**Employee Share Ownership Project**

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**Research Report**

# BROAD-BASED EMPLOYEE SHARE OWNERSHIP IN AUSTRALIAN LISTED COMPANIES:

# SURVEY REPORT

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**Ingrid Landau, Richard Mitchell, Ann O'Connell, Ian Ramsay and Shelley Marshall**

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The Employee Share Ownership Project is a joint initiative of the Centre for Corporate Law and Securities Regulation, the Centre for Employment and Labour Relations Law and The Tax Group at the Melbourne Law School. It is funded by an Australian Research Council Discovery Project Grant.

The project subjects the existing regulatory regime for employee share ownership plans in Australia – in tax, corporate and labour law – to technical and empirical scrutiny. It analyses how current legal regulation structures and constrains the use of ESOPs in Australian enterprises. It examines the current incidence and forms of ESOPs in Australia, the diversity of objectives that such schemes serve, the extent to which current corporate, tax and labour law inhibit ESOPs, and the case for reform of the regulatory framework.

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Employee Share Ownership Project

Melbourne Law School

The University of Melbourne

Victoria

Australia 3010

Phone: + 61 3 8344 1089

Fax: + 61 3 8344 5285

Email: law-esop@unimelb.edu.au

Website:http://cclsr.law.unimelb.edu.au/go/centreactivities/research/employeeshare-ownership-plans-current-practice-and-regulatory-reform

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## EXECUTIVE SUMMARY

This research report presents findings from a survey of employee share ownership practice in ASX-listed companies. The survey was administered by phone, internet and mail-out. It focused on broad-based employee share ownership plans (ESOPs): that is, plans that are open to a majority of employees within the company.

The purpose of this study was fourfold:

- to inform public policy debate on the issue of employee share ownership through providing, for the first time, a detailed account of employee share plan practice in companies listed on the Australian Securities Exchange (ASX);
- to examine how, if at all, the regulatory framework in taxation and corporate law is impacting upon the decision by companies to implement ESOPs and the design of their plans;
- to obtain company views on the adequacy of the current regulatory framework; and
- to test a range of hypotheses as to the determinants of ESOPs in the Australian context.

Key findings as to company practice include:

- Approximately 57 percent of companies responding to the survey had at least one broad-based employee share ownership plan.
- Significantly more companies reported having a broad-based plan than a narrow-based plan: that is, a plan that is only open to executives.
- The three most popular reasons for implementing a plan were ‘showing employees the company values them’; ‘sharing financial success with employees’; and ‘aligning employee interests with shareholder interests’.
- Over three quarters of companies that have a broad-based plan have adopted their plan since 2000.
- The most common type of broad-based ESOP was the plan structured to take advantage of the $1000 tax exemption in Division 13A of the *Income Tax Assessment Act 1936.*

- The most common type of equity offered under broad-based ESOPs was options (48.7 percent of plans), followed closely by shares (46.7 percent of plans).
- The majority of broad-based plans require a monetary contribution from the employee in order to participate.
- Employees and/or their representatives are rarely involved in the design or administration of plans; and
- Regulation in corporate and tax law appears to be more important in influencing the design of plans than in influencing the initial decision by a company whether or not to introduce a plan.

In relation to the impact of the regulatory framework, a key finding of this study is that the concessional framework in taxation law appears to have a significant – though far from overwhelming – impact on ESOP practice. Just over a third of companies believed that the availability of tax concessions influenced their decision to introduce an ESOP and around 45 percent of companies believed that the tax concessions influenced how they structured their ESOP. The corporate law framework also had a significant impact, though weaker than the taxation concessions. Around a quarter of companies surveyed believed that the relief from disclosure requirements offered by ASIC influenced their decision to both introduce an ESOP and the design of their ESOP.

This study found that many listed companies view the existing regulation of ESOPs in taxation law as constraining. Over three quarters of companies surveyed agreed that the $1000 tax concession currently available should be increased. There was also strong support for the proposition that tax deferral plans should, like exempt plans, be eligible for capital gains tax (CGT) treatment. There was also strong support for the proposition that all regulation of ESOPs should be brought together under a single piece of legislation. Our data on company views revealed a tension between the desire among many companies for clearer and simpler regulation in this area and a reluctance to encourage more business regulation. Nonetheless, there was considerable support for unifying and simplifying existing rules.

