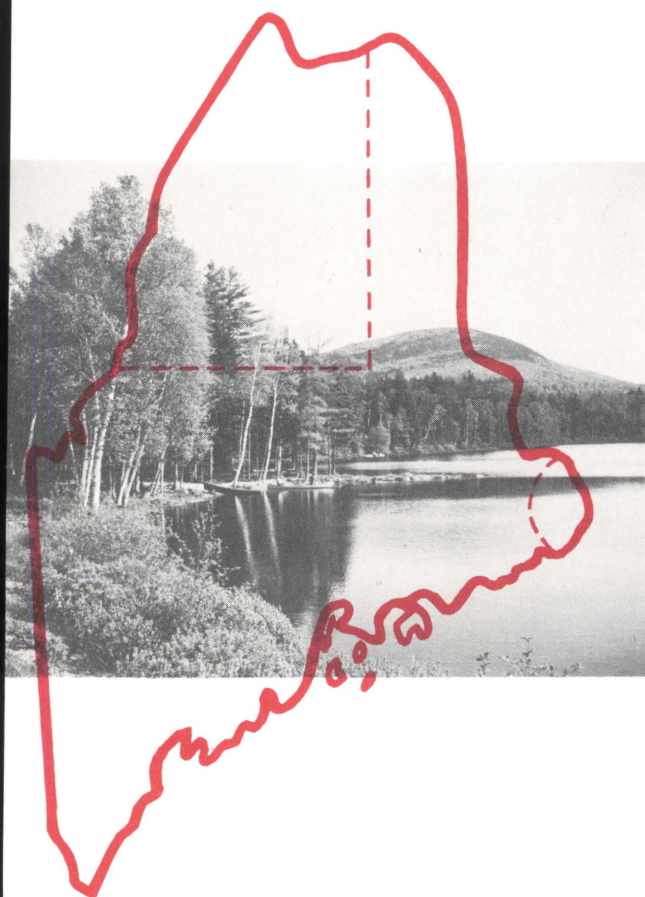


# NEW ENGLAND BUSINESS REVIEW

SEPTEMBER  
1964



## **New England's Last Frontier: Part I ... planning for its development**

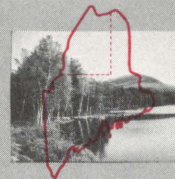
Three different plans are being promoted for the development of northern and eastern Maine. This article discusses the advantages and drawbacks of each plan.

## **Stock Options for Bankers**

Stock options, long thought useful for attracting and retaining executives, may be more costly than other incentives.

FEDERAL RESERVE BANK OF BOSTON





## New England's Last Frontier: Part I ... planning for its development

The forest lands and lakes of northern and eastern Maine cover about 11 million acres or about one quarter of the area of New England. A large part of this privately owned acreage is isolated wilderness located more than 10 miles from the nearest maintained graveled logging road. Except when pulpwood and timber are cut, few men set foot in the more remote parts of northern Maine.

This area, however, is beginning to attract more attention. Competing proposals for power and recreational development are being put forth by private, state, and Federal agencies. Each of these proposals, in one way or another, would encroach on the wilderness character of northern Maine. Those who enjoy remote out-

door recreation and other attributes of Maine's existing forest economy oppose most of the proposed changes. Those who are interested in economic development and who are primarily concerned about the lack of employment opportunities support proposals which they believe will stimulate the local economy. The best hope for the future, however, may rest in the possibility that appropriate project design and land use planning in the northern Maine region may make economic development compatible with an attractive wilderness atmosphere.

### **The Advantages of Wilderness**

To date, relatively little development has taken place in the northern Maine woods other than minor recreational development and timber harvesting for the pulp and paper industry. The harvesting of pulpwood has done little to harm the landscape. Hundreds of thousands of acres of lakes and a thousand or more miles of lake frontage are remote and undeveloped. Hundreds of miles of streams provide unique fishing and canoeing experience for the hardy visitor who has the physical endurance and the time to penetrate this wilderness. If and when this area is further developed, it will be-

**The New England Business Review is produced in the Research Department. Robert W. Eisenmenger was primarily responsible for the article, "New England's Last Frontier: Part I — planning for its development," and Prudence Slitor Crozier for "Stock Options for Bankers." Some of the information for the latter article was drawn from "Stock Options for Bank Executives," a thesis written by John Barrett for the Stonier Graduate School of Banking. Copies of the thesis may be obtained on request from this Bank's Research Department.**



come less attractive to the recreationist who wants a complete change from urban living. Thus, a lack of development has advantages for some individuals and private companies.

