



BOARD OF GOVERNORS  
OF THE  
**FEDERAL RESERVE SYSTEM**  
WASHINGTON, D. C. 20551

ALAN GREENSPAN  
CHAIRMAN

October 1, 2004

The Honorable Carl Levin  
United States Senate  
Washington, D.C. 20510

Dear Senator:

Thank you for your letter of September 28 concerning the importance of sound accounting principles and the need to safeguard the independence of the accounting standards-setting process.

Accurate accounting plays a critical role in maintaining the vibrancy of our financial markets. The process by which we set accounting standards dictates the quality of the end result. In passing the Sarbanes-Oxley Act of 2002, Congress recognized this connection by effectively granting statutory recognition to the Financial Accounting Standards Board (FASB) and by ensuring that it has an independent, stable source of funding that is insulated from outside pressures. I have always felt that the openness of the FASB's process allows all affected parties sufficient opportunity to contribute to the debate. Congress should be mindful that pending Congressional legislation to effectively block FASB from requiring the expensing of employee stock options could impair the ongoing accounting standards-setting process by subjecting it to unnecessary pressures. Stock options are a valuable component of employee compensation. There is nothing in the FASB rule that inhibits their issuance.

The purpose of accounting is to determine whether particular corporate strategies add more value than they consume, and whether companies are profitable or not. Labor costs, irrespective of the form in which they are paid, are a critical determinant of a company's profits from its current activities. Not expensing stock options may make individual firms look more profitable than they are. However, the point is not whether firms will look more or less profitable, but whether the figures are correct. An accurate accounting of profits is essential if our nation's resources are to be directed to their most efficient uses, and I am deeply concerned by the possibility of Congressional interference in FASB's efforts to achieve this result.

Sincerely,  
A handwritten signature of Alan Greenspan in black ink, written over the word "Sincerely,".