

June 14, 2004

Re: Consumer groups oppose HR 3574,
"Stock Option Accounting Reform Act"

Dear House Financial Services Committee Member:

We are writing on behalf of Consumers Union, Consumer Federation of America, U.S. Public Interest Research Group, and Consumer Action to urge you to oppose H.R. 3574 at tomorrow's markup. This bill would harm investors both by depriving them of valuable information about the true financial status of the companies in which they invest and by undermining the independence of the accounting standard-setting process.

The bill is being painted as a "compromise" by its supporters, because it would require companies to expense stock options paid to the five most highly compensated executive officers. At companies with more broadly based options plans, however, such an approach would leave much of the cost of the options out of the financial statements. Furthermore, numerous independent accounting experts agree that the approach the legislation would use to value the options would grossly understate their value. If this misguided legislation is adopted, investors will continue to be deprived of comprehensive and transparent financial information. Nor are additional disclosures about employee stock options a sufficient remedy to the distortions created by the current accounting in which certain employee stock options are not expensed in the income statement.

The delay of FASB's rule proposal is also not justified. There has been no rush to judgment on this issue. Instead, FASB's procedures have been a model of openness and due process. The board has shown itself to be highly responsive to the comments and suggestions of critics of the proposal. In the end, however, the accounting experts at FASB have reached the same conclusion reached by the Big Four accounting firms, the Association for Investment Management Research, Warren Buffet, Paul Volcker, Arthur Levitt, Alan Greenspan, and hundreds of companies that are already expensing stock options voluntarily – that stock options are an expense that should have to be reflected in the financial statements of the public companies that issue them.

Perhaps an even more important reason not to support the bill is the damage it would do to the independence of the standard-setting process. In the wake of the Enron collapse, many members of Congress – including some who have signed on as co-sponsors of this bill – were asking why the Financial Accounting Standards Board had been so slow to pursue standards on special purpose entities that could have made

it far more difficult for Enron to hide its deteriorating financial condition. But FASB had learned its lesson when stock option expensing came up a decade ago – the only rewards for tackling a tough issue sure to engender determined opposition from a powerful and well-heeled constituency were threats to the board’s continued existence as the standard-setting body and the possibility that it would once again be overridden by Congress.

Recognizing the need to protect FASB’s independence, the Sarbanes-Oxley Act gave the board a secure funding source and formal recognition as the accounting standard-setting body in return for several steps by the board to enhance the independence of its governance practices. Not two years have passed since Congress gave near unanimous approval to that legislation. Those reforms will have proven to be all but meaningless, however, if less than two years after they were enacted Congress reneges on its promise and once again subjects the “independent” standard-setting process to political interference.

If narrow interest groups are able to hold FASB hostage by taking their concerns to Congress any time the board issues a new proposal or ruling they don’t like, then the very existence of FASB as an independent standard-setting body is seriously threatened.

For all of these reasons, we urge you not to support this bill or any other efforts to delay or hinder FASB’s proposal for expensing stock options.

Sincerely,

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