

Comment,
VALUATION OF STOCK OPTIONS IN
DIVIDING MARITAL PROPERTY
UPON DISSOLUTION

I. Introduction

The granting of stock options, to executives in the corporate sector, is becoming increasingly common.¹ Today, high level executives are often given stock options as part of their employee benefits package. A stock option allows the holder to buy a predetermined number of shares, over a set number of years, at a set price.² The price per share is generally the price per share on the date of the grant,³ or the price could be a nominal amount, such as \$1.00 per share. The shares represent the capital stock of the company, and encourage the high level executives to perform at a level that benefits the company by increasing the value of its stock. As the stocks' market price increases, the value of the options also increases. Many variations to the basic stock option plan exist, such as "time of exercise limitations (waiting periods); manner of exercise (installment formula); manner of triggering the option (incentive stock options); and restrictions that affect rights in the stock (full rights accrued only after a specific time)."⁴

Today, the average distribution of stock options to employees of high-tech companies is 3.3 percent of its stock.⁵ For example, IBM is currently distributing 2.5 percent of its outstanding shares to employees in 1998.⁶ Of America's largest 200 companies, approximately twelve percent of the outstanding shares are

¹ Paul M. Barrett, 'Corporate Wife' Gains in a Divorce Ruling, WALL ST. J., Dec. 4, 1997, at B1.

² Donn C. Fullenweider, *Unlocking the Possibilities*, 5 FAM. ADVOC. 2, 5, Spring, 1983.

³ *Id.*

⁴ *Id.*

⁵ Ira Sager, *Stock Options: Lou Takes a Cue From Silicon Valley*, BUS. WK.; INDUS./TECH. ED., Mar. 30, 1998, at 34.

⁶ *Id.*

earmarked as stock options for employees.⁷ Some companies, such as Morgan Stanley, Travelers, Warner-Lambert, and Microsoft distribute over twenty percent of their outstanding shares to employees in stock options.⁸

These stock options are generally granted to high level executives, and may be granted to an executive for any number of reasons. For example, small, emerging companies may lack the requisite capital to attract quality employees with a large salary, so stock options are given to draw in these quality employees. The stock options represent an incentive for the executive employee to leave his current high paying job for a job that has a lesser salary, but a greater income potential from the stock options. Often, these high level executives have a direct bearing on the success of the company, so in a very real sense, the increased value of the company's stock is directly attributable to their efforts. Stock options have netted some executives huge sums of money, and often in a divorce, the stock options may be the most valuable asset between the spouses.

Stock options represent a contingent benefit which is difficult to ascertain and value. Courts diverge widely in the manner in which they divide stock options, and vary even more in whether or not they consider the options a portion of the marital estate. This comment will compare and contrast varying courts' interpretations regarding stock options, which are held by one spouse, when the couple is divorcing. Some courts have avoided the messy issue of valuation, by claiming that the stock options are the separate property of the employee spouse, hence they are not marital property subject to division upon dissolution. However, those courts are in the minority, and most courts have held that the options represent marital property, and must be valued before the marital estate can be divided. Exactly how the options are divided is another issue that is not readily ascertainable from the opinions. Some courts have not divided this asset upon dissolution, but retained jurisdiction to split the proceeds when, and if, the options are ever exercised at a profit.

This comment surveys the jurisdictions that have faced the issue of dividing stock options earned by one partner in a mar-

⁷ Donald Jay Korn, *Helping Clients Plan for Cash-Less Paydays*, FIN. PLAN., Nov. 1, 1997, at 1, available in WL 10306438.

⁸ *Id.*

riage. The first question to ask is whether the options are part of the marital estate, or whether they are the separate property of the employee spouse to whom the options were granted. If the unvested options are marital property, the next step is to determine to what percentage of the options each party is entitled. This is where the jurisdictions vary, and variations exist even within jurisdictions, since the formulas for determining each spouse's share must be flexible to take into consideration all aspects of the stock options, as well as the unique circumstances of the parties involved.

In many situations, once the stock options have been divided, courts reserve jurisdiction to divide the proceeds in the future, when the options are exercised. But, if a court takes on the task of valuing the options, as of the date of dissolution, this onerous task will require experts to assist in the valuation.

II. Are the Stock Options Marital Property?

Many courts have made the distinction that if the stock options are granted for consideration of past services, and these past services occurred during the marriage, the stock options will be deemed marital property upon their issuance. If the stock options are granted in consideration for future services, however, and the employee must perform future services to obtain the options, courts will often utilize a time rule formula to determine what portion of the stock options constitute a marital asset for distribution upon dissolution.

A. *Stock Options Which are Not Exercisable at the End of a Marriage are Not Marital Property*

1. *Indiana*

The Indiana appellate court ruled in *Hann v. Hann*⁹ that accrued, but unvested stock options were not marital property, because they were contingent upon the employee spouse continuing in his employment with the company.¹⁰ The court held that only those stock options that were exercisable as of the date of filing a petition for dissolution constitute marital property

⁹ 655 N.E.2d 566 (Ind. Ct. App. 1995).

¹⁰ *Id.* at 569.

due to this contingency.¹¹ Unvested, unmatured stock options are not marital property.¹²

Daniel Hann began working for Biomet, Inc. on July 3, 1989.¹³ The stock options in dispute were granted as follows:

1. February 21, 1990: 12,500 shares, fully vested at \$5.06 per share. They were exercisable from February 21, 1993 to February 20, 1995.¹⁴
2. June 25, 1992: 1,200 shares, fully vested at \$15.00 per share. They were exercisable from June 25, 1993 to June 24, 1995.¹⁵
3. July 21, 1993: 25,000 shares; unexercised, unvested, unmatured.¹⁶

If Daniel left Biomet, he could not reap the benefits of the stock options.¹⁷ The court considered the shares unvested since Daniel Hann could only exercise them in the future, if he continued in his employment with the company.¹⁸

Under Indiana law, marital property includes all property acquired before and during the marriage, and excludes property only after the final separation date.¹⁹ In defining property, Indiana courts have “consistently held that only property in which the party has a vested interest at the time of dissolution may be divided as a marital asset.”²⁰ This would include vested rights in a pension plan, present ability to withdraw funds from a pension, or benefits that will not be lost due to a termination of employment.²¹

In this case, Judge Chezem’s dissent artfully explained the practicalities of utilizing stock options in today’s corporate environment.²² The judge stated that the stock options are present compensation setoff by a lower current salary.²³ Since the stock options in effect reduce the executive’s current annual salary,

¹¹ *Id.* at 571.

¹² *Id.*

¹³ *Id.* at 568.

¹⁴ *Hann*, 655 N.E.2d at 568.

¹⁵ *Id.*

¹⁶ *Id.*

¹⁷ *Id.* at 569.

¹⁸ *Id.*

¹⁹ *Hann*, 655 N.E.2d at 569.

²⁰ *Id.* at 569 (citations omitted).

²¹ *Id.* at 569-70.

²² *Id.* at 572 (Chezem, J., dissenting).

²³ *Id.*

stock options are, in essence, paid with current marital income.²⁴ The dissenting judge held this opinion in spite of the fact that the plan documents were silent regarding whether the stock options are an exchange for a lower current salary.²⁵ In Indiana, the majority avoided the confusing tests in valuing stock options for apportionment between the parties, and deemed those unexercisable options as the sole property of the employee spouse.

