EQUITIES

Stock Options and the Lying Liars Who Dont Want to Expense Them

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Options are something of value even if they are out of the money. They are valuable because they will be exercised only when it is advantageous to the employee and harmful to the company's shareholders (when the future price exceeds the price at which the option was struck). That is, they will be exercised only when the optionholders can take part of the company from shareholders at below-market prices.

The right to do this, with no risk of loss, is valuable. When the company gives away options, it is giving away something of value, and that is called an expense.

Still, many executives argue against bringing option expenses up out of the footnotes and into the bright light of the income statement's top line. None of the arguments hold water. If options have no value when issued, then the executives should be happy to simply give them to me. No? The executives are keeping them? Really? How interesting.

A related argument against expensing is simply that issuing stock options involves no current outlay of cash, so it is not an expense. True. So what? Issuing a promissory note to pay for donuts in the commissary also involves no current outlay of cash, but it is an expense. Even simpler, paying with a credit card does not move an expense into the future. There are legitimate arguments and difficult issues related to how to go about expensing options. There are no credible arguments, however, for ignoring these expenses.

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