

**STATEMENT OF PHILLIPS W. SMITH**

**Before the**

**SUBCOMMITTEE ON CAPITAL MARKETS, INSURANCE &  
GOVERNMENT SPONSORED ENTITIES**

**COMMITTEE ON FINANCIAL SERVICES**

**April 21, 2004**

Thank you for allowing TASER International, AeA, and me personally to testify on the enormous impact stock options have on U.S. business development and job growth. I would like to commend the committee and you, in particular, Mr. Chairman, for your leadership on the Stock Option Accounting Reform Act. I support the legislation and urge the committee to act promptly to pass this important measure.

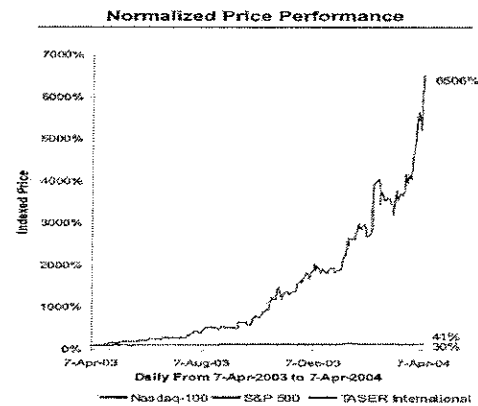
As an individual involved with five high technology start-ups as a CEO and Chairman of the Board, I have substantial experience in this area. Of the five companies I have helped launch, one was created in Denver without options in the early 1970's, one was built quite successfully in the Silicon Valley with options, and three additional companies have been started in Phoenix all with options. The most successful of those companies is the one I chair today, TASER International, Inc. In addition, I have a Ph.D. in Business Administration with a focus in the area of finance so I well understand the theoretical arguments being presented as to the expensing of all options, but I do not plan to take any of your time today discussing that as the topic has been covered by other people in far more depth.

TASER International, Inc., was founded in the 1990s with all the funding provided by myself and one other investor. We struggled through seven tough years prior to going public in 2001. Throughout the company's infancy, we used stock options for our office employees as a way to attract the best and brightest from larger companies. These people built the company to what it is today and I have a chart (see below) to show what the stock has done over the last year.

# TASR Liquidity Characteristics

Common Stock Data		TASR
Price:		\$98.04
Shares Outstanding:		12,675,000
Market Capitalization:		\$1,242,857,000
6-Month Average Daily Volume:		4,115,729
1% of Shares Outstanding:		126,750
Average Weekly Volume (past 4 weeks):		40,300,000
Dividend Yield:		0.00% (\$0.00 annual)
52-Week High:		\$98.04 (7-Apr-2004)
52-Week Low:		\$1.50 (8-Apr-2003)
Short Interest:		3,770,290
Float:		8,850,000
Call Open Interest: Apr-04 \$90.00:		3,238 contracts
Total:		51,140 contracts
Put Open Interest: Apr-04 \$90.00:		276 contracts
Total:		56,785 contracts
Stock Loan:	50,000 shares at -9% rate available	
Major Index:		Nasdaq Composite

Source: Bloomberg  
Data as of 7-Apr-2004



Just to put this in perspective, we have forty-two office employees that received early stock options. Our production employees are also now receiving stock options. Of the 42 employees plus four board members who received early options, 20 are now able to live their dreams because they have all achieved greater than \$1 million of net worth from those options. The pending proposal from FASB would have kept 38 of those people from receiving options because the financial exposure to a young company like TASER International would have been so high we could not afford to offer stock options to workers below the top five senior executives. The current FASB proposal would do nothing but take away the potential for non-executives to live their dreams.

I am not really here to give any theoretical concepts, as you have probably seen and heard enough of the accounting theory. But I am here to give a realistic appraisal of what this FASB proposal would do to a young company like ours. The impacts would be profound on job growth, economic development, corporate governance, and workers' lives.

## JOB GROWTH AND ECONOMIC DEVELOPMENT

First, on the stock options that were used to attract people to our company back in the early days. I have listed below a table of employment of our company and other suppliers in the Phoenix area.

Year	Number of Employees	% of Growth	Phoenix Area Supplier
2000	33		
2001	57	72	25 – 50
2002	73	28	50 – 100
2003	151	107	300 – 400

By looking at this table, you can see that we are one of the young growth “gazelle” companies that are big job creators for this country. And you can see that not only did we create new jobs for our own company, but there is a dramatic impact in the local marketplace because as we grow, it requires our suppliers to grow their employment base as well. Companies like TASER fuel the economic growth of our communities and the U.S. industrial base. We are the heart of our nation’s economic recovery.