2. North Carolina

The court ruled in *Hall v. Hall*²⁶ that stock options that were not exercisable when the couple separated were unvested, and since they could be lost due to events occurring afterwards, the options were deemed the separate property of the employee spouse.²⁷ The North Carolina court viewed the stock options as compensation not only for past services, but also for future services as an incentive for the employee to stay with the company.²⁸ So, only those shares that are either exercisable on the date of separation, or unable to be canceled, are vested and deemed marital property subject to division upon dissolution.²⁹ Shares that are exercisable are compensation for past services, while unvested shares are contingent upon future acts of the employee, and should be deemed that party's separate property.³⁰

This type of rule lends itself well in valuation of the stock options, since ascertaining the value of the exercisable options is a relatively easy task. In this case, the stock options that were vested and exercisable when the couple separated were valued and divided.³¹

²⁴ *Hann*, 655 N.E.2d at 572 (Chezem, J., dissenting).

²⁵ *Id.*

²⁶ 363 S.E.2d 189 (N.C. Ct. App. 1987).

²⁷ *Id.* at 196.

²⁸ *Id.*

²⁹ *Id.* at 195-96.

³⁰ *Id.* at 196.

³¹ *Hall*, 363 S.E.2d at 196.

3. *Ohio*

In *Demo v. Demo*,³² the court held that the husband's stock options with General Electric (GE) were not marital assets, because they were not exercised during their marriage, nor would marital funds be used to exercise the options.³³ The court ruled that the stock options were given to the husband based on his past job performance before the marriage.³⁴ The Demo's marriage was of a short duration, only fifteen months.³⁵ The parties married in May, 1991, and a petition for dissolution was filed in August, 1992.³⁶ On May 22, 1992, the husband was awarded stock options to purchase 500 shares exercisable at 125 shares annually beginning November, 1992 through November 1995.³⁷ The court stated that these options were in recognition for services performed before the marriage and awarded them as separate property to the employee spouse.³⁸

It is unclear from this opinion the duration of the husband's employment with GE. The options were granted to him in 1992, a year after his marriage, so even though the court determined that the options were consideration for past services, more than a year of these past services were performed during the marriage. Perhaps a short-term marriage is given less consideration when dividing marital assets that encompass long-term obligations and rewards.

4. *Oklahoma*

The parties in *Ettinger v. Ettinger*³⁹ signed a consent decree which awarded the wife fifty percent of all stock options, regardless of when they accrued.⁴⁰ The court ruled that it did not have jurisdiction to divide future stock options, since they are future acquired property.⁴¹

³² 655 N.E.2d 791 (Ohio Ct. App. 1995).

³³ *Id.* at 793.

³⁴ *Id.*

³⁵ *Id.* at 792.

³⁶ *Id.*

³⁷ *Demo*, 655 N.E.2d at 793.

³⁸ *Id.*

³⁹ 637 P.2d 63 (Okla. 1981).

⁴⁰ *Id.* at 63-64.

⁴¹ *Id.* at 64.

The parties in this case divorced in 1972, and the consent decree stated that the non-employee spouse was entitled to “one-half of any and all stock options that [employee spouse] shall have with . . . his present employer, even though said stock options shall or may accrue in the future.”⁴² The decree went on to state that the non-employee spouse would “receive one-half interest in all stock options that [employee spouse] now has or may have. . . .”⁴³ The non-employee spouse evidently interpreted this to include all options the employee spouse would ever receive from his employer, not merely unvested stock options which were granted during the marriage. This distinction is not made clear in the court’s opinion, and leaves one to assume that the court is ruling on stock options that were not in existence at the date of dissolution, but were subsequently granted to the employee spouse after the dissolution.

The court avoided this sticky issue by ruling that it did not have jurisdiction to divide property that was acquired in the future, and the parties were unable to grant this jurisdiction to the court.⁴⁴

B. *Various Mathematical Tests for Determining What Portion of the Stock Options are Marital Property*

1. *Arkansas*

In *Richardson v. Richardson*,⁴⁵ the stock options were vested and exercisable on the date of dissolution.⁴⁶ The husband had options for purchasing 3,000 shares of Murphy Oil Corp. at \$13.71 per share.⁴⁷ To determine the value to give the wife for the stock options, the court subtracted the cost of exercising from the stock price on the day of trial, and awarded the wife one-half of this amount.⁴⁸ The court was silent regarding fees or taxes involved in exercising the options, and subsequently selling the shares for this profit.

⁴² *Id.* at 63.

⁴³ *Id.* at 64.

⁴⁴ *Ettinger*, 637 P.2d at 64.

⁴⁵ 659 S.W.2d 510 (Ark. 1983).

⁴⁶ *Id.* at 513.

⁴⁷ *Id.*

⁴⁸ *Id.*

2. California

*In re Marriage of Hug*⁴⁹ was the seminal case that caused courts to take notice of stock options in the division of assets upon dissolution. The court noted that stock options may be delineated as compensation for past, present, or future services, and created a mathematical fraction to determine the number of stock options that were community property: numerator— “the period in months between the commencement of the spouse’s employment by the employer and the date of separation of the parties;” denominator— “the period in months between commencement of employment and the date when each option is first exercisable.”⁵⁰

The Hugs married in 1956 and separated on June 9, 1976.⁵¹ The husband began his employment with Amdahl in 1972.⁵² His first and second stock options were granted on August 9, 1974; one was for 1,000 shares at \$1.00 per share, the other was for 1,300 shares at \$1.00 per share.⁵³ The third stock option was granted on September 15, 1975 for 800 shares at \$5.00 per share.⁵⁴ The options were exercisable over four years with annual increments “of 30%, 25%, 25%, and 20%.”⁵⁵

The court fashioned a formula to determine what portion of the options was marital property, and subject to division.⁵⁶ The court created a fraction whose numerator represented the number of months the husband both worked for Amdahl and was married to the wife.⁵⁷ The denominator represented the number of months from the first day of employment to the time when an option could be first exercised.⁵⁸ This resulting fraction was multiplied by the number of shares of the stock option to arrive at a figure for the wife’s share.

⁴⁹ 201 Cal. Rptr. 676 (1984).

⁵⁰ *Id.* at 678.

⁵¹ *Id.*

⁵² *Id.*

⁵³ *Id.* at 678-79.

⁵⁴ *Hug*, 201 Cal. Rptr. at 679.

⁵⁵ *Id.*

⁵⁶ *Id.*

⁵⁷ *Id.*

⁵⁸ *Id.*

This formula, by utilizing the first day of work in the denominator as a starting point, intimates that the stock options are not only for future services, but for past services as well. But, the court stated that “no single characterization can be given to employee stock options.”⁵⁹ Regardless of their description as being compensation for past services or future services, the court should look at the particular circumstances in the granting of the stock options.⁶⁰ In this case, the husband’s service prior to the granting of the stock options contributed to the husband being granted the options.⁶¹ Specifically, the husband had been working for another company for seven years prior to his switch to Amdahl.⁶² Since his retirement benefits were almost vested at the former place of employment, Amdahl may have used the stock options as an inducement to lure the husband into accepting his position at Amdahl.⁶³ Additionally, the husband expected the options from the start, making it likely that Amdahl granted the stock options “in lieu of present compensation during the initial period of [husband]’s employment, a time when Amdahl’s success was limited.”⁶⁴

Although the time-rule formula was effective in the allocation of assets in this case, the court “stress[ed] that no single rule or formula is applicable to every dissolution case involving employee stock options.”⁶⁵ Trial courts are expected to use broad discretion in allocating marital assets to seek an equitable outcome, when employee stock options are exercisable after parties separate.⁶⁶

Two years later, the issue of dividing stock options was revisited in California with the case *In re Marriage of Nelson*.⁶⁷ The court used the *Hug* approach, but began the time period in the numerator at the time of stock issuance rather than the beginning of employment.⁶⁸

⁵⁹ *Hug*, 201 Cal. Rptr. at 681.

