



SENIC Battlecards

Stock Options anyone?

Considering offering stock options to employees? For evolving firms, stock options can level the playing field for recruiting the best and the brightest. By offering employees equity in your business, you can attract and retain talented employees, plus your employees will be highly motivated to see the value of your business increase.

Historically, stock options have been a powerful tool for evolving businesses to motivate their employees, especially during entrepreneurial periods when cash is tight and the need for a quality workforce is most critical. The payoff for the business is skilled labor at a discount and the payoff for employees is the promise of partial ownership once the business moves past the first organisational crisis. Sounds like a match made in heaven, right? But not everything is as it seems since the FASB (Financial Accounting Standards Board) passed new regulations. The impact of these regulations has had a dramatic effect on companies who offer stock options. Stock options are still an option, but only if you can live with the consequences.

What are stock options? Before deciding on stock options, you need to make sure you understand how they work. A stock option allows the owner of an option (the employee) to purchase stock at a certain price by a specified future date. The price of the option is usually set at the value of stock at the time the option is offered. If the price of stock goes up between the time the option is granted and the time it is exercised, the option has value because the employee can sell it at a profit. However, if the price of the stock

decreases or remains the same, the option is worthless because the employee does not realize a profit from the sale.

What are the new regulations? You can thank the recent string of business scandals for new regulations governing stock options. The new regs primarily deal with how stock options are treated on the company's financial statements. According to the FASB, companies are now required to expense stock options when they are granted rather than when they are exercised. The amount of the expense is based on an estimate of how much the option will be worth when it is ultimately cashed in by the employee. Upfront expensing of stock options is bad news for business owners because it requires you to record an expense that may or may not ever materialize. More expense means less profit (at least on paper), and jeopardizes your ability to attract investors.

What are my other "options"? Fortunately, there are other options available that might allow you to accomplish the same thing. Restricted stock is one of them. Under this scenario, employees are given a certain amount of stock in the company, but can't cash it in until the company achieves a specified goal or a specified period of time has passed. Employees retain value because once they are vested, they can sell the stock at any price and still realize a profit. From an accounting standpoint, companies also benefit because the financials reflect the actual amount of the expense rather than an imaginary inflated figure that may - or may not - actually come to pass.



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1800-GENESYS
info@genesys.ie
www.genesys.ie