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Letter of Comment No: 1530
File Reference: 1102-100

From: Michael Stevens (michstev) [michstev@cisco.com]
Sent: Thursday, April 22, 2004 1:35 PM
To: Director - FASB
Subject: Opposed to new Stock Option Expensing Rules (File Reference No. 1102-100)

Dear Chairman Herz:

I am writing as both an investor in the stock market and an employee of a high tech company. I am opposed to the currently proposed FASB rules on expensing stock options for the following reasons:

1) The new rule would double count the cost of options. Companies would have to both lower their net income number to account for the 'cost' of the options issued and increase the number of shares outstanding. So, the effect on earnings per share will be compounded.

2) The Black-Scholes model for estimating the cost of options is flawed, at best. Particularly when applied to employee stock option plans which have restrictions not anticipated in the Black-Scholes model, such as the employee loses the options if they leave the company.

Proposed Alternative:

Is not the 'cost' of a company issuing stock options to employees the interest carrying cost of the company buying the underlying stock on the street? Here is an example:

- Company X issues 1,000,000 options to employs at a strike price of $10/share with a 5 year vesting and 9 year expiration period.
- Company X could immediately buy back 1,000,000 shares on the open market at the current $10/share market price and hold them for the duration of the option life. The cost of doing so would be the opportunity loss of investing that $10M in other investment vehicles for the 5-9 year period and, therefore, would have to be deducted from income.
- As employees exercise options, the company recoups their $10/share.
- Any options/shares not exercised would have to be accounted for as a gain or loss by the company depending on the current stock price.
- Companies electing to not immediately purchase shares on the open market would still be required to deduct the interest carrying costs as if they had.
- The dilution effect, if any, would be reflected in the earnings per share number.

Thank you for your thoughtful consideration. Like you, I want to ensure accurate and fully transparent accounting in all companies.

Michael Stevens