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Employee Ownership

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Executive Summary

Survey on the Perceived Value of Stock Options

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**For questions regarding this document or the NCEO's employee surveys, contact
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Survey Overview & Summary

This report summarizes the results of the Perceived Value of Stock Options Survey. The purpose of the research is to explore the beliefs of companies with stock options about the gap between the perceived value of options (in the eyes of employees) and their actual value, as well as companies' level of interest in closing this gap through education.

The impetus behind this research is an academic report that found that executives dramatically undervalue (by 50% on average) their employee stock options relative to the Black-Scholes value of those options. The report explored the role of education in closing this cost-value gap. (A summary of the research is at: <http://ssrn.com/abstract=906020>.)

This research has been financially supported by generous contributions from Ameriprise Financial. In-kind and logistical support was provided by Net Worth Strategies, which also provided invaluable expertise in the design of the questionnaire.

Method

Two versions of the survey were used: one for companies with stock option plans, and the second for service providers to such companies. The surveys were hosted online and responses were collected in a secure database.

A pilot version of each study was posted and invitations issued by Net Worth Strategies. Data was collected using this pilot survey from August 16 to September 4, 2006. Based in part on responses to the survey, the text of the surveys was edited for use in the main wave of the study.

The main wave of data collection took place from September 6 to September 19, 2006. For the main wave, the NCEO emailed all eligible members of its customer database. Eligible recipients:

- Have an interest in stock options
- Have a valid email address
- Have not requested to be exempt from non-core business emails

To the extent possible, the data from this pilot wave of data collection were used in this report. The actual surveys, including the changes made between the pilot wave and the main wave, are in the full report.

As an inducement to complete the survey, potential respondents were offered both a \$10 Starbucks gift card and a copy of the survey results. The gift cards were provided by Ameriprise (for issuer company respondents) and by Net Worth Strategies (for service provider respondents).

Response Rate

The responses for each wave and each survey is in the table below.

Table 1: Responses by wave.

	Companies with Stock Options	Service Providers	Total
Pilot wave	26	15	41
Main wave	77	55	132
Total	103	70	173

Training and Retention

Respondents strongly believe that their option programs are effective at retaining executives, with only 3% of company respondents describing their option program as “not at all effective.” At the same time, only 20% see their programs as “very effective.” The full results are in the top row of **table 2**, below.

To explore further the role that current training programs play in making options more effective at retention, question 7 asks about the extent to which companies provide training. The majority (53%) provide none, and only 11% provide more than an hour of training per optionee per year. The companies’ current training practices do appear to make a difference in the perceived effectiveness of options as a tool for retention, although the difference is not dramatic, as shown in the bottom half of **table 2**.

Table 2: Question 6 (“How effective would you say your options program is at retaining executives?”) crossed with question 7 (“To what extent does your company currently provide training for option holders in understanding the value of options?”)

	Count	Not at all effective	Rather ineffective	Moderately effective	Very effective
All companies	97	3%	17%	59%	20%
Companies with:					
No training at all	51	6%	18%	55%	22%
One hour or less per employee per year	35	0%	17%	69%	14%
More than one hour of training per year	11	0%	18%	45%	36%

Credibility and Applicability of Prior Research

A brief overview of the research cited on page 3 of this report was included with the invitation to participate in this questionnaire, and respondents were asked about their perceptions of that research along two lines. First, question 8 (question 2 in the survey for service providers) asks how credible they believe the results are. Second, question 9 (company respondents only) asks respondents if they believe the results would apply to their companies.

Seventy percent of both company and service provider respondents feel that “these findings seem credible,” indicating that two-to-one majorities of both groups believe in both the existence of the cost-value gap and in the potential of education to close that gap. Only 6% of company respondents and 1% of service provider respondents believe that the research is “probably exaggerated or biased,” with the balance (25% of companies and 29% of service providers) feeling that the increase in perceived value from education “is probably less than indicated.”

Company respondents also indicate that they believe the research results would be duplicated at their companies. Seventy-seven percent of them believed it is “somewhat” or “highly” likely that “similar results would be experienced at [my] company.” Notably, people working in compensation and benefits are least likely to believe the results would apply at their companies, and HR directors / vice presidents are most likely. (For the full results of this item, see that data chart for item 9 in the full report.)

Closing the Gap

The survey asked respondents how likely different groups are to be interested in reducing the cost-value gap through education, rating their interest on a 5-point scale from “no interest” to “high interest.” According to both company respondents and service providers all groups are likely to have relatively high levels of interest, with one exception: both groups perceive institutional investors as least likely to be interested, and both groups rate institutional investors’ interest as below the mid-point score (a 3). Both groups also agreed in ranking HR executives as having the greatest interest.

The rankings of the groups are in **table 3**.

Table 3: Question 10 (for companies) and 3 (for service providers): “Assuming the research findings are valid, what level of interest is each of the following parties likely to have in closing the ‘cost-value gap’ through effective education?”

	As Ranked by Company Respondents	As Ranked by Service Providers
Greatest interest	HR Executive	HR Executive
Second	Stock Plan Administrator	Chair of Compensation Committee
Third	Corporate Officer	Corporate Officer
Fourth	Chair of Compensation Committee	Stock Plan Administrator
Least Interest	Institutional Investors	Institutional Investors

Drivers of Education Programs

The research project is also designed to explore what factors have the greatest effect on company motivation to undertake education about stock options. Both company respondents and service providers see the top motivator as retention. The two lowest-ranked items are “company responsibility to shareholders” and “consultant recommendation or industry endorsement.”

The rankings of the motivations are in **table 4**.

Table 4: Question 11 (for companies) and 4 (for service providers): “To what extent would the following factors make your company more likely to decide to provide effective stock option education?”

	As Ranked by Company Respondents	As Ranked by Service Providers
Greatest likelihood	Increase employee retention	Increase employee retention
Second	Increase employee motivation	Maintain competitiveness of equity compensation program
Third	Provide better equity compensation information	Increase employee motivation
Fourth	Maintain competitiveness of equity compensation program	Provide better equity compensation information
Fifth	Enhance the company’s ownership culture	Enhance the company’s ownership culture
Sixth	Responsibility to shareholders	Consultant recommendation / industry endorsement
Least likelihood	Consultant recommendation / industry endorsement	Responsibility to shareholders

Effect of Education Programs

If companies and service providers believe that option programs can be made substantially more effective through the use of education, their reaction is difficult to predict. They may believe that they can use fewer options to attain the effects they currently are, or they may take advantage of the increased effectiveness of options and increase their use.

The questionnaire asked both company respondents and service providers how an effective options education program would change their use of options. This item is exceptional in that the service providers and company respondents provide substantially different answers. The near-unanimous opinion of company respondents is that they would grant the same number of options. A slim majority of providers take the same position, but over a third, including a large number of CPAs, said that their client companies would “increase their use of options relative to stock.” In addition, one in seven feel that their clients would “grant fewer options.”