⁶⁰ *Id.*

⁶¹ *Id.* at 682.

⁶² *Id.*

⁶³ *Id.*

⁶⁴ *Hug*, 201 Cal. Rptr. at 682-83.

⁶⁵ *Id.* at 685.

⁶⁶ *Id.*

⁶⁷ 222 Cal. Rptr. 790 (Cal. Ct. App. 1986).

⁶⁸ *Id.* at 793.

These stock options were granted with a purchase price equal to the fair market value of the stock on the day of the grant.⁶⁹ In this case, the court determined that the stock options were intended as compensation after their issuance, rather than for past performance as the *Hug* circumstances warranted.⁷⁰ Additionally, this court reduced the value of the options to reflect the likely income tax imposed on the asset of twenty percent, and noted that if the actual tax reduction were more than this, the husband would be credited for the additional amount.⁷¹

Another case, *In re Marriage of Harrison*,⁷² used the term “golden handcuffs” to describe the stock options granted to an employee spouse “to encourage [him] to stay with the company.”⁷³ The court in *Harrison* altered the *Hug* formula to create a time-rule. In the numerator, as in *Nelson*, was the amount of time from the granting of the options to the date of separation.⁷⁴ The denominator number began with the granting of the stock options,⁷⁵ and ran until the “stock [was] received pursuant to the exercise of the option.”⁷⁶

The parties’ marriage lasted from February 2, 1974 to June 27, 1979.⁷⁷ The husband had four stock option grants; the first was a qualified option, while the others were nonqualified.⁷⁸ All of the options had been granted prior to the parties’ separation.⁷⁹

3. *Colorado*

*In re Miller*⁸⁰ rejected the notion that all stock options are granted for future compensation, and fashioned the step of determining whether the stock options are issued as consideration for past, present, or future services.⁸¹

⁶⁹ *Id.* at 795.

⁷⁰ *Id.* at 793.

⁷¹ *Id.*

⁷² 225 Cal. Rptr. 234 (Cal. Ct. App. 1986).

⁷³ *Id.* at 237.

⁷⁴ *Id.* at 237 n.1.

⁷⁵ *Id.*

⁷⁶ *Id.* at 238.

⁷⁷ *Harrison*, 225 Cal. Rptr. at 236.

⁷⁸ *Id.*

⁷⁹ *Id.*

⁸⁰ 915 P.2d 1314 (Colo. 1996).

⁸¹ *Id.* at 1319.

The Millers married on June 10, 1983 and divorced November 16, 1992.⁸² The husband was granted stock options by his employer on November 17, 1988, November 16, 1990, and November 21, 1991.⁸³ Each agreement allowed for the exercise of 25 percent, 50 percent, 75 percent, and 100 percent, of the option annually, respective to each options anniversary year.⁸⁴ The husband was also given 2,500 restricted shares on July 17, 1991.⁸⁵ These shares would vest in five years when the restriction period would expire.⁸⁶ Up until then the shares could not be transferred or pledged, yet all other rights, such as voting rights and the ability to receive cash dividends to the shares, were reserved to the husband.⁸⁷

In determining the marital portion of the options, the court stated that since an employee has no “right to compensation until the services for which the employee is being compensated have been performed . . . the [marital portion] under the option agreement . . . depends on the extent to which the options [are] granted in consideration of past or future services.”⁸⁸ If the stock options are issued based on past services, the options are marital property upon issuance, unless a portion of the past services is attributable to pre-marital service.⁸⁹ Conversely, those stock options issued for future services cannot be deemed marital property until the future services have been performed by the employee, and they are also contingent upon the marital unit still being intact.⁹⁰

The trial court ruled that the stock options were consideration for services, but did not designate to what extent the services were past or future services.⁹¹ The Colorado Supreme Court remanded to the trial court to determine what portion of the stock options were granted for past services and future services, so that

⁸² *Id.* at 1315-16.

⁸³ *Id.*

⁸⁴ *Id.* at 1315.

⁸⁵ *Miller*, 915 P.2d at 1315.

⁸⁶ *Id.*

⁸⁷ *Id.*

⁸⁸ *Id.* at 1318.

⁸⁹ *Id.* at 1319.

⁹⁰ *Miller*, 915 P.2d at 1319.

⁹¹ *Id.*

the marital portion could be divided between the parties.⁹² The court drew factors from the *Hug* court to determine the nature of the stock options, such as “the flexibility and variety of option plans as well as the size of the company and its need to offer incentives to employees to remain . . . [with] the company.”⁹³ With regards to the restricted stock, the court ruled that it was entirely marital property subject to division, as the husband retained significant rights over the stock, and also had actual physical possession of the shares.⁹⁴

The Colorado Court of Appeals had an opportunity to interpret and apply *Miller* with *In re Marriage of Sim*.⁹⁵ The court ruled that stock options are marital property to the extent they are granted for past services performed during the marriage.⁹⁶ The court further stated that the options must be classified, and divided, in accordance with *Miller*.⁹⁷

Recently, however, the Colorado Court of Appeals decided a case that seems to place Colorado in the minority of jurisdictions that do not recognize the marital nature of stock options. In *Huston v. Huston*⁹⁸ the wife’s unvested stock options were deemed marital property by the trial court. The husband was given twenty-five percent and the wife retained seventy-five percent of the options, while the husband was allowed to exercise one call per option.⁹⁹ The appellate court reversed stating that “[a] non-vested stock option is a mere expectancy and therefore not ‘property’ because the holder has no enforceable rights.”¹⁰⁰ The court considered *Miller*, and declared it erroneous.¹⁰¹ The court interpreted *Miller* as holding that stock options that are not vested cannot be property.¹⁰² However, even if a stock option is vested, it must be determined whether it is marital or separate

⁹² *Id.*

⁹³ *Id.* at 1319 n.9.

⁹⁴ *Id.* at 1319-20.

⁹⁵ 939 P.2d 504 (Colo. Ct. App. 1997).

⁹⁶ *Id.* at 508.

⁹⁷ *Id.* at 509.

⁹⁸ 967 P.2d 181 (Colo. Ct. App. 1998).

⁹⁹ *Id.* at 183.

¹⁰⁰ *Id.*

¹⁰¹ *Id.*

¹⁰² *Id.*

property of the employee spouse.¹⁰³ This case creates confusion, making it unclear what Colorado's position is on the classification of stock options granted to a married employee.

