CL 14

November 11, 2002

Sir David Tweetie
Chairman
IASB
30 Cannon Street
London EC4M 6XH
United Kingdom

Dear David:

In light of current public opinion that favors employee stock option (ESO) expensing and its potential influence on accounting rules and legislation, the Fabless Semiconductor Association (FSA) is working to inform the accounting regulators and legislators about the negative impact of ESO expensing on the technology sector in general and the fabless semiconductor segment in particular.

The FSA strongly opposes accounting changes and legislation that would treat broad-based employee stock options (ESOs) as an expense. The Association believes no accurate methodology for valuing ESOs currently exists and that expensing options would distort profitability and mislead investors.

If expensing is enacted through accounting changes or legislation, this would result in significantly less ESOs granted to non-executive employees, thus eliminating the most potent form of employee motivation used to encourage employees to take the necessary risk required for technology innovation, the lifeblood of a healthy economy.

In addition, the FSA believes that expensing ESOs would put U.S. semiconductor companies at a huge competitive disadvantage with the burgeoning group of semiconductor companies in Mainland China and Taiwan.

Our position on ESO expensing is not just about our member companies' objections to expensing, but also about the fate of the over 66,000 U.S. fabless employees that may potentially be affected by corresponding accounting changes and legislation. Each one has a vested interest in their company and deserves the right to share in the benefits of the innovation they helped to create.

Currently, the FSA is working with several other U.S. electronics organizations such as the AEA, SIA, SEMI and TechNet to lend our support to their efforts against this issue.

The FSA has conducted a survey of its constituents regarding their use of ESOs and has researched a number of other sources that could provide information critical to making an informed decision. Please take a few moments to review the enclosed packet.

If you would like further information on how expensing stock options would negatively impact technology companies, the FSA will happily facilitate discussions with semiconductor and other technology leaders, provide further research materials and answer any questions that will help you support the continuation non-expensed stock option grants to U.S. employees, especially in the technology sector. The FSA and its membership appreciate your support regarding this important issue.

Sincerely,

Jodi Shelton
FSA Co-Founder & Executive Director

FSA Summary Position

The FSA strongly opposes legislation and accounting changes that would treat broad-based employee stock options (ESOs) as an expense. The FSA believes that there is no accurate methodology for valuing ESOs and that expensing options would distort profitability and mislead investors.

If expensing is enacted through legislation or by accounting changes it would negatively affect the generous distribution policy of fabless companies and result in fewer ESOs granted to non-executive employees, thus eliminating the most potent form of employee motivation used to encourage employees to take the necessary risk required for innovation.

Additionally, the Association also believes that expensing ESOs would put U.S. fabless companies at a competitive disadvantage with the burgeoning group of semiconductor companies in Mainland China and Taiwan.

Overview of Major Position Points:

- The technology industry, specifically the fabless semiconductor industry, has been disproportionately responsible for job and wealth creation for the U.S. economy over the last decade. The creation of small companies that develop breakthrough products is a critical factor in moving the U.S. economy in a stable and healthy direction.

- The broad distribution of stock options establishes the risk/reward ratio necessary to attract key talent. This tool is vital to the entrepreneurial spirit of small- to medium-sized companies. Younger, growing companies use options to offset risks for employees when they join these nascent companies. However, profitability is also essential to pre-IPO and public companies. The broad distribution of ESOs to non-executive employees would be curtailed if it were to affect profit. And if the generous use of options to motivate talent is reduced, this would stifle innovation and U.S. economic growth.

- It is impossible to place an accurate value on an option in the year that it is granted because it may be exercised for some unknown price at an indeterminate time, or may not be exercised at all. The options granted to employees are not tradable; frequently have contractual lives of up to 10 years; typically vest over four years; and an employee must continue employment to maintain rights to those options. Expensing stock options could misrepresent their economic cost in financial statements.