Finally, this study examines a range of hypotheses, drawn from the international literature, relating to the determinants of employee share ownership plans. International studies have identified a number of structural variables that are associated with the presence of an employee share plan. The majority of hypotheses were not confirmed by this study. It is important to note that in most cases, the hypotheses were neither affirmed nor disaffirmed. Rather, the sample size was too limited to draw conclusive results. Nonetheless, three structural characteristics were found to have a significant and positive association with the presence of an employee share ownership plan. These were the presence of a centralised human resource function; company growth over the preceding 12 months (measured by the number of employees); and the composition of the workforce (the proportion of full-time to part-time and casual employees). We also found that companies with broad-based ESOPs were significantly more likely to have structures for communicating directly with employees.

# 1. INTRODUCTION[*]

Employee share ownership has long featured as a popular form of remuneration and reward for company executives. In more recent years, public policy interest has focused on the potential benefits of extending employee share ownership participation to non-executive employees through the use of 'broad-based' employee share ownership plans (ESOPs). There is now a considerable body of literature identifying, and evaluating, the potential benefits of ESOPs for companies, participating employees and society more broadly. [1]

Over the last decade, prominent figures on both sides of Australian politics have voiced a commitment to promoting broad-based employee share ownership.[2] In 1999, the then Minister for Employment and Workplace Relations, Peter Reith, requested the House of Representatives Standing Committee on Employment, Education and Workplace Relations to inquire into the extent to which employee share ownership schemes had been established in Australian enterprises and the resultant effects on workplace relations and productivity in enterprises, and the economy.[3] The Committee, chaired by Brendan Nelson MP, produced two reports - a Majority Report and a Dissenting Report from the Australian Labor Party committee members. The Majority Report, *Shared Endeavours*, recommended a raft of regulatory changes, many directed at reform of the corporate and taxation law framework underpinning employee share ownership in Australia. In its response to this report, the then Liberal/Coalition Government decided against adopting most of the report's recommendations, instead proceeding to pursue its objective of doubling the incidence of employee shareholders in Australia through the establishment of a promotional unit within the

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[*] The authors thank Malcolm Anderson for statistical analysis. The authors also thank Joe Tropeano for his comments on an earlier version of this report.

[1] For a review of this literature, see I Landau, R Mitchell, A O'Connell and I Ramsay, 'Employee Share Ownership: A Review of the Literature' (Research Report, Employee Share Ownership Project, Melbourne Law School, The University of Melbourne, March 2007).

[2] See, eg, Wayne Swan (then Shadow Treasurer), Keynote Address to the Labor Business Forum: Australia's Economic Future, 19 September 2006; for support by former Coalition ministers, see Peter Reith, Minister for Employment, Workplace Relations and Small Business, 'The Role of Employee Share Ownership in the New Workplace', Address to the Australian Employee Ownership Association Breakfast Briefing, Canberra, 29 June 1999; and Tony Abbott, Address to the CEDA/ Telstra Political and Economic Overview Conference, 2 February 2001.

[3] House of Representatives Standing Committee on Employment, Education and Workplace Relations, *Shared Endeavors - an Inquiry into Employee Share Ownership in Australia (Majority Report)* (2000) (hereinafter *Shared Endeavours)*, [1.2].

former Department of Employment and Workplace Relations (DEWR) and through relatively minor reforms to the legislative framework.[4] This promotional unit ceased to operate in 2007.

The extent to which the current Labor Government supports employee share ownership among non-executive employees is unclear. Nonetheless, calls for further reforms in this area persist. There continues to be a national association (the Australian Employee Ownership Association) and a corporate network (the Employee Ownership Group) dedicated to promoting regulatory reform in this area.

A recurring theme in Australian public policy debates over the desirability of, and need for, further legislative reform to employee share ownership regulation is the lack of reliable and comprehensive data on current practice. In 2000, *Shared Endeavours* observed that little is known in Australia about the nature, size and extent of employee share plans in Australia, and that this absence of consistent and reliable information was a major challenge facing the inquiry.[5] Almost a decade later, there remains a dearth of detailed data on company objectives and practice in this area. Yet such information is critical if the need for further legislative or public policy initiatives is to be evaluated.

This report seeks to inform public policy debate on the issue of employee share ownership by providing, for the first time, a detailed account of employee share plan practice in companies listed on the Australian Securities Exchange (ASX). It focuses on *broad-based* employee share ownership plans: that is, plans that are open to the majority of employees within the company, not just to executives. It presents detailed information on company objectives, current practice and the views of company representatives on the regulatory framework. It also examines the extent to which employees are involved in the design and ongoing administration of these plans.

