FASB Harsh Option Cost Rule Reversed

by Robert W. Wood • San Francisco

The Financial Accounting Standards Board ("FASB") proposed several years ago that companies would have to deduct from their earnings the cost of employee stock options. This has raised a great hue and cry over the last couple of years, particularly since companies that often want to compensate their employees with equity or options are often greatly concerned about downward pressure on their earnings. This has especially been true in high-tech fields.

After considerable controversy over this issue, the FASB has now determined (in a 5 to 2 vote) to require that companies simply disclose in footnotes to financial statements the impact of options on net profit and per share earnings. While the FASB simultaneously voted to encourage companies to *voluntarily* deduct the cost of options from earnings, few companies are expected to follow this missive. *See* "FASB Drops Plan to Force Companies to Deduct Option Costs from Earnings," Wall Street Journal, December 15, 1994, p. A2.

Home Run?

This softened approach, which was foreshadowed only recently, has been met with optimism. *See*

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"Accounting Board to Weigh Softening Its Controversia Stock-Option Proposal," Wall Street Journal, December 14, 1994, p. A2. Indeed, it is hard to imagine not being pleased with this result. Nonetheless, executives and compensation consultants in some circles are questioning whether investors will criticize generous stock option plans if the disclosure regarding the earnings effects of such plans is explicit. The fact that the FASB wants a specific value to be disclosed in footnotes is causing some concern, although clearly this footnote disclosure is considerably less troublesome than the prior proposal would have been.

Of course, some are also noting that a differently constituted FASB in the future could revisit the issue, requiring that the footnoted numbers be deducted from earnings. In the short run, though, it is a distinct victory. ■