4. Illinois

*In re Marriage of Frederick*¹⁰⁴ established that even when stock options are deemed marital property, the employee spouse deserves sole discretion in exercising options, but when he exercises those options, he must share half with the non-employee spouse.¹⁰⁵ The parties married in 1955 and divorced in 1989.¹⁰⁶ The husband had worked for Hilton Hotels for thirty-three years, and was a senior vice president.¹⁰⁷ At issue were 6,772 vested, but unexercised stock options of Hilton stock, and 11,000 shares of non-vested unexercised stock options.¹⁰⁸ The court determined that although valuation of the options was not proven, it was not the trial court's duty to determine their value.¹⁰⁹ Rather, the court would retain jurisdiction until the options were exercised, at which point the court would divide the net proceeds equally between the parties.¹¹⁰

Following *Frederick*, the court decided *In re Marriage of Isaacs*.¹¹¹ In this case, the marriage lasted from March 27, 1967 until a petition for dissolution was filed on October 6, 1989.¹¹² The court deemed unexercised stock options held by the wife as marital property only upon their exercise, since they were contingent upon her continued employment, and the passing of time.¹¹³ The appellate court directed, on remand, the trial court was to retain jurisdiction to divide the proceeds, if, and when, the options were exercised.¹¹⁴

¹⁰³ *Huston*, 967 P.2d at 183.

¹⁰⁴ 578 N.E.2d 612 (Ill. Ct. App. 1991).

¹⁰⁵ *Id.* at 619.

¹⁰⁶ *Id.* at 614.

¹⁰⁷ *Id.*

¹⁰⁸ *Id.*

¹⁰⁹ *Frederick*, 578 N.E.2d at 619.

¹¹⁰ *Id.*

¹¹¹ 632 N.E.2d 228 (Ill. Ct. App. 1994).

¹¹² *Id.* at 230.

¹¹³ *Id.* at 234.

¹¹⁴ *Id.*

5. Louisiana

In *Goodwyne v. Goodwyne*,¹¹⁵ the parties married in 1959, and the husband began working for Louisiana Land & Exploration in 1966.¹¹⁶ The couple divorced in 1985, and the husband retired in 1992.¹¹⁷ When they divorced, the husband did not disclose that he had stock options granted during the marriage; some vested, some unvested, because at the time of the divorce, the options were at a price above the fair market value of the shares, and he felt that they had no value.¹¹⁸ A stock valuation expert testified that the options did have value in 1985.¹¹⁹ Additionally, the husband was granted stock options in 1986, after the dissolution, yet the court partitioned this option along with the rest.¹²⁰ The husband argued that since the options were granted after dissolution, they were his separate property.¹²¹ The appellate court deemed the 1986 options were based on services performed during the marriage to which the wife had an interest.¹²² In so holding, the court stated that “the determinative factor is whether work performed during the existence of the community was taken into consideration in granting the option. Since the stock option was based partly upon work performed in 1985, the trial court’s factual finding”,¹²³ giving the wife part of the proceeds, was affirmed.¹²⁴

6. Maryland

In *Green v. Green*¹²⁵ the court determined the percentage each spouse would receive upon execution of the stock options. The decision did not force the employee spouse to exercise the stock options,¹²⁶ nor did it allow for the non-employee spouse to

¹¹⁵ 639 So. 2d 1210 (La. Ct. App. 1994).

¹¹⁶ *Id.* at 1210.

¹¹⁷ *Id.*

¹¹⁸ *Id.* at 1211.

¹¹⁹ *Id.* at 1212.

¹²⁰ *Goodwyne*, 639 So. 2d at 1213.

¹²¹ *Id.*

¹²² *Id.*

¹²³ *Id.*

¹²⁴ *Id.*

¹²⁵ 494 A.2d 721 (Md. Ct. Spec. App. 1985).

¹²⁶ *Id.* at 729.

have any interest in the stock options until after they were exercised by the employee spouse.¹²⁷

The employee husband claimed that even though some of the options were matured, and could have been exercised, since he hadn't exercised the options, they were worthless.¹²⁸ He claimed that "something not acquired during the marriage cannot be marital property."¹²⁹ Regarding the shares that were unexercisable, an expert witness claimed that the options had no value because they were unexercised, and he claimed that since the "options [were] personal to [him] and [could not] be assigned or sold,"¹³⁰ they had no value.¹³¹

The court determined that the stock options were marital property since they were acquired while the marriage was intact.¹³² This included both the matured and unmatured options, so the court suggested, on remand, that the trial court could "adopt an 'if, as and when' approach to the valuation and equitable allocation of the unexercised options, including the 2,500 matured options as well as the 2,500 unmatured options."¹³³ The appellate court gave further instructions to the trial court to establish a value, as of the date of the decree, by considering the market value of the shares on that date as well as the cost of exercising the option.¹³⁴ Then the court must determine an equitable percentage for division of the profits when the options are exercised.¹³⁵

7. Michigan

In *Everett v. Everett*¹³⁶ the parties married in 1965, and separated in June, 1986.¹³⁷ The stock options in dispute were 3,660 shares of the husband's employer's stock.¹³⁸ At trial, 200 shares

¹²⁷ *Id.*

¹²⁸ *Id.* at 726.

¹²⁹ *Id.*

¹³⁰ *Green*, 494 A.2d at 726.

¹³¹ *Id.*

¹³² *Id.* at 728.

¹³³ *Id.* at 729.

¹³⁴ *Id.*

¹³⁵ *Green*, 494 A.2d at 729.

¹³⁶ 489 N.W.2d 111 (Mich. Ct. App. 1992).

¹³⁷ *Id.* at 112.

¹³⁸ *Id.* at 113.

were yet unvested, while the remainder were vested.¹³⁹ For the shares that were vested, the court stated that the “present value of [the] stock options [could be] calculated by subtracting the option cost from the market price of the stock.”¹⁴⁰ However, the court went on to say that tax consequences must be factored into the valuation of the stock options.¹⁴¹ The appellate court remanded this issue back to the trial court with no further instructions on how to complete this task.¹⁴²

8. *Minnesota*

The Minnesota Court of Appeals applied the California *Hug* time rule in *Salstrom v. Salstrom*.¹⁴³ The parties married in 1967, after they both graduated from college.¹⁴⁴ The husband then went on to obtain a doctorate in molecular biology.¹⁴⁵ The husband began working for Endotronics, Inc. in February, 1984.¹⁴⁶ The parties were divorced in May, 1986.¹⁴⁷ Stock options had been granted to the husband in March 1984, August 1984, and July 1985.¹⁴⁸ Of these grants, the husband held options on 7,759 shares to be purchased in February 1987, and 7,759 shares to be purchased in February 1988.¹⁴⁹ The exercise price for all was \$3.22 per share.¹⁵⁰ The trial court awarded each party one-half of the shares, and retained jurisdiction to oversee this distribution.¹⁵¹ The appellate court ruled that since some of the shares would not vest until well after the divorce, a time-rule formula was appropriate to determine each party’s share.¹⁵² The shares would be multiplied by a marital fraction where the numerator consisted of the time “of marriage during which benefits were

¹³⁹ *Id.* at 114.

¹⁴⁰ *Id.* at 113.

¹⁴¹ *Everett*, 489 N.W.2d. at 114.

¹⁴² *Id.*

¹⁴³ 404 N.W.2d 848 (Minn. Ct. App. 1987).