The existing situation also has important tax advantages for landowners. Almost 9 million acres of undeveloped land in Maine are in unincorporated townships. These townships concentrated largely in northern and eastern sections of the state have no local government. Transportation is generally over paper company logging roads, communication via state forestry department and paper company radio and telephone systems. The few year-round residents must look to the counties and State of Maine for education, police, fire, and highway services. However, only a small fraction of the roads is publicly owned and only a small number of children live in the area. As a result, property taxes are substantially lower in most unincorporated townships than those in incorporated towns throughout Maine. Thus, the landowners in much of northern and eastern Maine have avoided the high tax rate situation which exists in many of the cutover forested areas in the United States. In the South, the Lake States, and the Northwest, many families have built homes in remote areas and local governments have been forced to bring education, roads, and welfare services to them at a very high per capita cost. Maine's fortunate situation might change if, as a result of economic development, a large number of families established year-round residence in the area.

An important advantage of the existing situation in northern Maine is that all forest land is at least potentially productive. Most hydroelectric power developments would permanently inundate many thousands of acres

of forest land. Although this would create no immediate shortage of pulpwood, it could conceivably slow the growth of the pulp and paper industry in Maine in the long run. Some of the proposed reservoirs have the additional disadvantage of fluctuating substantially during the recreational season. These fluctuations would destroy much of the recreational, wildlife, and fishing potential of the reservoirs.

### **The Advantages of Development**

In the coming decades the wilderness character in northern Maine will almost certainly change. Higher incomes and the new interstate highway systems enable more people to travel to Maine each year. Already much of the land surrounding the more accessible lakes in the Maine woods has been leased or sold to a variety of summer residents including a large number of children's summer camps. Thus, northern Maine is beginning to help satisfy the rapidly growing outdoor recreation needs of the population of northeastern United States.

Gradually, also, the paper companies are increasing their cut of pulpwood. Although the annual cut on a 20-year cycle is still far less than the annual growth, in the future pulpwood harvesting will occur more frequently. Northern Maine will be helping to meet the Nation's growing needs for paper. However, the result will also be more logging roads and a more disrupted forest landscape.

Technology is also bringing changes. New engineering techniques for building dams and for moving electric power long distances have encouraged governmental and private groups to propose several large hydroelectric power projects for northern Maine. Each of these proposals calls for a high voltage transmission line interconnection between the utility systems of

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Maine and southern New England. In this manner power users throughout New England could benefit from what is thought to be northern Maine's low cost hydroelectric peaking power. Additional savings would be possible if utilities in Maine and southern New England could pool their efforts when they generate power with conventional steam plants. This cooperation would be facilitated if these groups of utilities were interconnected with a high voltage transmission line.

Northern and eastern parts of Maine are among the lowest income areas in New England. As a result, public pressure for economic development is becoming increasingly insistent. Recent Federal Government proposals for hydroelectric power installation are partially justified on the basis of area redevelopment benefits. Moreover, local interests are asking the State of Maine to build additional highways directly through parts of the Maine wilderness so that northern Maine can be directly linked to population centers in the Province of Quebec.

### **Comprehensive Planning**

Comprehensive planning for multipurpose development of land and water resources has been advocated since Theodore Roosevelt's Inland Waterways Commission Report in 1907 but has been more often discussed than acted upon. Unfortunately, the characteristics of land and water resources which make comprehensive planning desirable are also those which create difficulties.

The natural resources of any area can be developed for a variety of purposes. These purposes are sometimes complementary but they are often contradictory. Federal, state, and private agencies promote those projects

