

# The Financial Services Policy Institute

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April 6, 2004

Letter of Comment No: 89  
File Reference: 1102-100

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

## File Reference No. 1102-100, Re: Stock Option Accounting Reform Act

Dear Director of Major Projects:

By way of reference, I was asked to forward a letter to you by **Charlie Cray, formerly of Public Citizen and now with the Center for Corporate Policy.**

**Attached is my Curriculum Vitae so that you know what my credentials are in submitting an opinion to FASB on this matter.**

I represent the **Financial Services Policy Institute (FSPI)**. FSPI was established in early of 2002 with a donation from a member of the National Association of Investment Professionals ([www.naip.com](http://www.naip.com)). The Institute is a nonprofit organization dedicated to public policy in the financial services industry through independent, objective, nonpartisan research. The organization has filed for 501c3 status under the IRS tax code and does research on the policies of financial services organizations and how they interact with U.S. government agencies.

I also represent the interests of individual investors through a new organization called **Investors United (IU)**. This organization has filed for 501c6 status under the IRS tax code. IU represents the interest of individual investors on Wall Street and in Washington.

My official comment follows. We appreciate you taking the time to consider our opinion.

Sincerely,

Thomas S. O'Keefe  
President  
Financial Services Policy Institute

**Official Comment of Financial Services Policy Institute to Financial Accounting Standard Board on Corporate Stock Options, April 6, 2004.**

In our opinion, employee stock option compensation should be treated as an expense on corporate financial statements.

For too long companies have been providing a “free lunch” option to employees to buy company stock. This lack of requirement to recognize stock-option compensation as a company expense has encouraged companies like Enron to approve pay packages for their executives in the hundreds of millions of dollars - per company. This practice provides fertile ground for abuse and should be modified so that U.S. companies will have to follow the same standards as those prescribed by the International Accounting Standards Board.

Congress should NOT again give into the pressure by the high tech industry and the Employee Stock Options Coalition, as they did in the mid-1990’s. **Millions of investors are tracking what Congress does this time regarding this topic.** Should another Enron situation develop as a result of Congress caving into pressure from the high-tech lobby, the investing public will be furious.

I challenge Congressman Richard Baker to produce evidence he recently referred to in a trade publication (See Investment News, April 5, 2004). In this article, entitled “*Stock Options Stir Debate*” the Congressman claims that “There is mounting evidence of the terrible impact this rule would have on our economy at the very time we are fighting through a jobless recovery.”

It is obvious that the Congressman feels safe raising doubt on the option rule after the Enron controversy has died down. I would ask Mr. Baker to produce solid evidence that his bill – H.R. 3574, the so-called “Stock Option Accounting Reform Act” – would create more jobs in the U.S., or at the very least, re-patriate jobs back to the U.S. that have moved overseas. It again appears that Mr. Baker’s psychic abilities have been finely tuned by the high-tech community regarding the impact of expensing options. This is puzzling since H.R. 3574 itself states the following:

**SEC. 3. PROHIBITION ON EXPENSING AND ECONOMIC IMPACT STUDY.**

(a) PROHIBITION- Section 19(b) of the Securities Act of 1933 is amended by adding at the end the following:

(3) PROHIBITION ON EXPENSING STANDARDS-

(A) IN GENERAL- The Commission shall not recognize as ‘generally accepted’ any accounting principle established by a standard setting body relating to the expensing of stock options unless-

(i) it complies with the requirements of subparagraph (B); and

(i) the economic impact study required under section 3(b) of the Stock Option Accounting Reform Act of 2003 has been completed.

Two facts are blaringly obvious from the above:

1. Mr. Baker really doesn't have the evidence he referred to in the above paragraph.
2. He, the co-sponsors of the bill, and the lobby that supports them, want to delay implementation of the FASB standards indefinitely.

The lack of corporate accountability has harmed millions of investors. But the memory of many in Congress is short. Loopholes allow companies to treat stock options as if they were different from any other kind of expense have gone on too long. We've seen numerous abuses of these rules, which can be used to essentially hide payments to corporate executives, inflating profits and deceiving investors. These rules would make it much clearer to investors how much money a company is making or losing.

Options cost money - money that could be reinvested back into the companies or given to investors in dividends. In short, it takes money from investors and puts it in the pockets of high-ranking people in the company.

As you know, support for this proposal within the financial community is widespread. Federal Reserve Chairman Alan Greenspan and the Securities and Exchange Commission are in favor of it, as are the hundreds of publicly traded companies who already expense their options in this way. A recent Congressional Budget Office report supported the measure, and the International Accounting Standards Board has already approved the expensing of stock options in a similar way.

Accounting is about giving a good picture of where a company is financially, and how much money they have gained or lost. By treating options as if they do not affect the company financially, accounting statements are less valuable. As the group that protects the integrity of accounting standards, you ought to do everything possible to make accounting statements important to investors.

Options packages have led to corruption in many cases throughout the corporate world. Without including their costs in accounting statements, they are essentially an under the table payment to corporate executives. Without the implementation of these rules, boards of directors will continue to give exorbitant options packages to their wealthy executive peers, and shareholders will be the ones left paying the bills.

Finally, let's I'd also like to note how this will hurt tax revenue in a time of a growing Federal budget deficit. Even though companies don't currently treat options as an expense for accounting purposes they nevertheless DO receive tax deductions "whose size is based on the prices at which employees exercise their options. Presently, companies are permitted to classify all such tax benefits as a boost to cash flow from operating activities." (See *Wall Street Journal*, April 1, 2004, article entitled "Stock Options to Be Expensed Under Proposal")

Please pass these proposed rules, and help restore the trust of investors in the financial markets. Thank you for accepting my comments.

Sincerely,

Thomas S. O'Keefe  
President, Financial Services Policy Institute

CC: Congressman Richard Baker, (R- LA)  
Mr. William Donaldson, Chairman of the SEC  
Senator Richard Shelby, (R- AL, Chair of the Senate Banking Committee)  
Senator Carl Levin, (D- MI, Government Affairs Committee)