¹⁴⁴ *Id.* at 849.

¹⁴⁵ *Id.*

¹⁴⁶ *Id.*

¹⁴⁷ *Id.* at 850.

¹⁴⁸ *Salstrom*, 404 N.W.2d at 850.

¹⁴⁹ *Id.*

¹⁵⁰ *Id.*

¹⁵¹ *Id.*

¹⁵² *Id.* at 851.

being accumulated.”¹⁵³ The denominator consisted of the time “during which benefits were accumulated prior to when paid.”¹⁵⁴ The appellate court further ruled that the trial court would retain jurisdiction to award the wife her marital interest.¹⁵⁵

9. *Missouri*

The husband attempted to characterize his unvested stock options as his separate property in *Smith v. Smith*¹⁵⁶ by claiming that since the options were “contingent upon his continued employment,” the options were unvested and his sole property.¹⁵⁷ The court stated that the future options, although contingent upon the husband continuing in his employment, were marital assets since they had already been earned, and divided the options equally.¹⁵⁸ However, the court did not sever the options, and provided that if the husband was to exercise an option in the future, he was to give the wife thirty days notice so that she could purchase her fifty percent of the shares.¹⁵⁹ If she could not pay him her fifty percent, she would forfeit her portion of the option.¹⁶⁰ In denying severance of the claims to the stock options, the court stated that although severance is preferable, there were “sound economic reasons why severance [was] not feasible or advisable, [and] the parties [were] left as tenants in common.”¹⁶¹

10. *New Jersey*

In *Callahan v. Callahan*,¹⁶² the court determined that stock options granted by an employer were a form of compensation and constituted marital property.¹⁶³ The husband, an executive, was granted stock options during the marriage.¹⁶⁴ The court compared stock options to pensions and profit-sharing plans, and

¹⁵³ *Salstrom*, 404 N.W.2d at 851.

¹⁵⁴ *Id.*

¹⁵⁵ *Id.*

¹⁵⁶ 682 S.W.2d 834 (Mo. Ct. App. 1984).

¹⁵⁷ *Id.* at 837.

¹⁵⁸ *Id.*

¹⁵⁹ *Id.*

¹⁶⁰ *Id.*

¹⁶¹ *Smith*, 682 S.W.2d at 837.

¹⁶² 361 A.2d 561 (N.J. Super. Ct. Ch. Div. 1976).

¹⁶³ *Id.* at 563.

¹⁶⁴ *Id.* at 562.

found them to be similar.¹⁶⁵ The court determined that the wife was entitled to twenty-five percent of each stock option, and created a constructive trust in favor of the wife, for her portion of the stock options.¹⁶⁶

In *Pascale v. Pascale*,¹⁶⁷ the court removed stock options granted ten days after the dissolution petition from marital property, and awarded them as separate property to the employee spouse.¹⁶⁸ The parties were married in June, 1977, and a divorce complaint was filed by wife on October 28, 1990.¹⁶⁹ At trial on April 3, 1992, the wife was earning \$52,500 per year and the husband was earning \$72,500 per year.¹⁷⁰ The wife began working for Liposome Company April 14, 1987, and was granted several stock options over the next few years.¹⁷¹ At issue were stock options issued on November 7, 1990, only ten days after her filing for divorce.¹⁷² There were two grants issued to wife on this date, one was for 4,000 shares and the other for 1,800 shares.¹⁷³ Although she admitted that the 1,800 shares were granted for her past services, she argued that the 4,000 shares constituted compensation recognizing her for a promotion with increased responsibilities, thus, they should be viewed as compensation for future services, and separate property.¹⁷⁴ The trial court deemed both parties' stock options marital property, and should be distributed equally. On appeal, the appellate court ruled that the 1,800 shares were marital property and the 4,000 shares were not.¹⁷⁵

The appellate court found that the 4,000 shares were issued to "enhance [wife's] future employment efforts," so she alone should be entitled to them.¹⁷⁶ The New Jersey Supreme Court, however, ruled that both of these options were marital assets and

¹⁶⁵ *Id.* at 562-63.

¹⁶⁶ *Callahan*, 361 A.2d at 564.

¹⁶⁷ 660 A.2d 485 (N.J. 1995).

¹⁶⁸ *Id.* at 497.

¹⁶⁹ *Id.* at 487.

¹⁷⁰ *Id.* at 488.

¹⁷¹ *Pascale*, 660 A.2d at 497.

¹⁷² *Id.*

¹⁷³ *Id.*

¹⁷⁴ *Id.*

¹⁷⁵ *Id.*

¹⁷⁶ *Pascale*, 660 A.2d at 497.

subject to division.¹⁷⁷ The court focused on “whether the nature of the asset is one that is the result of efforts put forth ‘during the marriage’ by the spouses jointly, making it subject to equitable distribution.”¹⁷⁸ Here the promotion of the wife was found to be “a result of the excellent service that she had provided to the company during her marriage.”¹⁷⁹ The court recognized that although some stock options are granted for past services, these were more appropriately deemed to encourage the employee’s future performance.¹⁸⁰ The court stated that even though these stock options were granted after the wife filed for divorce, the existence of the options were due to marital efforts and should be shared by both spouses.¹⁸¹

11. *New Mexico*

In *Garcia v. Mayer*,¹⁸² stock options vested a day after divorce, and the wife sought her share of the profits.¹⁸³ Since a portion of the labor required to earn the stock options occurred during the marriage, the marital community had a share in the profits.¹⁸⁴ The trial court first had to determine whether the options were granted for past or future services.¹⁸⁵

In this case, the spouses executed a property settlement agreement that divided the husband’s vested stock options, but was silent regarding his unvested options.¹⁸⁶ A day after their divorce, the husband’s company merged with another company. The stock options vested, and increased dramatically in value.¹⁸⁷ The husband exercised his options at a significant gain.¹⁸⁸ The wife then sought her share of these options.¹⁸⁹ Although the husband claimed that the property settlement agreement inferen-

¹⁷⁷ *Id.* at 498.

¹⁷⁸ *Id.*

¹⁷⁹ *Id.*

¹⁸⁰ *Id.* at 497.

¹⁸¹ *Pascale*, 660 A.2d at 498-99.

¹⁸² 920 P.2d 522 (N.M. Ct. App. 1996).

¹⁸³ *Id.* at 523.

¹⁸⁴ *Id.* at 524.

¹⁸⁵ *Id.* at 525.

¹⁸⁶ *Id.* at 523.

¹⁸⁷ *Garcia*, 920 P.2d at 523.

¹⁸⁸ *Id.*

¹⁸⁹ *Id.*

tially awarded him 100 percent of these unvested options, the trial court found the agreement to be ambiguous in its silence.¹⁹⁰

The trial court looked to the time rule formulas of *Hug* and *Harrison*.¹⁹¹ The difference between the two time rules is that the *Hug* rule includes service with the company from the first day of employment in its fraction, while the *Harrison* rule begins service on the day the stock options are granted. The *Hug* rule, thus, implies that the stock options granted are based not only on future services, but on past services as well, while the *Harrison* rule suggests that the stock options are granted for future services only.

