Statement of Statutory Accounting Principles No. 13

Stock Options and Stock Purchase Plans

STATUS
Type of Issue: Common Area
Issued: Initial Draft
Effective Date: January 1, 2001
Affects: No other pronouncements
Affected by: Superseded by SSAP No. 104
Interpreted by: INT 99-00, INT 99-17, INT 00-06, INT 00-32, INT 01-14
**Stock Options and Stock Purchase Plans**

**SCOPE OF STATEMENT**

1. This statement establishes statutory accounting principles for employee stock options and stock purchase plans.

**SUMMARY CONCLUSION**

2. A stock purchase or stock option plan is any arrangement to issue stock to officers and employees, as a group or individually. A plan shall be classified as either noncompensatory or compensatory.

**Noncompensatory Plans**

3. A reporting entity recognizes no compensation expense for services received in return for stock issued through noncompensatory plans. The following four characteristics are essential in a noncompensatory plan:

   a. Substantially all full-time employees meeting limited employment qualifications may participate (employees owning a specified percent of the outstanding stock and executives may be excluded);

   b. Stock is offered to eligible employees equally or based on a uniform percentage of salary or wages (the plan may limit the number of shares of stock an employee may purchase through the plan);

   c. The time permitted for exercise of an option or purchase right is limited to a reasonable period; and

   d. The discount from the fair value of the stock is no greater than would be reasonable in an offer of stock to stockholders or others.

**Compensatory Plans**

4. Stock purchase and stock option plans which do not meet the criteria of a noncompensatory plan shall be classified as compensatory.

5. Consideration that a reporting entity receives for stock issued through employee stock option, purchase, and award plans in the form of services shall be measured by the fair value of the stock at the measurement date less the amount, if any, that the employee is required to pay.

6. The measurement date for determining compensation cost in stock option, purchase, and award plans is the first date on which are known both (a) the number of shares that an individual employee is entitled to receive and (b) the option or purchase price, if any. That date for many or most plans is the date an option or purchase right is granted or stock is awarded to an individual employee. However, the measurement date may be later than the date of grant or award in plans with variable terms that depend on events after the date of grant or award. Thus, a reporting entity recognizes compensation cost for stock issued through compensatory plans unless the employee pays an amount that is at least equal to the quoted fair value of the stock at the measurement date.

7. Compensation cost in stock option, purchase, and award plans shall be recognized as an expense of one or more periods in which an employee performs services and also as part or all of the consideration received for stock issued to the employee through a plan. The grant or award may specify the period or periods during which the employee performs services, or the period or periods may be inferred from the...
terms or from the past pattern of grants or awards. An employee may perform services in several periods before a reporting entity issues stock for those services. The reporting entity shall accrue compensation expense in each period in which the services are performed. If the measurement date is later than the date of grant or award, a reporting entity shall record the compensation expense each period from date of grant or award to date of measurement based on the fair value of the stock at the end of each period.

8. If stock is issued in a plan before some or all of the services are performed, part of the consideration recorded for the stock issued is unearned compensation and shall be reported as a component of unassigned funds (surplus). The unearned compensation shall be accounted for as expense of the period or periods in which the employee performs service.

Accounting for Income Tax Benefits

9. A reporting entity may obtain an income tax benefit related to stock issued to an employee through a stock option, purchase, or award plan. Generally, the reporting entity is entitled to a deduction for income tax purposes of the amount that an employee reports as ordinary income, and the deduction is allowable to the corporation in the year in which the amount is includable in the gross income of the employee. Thus, the amount and timing of the deduction for income tax purposes, if any, may differ from the related compensation expense recognized in the financial statements. For example, the reporting entity may be entitled to a deduction for income tax purposes even though no compensation expense is recognized in measuring net income.