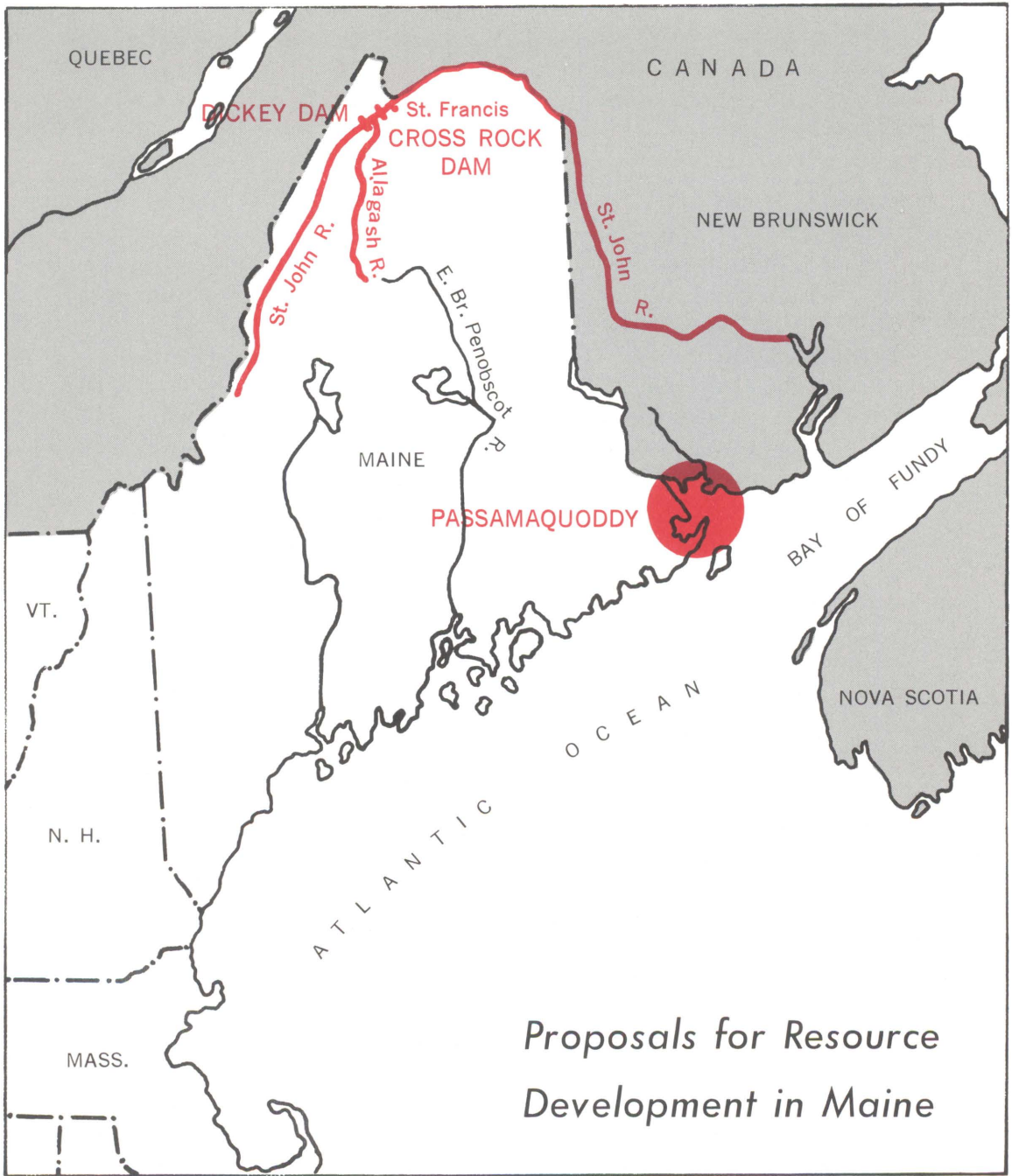
for which they have functional responsibility. They generally oppose those projects which will interfere with their assigned mission. Similarly, individuals and business support those agencies whose work benefits them; they naturally object to the work of an agency if it affects them adversely.

Thus, resource development planning generally takes place in a controversial environment. Development planning in Maine is no exception. As described below, three entirely different plans are now being promoted for development of northern and eastern Maine. The issue is whether any one of these plans is sufficiently comprehensive and efficient to deserve the support of the general public in Maine and in the Nation.

### **The Proposed Cross Rock Development**

A private engineering firm has proposed that the Maine legislature create a Maine Power Authority to construct a 450-foot-high conventional hydropower dam on the St. John River near the town of St. Francis, Maine. Total cost of the structure, power plant, and associated transmission lines to the New Hampshire border, as estimated by the promoters, would be \$220 million. The height of the dam and its location are important for several reasons:

- (1) Because of the substantial flow of water in the St. John River at this location, the Cross Rock project would have an installed capacity of 760,000 kilowatts of low cost peaking power and would produce something over 1.6 billion kilowatt hours of electrical energy annually. Much of this power is surplus to present needs in Maine and would be transmitted to benefit power users in southern New England. A by-product benefit of the project is that it would





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tie together with a high voltage transmission line the utilities of Maine with the Maritime provinces of Canada and southern New England. Moreover, the Maine Power Authority would be required to pay the State in lieu of taxes one mill per kilowatt hour generated, or approximately \$1.6 million annually.

(2) The proposed dam would largely control the flow of water in the upper reaches of the St. John River drainage basin. As a result, electric utilities and paper companies on the lower part of the St. John River in Canada would benefit from the controlled release of water for power generation purposes. In addition, minimum summer streamflows would be augmented so that pollution problems in Canada would be alleviated.