In this case, the trial court determined that the husband's stock options were granted for both prior and future services, and used the *Hug* time rule.¹⁹² Employing this formula, the court used the dates that the stock options were scheduled to vest.¹⁹³ In fact, the stock options vested only one day after this court order.¹⁹⁴ The husband appealed the court ruling, claiming that his prior services were irrelevant to the stock options which were "golden handcuffs" intended to inspire his future efforts with the company.¹⁹⁵ The appellate court agreed with the husband that the options were granted for the purpose of inducing his future efforts, but stated that the husband should be grateful that the stock options were determined using the time rule formula, based on the *intended* vesting date, rather than the actual vesting date.¹⁹⁶ If the trial court had retained jurisdiction to divide the stock options, as of the date they actually vested, the result would have been that the stock options were virtually 100 percent community property.¹⁹⁷

The appellate court upheld the division, since it was within the broad discretion of the trial court to divide the stock options.¹⁹⁸ In affirming, the appellate court stated that "[h]usband

¹⁹⁰ *Id.*

¹⁹¹ *Id.* at 525-26.

¹⁹² *Garcia*, 920 P.2d at 526.

¹⁹³ *Id.*

¹⁹⁴ *Id.*

¹⁹⁵ *Id.*

¹⁹⁶ *Id.* at 526-27.

¹⁹⁷ *Garcia*, 920 P.2d at 527.

¹⁹⁸ *Id.* at 526.

cannot complain that the district court used a coverture factor more favorable to him than it might have.”¹⁹⁹

12. New York

The court in *DeJesus v. DeJesus*²⁰⁰ adopted the Maryland *Miller* four-step analysis, a time-based formula, to determine the marital value in stock options.²⁰¹ The appellate court lacked sufficient information to complete the four steps in dividing the property, so it reversed the case, and remitted it to the Supreme Court.²⁰²

The court stated factors to consider in determining the portions of stock plans which were granted for past or future services. These “relevant factors would include whether the stock plans are offered as a bonus or as an alternative to fixed salary, whether the value or quantity of the employee’s shares is tied to future performance, and whether the plan is being used to attract key personnel from other companies.”²⁰³

The court fashioned a time rule for compensation for past services.²⁰⁴ The numerator begins with either the time the employee spouse began employment with the company issuing the stock options or the date of marriage, whichever is later, to the date of the issuance of the stock option.²⁰⁵ The denominator begins from the time the employee spouse began employment to the date of the issuance of the stock option.²⁰⁶

For future services the court constructed another time rule, with a numerator beginning with the date of the issuance of the stock option to the end of the marital union, which is determined as the earlier of either the date of a separation agreement or filing of the matrimonial suit.²⁰⁷ The denominator begins with the date of the issuance of the stock option to the date when the stock option will mature.²⁰⁸

¹⁹⁹ *Id.* at 527.

²⁰⁰ 665 N.Y.S. 2d 36 (Ct. App. 1997).

²⁰¹ *Id.* at 40.

²⁰² *Id.* at 41.

²⁰³ *Id.*

²⁰⁴ *Id.*

²⁰⁵ *DeJesus*, 665 N.Y.S. 2d at 41.

²⁰⁶ *Id.*

²⁰⁷ *Id.*

²⁰⁸ *Id.*

13. *Oregon*

The Oregon court used a time factor rule in *In re Marriage of Powell*²⁰⁹ to determine the wife's proportional profit share.²¹⁰ The stock options in dispute were unvested, and over half were tied to future performance goals.²¹¹ The options tied to future performance goals eventually would vest, even if the performance goals were not met.²¹² The others required only continuing employment by the husband.²¹³

The court determined that the stock options were intended to keep Mr. Powell in the company, ensuring that he would "work hard for the company in future years."²¹⁴ Since this would encompass service years after a marital dissolution, the court "emphasize[d] the length of time that must pass before the options vest."²¹⁵

In determining how to divide the stock options, valued at \$1,410,000, the trial court applied a time factor test, to establish a fraction to multiply by the value of the stock options in awarding the wife her portion.²¹⁶ The court used the "[n]umber of months from date of option grant to date of dissolution" as the numerator, and the "[n]umber of months from date of option grant to date of vesting" as the denominator.²¹⁷ The trial court then allowed the wife to exercise her portion of the purchase options as the options vest.²¹⁸

14. *Texas*

In *Bodin v. Bodin*,²¹⁹ the husband argued that since his stock options were both unvested, and contingent upon his continued employment, they were not marital assets subject to division upon dissolution.²²⁰ The court compared stock options to contin-

²⁰⁹ 934 P.2d 612 (Or. Ct. App. 1997).

²¹⁰ *Id.* at 615.

²¹¹ *Id.* at 613.

²¹² *Id.*

²¹³ *Id.*

²¹⁴ *Powell*, 934 P.2d at 615.

²¹⁵ *Id.*

²¹⁶ *Id.* at 613-14.

²¹⁷ *Id.*

²¹⁸ *Powell*, 934 P.2d at 614.

²¹⁹ 955 S.W.2d 380 (Tex. Ct. App. 1997).

²²⁰ *Id.* at 381.

gent interests in property, which “are a community asset subject to consideration along with other property in the disposition of the parties’ estate.”²²¹ The court also compared stock options to military pensions, which were unvested, yet were a contingent interest, and must become part of the marital property.²²² The Texas court noted that the majority of states, that have ruled on this issue, have included unvested stock options in the marital pool of assets.²²³ More notable to the court was that all the community property states, that have addressed this issue, have all ruled consistently that the stock options constitute marital property, subject to division upon dissolution.²²⁴ While a few states have held that unvested stock options are the separate property of the employee spouse, none of these states “is a community property state.”²²⁵

15. *Virginia*

In *Dietz v. Dietz*,²²⁶ the trial court divided the husband’s stock options, in the same manner that it would divide an unvested pension, since the options were deferred compensation for the husband.²²⁷ The husband’s stock options were divided as marital property, using a fraction.²²⁸ The numerator included “the number of months the [husband] was covered by the identified plan, prior to [the date of final separation],” while the denominator included “the total number of months the [husband] is covered by the plan.”²²⁹ This fraction determined what portion of the stock options were marital property.

Of this marital portion, the court ordered that fifty-three percent of the net proceeds from the sale of these marital shares would be paid to the wife.²³⁰ Since, the Virginia statute which covers deferred compensation plans did not allow apportionment

²²¹ *Id.*

²²² *Id.*

²²³ *Id.*

²²⁴ *Bodin*, 955 S.W.2d at 381.

²²⁵ *Id.* at 382.

²²⁶ 436 S.E.2d 463 (Va. Ct. App. 1993).

²²⁷ *Id.* at 470.

²²⁸ *Id.*

²²⁹ *Id.*

²³⁰ *Id.* at 469-70.

of more than fifty percent of the marital portion,²³¹ the appellate court remanded to the trial court for reconsideration.²³²

16. *Washington*

*In re Marriage of Short*²³³ determined that to divide stock options, courts must first determine whether options were given for past, present, or future services.²³⁴ If stock options are unvested and for present services, the stock options are deemed marital property, if the marital unit is intact.²³⁵ Unvested stock options, issued for future services, are subject to the time rule in determining apportionment.²³⁶ Here, the court only applied the time-rule to the first stock option to vest after the date of separation.²³⁷ The remainder was deemed separate property.²³⁸

In this case, the husband had worked for Digital Corporation as a supervisor for ten years.²³⁹ After Digital canceled a project that he was supervising, the husband and other former Digital employees explored creating a new computer technology company.²⁴⁰ When Microsoft heard of this, the Chairman met with the husband and the others, and offered them employment with Microsoft.²⁴¹ Included in the husband's compensation package were stock options on 25,000 shares of Microsoft common stock for \$46 per share.²⁴² He began his employment with Microsoft in November 1988, and the parties separated in January 1989.²⁴³ The husband filed a petition for dissolution in February 1990, and the decree of dissolution was final in May 1991.²⁴⁴ The stock split in April, 1990, and the husband's options

²³¹ VA. CODE. ANN. § 20-108.3(G) (Michie 1995).

