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## The National Center for Employee Ownership

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## Comments on proposed accounting standards for employee stock purchase plans and broad-based equity plans

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The National Center for Employee Ownership (NCEO) is a private, non-profit information, research and membership organization. We do not lobby or take positions on regulatory or legislative issues. The NCEO takes no formal organizational position on accounting for equity compensation, Instead, I am writing in my capacity as director to review the research on ESPPs and other forms of broad-based equity and how companies use them in the hopes that this may be useful in your deliberations.

The NCEO estimates that approximately 15 million employees participate in ESPPs. These estimates are consistent with estimates from Joseph Blasi and Douglas Kruse of Rutgers University using a somewhat different technique. Other estimates put the number within 20% of this figure one way or another.

In addition, we estimate that about 10 million employees currently have stock options, although only a third of that number get them annually. However, the General Social Survey of the National Opinion Research Center estimated this year that 14 million employees currently have stock options. A variety of surveys of public companies indicate that about 15%, give or take a few percent, provide options to 50% or more of their full-time workers. Note that this is different than making employees eligible for options; many more companies do that, but do not necessarily ever grant them to everyone who is eligible.

While most technology companies have these plans, just 10% to 12% of non-technology companies have them. In companies that do grant options broadly, an average of about 30% of all options go to nonmanagement employees. There is some industry variation, but not as much as many expect. Technology companies with broad option plans, for instance, provide 33% of options to non-management employees. By management, we mean any employee with supervisory responsibilities. Senior executives (including, but not limited to, the top five officers) get about 40 times as many options as hourly non-technical employees and four times as many as middle managers.

ESPPs are, of course, quite different, in that by law they must be non-discriminatory and broad-based. Employees and companies see them more as an employee benefit and a way for employees to buy into the company than as a way to make potentially very leveraged returns on stock growth. Almost all the ESPP companies we surveyed have a look-back period, with 46% having a six-month period, 11% three months, 12% twelve months, and 22% twenty-four months. 86% of respondents offer a 15% discount off the lower of the price at the beginning or end of the offering period. Participation is high, with 44% of hourly employees deferring an average of 5.6% of pay, and 55% to 65% of other categories of employees deferring 7% to 9% of pay. Contrary to popular belief, employees at all levels have similar holding periods for the stock post-exercise, with the median just under one year for most employees. Only senior executives and senior managers hold on longer (22 months).

Surveys indicate that about half of all companies will reduce their broad-based option plans and about half will cut back the benefits of ESPPs if they have to expense these plans. Actual experience after expensing will probably be somewhat less, but still significant.

Research is also very clear that broad-based ownership plans improve corporate performance. In stark contrast, plans focused on senior executives are unrelated or negatively related to corporate performance, according to most studies. Yet the surveys also shows that companies do not plan major changes in the magnitude of executive equity compensation post-expensing.