- Emerging economies recognize the value of equity incentives and will continue to use them competitively to the United States' disadvantage. If the United States adopts punitive accounting rules for expensing options, the U.S. fabless semiconductor industry will be less competitive with the Taiwanese and Chinese industry, where stock grants are a regular part of the compensation package to virtually all employees. Mainland China and Taiwan are becoming increasingly competitive in the semiconductor arena with the number of fabless companies in these areas proliferating. There are reportedly more than 250 companies in Mainland China and Taiwan. Asian emerging economies have very progressive stock plans for high-tech employees. If the practice of rewarding employees with stock continues in these areas, while retreating in the United States, it could place the U.S. semiconductor industry at a serious competitive disadvantage.

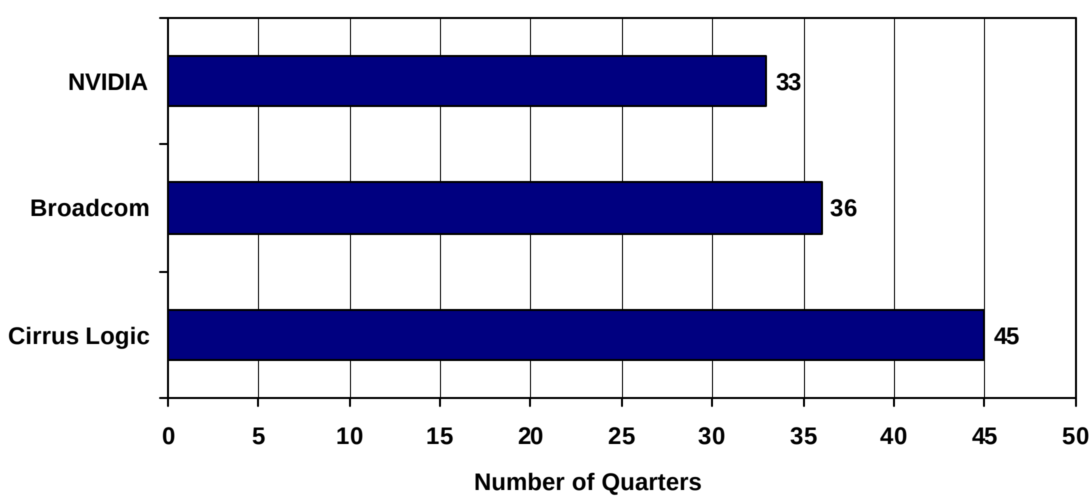
FSA Position Paper
Stock Option Expensing:
A Threat to the Fabless Industry

FSA Board of Directors
Jodi Shelton, FSA Executive Director

October 2002

The Fabless Semiconductor Association (FSA) represents emerging businesses as well as small- and medium-sized public and private companies. The primary group represented by the FSA is the fabless semiconductor segment. "Fabless," simply stated, defines a semiconductor company that does not own or operate its own manufacturing facility, also known as a "fab." The fabless semiconductor outsourcing business model was established in the 1980s and proliferated in the 1990s. Currently more than 500 fabless semiconductor companies operate in North America. Furthermore, even larger, established semiconductor companies have adopted this business model because of the onerous costs of building a fab and the need to focus on designing more innovative semiconductor solutions.

The fabless segment is comprised of start-up companies that are in the idea formation or product definition mode, pre-IPO companies and larger, established public companies. Some of the most successful fabless companies such as Xilinx, Broadcom, Nvidia, Qualcomm CDMA Technologies, ATI Technologies and Altera have annual revenues near or in excess of $1 billion. Because of the relatively small size of fabless companies, they are heavily dependent upon employee stock options (ESOs) to attract and retain talent, and to date it has worked! The fabless industry is a key example of value creation for the U.S. economy over the last decade. Fabless companies have pioneered several of the most lucrative end markets for semiconductors, including the FPGA market, networking processors, graphics and communications. Fabless companies are responsible for many of the industry's most innovative products. They have also been the fastest-growing group within the semiconductor segment. Fabless growth has outpaced the growth of the semiconductor industry in both up and down markets. Also, three fabless companies have held the honor of the fastest-growth semiconductor companies to achieve $1 billion in annual sales – Cirrus Logic, Broadcom and Nvidia.
The FSA believes that fabless companies will be the group most negatively affected by mandatory expensing of ESOs because employees of fabless companies are traditionally



paid less in salary and expected to work more hours, with the motivating factor being the distribution of stock options. The idea is that hard work, combined with innovative products and a growth market with the right vision may result in personal wealth for these employees. If ESO expensing were mandatory, there would be less opportunity for companies to offer options, meaning hard-working employees would reap less reward for their dedication and, therefore, be less motivated to innovate. U.S. innovation could be stifled without the continuing development of breakthrough products that this segment continues to drive.