²³² *Dietz*, 436 S.E.2d at 470.

²³³ 890 P.2d 12 (Wash. 1995) (en banc).

²³⁴ *Id.* at 16.

²³⁵ *Id.*

²³⁶ *Id.* at 16-17.

²³⁷ *Id.* at 17.

²³⁸ *Short*, 890 P.2d at 17.

²³⁹ *Id.* at 13.

²⁴⁰ *Id.*

²⁴¹ *Id.*

²⁴² *Id.*

²⁴³ *Short*, 890 P.2d at 13-14.

²⁴⁴ *Id.* at 14.

increased to 50,000 shares at \$23 per share.²⁴⁵ The options were exercisable as follows: 12,500 shares on May 17, 1990; 6,250 shares on November 17, 1990; 6,250 shares on May 17, 1991; 6,250 shares on November 17, 1991; 6,250 shares on May 17, 1992; 6,250 shares on November 17, 1992; and 6,250 shares on May 17, 1993.²⁴⁶ In May 1990, the husband exercised his stock options on 12,000 shares, sold the shares, and realized a profit of approximately \$500,000 before tax deductions.²⁴⁷ The trial court determined that some of the options were acquired during the marriage, and were divisible as marital property, while a majority of the options were separate property acquired by the husband after separation.²⁴⁸ The court gave the wife fifty percent of the May 1990 profits, twenty-five percent of the excess 500 shares that were exercisable in May 1990, and twenty-five percent of those shares due to become exercisable in November 1990.²⁴⁹ The remainder was deemed the husband's separate property not subject to division.²⁵⁰

The wife appealed and the appellate court found that all of the stock options were community property, since they were acquired during the marriage.²⁵¹ The Washington Supreme Court granted review, and stated a new rule in determining what portions of unvested stock options granted during a marriage constituted marital property subject to division. The first step is to determine whether the options are granted for past, present or future services.²⁵² This is a case-by-case determination, based on the specific facts and circumstances surrounding each granted option.²⁵³

Supporting the notion that the options were granted for present services, was the fact that the options were granted as part of the husband's compensation package, and to deter him from starting a competing business with Microsoft, as well as the

²⁴⁵ *Id.*

²⁴⁶ *Id.*

²⁴⁷ *Id.*

²⁴⁸ *Short*, 890 P.2d at 14.

²⁴⁹ *Id.*

²⁵⁰ *Id.*

²⁵¹ *Id.*

²⁵² *Id.* at 16.

²⁵³ *Short*, 890 P.2d at 16.

fact that the stock grants were front-loaded.²⁵⁴ To support the notion that the options were granted for future services, the husband submitted the option contract, which corroborated this assertion.²⁵⁵

The Supreme Court determined that the evidence supported the superior court's ruling regarding the characterization of the options as part marital and part separate.²⁵⁶ Next, the Supreme Court applied the time rule to determine what portion of the first stock options that vested after marriage would be deemed marital property subject to division.²⁵⁷ This included the 12,500 shares that vested on May 17, 1990, and the court accepted the trial court's characterization of the 12,000 shares that were acquired and sold for a profit.²⁵⁸ The superior court had determined that the wife was entitled to twenty-five percent of the unexercised shares that vested on May 17, 1990.²⁵⁹ Of the 250 shares that were not characterized, the Supreme Court applied a time rule and determined that twenty-eight shares would be characterized as marital property.²⁶⁰ In its interpretation of the time rule, the court used a different formula than the *Hug* court, applying the rule only to "the first stock option to vest after the parties are found to be 'living separate and apart.'"²⁶¹ In refusing to apply the time rule to all options acquired during the marriage, but vesting after the parties separate, the court stated that to apply the time rule to all of the future options "ignores the separate property provisions of RCW 26.16."²⁶² So, the wife was prevented from gaining any rights over the stock options other than the options that vested on May 17, 1990.

In *Stachofsky v. Stachofsky*,²⁶³ the court scrutinized stock options granted to a husband late in his career, where a signifi-

²⁵⁴ *Id.*

²⁵⁵ *Id.*

²⁵⁶ *Id.* at 16.

²⁵⁷ *Id.* at 17.

²⁵⁸ *Short*, 890 P.2d at 17.

²⁵⁹ *Id.* at 14.

²⁶⁰ *Id.* at 17.

²⁶¹ *Id.*

²⁶² *Id.* (Property acquired prior to marriage or after marriage by gift, bequest, devise, or descent is treated as separate property, and is not subject to division upon dissolution of the marriage).

²⁶³ 951 P.2d 346 (Wash. Ct. App. 1998).

cant portion of his early years with the company were spent climbing the ladder, to management.²⁶⁴ He attempted to exempt a portion of his stock options by characterizing them as being partially for past services performed by him as he rose up the management ladder, and before he was married.²⁶⁵ The trial court deemed shares that vested after separation were fifty percent marital property and fifty percent separate property of the husband.²⁶⁶ The appellate court found that the *Short* rule could apply to 20,000 shares that were granted for present and future services, but since the trial court would have divided the property in the same manner, notwithstanding the mischaracterization, a remand was not required.²⁶⁷ Since a “trial court may dispose of both community property and separate property ‘as shall appear just and equitable’ considering all relevant factors,”²⁶⁸ the judgment was affirmed.²⁶⁹

17. *Wisconsin*

In *Chen v. Chen*,²⁷⁰ the appellate court ruled that non-vested stock options are entirely marital property.²⁷¹ Marital assets are not limited to those in existence on the date of separation, but included assets in existence at time of dissolution.²⁷² The court ruled that stock options, although not exercisable before separation, were an economic asset acquired by the marital unit.²⁷³ The court compared a stock option to an unvested pension, and deemed it a form of property.²⁷⁴

The parties married in 1971, and the husband began working for his employer in 1979.²⁷⁵ Upon divorce, the court granted the wife a one-half interest in all stock options, including those that

²⁶⁴ *Id.* at 348.

²⁶⁵ *Id.* at 350.

²⁶⁶ *Id.* at 349.

²⁶⁷ *Id.* at 352.

²⁶⁸ *Stachofsky*, 951 P.2d at 352.

²⁶⁹ *Id.* at 353.

²⁷⁰ 416 N.W.2d 661 (Wis. Ct. App. 1987).

²⁷¹ *Id.* at 662-63.

²⁷² *Id.* at 663.

²⁷³ *Id.* at 662-63.

²⁷⁴ *Id.* at 663.

