is a high degree of risk associated with these options - many start up companies fail to achieve profitability and close, the options in these companies never generate cash to the holder and the employees do not recover forgone compensation. Without these options each member of the senior management team would have pursued positions at other more established companies at a significantly higher compensation level. A startup company does not have the funds to compensate its' employees at a competitive wage and needs to be able to use stock options to attract executives.

The options have a perceived value to the members of the management team because they believe (correctly or incorrectly) that with their unique abilities and insights the company will become profitable. Outside buyers may not have the same view of management – if they did then funding of new companies would be much easier and the number of startup companies failing would be significantly lower – and would not desire to purchase these options.

A major question with the new procedure would be how to value the options? The stock of a startup company with no track record and an unproven business plan has no value. There are no comparable companies to use in valuing – each company that could be a comparable has a track record and a proven business plan which is a major difference to the startup company.

In paragraph C69 "The Board continues to believe that in concept, public and non-public entities should use the same measurement method, and this statement establishes the fair value method as preferable for purposes of justifying a change in accounting principal." Fair value is defined as "the amount at which an asset could be bought or sold in a current transaction between willing parties, that is, other than a forced or liquidation sale". Is there a market or willing buyer for a company that has no revenue track record and has never been profitable?



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Based on the above scenario there would not be a comparable market value for the options and the future value is an unknown. In paragraph C72 the board alludes to other estimates used in Financial Statements such as those required for health care costs, depreciation, and asset impairment. All of these estimates are made using external factors that have a track record. Insurance costs can be estimated based on economic information based on long-term trends. Depreciation is based on an estimate of a life of an asset and can be supported with engineering studies.

When startups are funded by Venture Capital organizations an arbitrary value is established for the securities at the time of the transaction. However, the Venture Capital organizations realize that the successful company is dependent on its' managements ability to execute the stated business plan. The Venture Capital organizations also realize that the value of their investment will decrease before any appreciation will occur. Since most employees are hired after a funding occurs and there is no market value for the stock only the arbitrary funding value, how do you value the options from the time of the initial funding to the next funding event (if any)?

Most of the innovation and economic growth in the United States is initiated by small startup companies and not by the publicly trade companies. The innovation comes at an economic risk to the founder and the management of the companies and an economic reward must be available to these people to reward them for taking the risks. The proposed method of accounting for options will stifle the ability of the small companies to obtain funding and to reward the risk takers.

I believe that for a start up company to have a value imputed to the options would materially misstate the company's Financial Statements. I also believe that the options issued to a start up company should only be valued when exercised even if the company is successful and does

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| develop to the stature that a fa | air value can be computed for its' | options. Options issued after a |
| company's fair value can be d    | letermined could be valued using   | the fair value method but the   |
| method should not be applied     | retroactively.                     |                                 |
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Lawrence M. Baird CPA

Sincerely;