The ASX listed sector is an important sample group, even though it only constitutes less than 0.5 percent of companies in Australia.[6] First, existing research suggests that publicly listed companies

[4] See Peter Costello MP, Treasurer, 'Government Response to Shared Endeavours: An Inquiry into Employee Share Ownership in Australia,' available at www.treasurer.gov.au (last accessed 17 April 2008); and Kevin Andrews MP, Minister for Employment and Workplace Relations, 'Media Release 04/104 – Promoting Employee Ownership' (2004).
[5] *Shared Endeavours*, above n 3, xxvi and 18.
[6] Approximately 0.13 percent, based on an approximate 2000 ASX-listed companies (the precise number varies frequently). As of November 2007 (when this survey was undertaken), there were 1,598,847 companies registered in Australia: ASIC, *2007 Company Registration Statistics* *http://www.asic.gov.au/asic/asic.nsf/byheadline/2007+company+registration+statistics?openDocument* (last accessed 25 January 2009).

are significantly more likely to have employee share ownership plans.[7] The relatively high incidence of employee share ownership in this sector enabled us to gather detailed data on share plan practice. Second, companies listed on the ASX tend to be more visible and are more often the focus of public interest than other companies. They also tend to be at the forefront of the adoption of innovative and strategic remuneration practices.[8] It is important to note, however, that these findings, and the implications we draw from them, are largely restricted to this sector. Australia's listed sector is generally characterised by relatively dispersed shareholding: in contrast to other sectors in which there may be more concentrated shareholding and possibly more employee ownership.

This report forms part of a broader project on employee share ownership at The University of Melbourne Law School. This three-year project, funded by the Australian Research Council, is a joint initiative of the Centre for Corporate Law and Securities Regulation, the Centre for Employment and Labour Relations Law and The Tax Group. The project subjects the existing regulatory regime for employee share ownership plans in Australia – in tax, corporate and labour law – to technical and empirical scrutiny. It seeks to analyse how current legal regulation structures constrain the use of ESOPs in Australia. This involves examining the current incidence and forms of ESOPs in Australia, the diversity of objectives that such schemes serve, the extent to which current corporate, tax and labour law inhibits ESOPs, and the case for reform of the regulatory framework.[9]

The report is structured as follows: Part 2 provides an overview of existing empirical research into ESOPs in Australia. It also provides a brief sketch of the current regulation of employee share plans. In Part 3, we outline the methodology used in this study. Part 4 presents the basic characteristics of the sample group. Part 5 reports on the incidence of employee share plans, and on the key design features of these plans. Part 6 presents findings on respondent's views on the adequacy of the current regulatory framework. In Part 7, we test a number of hypotheses on the

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[7] R J Long and J L Shields, 'Performance Pay in Canadian and Australian Firms: a Comparative Study' (2005) 16 *International Journal of Human Resource Management* 1783; and A Pendleton, E Poutsma, J Van Ommeren and C Brewster, 'The Incidence and Determinants of Employee Share Ownership and Profit Sharing in Europe' in T Kato and J Pliskin (eds), *The Determinants of the Incidence and the Effects of Participatory Organisations*, 2003: 141, 164; and TNS Social Research, 'Employee Share Ownership: Executive Summary' (Research report commissioned by the Department of Employment and Workplace Relations, 2004)(hereinafter 'ESODU research').

[8] Pendleton et al, 'The Incidence and Determinants of Employee Share Ownership and Profit Sharing in Europe', above n 7, 164.

[9] More information on the Employee Share Ownership Project may be found at: http://cclsr.law.unimelb.edu.au/go/centreactivities/research/employeeshare-ownership-plans-current-practice-and-regulatory-reform

determinants of employee share ownership plans, drawn from the international literature. We conclude in Part 8 with some broad observations from our study.

