Stock options-acc 499 capstone assignment

Business

Name April 10, 2011 ACC499-Accounting Capstone Professor According FASB, compensation plans include all arrangements by which employees receive shares of stock or other equity instruments of the employer or the employer incurs liabilities to employees in amounts based on the price of the employer's stock. Compensation cost should be measured at the grant date based on the value of the award and is recognized over the service period, which is usually the vesting period, under the fair value based method.

Compensation costs are recognized for other types of stock-based compensation plans under Opinion 25, including plans with variable, usually performance-based, features. Some stock-based compensation plans require an employer to pay an employee, either on demand or at a specified date, a cash amount determined by the increase in the employer's stock price from a specified level. An entity must measure compensation cost for that award in the amount of the changes in the stock price in the periods in which the changes occur.

Regarding stock options, fair value is determined using an option-pricing model that takes into account the stock price at the grant date, the exercise price, the expected life of the option, the volatility of the underlying stock and the expected dividends on it, and the risk-free interest rate over the expected life of the option. Under the provisions of the statement 123 of the FASB it is a requirement that companies report stock options on the income statement as an expense.

The provision was revised in 2005 due to the prior issues dealing with overstated income on financial statement. The method chosen must meet

FASB (107) requirements. In order to determine the fair value of the stock some variables must be used to determine the fair value: * Exercise price (call option or put option) * Expected dividends (amount paid out) * Expected volatility of the stock (Up and down of stock prices) * Expected term (Years of service before vesting) * Expected risk-Free rate of return during the term (a risk-less interest ate) * Current market price (the highest price that a buyer is willing to pay) Taken in account this variable the compensation amount is then produced (fair value per share multiplied by shares awarded). The compensation amount is then reported on the income statement as an expense. The expense is allocated over the service period until fully vested and are to be reported quarterly, journalized as compensation expense debited and paid in capital credited. If forfeiture occurs, the journal entry is to be reversed and the fair income statement and may change during the service period.

The current estimate of compensation is multiplied by the new estimate and it equals the new compensation amount. Balance it out by using the new compensation and multiplying it by the amount of time the initial estimate service time. The remaining amount must be recorded in the current year and the new estimate can be recorded in the forgoing years. There is no change to the financial statement if a stock lapse after vesting. A movement in equity to show there are no outstanding shares can be recorded. The lapsing of share does not represent a gain to the company because there is no change in net assets.

A current as well as a major issue are executive compensation and since the bank bailout it has brought excessive pay, bonuses and benefits to the forefront. In 2009, almost two years ago to date, Forbes magazine announced after a 15% collective pay cut in 2007, chief executives of the 500 biggest companies in the U. S. and took another 11% reduction in total compensation for 2008. The last time the big executives took a pay hit for two consecutive years was in 2001 and 2002. Collectively these 500 executives earned $5. 7 billion in 2008, which averaged out to $11. million individually and calculated to less than 1% of total revenues and 3% of total profits of their companies. While company executives receive huge bonuses and other great benefits, the underdogs are suffering with company cut-backs, shortage of hours and no incentives. The ccomponents of executive compensation include: * Salary: Annual base salary earned during the fiscal year. * Bonus: Annual non-equity incentives earned during the fiscal year, plus discretionary bonuses. * Other: Includes long-term, non-equity incentive payouts, the value realized from vesting of restricted stock and performance shares.

Also includes other executive personal benefits, such as premiums for supplemental life insurance, annual medical examinations, tax preparation and financial counseling fees, club memberships, security services and the use of corporate aircraft. * Stock gains: Value realized during the fiscal year by exercising vested options granted in previous years. The gain is the difference between the stock price on the date of exercise and the exercise price of the option. (Forbes) Stock options are another main concern and are based upon the performance of a company.

A lot of companies are in a low return and low compensation which then caused bad business and it’s about 400 times that amount. I believe the government is trying to tighten down on excessive executive compensation with implementing salary caps. Executives are unrealistic with common life and way of living therefore; they do not take any consideration with the underdogs of the company or the world. The economy does have hope but it’s a long way from being stabilized once again. References DeCarlo, S. (2009, April 22). What The Boss Makes. Forbes.

Retrieved April 10, 2011 from http://www. forbes. com/2009/04/22/compensation-chief-executive-salary-leadership Summary of Statement. Retrieved April 10, 2011, from http://www. fasb. org/jsp/FASB/Pronouncement_C/SummaryPage&cid Summary of Interpretation. Retrieved April 10, 2011, from http://www. fasb. org/jsp/FASB/Pronouncement_C/SummaryPage&cid Update No. 2010-25??? Plan Accounting??? Defined Contribution Pension Plans (Topic 962): Reporting Loans to Participants by Defined Contribution Pension Plans. Retrieved April 10, 2011, from http://www. fasb. org