Most fabless companies are private, with the ambition of becoming public. Any action that might affect a company's profitability jeopardizes the potential for their initial public offerings (IPOs). Private fabless companies face a competitive environment, where they are fighting to retain experienced design staff. Therefore, to build their companies, entrepreneurs must be allowed to offer stock options to prospective employees as an enticement for individuals to invest themselves in a company. And the entrepreneurs who create companies should be rewarded for the risk of leaving established industry positions to create opportunities for others. The typical salary of a private fabless CEO ranges between $150,000 and $200,000. Fabless CEOs are taking less compensation to preserve cash in hopes that they will create viable, successful companies. In the end, their ultimate reward, and that of their employees, will be based on the success of the company — the formula every investor wants!

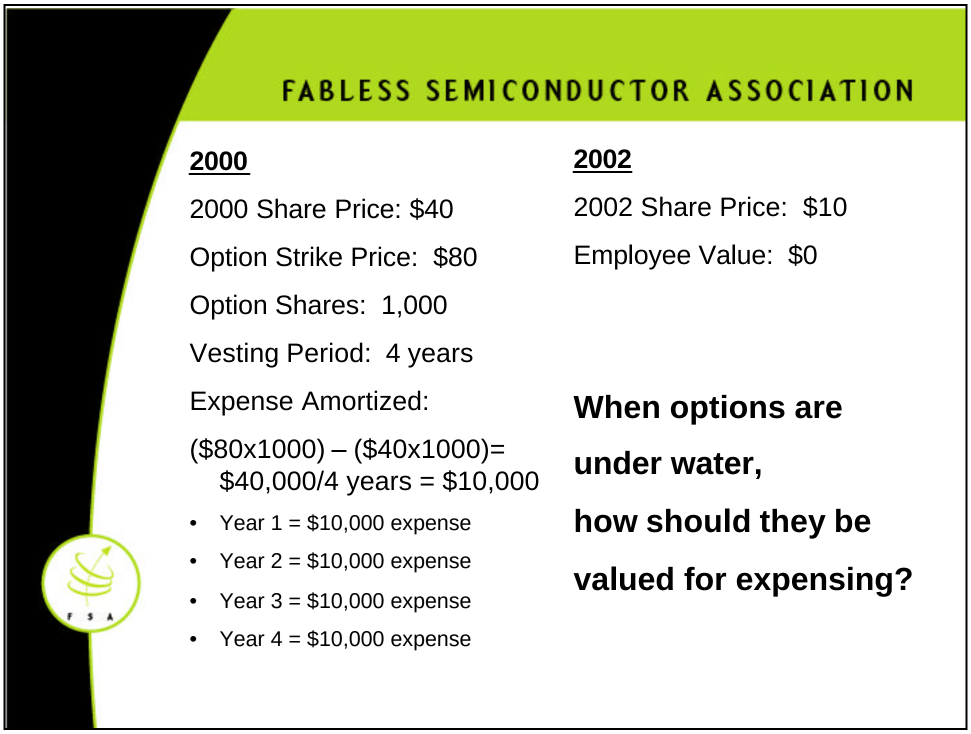
It is apparent that ESO expensing would be a direct and painful assault on fabless employees, that, until now, have shared in the ownership of companies created by their hard work. Ironically enough, most pundits agree that although there would be a major retreat in the distribution practice of ESOs to non-executives if expensing were to occur, executives would still be granted options, or would be otherwise compensated.