(3) At the same time the Cross Rock Dam proposed under the Maine Power Authority would create a large new but entirely different water recreational facility. The reservoir would be composed of two narrow interconnected bodies of water approximately 50 miles in length which would cover an area equivalent to about seven-eighths of the surface of Cape Cod. The shore line of this artificial lake would be about the same as the outer boundary of Cape Cod. Seasonal fluctuations in the water level would be minor and entirely compatible with the development of many types of fish, wildlife, and recreational areas. No provision is made for controlled development or zoning of any of the lands surrounding the reservoir. However, the proposal does call for a 20,000-acre park north of the dam site.

Finally, the proposal provides for developing a canoe trip which would link the headwaters of the St. John River with the east branch of the Penobscot River. The construction of two

check dams on the upper St. John River would make possible a combination of existing canoe trips. The dams would be operated so as to release enough water during the summer to provide in a wilderness environment a 215-mile canoe trip on lakes and streams with substantial portions of rushing water.

(4) The dam would inundate about 210,000 acres of land, 30,000 of which are now in lakes, streams, and swamps. Although the flooded land is less than 2 percent of the forested acreage in northern and eastern Maine, this reduction might possibly slow the longrun growth of the State's pulp and paper industry. There is controversy as to whether or not the reservoir would make it easier or more difficult to transport pulpwood from the forests of northwestern Maine to the pulp mills in central Maine.

(5) The proposed project would completely inundate the Allagash River. This river provides a nationally known canoe trip taken by over 1000 hardy sportsmen each year. While the Allagash River itself is only 65 miles long, the canoeist can travel more than 100 miles along a network of lakes, streams, and river with alternatingly placid and fast-moving water in a wilderness environment. The Cross Rock Development would mean giving up this unique recreational resource.

### **The Passamaquoddy-Dickey Proposal**

The United States Department of the Interior is responsible for Federal parks and recreation areas. It is also one of the agencies responsible for Federal power development. This Department has proposed a plan which would develop hydroelectric power *and* preserve the Allagash:

(1) The Federal plan calls for the development of a combination of two hydroelectric projects, one conventional river hydropower, the other tidal power, and a high voltage transmission tie to delivery points in Maine and southern New England at a cost of almost \$900 million. The tidal project would be a 500,000 kilowatt capacity dam and power plant at Passamaquoddy Bay in eastern Maine. The conventional hydro project would be located at the Dickey site on the St. John River *above* its confluence with the Allagash. When tied together the two projects would produce about 3 billion kilowatt hours of energy annually. Most of this power would be generated during the two late afternoon hours of each day when there is an abrupt peaking in household energy usage. It is improbable, however, that because of the high cost of the extensive network of dams this power can be produced at a cost competitive with other types of Federally financed power projects. As a future article will make clear, it would be substantially higher cost peaking power than that of Cross Rock or pump storage.

(2) The Dickey hydroelectric project would inundate almost 89,000 acres, most of it productive forest land. Moreover, the power pool would fluctuate up to 30 feet during the recreational season. Shoreline conditions would not be aesthetically pleasing and in general the reservoir would be unsuitable for fish or wildlife.

(3) A 150,000-acre "National Riverway" would be established on the land immediately surrounding the Allagash River. On this land road access would be carefully limited. Motorboats and airplanes equipped with floats or skis would be excluded. Although hunting and fishing would be permitted, no timber cutting or mineral development would be al-

lowed. Altogether the combined Dickey and National Riverway projects would withdraw more land from forest production than would the Cross Rock proposal.

The National Riverway proposal also authorizes the Federal Government to purchase a "scenic easement" zone for a distance of up to one-half mile outside the "Riverway." The private owners of this restricted land would be expected to continue their present policy of discouraging the general public, except hunters and fishermen, from using their lands. Only controlled timber cutting would be permitted to preserve the aesthetic characteristics of the wilderness.

#### Relying on New Technology

A third course of action for the development of northern Maine is advocated by some conservationists as well as by paper companies and private utilities. In general, this segment of the public opposes any public power development in northern Maine. The private companies generally oppose Federal land acquisition as well.

These groups point out that nuclear power generation is rapidly becoming the least cost way of providing baseload power in northeastern United States. Within about 20 years all additional baseload power in New England probably will be provided by nuclear reactors.

