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Mr. Lawrence W. Smith
Director of Technical Application and Implementation Activities
Financial Accounting Standards Board
P.O. Box 5116
Norwalk. CT 06856-5116

Dear Mr. Smith:

I would like to submit the following commentary for consideration of the proposal to expense stock options in financial income statements.

Stock Option Expensing—Chasing the fox with wolves

As a public company Audit Committee Chairman. it is with great dismay and considerable chagrin that I am witnessing the imminence of the FASB mandating the expensing of stock options for GAAP. It is particularly distressing because I believe the public debate of this issue has appeared to have overlooked some instrumental financial reporting issues and concentrated instead on emotional lynching reactions to political drama rather than conceptual framework. I am professionally concerned that. after decades of respect. GAAP will now suffer a second creditability blow in less than five years in order to punish an invisible foe. It will be akin to giving jail time to homeowners in order to force them to fortify their houses to reduce burglary crimes. Cooler heads and more integral cause and effect need to prevail.

I am greatly concerned about the reliability and significance of financial reporting for US financial income statements. First of all. I hope to assure you that I am not skewed to a particular advocacy on this subject. In addition to having been the Chairman of Audit committees for a number of public and private companies. I have been a CFO and controller at numerous public firms. COO. capital markets executive and an adjunct teacher of Business Analysis & Valuation for a 2nd year MBA financial reporting course at a large university. Also, I have been a member of two national industry accounting and finance committees and had the privilege of successfully presenting to the staff at the SEC for accounting treatments based both on technical substance and the meaningfulness of financial reporting.

Truly, the causal lessons of the past several years of securities deceptions have been lost upon the politicians. academics and less courageous officers. auditors and directors of the business world. I am afraid that the very burdensome errors of ethereal financial reporting this past decade that permitted the distortion of economic performance are. in fact. in the

process of being expanded by virtuous. theoretical naiveté. The issue is not just the double counting of the cost of stock options. but the distortion of the meaningfulness of income statements for investors. The crusade by some accounting academics to produce one net income number that all investors can rely upon should be abandoned. Otherwise. they will make the night so dark with opaque financial statements that self-serving white collar criminals can again reign at shareholders' expenses as was prevalent in the 2000 debacle. Once again. pro forma accounting will become fertile ground for creativity and confusion since all of us will adjust fully diluted EPS for stock option expenses and other nefarious theoretical accounting adaptations for cognitive intramurals.

I would proffer my opinion that much of the financial criminality of 1995-2002 that exploited hungry investors was facilitated by confusion injected into the financial income statements by some accounting overseers, reduced funding of the SEC and dwindling efficacy by a number of public auditors in performing their jobs. The resulting confusion allowed the emergence of pro forma accounting and a complex web of accounting entities used to evade and obscure with mathematical alchemy. Accounting is one of the few deterministic sciences where current economic events are to be translated into financial results. Estimable values for results. losses. expenses and assets and liabilities are supposed to deal with today's facts. not tomorrow's theoretical capital asset value theories for capital budgeting exercises. Leave the academic excitement of novel discoveries to the scientific communities and ensure that financial reporting is credible. useable and representative of today's economic reality. Here are some specific arguments that I have failed to see in the emotionally charged debate between businessmen and accounting professionals. as to why stock options should not be expensed:

1) DOUBLE COUNTING--Expensing of stock options "double dip" the shareholder through duplicative "costs" in the income statement. Basic accounting already works because the cost of an option incentive translates into dilution as the options vest and if stock prices rise. This is economic reality. Expensing stock options artificially reduces net income (and EPS) and then the inclusion of options in fully diluted shares increases the denominator in the EPS calculation. thereby redundantly impacting EPS and shareholders.

2) ASSYMTRICAL ACCOUNTING--Expensing of stock options are improperly asymmetrical in that they force one punishment, but allow no recovery or offsetting entry. What if the stock price never rises above its exercise price? If prices fall, or employees quit before vesting, how can you reverse or recover the expenses other than relying on the law of large average numbers? What is the offsetting income entry for the employee? If the employee only recognizes income at actual exercise, why should the company recognize an expense at the time of grant on speculation? Taxes have it correct; income taxes for the employee and deductions under particular circumstances at the time of exercise for companies. Perhaps we should start to estimate the value of executive and employee bonus programs and throw some expenses into the income statement at the time Boards of Directors approve them? Are we so mad at executives that sneaked

largess past their directors and shareholders that we want to punish all shareholders for an economic event yet to occur? Are employee stock options any different than non-employee stock options? What about warrants?

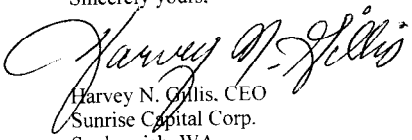
3) FINANCIAL REPORTING MEANINGFULNESS--What about the meaningfulness of the financial statements in reflecting economic events? Since when should binomial-based or Black-Scholes pricing models of discounted cash flow values of future events be used in adjusting today's transactions? In fact, stock options are capital account transactions, not income statement entries. What about the value expected to accrue to revenues and margins through the motivation of talented or critical employees? Maybe we should use multiple regressions to estimate the impacts of stock option grants and add it to revenues and gross margins! By suddenly imposing large, future, theoretical estimates of values for today's stock options granted at market prices, we are distorting the actual operating results of the reporting entity. So much so, that investors and analysts like me will adjust or back out all of the obfuscatory stock option expenses artificially imposed on the net income. Stock options will never be a cash cost to the company. Everything else on the balance sheet or income statement has been, or, will be a cash item for the company at some point. Right now, as an investor, I prefer to look at the dilution, exercise prices, vesting and distribution of stock options. In fact, I will not invest in a company that has not aligned employees' interests with those of shareholders through the granting of stock options. Virtually all investors will be unable to interpret results with this cannonball rolling around the deck of the profit and loss statement! If you were the aging owner of a small store and wanted to hire a new young competitor by giving him/her stock options equal to a large percentage of your firm, would you do it through shareholder dilution in fully diluted shares or reporting a huge, imaginary loss to your bank, vendors, landlord and the IRS? If the decision is wise, the old firm will thrive with revenues and profits growing by more than the new shares issued for the exercises of the stock options of the younger executive.

4) SUBSTANCE & PUBLIC POLICY--You are transposing a motivating capital incentive into an entitlement. Companies that hope to grow, that replace stock options with restricted stock, lose their stimulus for performance to an inducement to just occupy space and time (which increases gravity not altitude). This will stifle risk-taking, innovation and initiative in the entrepreneurial communities of American industry. It is dysfunctional not to examine the reality of the implications of your cruel and unusual punishment to allay your guilt of what a few narcissistic executives got away with during a stock market bubble. Stock options work exactly for what they were designed for: supplementing cash compensation to accept high risk, work long hours and attract talents to challenges for future value creation. Cash and entitlements are rewards for past service and performing a well established function.

There has just become too much politically correct populism in this world which leads to ever more confusion and technicalities behind which criminals can hide. Will some of the people involved with this decision investigate beyond the revengeful emotions that are

politically at play and demonstrate the courage to put substance over form in how to continue to treat stock options? Expensing stock options will be the twenty first century's version of blood letting. It will hurt--and it will accomplish nothing. Thank you.

Sincerely yours,



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Cc: U.S. Securities and Exchange Commission

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