Quiz

1. Which one of the following generally represents the largest portion of the compensation provided to the highest paid corporate CEOs?

A. long-term compensation
B. retirement contributions
C. options
D. employer provided insurance benefits
E. annual bonuses

Options generally represent the largest portion of a top CEOs compensation package.

2. Ms. Senior Manager was just granted some stock options by her employer. How is the face value of those options computed?

A. Number of options × Par value of stock
B. Number of options × Stock price
C. Number of options × Book value per share
D. Number of options × (Stock price − Par value per share)
E. Number of options × (Stock price − Book value per share)

Face value = Number of options × Stock price.

3. Which one of the following is generally true at the time stock options are granted to a corporate executive?

A. The options are deeply out of the money.
B. The options are deeply in the money.
C. The exercise price of the options is equal to the book value of the stock.
D. The exercise price of the options is equal to the difference between the market price and the book value of the stock.
E. **The exercise price of the options is equal to the market price of the stock**.

At the time the options are granted, the exercise price is generally equal to the market price of the stock.

4. Which one of the following correctly states a reason for granting at the money stock options to a company executive?

A. At the money stock options are taxed when issued based on the at the money option value.
B. Stock options help ensure the executive makes decisions based on the best interests of the shareholders.
C. Stock options increase the base pay of the executive which lowers the taxable income of the firm.
D. Stock options guarantee a base amount of compensation to the executive.
E. Stock options provide a stated financial benefit to the executive regardless of the firm's performance or stock price movements.

At the money options are taxed only if and when they are exercised

5. Which one of the following is correct concerning the granting of stock options by corporations?

A. Stock options granted to company executives must be issued out of the money.
B. Corporations are restricted to granting stock options only to individuals holding positions at the vice-president level and above.
C. The option exercise price is generally ten percent above the stock price when an option is granted to a company executive to encourage the executive to improve company profits.
D. Company executives are granted options in a manner which guarantees the executive a profit when the options are exercised.
E. Stock options can be awarded to an employee irrespective of his or her position or level of compensation.

Stock options can be granted to all employees.

6. Which one of the following terms is defined as the period of time between the date when an executive is granted stock options and the date on which the executive is granted the right to exercise those options?

A. exercise period
B. grant period
C. out of the money period
D. freeze-out period
E. tenure period

The fixed period of time an executive must hold his or her options is called the freeze-out period.

7. Connie Roach is the CEO of Movers United. She was recently granted one million European at the money stock options. The average stock price on the date of the grant was $42.15. The options expire in six years, the continuously compounded interest rate is 4.5 percent, and the variance of the stock is .0576. What is the total value of Ms. Roach's stock options based on the Black-Scholes model?

A. $11.79 million
B. $12.33 million
C. $13.87 million
D. $14.44 million
E. $16.01 million

$N(d_1)$ is .774341 and $N(d_2)$ is .565662.

8 Mr. Alexander Hamilton was granted 3 million European stock options this morning as part of his CEO compensation package. The options expire in five years and were issued at the money based on the current stock price of $48.30. The variance of the stock is .042025 and the continuously compounded interest rate is five percent. What is the total value of the options Mr. Hamilton received?

A. $39.86 million
B. $42.70 million
C. $43.08 million
D. $43.56 million
E. $44.14 million

$N(d_1)$ is .780706 and $N(d_2)$ is .6240699.

9. Mrs. Tracy is the CFO of West Coast Insurance. Last week, the firm granted her 15,000 European at the money options. The average stock price when the options were granted was $21.60. The continuously compounded interest rate is 5.2 percent. The options expire in seven years and the stock has a variance of .051984. What is the value of each option?

A. $8.37
B. $8.82
C. $9.01
D. $9.47
E. $9.63

$N(d_1)$ is .817276 and $N(d_2)$ is .618598

10. Blue Bird Flights just issued 10,000 European options to its CEO. The options expire in four years and have an exercise price that equaled the average stock price of $18 at the time of issuance. The variance of the stock is .026244 and the continuously compounded interest rate is 4 percent. What is the value of these options to the CEO?

A. $2.42
B. $3.09

C. **$3.73**
D. $4.16
E. $5.08

$N(d_1)$ is .744032 and $N(d_2)$ is .62999.