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## An option on stock options

By **MARY ANN MILBOURN**

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Reporting unvested employee stock options as an expense can be a major hit on the bottom line for company earnings, but some firms have gotten around it with a new trick: accelerated vesting.

Normally, companies require employees to claim their options over a period of years, called vesting. For instance, the options may vest over five years and the employee can claim a portion each year.

But new accounting rules that took effect this year now require companies to report the value of any unvested stock options on their income statements. To avoid having to report options as an expense, many firms decided to accelerate the vesting period prior to the new accounting rules.

Since all their options are now vested, their value doesn't have to be reported.

At least 15 Orange County companies took advantage of accelerated vesting last year, in some cases avoiding having to report millions of dollars in expenses, according to an analysis by the Center for Corporate Reporting & Governance at Cal State Fullerton.

**Gateway Inc.** accelerated options on 30 million shares last September. As a result, the Irvine computer maker will not have to report \$54 million as expenses on its income statement in coming years.

**Microsemi Corp.** in Irvine accelerated 5.1 million options last August for a \$35.7 million savings in future expenses. The semiconductor maker, however, imposed restrictions that prevent employees from selling any shares acquired by exercising the accelerated options until the date in the original vesting schedule.

Vivek Mande, director of the Center for Corporate Reporting & Governance, says accelerated vesting, while legal, should raise red flags for investors on several fronts.

In most cases, companies accelerate vesting to avoid reporting bad news.

"Generally, there is no valid economic reason to do it other than to make your earnings reports look better than they are," Mande says.

It also removes the primary reason for granting options – to give employees an incentive to work hard over several years so they can claim their stock reward.

"They may have actually destroyed these incentives," Mande says. "And what have you saved? Paper dollars. Why would you do that?"

Some companies argue that accelerating vesting improves employee morale and helps with worker retention.

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