Emerging economies understand the value of equity incentives and have adopted this tool to build technological prowess. Specifically, Taiwan and Mainland China have been aggressive in their distribution of stock options to employees as compensation.

The FSA bases its strong opposition to legislation and accounting changes that would treat broad-based ESOs as an expense on the fact that there is no accurate methodology for valuing ESOs, and expensing them would distort profitability and mislead investors.

It is impossible to place an accurate value on an option in the year it is granted, since it may be exercised for some unknown price at an indeterminate date, or may not be exercised at all. Stock options give one the right, but not the obligation to buy stock at some point in the future for a set price. There is no reliable way to predict when, or if, an employee will exercise the option and what value it will have at that time. The options typically vest over four years, and the employee must continue employment with the company in order to vest. We all know now, more than ever, how volatile the stock market can be. This volatility has placed many fabless employees in a situation where options that were granted some time during the last five years are worth less today than when the option was originally granted.

For example, suppose an engineer was granted an option to buy 1,000 shares of a company's stock for $80 per share in 2000 (as of that date in 2000, the share price was $40) on a four-year vesting schedule. In 2002, he is two years vested; however, the company's shares are at $10 per share. How should the expensing of these ESOs be handled? In one scenario, the expensing charge would be amortized over the vesting period, and the company would be charged $10,000 per year against earnings over the vesting period. The company would record that $10,000 per year as compensation. The company's profit would decrease by this amount, but no cash would change hands. This employee cannot get any value from these options. So what happens when reality differs from this formula? Are they restated, and if so, how often and in what way?



Including an unreliable estimate of the fair value of options in a company's income statement would distort earnings. The potential overstatement of the options' economic cost in the financial statement would definitely curtail their use. It is unwise to put a presumably faulty estimate of a future cost into a current income statement or to reverse it when the fault is realized.

Despite what seems like a progressive grass roots program, public opinion appears to favor ESO expensing and, thus, may influence congressional action and/or accounting rule changes. But this opinion is misdirected. Investors are dissatisfied with overall corporate governance abuses by such companies as Enron, Adelphia and Worldcom. The issue of ESO expensing has been improperly confused with overt abuses in executive compensation.

The FSA urges its member companies and their employees to be proactive and vocal in opposing ESO expensing. The FSA will be working hard with other organizations to influence FASB. But we must also work to change public opinion by identifying the real issues and getting the truth out. Please help — write letters, talk to friends and vote.

FSA Contact:
Vivian Pangburn
Director of Marketing & Membership
Fabless Semiconductor Association
(972) 866-7579, ext. 140
vpangburn@fsa.org

Media Contact:
Helen Garrett
Account Executive
Shelton PR
(972) 239-5119, ext. 136
hgarrett@sheltongroup.com

FSA SURVEY SHOWS FABLESS COMPANY EMPLOYEE STOCK OPTION PLANS AMONG THE MOST GENEROUS

97 Percent of all Fabless Employees Receive Stock Options
Expensing Stock Options Will Negatively Affect U.S. Competitiveness

SAN JOSE, Calif. (October 28, 2002) – The Fabless Semiconductor Association (FSA), a premier semiconductor trade association, recently completed a Survey of its constituents to gauge their practice for distributing employee stock options (ESOs). The Survey results show that the fabless semiconductor sector is among the most aggressive in its distribution of ESOs, distributing options to 97 percent of all employees. Public companies responding to the Survey allocate nearly 70 percent of their options to non-executive employees.

“The perception that stock options only enrich the lives of executives is misleading. Of course, executives are going to be compensated with options, but at fabless companies, the employees are the force behind innovation and are rewarded accordingly,” stated Wim Roelandts, FSA chairman of the board and president and CEO of Xilinx. “At Xilinx all of our 2,600 employees are shareholders and we direct 82 percent of ESOs to non-executive employees,” Roelandts added. Xilinx is one of the fastest-growing fabless companies. Over the past 10 years, revenues have grown nearly 650 percent.