## 2. BACKGROUND

### 2.1 Existing studies

This research is informed by, and builds upon, the small body of existing empirical studies on employee share ownership in Australia. Over the past decade, several private consulting companies have conducted surveys of employee share ownership practice. In 2003, KPMG surveyed 800 Australian businesses, focusing on all employee share plans, not just broad-based ones. It observed the characteristics of ESOP companies; the types of plans; reasons for plans; hurdles to creating and administering plans; perceptions of board or management on the effect of ESOPs on employee behaviour and attitudes; and reasons for implementing or rejecting plans.[10] Remuneration Planning Corporation (RPC) also carried out analyses of employee share plan practices in 1995, 1997 and 1999, based on publicly disclosed information from Australia's top 350 public listed companies.[11] Limited information is also available from the 1990 and 1995 Australian Workplace Industrial Relations Survey (AWIRS) data, which was collected from private sector workplaces with 20 or more employees.[12]

The most recent data on employee share ownership in Australia was published in 2004. The first study, commissioned by DEWR's Employee Share Ownership Development Unit (ESODU), involved in-depth interviews with advisors, human resource managers and business owners in businesses with and without ESOPs; case studies of businesses with ESOPs, including interviews with CEOs, senior managers, human resource managers, finance officers and employees; and, finally, a quantitative survey of 1000 sample businesses.[13] The survey was limited to businesses with five or more employees and stratification included business size and major industry groups. The survey covered a number of issues associated with employee share ownership, including incidence; level of awareness; reasons for implementing ESOPs; barriers to take up of ESOPs; effects of ESOPs**;** and effectiveness of plans in relation to their objectives. Also in 2004, the Australian Bureau of Statistics (ABS) measured the incidence of employee share ownership using

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[10] KPMG, 'Employee Share and Option Schemes Survey Report' (August 2003).
[11] See, eg, RPC survey, cited in *Shared Endeavours,* above n 3, 24.
[12] A Morehead et al, *Changes at Work: The 1995 Australian Workplace Industrial Relations Survey* (1997).
[13] ESODU research, above n 7.

statistics compiled from the *Employee Earnings, Benefits and Trade Union Membership Survey*, conducted as a supplement to the ABS monthly *Labour Force Survey* (LFS) in August 2004.[14]

While the studies identified above have provided important insights into the extent and nature of employee share ownership in Australia, many important questions remain unanswered. These include, for example, details of the type of plans in operation; the extent of company and employee contributions; and common vesting restrictions placed on employee securities. There is also no information available on the extent to which employees and their representatives play a role in driving and shaping practice in this area. This report seeks to address these existing gaps in the research. Where possible, we make reference to existing studies in this report insofar as they confirm or disaffirm our own findings.

### 2.2 The regulatory framework

One of the key objectives of this research was to examine the influence of the current regulatory framework in taxation and corporate law on the decision to implement a plan and the design of the plan. We also sought to obtain company views on the adequacy of the current framework.

The main public regulation of employee share ownership in Australia is found in the area of tax concessions.[15] The general rule governing the taxation treatment of employee shares is that the issuing of shares or rights under an employee share scheme is treated as a substitute for cash income for services. Tax is imposed, at marginal income tax rates, at the time the share or right is acquired. The amount to be included in the employee's assessable employment income is the difference between the market value of the share or right and any consideration provided: that is, the amount of the discount provided to the employee or service provider.[16] Division 13A of Part III of the *Income Tax Assessment Act 1936* (Cth) (the ITAA 1936) provides two alternative concessions from the existing income tax regime for broad-based employee share ownership plans. The first type of concession allows for discounts of up to $1000 to be provided tax free to an employee per income year (the *exemption concession*). The second type of concession allows for tax on the discount to be deferred for up to 10 years (the *deferral concession*). In order to be eligible for either concession, the shares or rights issued under the ESOP must satisfy a number of conditions, including:

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[14] Australian Bureau of Statistics, *Spotlight: Employee Share Schemes,* Australian Labour Market Statistics, Cat. No. 6105.0, 2005.

[15] For a more detailed discussion of the history of, and current, taxation laws relevant to ESOPs, see A O'Connell, 'Employee Share Ownership Plans in Australia: the Taxation Law Framework' (Research Report, Employee Share Ownership Project, March 2007).

- the share must be in the company which is the employer of the taxpayer or in the holding company of the employer company. The concessions are not available if the recipient is not in an employment relationship (i.e. if the person is not engaged under a contract of employment in the strict sense, but is, for example, a contractor), or if shares or rights are acquired by an associate of an employee, or if the shares are shares in an unrelated company;

- the share must be an ordinary share and the right must be a right to acquire an ordinary share;[17]

- in the case of shares, at least 75 percent of 'permanent employees' must be entitled (or have been entitled) to participate in this or another employee share scheme. Permanent employees are those employed full-time or permanent part-time with 36 months prior service;

- the employee's legal or beneficial interest in shares of the company must not exceed 5 percent; and

- the employee must not be in a position to control more than 5 percent of the votes that could be cast at a general meeting of the company.

