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## **THE PROS AND CONS OF STOCK OPTIONS AS A PART OF CEO COMPENSATION**

In post-crises period there was a tendency to reduce stock options as a part of managerial compensation, correlating with the period before financial crisis. Many discussions were organized around executives' remuneration by specialist in corporate governance.

Despite of its not so long history, options is one of the most interesting way to tie managerial and shareholders' interests, which leads to sustainable development of a corporation. Curtis in 2010 pointed that options as a part of executive compensation have been used in the world since the late 1970s. One of the pioneers in this business was the company Toys “R” Us - the largest U.S. chain of shops on selling toys. In the late 70's Toys “R” Us incorporated on and invited its top managers and sellers stock options. In the early 1980s, the mechanism of options began to use Apple Computer and General Electric, and then the other well-known companies. In 1992 top managers in about 82% of the companies of Standard & Poor`s 500 were stimulated in such way. Incomes from stock options were about 25% of the salary of senior officials of these companies, and in 1998 - 40%. In 2000 about 70% of all U.S. public companies used stock options as compensation.

Enron bankruptcy in 2001 together with the number of earlier scandals has lead to situation when such form of compensation was under the substantial amount of critics. Moreover, problems and scandals of banks and other corporations caused by crises of 2008-2009 forced scientific society to rethink their attitude to the issues of directors' remuneration.

Stock options as a part of effective long-term incentive system must correspond two basic criteria:

- must be competitive;
- should correspond the strategy and corporate culture of the company.

Let's see the potential benefits of using stock options for shareholders:

- Stock option scheme is beneficial for employer and employee. The company in such way keeps valuable employees because optional programs are on average from five to seven years. Applying such kind of scheme of interest alignment, principals can save on the increasing of the fixed salary.
- It is believed that fixed salaries and bonuses motivate executives “here and now”, and the options help to tie long-term interests of shareholders and executives.
- Ensuring of the growth of the company. Option is usually to make agents to work in the hardest way to achieve results for a company. This is justified when corporation plans to increase its value, expansion, etc.

In option programs two sides are always present. On the one hand, it's money. On the other hand it is the respect and recognition of certain merit of executives to the company. So the company demonstrates to employees the recognition and support of certain performance, sets benchmarks for success.

Canyon and Mallin have a point of view according to which executives, who received an options, have become potential shareholder and began to share the position of other shareholders and make decisions based on their interests.

However, the options have serious limitations that cannot be ignored when making a decision on the implementation of stock option incentive program for executives:

- Company's value in the market depends not only on the management, but also on a number of other factors that cannot always be controlled, especially in the situation of uncertainty. Growth or decline in share prices can be attributed to external factors.

- Options often lead to abuse by managers who are beginning to shift the focus to increase stock price more than on the balanced growth. According to a survey World at Work journal, from 7% to 38% of employers fear the introduction of stock options in connection with the scandal around the high income executives in the U.S.A.
- Division by manager risks with the company. Murphy stated that if the shares are not rising in price, the managers may not get anything. In this connection options can be considered as a very “risky” incentive mechanism. For example, the market can change for independent of the company reasons and the manager will have to share the risks along with his firm. In this case, the decline of stock price will lead to a sharp decline in the motivation of executives.

As a rule stock options are one of the parts of remuneration system for executives and are well introduced in regions with well developed stock exchange market. Combined programs of long-term compensation, including bonus shares, phantom shares, shares with limitations, combination of option program with awards for the year are quite popular as it gives some flexibility in design of remuneration system.

There is a sense of using stock options as a part of agents’ remuneration for principals (shareholders). It takes a lot of benefits for both sides. However, some negative consequences of misunderstandings and ineffective realization of such part of remuneration system caused critics. It should be outlined that further studies as for stock options and appropriate remuneration system have to be done to find out the most suitable one. It will assist in achieving sustainable development of a company and its strategic goals.

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