As the use of nuclear energy to generate base power increases, low cost nuclear power will gradually replace higher cost conventional plants, thus making available cheaper offpeak power for use in pump storage operations. During the early morning hours of each day regular residential, commercial, and industrial use of power always drops off rapidly. In the future, utilities will have the option of shutting

their reactors down during this period or, at a very small incremental cost, providing energy for the operation of pump storage generation plants. During offpeak periods water would be pumped to a high-elevation reservoir and stored for release through a turbine at a low-elevation reservoir to produce power at peak-load periods. Although energy is lost in the conversion of offpeak to peaking power (about three kilowatt hours of input for every two kilowatt hours of output), this new system will probably be the most inexpensive method of producing peaking power in the coming decades.

It is unlikely that conventional hydroelectric projects of the sort possible on the St. John will be economically justified in the coming decades. If they are to be justified, they will have to be built in the near future before these new low cost technologies are widely put into operation.

Generally, private utilities see no need for public power development. Similarly, paper companies oppose Federal land use restrictions in the same area. They question the need for substantial Federal ownership dedicated exclusively to wilderness recreation. They point out that foresters can arrange for selective cutting of timberlands and that as a result timber cutting leaves very little longrun impact on the forest landscape. They contend that most areas of forest land can be managed for multiple purposes — forest production, preservation of wildlife, and recreational uses. They further argue that wildlife is almost always more abundant in areas where timber cutting takes place than in areas where cutting is forbidden. The dense shade of permanently protected forest provides a poor habitat for most types of wildlife.

### **Comparing the Plans**

These three competing plans for the development of northern Maine are difficult to compare as each emphasizes benefits for a different segment of the public. A few observations are in order, however.

The third course of action based on new technology is not really a "plan." It points out weaknesses in the other plans and presents technical facts which are generally overlooked by partisan conservationists and supporters of public power projects. However, no mechanism is provided for tying together the utilities of Maine and southern New England with a high voltage transmission line. It provides no specific proposal for relieving the depressed conditions in northern and eastern Maine. Finally, it provides no scheme for bringing about an integrated or comprehensive development of the northern Maine wilderness. As mentioned earlier, recreational development, i.e., camps, cottages, summer homes, is now taking place in many of the fringe areas of the northern Maine woods without any overall development plan, highway and access plan, or zoning. In this way the wilderness atmosphere and scenic values in much of northern Maine may be gradually lost without any substantial benefits accruing to the area. The developments which take place in the years immediately ahead will probably set the tone for the economy of northern Maine in succeeding decades.

In many ways the Cross Rock proposal is the most interesting one. It provides for relatively low cost hydroelectric power and it proposes a large new supply of recreational water in a wilderness atmosphere. One weakness is that no specific provision is made for controlling



land use on the area surrounding the huge recreational reservoir. The most difficult question is whether in the long run the loss of the Allagash and almost 200,000 acres of forest land are more important than the shortrun power and development benefits and the longrun recreational benefits of the giant reservoir.

The Department of the Interior's plan is comprehensive in that it provides for power development, the preservation of a wilderness canoe trip, a high voltage transmission line tie to southern New England, and substantial

Federal construction expenditures which would help stimulate, at least temporarily, the depressed economy of northern and eastern Maine. The controversy regarding Interior's proposals relates to their efficiency and whether other Federally financed projects could accomplish many of the same objectives at a substantially lower cost.

Additional technical aspects of power development and forest and recreational planning will be discussed in future articles on "New England's Last Frontier."



# Stock Options For Bankers

In the industrial world stock options have for some time had their champions and detractors. This controversial method of executive compensation has been investigated but has never been widely used by the banking community. Among the more important factors to be considered by interested bankers are what the plan is intended to accomplish, how it is to be constructed, and what costs are involved as opposed to the alternatives for accomplishing these same objectives.

## **What Are Stock Options ?**

Stock option plans are designed to reward an executive's efforts by giving him an opportunity or "option" to buy ownership in the bank at what is intended to be a price less than the market value. Optionees, who are generally high-level executives, receive an allotment of shares that they may buy during the plan's 5-year term at the option price which is the market price on the date the option was granted. The optioned shares may be granted in lump sum or on an installment basis. This latter method allows the executive to buy his stock in equal allotments each year or to accumulate his allotment and purchase the stock at the end of the 5-year agreement. Hopefully, the market price of the stock will rise during this time permitting the executive to show an immediate paper profit on his investment.

For example, suppose a banker is granted the option to buy, within the next five years, 100 shares of his bank's stock at \$50 per share, the market price on the day the shares were optioned. If the price rises to, say, \$60, the banker will record a profit of \$10 per share by exercising

the option to purchase at \$50. Moreover, his profits are not taxed until he sells the stock and then only at the lower capital gains rate.