As a result of the Survey findings, the FSA announced its strong opposition to legislation and accounting changes that would treat broad-based ESOs as an expense. The FSA has found that there is no accurate methodology for valuing ESOs and expensing them using any existing valuation formula would distort profitability, making transparency more difficult for investors.

The FSA believes that if expensing were enacted, it would negatively affect the distribution policy of fabless companies, resulting in fewer stock options granted to employees and eliminating the most potent form of employee motivation, aimed at encouraging employees to take the necessary risk required for innovation. The Association also predicts that expensing stock would put U.S. fabless companies, in fact the U.S. semiconductor industry at large, at a disadvantage with Mainland China and Taiwan because of their liberal use of stock options to encourage and retain employees.

FSA Survey Shows Fabless Employee Stock Option Plans Among Most Generous

“Our position on ESO expensing is not just about our member companies’ objections to expensing, but about the fate of the 66,000 U.S. fabless employees. Each one has a vested interest in their company and deserves the right to share in the benefits of the innovation they helped to create,” stated Jodi Shelton, executive director, Fabless Semiconductor Association.

“This is a critical issue for the success of the fabless business model, which is based on a talent-driven rather than capital-driven model. For the fabless semiconductor company, human innovation has been the catalyst for consistent growth,” stated Dwight Decker, FSA director and president and CEO, Conexant. “The fabless industry is a key example of value creation for the U.S. economy over the last decade. Fabless growth has consistently outpaced the overall industry in both up and down markets. There are several reasons for this, not the least of which is the liberal distribution of stock options. However, if corporate profitability is threatened then there will be a reduction of these practices.”

For more information about the FSA Survey on stock option expensing, please visit the FSA Web site at www.fsa.org/survey/stockoptions/results.

About the Survey:

The FSA Survey was conducted from August 20 to September 20, 2002, of private and public fabless companies to determine how broad-based fabless Employee Stock Option (ESO) plans are and how important the ESOs are to the fabless semiconductor industry. The findings are reported in the table below.

FSA Survey of Fabless Semiconductor Companies
The Impact of Expensing Employee Stock Options

	% Stock Options Granted to Employees	Top 5 Executives	All Executives	Non-Executive Employees	Opinion: expensing impact on retention of employees	Opinion: expensing impact on innovation
Public Fabless Companies	97%	19%	32%	68%	Yes=82%	Yes=74%
Private Fabless Companies	98%	29%	45%	55%	Yes=73%	Yes=65%

About the Fabless Semiconductor Association:

In 1994, industry leaders incorporated the FSA (www.fsa.org) to achieve a more optimal balance between wafer demand and capacity. Its nearly 400 corporate members represent fabless companies, integrated device manufacturers, foundry providers, packaging/assembly houses, electronic design automation companies, investment bankers, intellectual property providers and other companies.

The organization encourages the relationship between fabless companies and suppliers; facilitates business partnerships; creates awareness of the fabless/outsourcing business model; disseminates relevant data; and fosters standards and policies.

The FSA's vision is that by 2010 half of all integrated circuit revenue will come from outsourced operations.

FSA Stock Option Survey - 2002

1) Over the past three years, what percentage of your employees were granted stock options?

2) Of this percentage, what percent is allocated to each of the levels listed below:
   a. Top five executives ________________
   b. Founders ________________
   c. Executives (Vice President and above) ________________
   d. Rank and file employees (Below VP level) ________________

3) What is the latest round of funding that your company has finalized?

4) Do you believe stock option expensing would adversely impact your ability to attract and retain employees?

5) 5) Do you believe stock option expensing would adversely impact innovation?

6) 6) Please provide the salary range for your:
   a. President ________________
   b. CEO ________________

7) What are you currently doing to prepare your company should stock option expensing become mandatory?

8) What do you feel the FSA should be doing on behalf of members on this issue?

Question and Answers
Helping You Understand What Stock Option Expensing Could Mean to the Average Fabless Employee

Q. Shouldn't fabless companies proactively move toward ESO expensing the way companies such as Coca Cola, General Electric, General Motors, Procter & Gamble, Amazon.com and Computer Associates have after announcing their intent to expense ESOs?