²⁷⁵ *Chen*, 416 N.W.2d at 662.

were unvested, but in existence at the time of divorce.²⁷⁶ The husband argued that the wife's one-half interest should be determined on the date of separation, but the Wisconsin appellate court stated that "[t]he marital estate . . . include[s] assets as they exist at the time of the divorce"²⁷⁷ rather than at separation.²⁷⁸ He also argued that the wife's benefit from the increase in value in the stock options, to be exercised in the future, should be limited through the use of a "time-rule", which would distinguish his post-marital efforts from those exerted during the marriage.²⁷⁹ But, the court stated that it was not obligated to utilize such a formula, even though the Wisconsin marital property statute 766.62 utilizes a similar formula.²⁸⁰ The lawsuit was filed in November, 1985, and the statute went into effect January 1, 1986.²⁸¹ The parties did not litigate the applicability of the statute, nor ask the court to apply it, therefore, the court refused to consider it.²⁸²

In dividing the stock options, the court determined that to assign a present value was impossible.²⁸³ The trial court had determined a percentage of the marital estate to which the wife was entitled, and the appellate court stated that she was to receive this same percentage of the profits from the stock options when they were sold in the future, at a profit.²⁸⁴ The court was careful in crafting an equitable division, while not constraining the husband's rights regarding his exercise of the stock options. The court specifically stated that the husband was free to exercise the options whenever he desired, but when the stock was sold, the wife was to receive one-half of the net profit.²⁸⁵ If, after eighteen months, the husband had not sold the stock acquired by the options, the wife may elect to receive a sum based on a formula which ascertains what profits could be realized at that time.²⁸⁶ The wife must elect this option at that time, and if she does not

²⁷⁶ *Id.*

²⁷⁷ *Id.* at 663.

²⁷⁸ *Id.*

²⁷⁹ *Id.*

²⁸⁰ *Chen*, 416 N.W.2d at 663.

²⁸¹ *Id.* at 663 n. 1.

²⁸² *Id.*

²⁸³ *Id.* at 662.

²⁸⁴ *Id.* at 664.

²⁸⁵ *Chen*, 416 N.W.2d at 664.

²⁸⁶ *Id.*

do this within nineteen months from the exercise date, she must wait until the stock is eventually sold to receive her share of the profits.²⁸⁷

The court protected the wife, who could not participate in the decisions regarding the timing of the purchase and sale of the shares, by stating that she would not be responsible for her share of losses if the stock was sold for a loss.²⁸⁸

In *Wikel v. Wikel*,²⁸⁹ the parties' twenty-five year marriage ended in dissolution.²⁹⁰ The court affirmed the trial court's ruling that only those stock options which were exercisable on the first day of trial were subject to division.²⁹¹ The court did not mention *Chen* or any other jurisdiction, or give any explanation for this determination.

III. Placing a Value on the Options

Valuing stock options is difficult. A variety of methods exist to determine the value, and each method finds its niche in various situations.

A. The Intrinsic Value Method

This method is less complex than the other methods. It is an accounting tool to ascertain compensation values of stock options. To determine the intrinsic value of a stock option, the option's exercise price is subtracted from the stock's market price.²⁹² This simplified formula is easy to compute, if the stock is a regularly traded commodity. But, this formula does not take into account factors such as the cost of exercising, the tax consequences of exercising, and the contingencies, such as continued employment, which are inherent in stock options, especially those that are unvested. The formula also fails to address risk

²⁸⁷ *Id.*

²⁸⁸ *Id.* at 664-65.

²⁸⁹ 483 N.W.2d 292 (Wis. Ct. App. 1992).

²⁹⁰ *Id.* at 293.

²⁹¹ *Id.* at 294.

²⁹² Reva B. Steinberg, *Take Stock of Your Options — Understanding the New Accounting Rules for Stock-Based Compensation*, 10 No. 5 INSIGHTS 24, 25 (May 1996).

and volatility.²⁹³ Since the formula fails to address these concerns, it “is an inadequate method of evaluating stock options in a marital context.”²⁹⁴

B. *The Black-Scholes Method*

One method that is widely used in the valuation of stock options is the Black-Scholes Option Pricing Model.²⁹⁵ This formula was originated by Fischer Black and Myron Scholes in 1973.²⁹⁶ Black died in 1995, and Robert Merton of Harvard University assisted Scholes, a professor of finance at Stanford Business School, in modifying the formula to make it more widely applicable.²⁹⁷ Recently, Scholes and Merton won the Nobel Prize for economics for their formula in valuing stock options.²⁹⁸ The formula is a complicated one, but there are computer programs and calculators, with the formula integrated into them, which allow the user to enter variables to ascertain the value of stock options.²⁹⁹

Among the many factors, “[t]here are five factors which affect the market value of an executive stock option:

- An option’s intrinsic value,
- An option’s time to execution,
- The value of the underlying security,
- Market interest rates, and
- Dividends.”³⁰⁰

The Black-Scholes method integrates six variables affecting the stock options.³⁰¹ They are:

²⁹³ *Wendt v. Wendt*, No. FA96 0149562 S., 1998 WL 161165, at *192 (Conn. Super. Ct. Mar. 31, 1998) (mem).

²⁹⁴ *Id.*

²⁹⁵ Korn, *supra* note 7, at 3

²⁹⁶ Eric Brazil, *Stanford Economist Wins Nobel, Shares Award With Harvard Colleague For Pioneering Formula to Value Stock Options*, S. F. EXAMINER, Oct. 14, 1997 at A1; Elliot H. Gourvitz & Lawrence J. Cutler, *Distribution of Contingent Property Interests*, 8 FAIR\$HARE 5, 7, Aug. 1994.

²⁹⁷ Brazil, *supra* note 296, at A1.

²⁹⁸ *Id.*

²⁹⁹ *Wendt*, 1998 WL 161165, at *195.

³⁰⁰ Gourvitz & Cutler, *supra* note 296 at 6.

³⁰¹ Gregory J. Cowhey, Lester Barenbaum, Sandra R. Klevan, *Putting a Price Tag on the Company*, 17 FAM. ADVOC. 44, 52, Spring, 1995.

1. The exercise price of the option;
2. The market price of the underlying security;
3. The expiration date of the option;
4. The underlying security's volatility;
5. Current interest rates; and
6. The dividends of the underlying security.³⁰²

C. Variations of the Black-Scholes Method

A variation of the formula attempts to value a call option, considering current interest rates, stock fluctuation, and the probability of exercise of the option.³⁰³

IV. Conclusion

The first hurdle to overcome, in representing parties who have stock options, is to research the law in your jurisdiction to see whether the options will be classified as marital property, or the separate property of the employee spouse. The majority of jurisdictions are settled that the vested options will be deemed marital, and subject to division. The unvested options may be partially marital property, and the correct formula for determining the marital portion must be ascertained. Once the marital portion of the options have been ascertained, many courts will retain jurisdiction to divide the proceeds at a future date. However, if the stock options must be divided at dissolution, there are many complicated formulas to determine the value of the options, at that time, for division. An expert witness will be required to aid the court in this valuation. It is beyond the scope of this paper to address the specifics involved in such technical and complicated steps that are involved in the process of stock valuation. There are experts, who are knowledgeable in this area, to aid the practitioner in furthering the goal of dividing the marital estate.

Lynn Curtis

³⁰² *Id.*

³⁰³ *See supra*, note 7.