In the last session of Congress laws regarding stock options were tightened — largely due to widely publicized abuses outside the banking community. There is some evidence to suggest that the bloom has been partially removed from the stock option rose by these new, more stringent laws and by lower ordinary income tax rates. The new laws are framed with the idea that the device is a privilege which should receive special tax treatment only when used as a true incentive. Accordingly, under current provisions, to qualify for long-term capital gains tax treatment, the option price must be 100 percent of the market price when the option is granted instead of the more generous 85 percent which formerly applied. In addition, the option price may no longer be reset at a lower figure if the market price subsequently falls. The stock now must be held for at least three years, one year longer than under previous legislation. The term of the stock option agreement itself has been shortened from 10 years to 5 — thus reducing the span during which the executive might benefit from market appreciation. Finally, favorable stock option tax treatment has been denied to "substantial" stockholders — that is, those holding 5 percent or more of the voting stock.

## **What the Proponents Say**

Proponents of stock options argue that they provide important managerial incentives which will help to attract the best executive talent to the bank. They stress that executive stock



ownership encourages a proprietary interest in the business and creates a group of "owner-managers" rather than mere employees. In this way the stock option may be considered a partial substitute for the ownership incentives that originally created our free-enterprise system. Stock options offer the bank executive a new stimulus to grow with his bank and do so in a particularly attractive way since his eventual investment can be a hedge against inflation and a building block in his estate. In addition, judicious planning can defer the receipt of income to advantageous tax years.

At the same time, the bank need not incur additional overhead costs of heavy salary payments to retain its top management group. The employer can offer the stock option incentive and not pay it unless and until the executive has indeed improved the bank's profitability. Assuming that the stock's market price is a meaningful barometer of the executive's contribution — which it frequently is not — he would probably not be exercising his option until he had successfully performed as part of the bank's management. This incentive has been achieved at no cost to the bank until the stock's market price rises attractively above the option price and the option is exercised.

Moreover, the proponents believe that the individual bank is strengthened by having stock options as a tool for recruiting. They suggest that this incentive puts the bank in a better bargaining position to attract and keep able personnel. From the standpoint of the entire banking industry stock options are favored to enable banks to compete more vigorously with other industries for personnel.

Furthermore, for the smaller bank, stock options provide an opportunity to offer substan-

tial rewards to needed key executives without depleting necessary working funds. By using unissued stock the extra compensation can be paid without a drain on the bank's cash position.

#### What the Critics Say

On the other hand, critics voice doubts about the underlying justice of granting capital gains tax rates to an investment which involves no risk. Insofar as the optionee never has to pay the full market price for the stock and incurs no risk until after the option is exercised, they would say there is scant justification for the favorable capital gains treatment.

Opponents further contend that a bank's unique fiduciary relationship could be jeopardized by the use of stock options. They fear that profit-minded optionees might be tempted to make marginal loans or investments for speculative reasons. Officers might be too interested in increasing earnings, and thus the value of the bank's stock, at the expense of the quality of assets.

Another problem may arise when executives need to borrow money to pay for stock acquired under option plans. Bank stocks have not customarily been listed on securities exchanges; therefore, loans made by banks to finance purchases of stock by optionees are not subject to margin requirements. Imprudent use of borrowing by optionees is one of the dangers which must be considered in administering such programs.

Furthermore, it is difficult to establish the fair market value of a share of stock which is not actively traded as is the case with many bank stocks. Smaller banks in particular might encounter problems in establishing an option plan because of this dilemma of valuing the

stock. In cases where values are disputed the threat exists that at least some of the gains may be taxed at ordinary income tax rates.

Critics also argue that it often is difficult to pinpoint an individual executive's contribution or measure his impact on overall profitability. As such the option may have little value to the bank as a unique device for compensation. Even if a careful evaluation of the executive's performance can be made, the stock's market price may be reacting to a variety of national and industrial forces completely outside the optionee's control.

### Cost of Stock Options

Some critics point out that the twofold cost of stock options is not given proper consideration. In calculating these costs the significant date to consider is the earliest possible time the stock can be resold (three years) and still receive the favorable capital gains tax treatment. The difference between the option price and the market value of the stock in three years is one element of cost. This spread represents the amount of capital lost by selling the stock to the optionee rather than on the open market. This difference is *not* classified as a compensatory payment to the optionee, and no deduction is allowed on the bank's tax return. If the same amount had been paid to the executive as salary, however, it would have been deductible for income tax purposes. The critics would say that this second element of cost, the bank's loss of a 50-cent tax deduction for each dollar of stock option incentive should be added to the capital foregone to determine the total cost to the bank. As a result, the net cost of stock options to the bank can be greater than other forms of compensation.

