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U.S. House of Representatives
 Committee on Energy and Commerce
 Room 2125, Rayburn House Office Building
 Washington, DC 20515-6115

March 28, 1994

ALAN J. ROTH, STAFF DIRECTOR AND CHIEF COUNSEL
 DENNIS B. FITZGIBBONS, DEPUTY STAFF DIRECTOR

Mr. Robert W. Holleyman II
 President
 Business Software Alliance
 2001 L Street, N.W.
 Suite 400
 Washington, D.C. 20036

Dear Mr. Holleyman:

I appreciate receiving your letter of March 14, 1994 with respect to the concerns of the Business Software Alliance about the Financial Accounting Standard Board's (the Board or FASB) proposed standards for stock option accounting. You ask my assistance in contacting the FASB and the SEC to pass along your concerns.

The Board issued its Exposure Draft in July 1993 with a request for public comments through December 31, 1993. During the comment period, the Board, in conjunction with KPMG Peat Marwick, conducted a field test of its proposal. Several companies volunteered to participate. This month FASB held public hearings on the issues, including the ones you raise. FASB follows extensive due process procedures designed to ensure that all interested or affected parties have an opportunity to make their views known and that unintended consequences are negated.

While I appreciate the sincerity of your views, I am not inclined to oppose or support the FASB draft, in advance of reviewing the specifics of the FASB proposal, the substance of the comments received, the experience of the field testing, especially as to the applicable valuation models, and the results of the public hearings as well as any amendments FASB decides to make as a result thereof.

The record shows that FASB added this project to its agenda in 1984 because the current rules for accounting for stock-based compensation, including stock options, are biased. Depending on the type of option issued, the accounting is substantially

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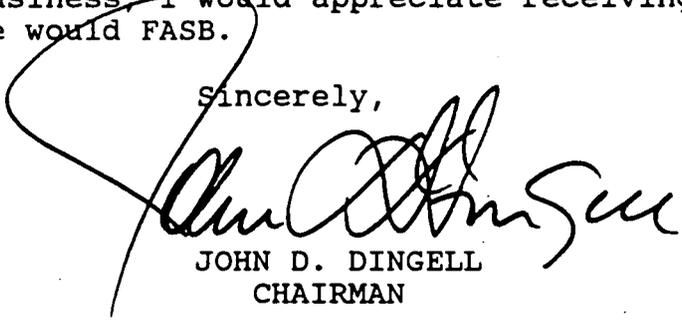
different. If a certain number of stock options are issued with an exercise price equal to market price (the fixed plan most commonly issued today), no expense is recognized. However, similar options could be issued with a performance condition: for example, a target level of sales must be achieved, before they are earned. This "performance option" would result in expense if the stock price rises. (See attached examples.) There is no rational reason for this disparity. All stock options, with or without performance conditions, are a form of compensation and that compensation should be included in an entity's reporting of its costs. The FASB proposal would apply the same basic accounting provisions to all types of options. The current financial reporting result is simply not credible and has discouraged the use of performance-based options, which many experts contend are in the best interest of companies and their shareholders.

This Committee has jurisdiction over accounting matters and has always supported good accounting and, instrumental to that, FASB's independence. We conduct vigorous oversight of these matters and will monitor this proposal, focusing on the results of the comment period and the field test, as well as the hearing record, to see that any final change in accounting standards for stock option accounting does improve financial reporting and that legitimate concerns are addressed.

In that regard, I am troubled by the suggestion in your letter that the estimates of stock option values to be charged against earnings would be "highly questionable." This raises a number of serious questions about what companies are doing now. Moreover, studies tend to show that business claims with respect to the dire consequences of FASB accounting rules prove to be overstated. See e.g., "Effect of New FASB Rule on Benefits For Retirees Is Less Than Expected," Wall Street Journal, Thursday, December 23, 1993.

Thank you for sharing your views with me. I will give them full consideration as we evaluate FASB's proposal and arrive at a position on it. If you have any constructive suggestions for amending the FASB proposal in order to address the special problems of small business, I would appreciate receiving that advice, as I believe would FASB.

Sincerely,



JOHN D. DINGELL
CHAIRMAN