

CALIFORNIA STOCK OPTIONS

An option to buy stock gives the holder the exclusive right for a specified period of time to purchase stock at the price and under the terms and conditions specified in the agreement. Although the option grantor is bound by the option and generally cannot revoke it, the option holder is not bound unless he exercises the option. Options are regarded as capital assets if the underlying property constitutes, or if acquired would constitute, a capital asset in the hands of the holder.

Tax consequences to option grantor:

The receipt of consideration for the option is not taxable until the option either is exercised or has lapsed. If the option is exercised, the consideration is treated as part of the selling price and included in computing the gain or loss in the sale of the stock. Since stock is generally a capital asset, gain or loss on the sale would be entitled to capital treatment, either long-term or short-term. The holding period for qualification for long-term capital treatment is more than one year. The seller's holding period for the stock sold includes the period during which the option is outstanding.

Upon the failure of the option holder to exercise the option, if the consideration is forfeited, the option grantor generally realizes short-term capital gain, but income is not realized until the time of forfeiture.

Tax consequences to option holder:

An option holder's gain or loss upon a sale of the option, or loss upon a failure to exercise the option, would be entitled to capital gain treatment. The holding period of the option will determine whether long-term or short-term capital gain or loss is realized. For this purpose, if the loss is attributable to a failure to exercise the option, the option is deemed to have been sold on the day it expired.

If the option is exercised, the consideration for the option is treated as part of the purchase price and is included in the option holder's basis for the stock purchased. The purchaser's holding period does not include the period during which the option is outstanding.

Stock options can be utilized very effectively by an entrepreneur, for example:

- Stock is given to an employee, but if he leaves the employ, the corporation has the option to repurchase the employees stock at fixed or variable price.
- Stock in the corporation is sold to raise needed capital, but the corporation has the right to repurchase the stock in the future.
- For whatever reason a person would like to be a shareholder in the corporation but not now, an option to purchase stock is purchased from the corporation.

The stock option can be an on-target management incentive or control device. Stock options can be used in employment agreements, consultants agreements, incentive agreements, as means of raising equity capital or borrowing funds.

To order a Stock Option for your corporation, call the Spiegel & Utrera office nearest to you:

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