Moreover, for most middle bracket executives stock options are rarely as rewarding as

other forms of compensation — such as bonus payments. Assuming that the net costs to the company are equal in both cases, these executives would receive more income after tax from cash payments than from stock options. Only if the executive has a taxable income of more than \$76,000 will he gain more after tax income with stock options than with cash.

To illustrate, assume that a key bank executive receives a salary of \$30,000. The bank may deduct salary payments from its taxable income. With the current 50 percent corporate tax rate, therefore, the net aftertax cost to the corporation of the executive's \$30,000 salary is, in effect, \$15,000.

Suppose that the bank wishes to provide an added incentive to the executive by granting him either a stock option or a cash bonus. The corporation foregoes a deduction amounting to 50 cents for each dollar of compensation paid through a qualified stock option. Accordingly, for each \$100 of compensation provided through such an option, the corporation could, at the same cost to itself, make a deductible salary payment of \$200. The question is which incentive provides a more handsome reward to the banker. Would he receive greater benefits from a stock option or from a cash bonus?

In the first instance let us assume that he receives stock option benefits of \$5,000 in addition to his \$30,000 salary and that he eventually pays a capital gains tax on the stock option benefits when he is still in the same \$30,000 bracket. In this example the executive would pay \$7,505 in taxes on his salary and \$938 in taxes on the stock option benefits. He enjoys \$26,556 of aftertax income.\*

\*These calculations are based on the assumptions that the taxpayer is married, files a joint return, and takes the standard deduction.



If instead of the stock option benefits he receives in addition to his \$30,000 salary a cash bonus of \$10,000 which could be paid at the same cost to the bank as \$5,000 of stock option benefits, he would pay ordinary income tax on the entire \$40,000. The result would be a tax bill of \$11,855 and a greater aftertax income of \$28,145. In this example, at the *same* net cost to the bank, the executive would receive greater benefits from the cash bonus alternative. Of course, the executive may choose to defer selling his stock until retirement years when a lower taxable income would result in a lower capital gains tax. For purposes of immediate income, however, the executive might well prefer a cash bonus.

Since cash bonus plans are less expensive for the company than stock option plans in the majority of cases, why are stock option plans still advocated? There seem to be several reasons. First, some companies may look at stock options as being almost costless since they do not involve a direct cash outlay. The stockholders are, in effect, giving up a share in the company in an indirect way rather than paying out cash directly. Thus, boards of directors may vote more readily for such a plan rather than commit the company to actual cash outlays.

Second, some executives may prefer option plans because they view their chances of gain as being greater than with bonus plans. Stock prices often rise even if profit levels do not increase, so the executive can make a good gain even if the company's profitability has not risen. This is especially likely in periods of general advance in stock prices as has occurred since 1950.

### Stock Options in Banking

Stock options are a relatively new phenomenon on the banking scene. It was not until 1962 that a regulation by the Comptroller of the Currency allowed national banks to use the stock option device. Available evidence suggests that they are, as yet, infrequently used. A nationwide survey in 1963 showed that only 15 of 6,000 national banks had adopted a stock option plan. There seems to be little increase in the number since that time. In New England, for example, one national bank in central Massachusetts is the only bank with a stock option program for its executives.

This same pattern is found among state-chartered banks. Laws permitting these banks to adopt stock option programs have been passed by nine states — Connecticut, Indiana, Massachusetts, Michigan, Missouri, New York, North Carolina, Pennsylvania, and Utah. Of the nine states with specific authorizing legislation, only four have banks with option plans. Missouri leads with seven plans, Michigan and New York follow with three each, and Indiana reports two. Although two New England states, Connecticut and Massachusetts, pioneered with stock option legislation passed in 1958 and 1961 respectively, no New England state-chartered bank has as yet adopted a stock option plan.

### Stock Plans in Operation in New England

Some banks use stock plans without the option feature. A small state bank in Maine, for example, has an informal system which allows officers to buy stock at a price set below the book value. A national bank in New Hampshire has adopted an employee stock purchase plan open to all officers and employees. Under this program all participants are permitted to buy annually, at 85 percent of book

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or market value — whichever is greater — one share of stock for each \$500 of salary.

The only full fledged bank stock option plan in New England was adopted in January 1964 and is designed primarily as an incentive for the existing top management group. Participation is limited to a small nucleus of officers who form the high-level management of the bank. Its usefulness for recruiting is a secondary and minor consideration.