10. The income tax reduction, if any, related to a stock option, purchase, or award plan shall be accounted for within one or more of the following three components:

   a. Income tax expense for a period shall be reduced by no more than the income tax reduction related to the stock option, purchase, or award plan that is proportionate to compensation expense recognized during the period, for such plan;

   b. Compensation expense that is deductible in the income tax return for a period different from the one in which such expense is reported in measuring net income results in a temporary difference. Deferred income taxes shall be recognized for such differences and included with all deferred income taxes as a separate component of gains and losses in surplus consistent with SSAP No. 101—Income Taxes, A Replacement of SSAP No. 10R and SSAP No. 10 (SSAP No. 101);

   c. The remainder of the income tax reduction, if any, is related to an amount that is deductible for income tax purposes but does not affect net income. The remainder of the income tax reduction shall not be included in income, but shall be added to capital stock or gross paid-in and contributed surplus in the period of the income tax reduction. Conversely, a tax reduction may be less than if recorded compensation expenses were deductible for income tax purposes. If so, the reporting entity may deduct the difference from capital stock or gross paid-in and contributed surplus in the period of the income tax reduction, to the extent that income tax reductions under the same or similar compensatory stock option, purchase, or award plans have been included in capital stock or gross paid-in and contributed surplus.

11. In certain situations, it may be advantageous to the reporting entity to compensate an employee to make an option that is detrimental to him but advantageous to the company. A reporting entity may, either by cash payment or otherwise, reimburse an employee for his action related to a stock option, purchase, or award plan that results in a reduction of income taxes of the reporting entity; for example, for incentive stock purchase plans, a reduction in the purchase price of stock is allowed. The reporting entity shall include this reimbursement as an expense.
12. Stock option, purchase, and award plans of the principal stockholder (i.e., a holding company) or equity instruments granted or otherwise transferred directly to an employee by a principal stockholder shall be treated as contributed surplus by the principal stockholder with the offsetting charge accounted for in accordance with this statement, unless such transfers are clearly for a purpose other than compensation for services rendered the reporting entity.

13. Compensation expense related to stock appreciation rights and other variable stock option or award plans shall be measured at the end of each period as the amount by which the quoted fair value of the shares of the enterprise’s stock covered by a grant exceeds the option price or value specified under the plan and should be accrued as a charge to expense over the periods the employee performs the related services. Changes in the quoted fair value should be reflected as an adjustment of accrued compensation and compensation expense in the periods in which the changes occur until the date the number of shares and purchase price, if any, are both known.

Disclosures

14. The financial statements shall disclose deferred stock compensation plans for employees such as profit sharing, stock option, or incentive plans. If warranted by materiality, the following information with regard to stock options shall be furnished and analogous information shall be supplied for warrants or rights:

   a. A brief description of the terms of each option arrangement including the title and amount of securities to option; the year or years during which the options were granted; and the year or years during which the optionees became, or will become, entitled to exercise the options; and

   b. The number of shares under option, the option price and the number of shares as to which options were exercisable; as to options exercised during the period, the number of shares involved and the option price thereof.

The required information may be summarized by category as appropriate and shall be disclosed separately for agents and brokers, employees and officers, and others. The disclosures shall be supplied whether the stock involved relates to the reporting entity, the parent of the reporting entity, a subsidiary of the reporting entity, or an affiliated corporation.

15. Refer to the preamble for further discussion regarding disclosure requirements. The disclosures in paragraph 14 above shall be included in the annual audited statutory financial reports only.

Relevant Literature

16. This statement rejects FASB Statement No. 123, Accounting for Stock-Based Compensation (FAS 123) and FASB Statement No. 148: Accounting for Stock-Based Compensation – Transition and Disclosure – an amendment of FASB Statement No. 123 (FAS 148).

17. This statement adopts APB Opinion No. 25, Accounting for Stock Issued to Employees, except for paragraph 19 regarding disclosure. The disclosure required by this statement is consistent with the disclosure requirements of Accounting Research Bulletin No. 43, Restatement and Revision of Accounting Research Bulletins (ARB 43), “Chapter 13, Compensation, Section B—Compensation Involved in Stock Option and Stock Purchase Plans,” prior to its amendment by FAS 123.

18. This statement adopts ARB 43, Chapter 13, Section B, with modification to exclude the additions to paragraph 2 and the deletion of paragraph 15 pursuant to FAS 123. This statement also adopts AICPA Accounting Interpretations, Accounting for Stock Issued to Employees: Accounting Interpretations of APB Opinion No. 25, FASB Interpretation No. 28, Accounting for Stock Appreciation Rights and Other
Variable Stock Option or Award Plans, and FASB Interpretation No. 38, Determining the Measurement Date for Stock Option, Purchase, and Award Plans Involving Junior Stock.

