

Case study #4: Cap table re-pricing, how does this affect your stock options?

Solution: Early stage employee and consortium, was able to convince management to get a 409A valuation report and issue newly priced options.

Savings=client recouped 6 figures of stock value.

What do you do when your company is struggling with valuation? The reality with crashing public market comps, with tech stock indexes halved in the first half of FY22, is that your company's valuation, especially if private, will likely be affected by this. Whether it is a markdown from the 409A valuation report or a down round for the most recent funding round, the company will likely suffer a drop in valuation. What does this mean for an employee of a private company with stock options? Well simply put, your stock options may be underwater, meaning your exercise price is below the strike price. Let's keep in mind the underlying math behind stock options. Options are the option, but not the obligation, to buy the underlying stock in the company. It is a right to buy stock in the company at a set price. For example, underwater stock options may look like this: stock option gives you the right to buy stock for \$22 a share and its current fair market value is \$15.

What does this private company do to assuage the concerns of angry employees with worthless stock options? They get a 409A valuation report with the latest fair market value. A 409A report is issued by a 3rd party valuation firm, hired by management team, whenever the company goes through a significant event that would affect valuation, and usually performed at least once a year for tax purposes. Once the company has an established fair market value, they can get the board of directors to issue new stock options to employees at an appropriate strike price, that makes the shares worth something. This can be controversial and difficult to perform the accounting; however, it can be necessary and a normal course of action for companies in this situation. If you are an employee in this situation, you should listen to what is happening in the company and understand what this means for you.