To implement the plan the stockholders approved an increase of 20,925 shares of authorized capital stock, 5 percent of the bank's common stock, with a par value of \$10 per share. The stock's option price, or fair market value, was set at the midpoint between the "asked" and the "bid" price on the day of the agreement. To date, approximately one-third of the stock has been allotted to the participants. There have been, as yet, no purchases under this relatively new plan.

In an interview an officer expressed concern about the new tax laws which have removed five years of potential market appreciation from the option's life. However, he remained confident that the option plan provided an invaluable incentive for the key management group to remain with the bank and to make

even greater efforts toward the bank's success.

### **The Alternatives**

Deciding for or against stock options is not a simple matter. The complexities of such plans often match the complexity of the purposes for which their use is intended. However, it remains clearly evident that they may be a costly way of providing management incentive. The need for incentives to attract superior bank management is apparent; however, the use of stock options to provide these incentives may be hard to justify on a cost basis.

The interested banker, spurred by the cost and uncertain tax future of stock options, must consider the available alternatives for accomplishing the same objectives. For instance, cash bonuses, which can be deducted from the bank's tax liability, could be awarded to the executive. As shown in the calculations above, a cash payment would result in more immediate income to the executive than comparable stock option benefits unless his present taxable income is above \$76,000. According to the *Wall Street Journal*, programs of cash incentives are enjoying increasing popularity among industrial concerns. This trend could well be repeated in the banking community.



# Here's New England -

MANUFACTURING INDEXES (seasonally adjusted) 1957-59 = 100	NEW ENGLAND			UNITED STATES		
	pJuly '64	June '64	July '63	July '64	June '64	July '63
All Manufacturing	122	121	120	134	132	126
Nonelectrical Machinery	131	131	125	143	142	127
Electrical Machinery	129	129	129	139	137	133
Transportation Equipment	132	140	145	134	135	128
<i>Textiles, Apparel, Leather</i>	103	101	104	125	123	119
Textiles	103	101	110	122	119	118
Apparel	109	107	104	135	134	126
Leather and Shoes	99	96	96	n.a.	97	100
Paper	118	115	116	132	130	126
	<u>Percent Change From:</u>			<u>Percent Change From:</u>		
<b>BANKING AND CREDIT</b>	July '64	June '64	July '63	July '64	June '64	July '63
Commercial and Industrial Loans (\$ millions) (Weekly Reporting Member Banks)	1,820	+ 1	+11	38,614	0	+10
Deposits (\$ millions) (Weekly Reporting Member Banks)	5,560	+ 1	+ 8	142,874	+1	+ 7
Check Payments (\$ millions) (Selected Cities)	12,910	+ 3	+ 6	208,258	+3	+10
Consumer Installment Credit Outstanding (index, seas. adj. 1957-59 = 100)	145.6	0	+ 8	167.1	+1	+11
<b>DEPARTMENT STORE SALES</b> (index, seas. adj. 1957-59 = 100)	128	+ 7	+ 8	n.a.	n.a.	n.a.
<b>EMPLOYMENT, PRICES, MAN-HOURS &amp; EARNINGS</b>						
Nonagricultural Employment (thousands)	3,890	0	+ 1	58,968	-3	+ 3
Insured Unemployment (thousands) (excl. R.R. and temporary programs)	122	+13	-10	1,368	+4	-11
Consumer Prices (index, 1957-59 = 100) (Mass.)	110.6	+ 1	+ 2	108.3	0	+ 1
Production-Worker Man-Hours (index, 1957-59 = 100)	94.0	- 2	- 1	104.1	-1	+ 2
Weekly Earnings in Manufacturing (\$) (Mass.)	94.16	- 1	+ 4	102.97	-1	+ 4
<b>OTHER INDICATORS</b>						
Total Construction Contract Awards* (\$ thous.)	240,524	- 6	- 6	4,581,595	+2	+ 3
Residential	106,982	- 5	+13	2,015,569	0	+ 1
Nonresidential	77,688	- 7	-13	1,436,669	+3	+ 3
Public Works and Utilities	55,854	- 8	-21	1,129,357	+4	+ 5
Electrical Energy Production (4 weeks ending July 11, 1964) (index, seas. adj. 1957-59 = 100)	147	+ 4	+ 7	155	+3	+11
Business Failures (number)	56	- 7	+10	1,096	-5	- 5
New Business Incorporations (number)	990	-11	- 2	17,145	+2	+ 7
*3-mos. moving averages May, June, July						
	p = preliminary			n.a. = not available		