A. There are several major differences between large non-technology companies that have announced their intent and the companies represented by the FSA, AEA, SEMI, SIA and TechNet.

First, these companies do not have broad-based ESO programs, and their success is primarily tied to a brand or product and does not depend on the retention of rare talent. Most of the companies that have announced their intent to expense stock options only allocate options to executives. So it really is an issue for these companies of executive compensation. For example, Centex recently announced that it would expense options because it "provides a more accurate reflection of our compensation cost and is a continuation of full disclosure in our financial statements." But for Centex this is an easy adjustment to make such a statement because its option distribution is not broad-based. Of its 15,000 employees, only 125 have options, thus options are not an integral part of Centex's corporate culture, as they are in the fabless technology sector.

Second, expensing these options would have a negligible effect on these companies' profitability. The move by Coca Cola to expense ESOs would have reduced its 2001 earnings by 5 percent. Yet if Xilinx or Altera had expensed options in 2001, they would have had to report significantly lower earnings.

Stock options are not an integral part of large business practices, but have been the secret ingredient to technology success in the U.S. According to Merrill Lynch, if technology companies had been required to expense stock options in 2001, their earnings would have been slashed by an average of 39 percent. Using 2002 estimates, tech earnings would have been down 70 percent.

The Merrill Lynch analysis shows, on average, reported GAAP net income for semiconductor companies would have declined by 43 percent in 1999, 31 percent in 2000 and 69 percent in 2001 if companies expensed stock options. Of this group of semiconductor companies, the fabless companies covered by Merrill Lynch (Xilinx, Broadcom, Conexant, Exar, PMC-Sierra, Nvidia TranSwitch, Altera, SanDisk, Marvell and PLX Technology) would have declined by 74 percent in 1999, 41 percent in 2000 and 76 percent in 2001.

If profitability of these growth companies looks less attractive, there will be less investment allocated to this area. Reallocation of investment away from growth companies would stagnate innovation and progress.

Q. Why are stock options so prevalent in the technology arena, specifically fabless?

A. Technology companies use options as a way to offset risk. This might be necessary because employees are working on a product that is innovative and not yet proven. Some technology companies start with just an idea, and the successful implementation of this idea is going to include incredible risk and time. Talent is the key to bringing a product to market.

Furthermore, these companies are typically strapped for cash, initially resulting in lower than industry average salaries. The method of distributing stock options allows a company to grow without burning as much cash. As these companies grow, the options are used to continue to motivate employees to work hard and keep their interests aligned with investors.

Q. How do investors know the value or number of options issued?

A. Currently, public companies disclose this information in their 10-K. Under the current FASB rules, each year in the 10-K, companies disclose how many shares were granted during the year; how many shares employees exercised; and how many shares were forfeited after an employee left the company. There may also be a table in the 10-K that shows the number of options outstanding and the average exercise prices, along with the number of years that the options have remaining. Most companies use Black-Scholes as their valuation method, but it is a complex formula that is not easily explained to investors.

Q. How will ESO expensing negatively affect U.S. competitiveness?

A. Beyond inhibiting U.S. companies' ability to attract, motivate and retain talented employees, the FSA believes that Mainland China and Taiwan will pose a competitive threat to U.S. semiconductor companies over the next five years. There are as more than 250 fabless companies in these two geographical regions.

Technology companies in China and Taiwan are very liberal in their distribution of stock to employees. For many companies, they distribute stock at par value rather than options. Employees receive stock as bonuses.

Q. Isn't the FSA commenting on this topic a bit too late?

A. The FSA's role is to help its members understand the negative impact of ESO expensing on the fabless segment. The FSA is taking a number of steps on the semiconductor industry's behalf to ensure that the fabless segment has a voice in this debate. We believe our job is one of public relations, marketing and education. We have not traditionally been involved in lobbying efforts. But because we believe this will affect fabless companies adversely, we want to make our opinion known. We also want to make sure fabless employees understand the implications.