## **CORPORATE GOVERNANCE**

The next area where options have been particularly critical has been in TASER’s ability to attract really top quality board members to help guide the company strategically through a period of high growth. Let me describe our board members’ backgrounds:

The first individual we recruited after going public was Bernie Kerik. Bernie was the New York Police Commissioner under Mayor Guiliani during the 9/11 crisis. He later went to Iraq to serve as the Minister of the Interior. To get a man of that caliber on the board of a young company like TASER, a company that just went public with lots of potential liability, we had to offer something above and beyond our incentive package of \$1,000 per meeting. Options were the only incentive we could provide. They turned out to be lucrative, but at the time Commissioner Kerik joined us he took a chance and accepted the potential liability hoping it would work out.

Our second Board member is Dr. Mark Kroll. He is the chief technology officer for St. Jude Medical, a very large, well recognized and highly respected medical device company. Dr. Kroll is the chief technology officer for St. Jude Medical’s heart and rhythm division. He is also a world-renowned expert in pace-makers and implantable cardiac defibrillators. How do you get a world-class scientist with 156 personal patents in his own portfolio to join a board like ours and effectively be our chief science advisor? The way we did it was to offer him options.

The third member of TASER’s board is Dr. Matt McBrady, a Finance Professor at the Darden School of Business at the University of Virginia. Dr. McBrady is our financial expert and advises in complying with the Sarbanes-Oxley requirements. To get Dr. McBrady on our board, again we provided options.

Our fourth outside director is TASER’s other original investor with me, Mr. Bruce Culver. Mr. Culver has founded two companies that are currently listed on the NASDAQ. He is a very well known entrepreneur and came on the board because he had a lot of stock in the company, but also because he got options to take the risk of being a board member.

So you can see simply by looking at these four individuals how essential it is that young companies have stock options to attract the management talent they need for direction and advice, particularly through the early high growth days of their development.

## **WORKERS' LIVES**

Finally, returning to TASER's employees, we are incredibly proud of the pay-off our workforce has enjoyed through TASER's success. The options we used to attract high-level talent and the sacrifices our employees made throughout our early years have created 20 new millionaires living the American dream. Our strategy for growth and continued use of options will allow others to follow in their footsteps and achieve that same level of success.

The reality is that options serve a variety of purposes. The legislation you have proposed, Mr. Chairman, as I understand it, will basically address the egregious compensation concerns some Members of Congress have with the top five corporate officers, without affecting rank and file employees. If changes must be made, I believe your approach strikes a balance in targeting abuse while giving companies the ability to attract the individuals they need to succeed. Under your approach, companies like TASER could continue to grow.

I can tell you from a personal standpoint, having done five high technology start-ups myself, that if all stock options are expensed as recommended by the current FASB proposal, all that will be accomplished is to take away opportunity from the workers who really make these companies successful. It will close the door on people who spend their lives fostering these start-up companies and helping them grow.

We at TASER International provided stock options to our employees not only to attract their talent, but also because we believe it is right for people who put their shoulder to the wheel to personally share in the financial success of our company.

There seems to be a lot of pressure to make us (the USA) like everybody else. Yet as we developed the greatest growth engines in the world, starting in the Silicon Valley through the beltway outside of Washington, we did it by using stock options. I can't tell you today that options were the only reason for that great growth, but I can tell you this, we all know that jobs are being exported. We know that we need to get people back to work and to create new jobs. It's young companies like TASER that are creating those jobs. Options are not the only reason companies get started or are successful, but they are one of the tools that help create growth. By tampering with that very successful model for growth and disassembling parts of it, by taking away options and forcing the expensing of these options, FASB is tampering with a model that has worked very well. The system is not broken. There is no need to change the way options have been treated.

Finally, I'd like to raise one additional point for the committee's consideration. It is that this FASB proposal would disproportionately hurt smaller companies in relation to big companies.

I had to chuckle when Coca-Cola said they said were going to expense options. If you look how few people in Coca-Cola even get options and secondly, the way the valuation for stock options is computed, big companies enjoy a large advantage in expensing options in their profit and loss statements. The FASB valuation formula hurts young companies. Our stock is very volatile. I showed you the chart earlier. That chart reflects

a lot of volatility in TASER's stock. Forcing us to expense stock options would provide us a double whammy. Because the stock of small companies is most volatile, expensing it under the FASB formula is a much bigger accounting hit to a small company, especially where the small company gives options to all employees. I urge the committee to consider the disparate impact of the FASB valuation formula as it moves forward in the coming months.

In conclusion, I do not think this is the intent of the Congress or its agents to penalize the engines of growth that are the biggest job creators. Yet, recognizing the pressure behind this options expensing movement, it is my hope that we can get the Stock Option Accounting Reform Act to the President before year-end. Bringing certainty, closure, and responsible reform to the options controversy would permit us to keep this excellent recruiting and motivating tool available to all people within our companies and not just the top five Executives.

Thank you for the opportunity to be here today.