19. This statement adopts the following pronouncements which clarify and/or provide guidance in certain circumstances:

   a. FASB Emerging Issues Task Force No. 84-13, Purchase of Stock Options and Stock Appreciation Rights in a Leveraged Buyout;

   b. FASB Emerging Issues Task Force No. 84-18, Stock Option Pyramiding;

   c. FASB Emerging Issues Task Force No. 85-45, Business Combinations: Settlement of Stock Options and Awards;

   d. FASB Emerging Issues Task Force No. 87-6, Adjustments Relating to Stock Compensation Plans;

   e. FASB Emerging Issues Task Force No. 87-23, Book Value Stock Purchase Plans;

   f. FASB Emerging Issues Task Force No. 87-33, Stock Compensation Issues Related to Market Decline;

   g. FASB Emerging Issues Task Force No. 88-6, Book Value Plans in an Initial Public Offering;

   h. FASB Emerging Issues Task Force No. 90-7, Accounting for a Reload Stock Option;

   i. FASB Emerging Issues Task Force No. 90-9, Changes to Fixed Employee Stock Option Plans as a Result of Equity Restructuring;

   j. FASB Emerging Issues Task Force No. 94-6, Accounting for the Buyout of Compensatory Stock Options;

   k. FASB Emerging Issues Task Force No. 95-16, Accounting for Stock Compensation Arrangements with Employer Loan Features under APB Opinion No. 25.

20. This statement rejects FASB Emerging Issues Task Force No 96-3, Accounting for Equity Instruments That Are Issued for Consideration Other Than Employee Services under FASB Statement No. 123 and FASB Emerging Issues Task Force No 96-18, Accounting for Equity Instruments with Variable Terms That Are Issued for Consideration Other Than Employee Services under FASB Statement No. 123.

Effective Date and Transition

21. This statement is effective for years beginning January 1, 2001. A change resulting from the adoption of this statement shall be accounted for as a change in accounting principle in accordance with SSAP No. 3—Accounting Changes and Corrections of Errors.

AUTHORITATIVE LITERATURE

Generally Accepted Accounting Principles

- APB Opinion No. 25, Accounting for Stock Issued to Employees

- Accounting Research Bulletin No. 43, Restatement and Revision of Accounting Research Bulletins, Chapter 13B before modification by FAS 123
• Accounting Interpretation of APB Opinion No. 25, Accounting for Stock Issued to Employees

• FASB Interpretation No. 28, Accounting for Stock Appreciation Rights and Other Variable Stock Option or Award Plans

• FASB Interpretation No. 38, Determining the Measurement Date for Stock Option, Purchase, and Award Plans Involving Junior Stock

• FASB Emerging Issues Task Force No. 84-13, Purchase of Stock Options and Stock Appreciation Rights in a Leveraged Buyout

• FASB Emerging Issues Task Force No. 84-18, Stock Option Pyramiding

• FASB Emerging Issues Task Force No. 85-45, Business Combinations: Settlement of Stock Options and Awards

• FASB Emerging Issues Task Force No. 87-6, Adjustments Relating to Stock Compensation Plans

• FASB Emerging Issues Task Force No. 87-23, Book Value Stock Purchase Plans

• FASB Emerging Issues Task Force No. 87-33, Stock Compensation Issues Related to Market Decline

• FASB Emerging Issues Task Force No. 88-6, Book Value Plans in an Initial Public Offering

• FASB Emerging Issues Task Force No. 90-7, Accounting for a Reload Stock Option

• FASB Emerging Issues Task Force No. 90-9, Changes to Fixed Employee Stock Option Plans as a Result of Equity Restructuring

• FASB Emerging Issues Task Force No. 94-6, Accounting for the Buyout of Compensatory Stock Options

• FASB Emerging Issues Task Force No. 95-16, Accounting for Stock Compensation Arrangements with Employer Loan Features under APB Opinion No. 25

RELEVANT ISSUE PAPERS

• Issue Paper No. 82—Stock Options and Stock Purchase Plans