Companies may, of course, issue securities under a non-qualifying ESOP, the effect of which is that employees are taxed immediately at their marginal tax rate on the market value of the ESOP benefit as it is received.[18]

Another source of regulatory constraint on employee share ownership is found in corporate law.[19] Here, a range of provisions directed principally at protecting investors in relation to public share offerings also apply to the issuing of securities to employees under ESOPs. The Australian Securities and Investments Commission (ASIC) has issued a Regulatory Guide and Class Order, the effects of which are to provide to companies some relief from a raft of fundraising, licensing and hawking provisions in the *Corporations Act 2001* (Cth).[20] This relief is offered, according to ASIC, in recognition of the fact that the primary objective of employee share ownership plans is to foster

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[16] Sections 139B(2) and 139CC(2) ITAA 1936.
[17] The definition of 'ordinary share' for the purpose of employee share ownership plans now includes 'stapled securities'.
[18] Section 139B(1) ITAA 1936.
[19] For a detailed discussion of the corporate law framework underpinning employee share plans in Australia, see I Landau and I Ramsay, 'Employee Share Ownership Plans in Australia: the Corporate Law Framework' (Research Report, Employee Share Ownership Project, March 2007).
[20] See Regulatory Guide 49 (RG 49) and Class Order 03/ 184.

the ongoing and mutually interdependent relationship between employer and employee rather than fundraising.[21] Class Order relief is subject to a number of conditions, including:

- that the shares or options are issued free or for nominal consideration;
- a 5 percent cap on the number of shares that can be issued as part of an ESOP;
- offers under the ESOP are made to full-time or part-time employees;[22] and
- adequate disclosure is provided to investors. This not only requires some prescribed forms of disclosure (less onerous than a disclosure document) but limits the relief to shares that are in a class that is listed on the ASX or on an approved foreign exchange.

In the case of listed companies, regulatory principles may also be found generally in the ASX Listing Rules and the Employee Share Scheme Guidelines (endorsed by the Australian Institute of Company Directors, the Australian Shareholders Association and the Australian Employee Ownership Association).

[21] Regulatory Guide 49, [49.3] – [49.5].

[22] Note, however, that while class order relief does not extend to casual employees, ASIC will consider extending relief to offers made to casual employees or contractors on a case-by-case basis: [RG 49.38] – [RG 49.40].

## 3. METHOD

### 3.1. Sample selection

The Employee Share Plan Survey was administered to 1711 companies in October and November 2007. These were all of the companies listed on the ASX at 12 September 2007 upon which we were able to obtain reliable contact information. Contact details were obtained through Connect4, a company that specialises in providing information on companies listed on the ASX.[23] We initially developed a sample of 1000 companies, based on location, industry and size. However, after attempting to contact and interview representatives from this sample, we proceeded to contact all companies on our list. As our final sample constitutes the vast majority of ASX-listed companies as of that date, this survey more closely resembles a census than a sample.

Part A of the survey asked basic questions about the company, including whether the company had a broad-based ESOP. The response rate for Part A of the survey was 24 per cent (419 completed surveys). This is a very good response rate for these types of surveys, in which the respondents are high-level employees.[24] Two hundred and thirty-eight companies had a broad-based employee share plan, and thus could complete Parts B, C and D of the survey. These parts of the survey inquired into the features of the ESOP(s) operating within the company, the extent of employee involvement in the implementation and administration of the plan, and respondent views of the current regulatory framework. Of the 238 companies who could complete Parts B - D, 139 companies did so. Ninety-nine companies who said they had a broad-based ESOP failed to complete Parts B - D. The majority of respondents were company secretaries or HR managers, as these tend to be the individuals responsible for the administration of employee share plans.

Several measures were taken to reduce non-response rates. Potential respondents were contacted initially by telephone, and were given the option of being called back to participate in the survey at a specific time and date convenient to them. They were also given the option of completing Parts B – D of the survey via telephone, online or by mail out. In addition, respondents who had completed

[23] See www.connect4.com.au.

[24] See, eg, M Jones, S Marshall, R Mitchell and I Ramsay, 'Company Director Views Regarding Stakeholders' (Research Report, Corporate Governance and Workplace Partnerships Project, Faculty of Law, The University of Melbourne, 2007) 21; and S Jacoby, E M Nason and K Saguchi, 'The Role of the Senior HR Executive in Japan and the Untied States: Employment Relations, Corporate Governance and Value' (2005) 44 *Industrial Relations* 207, 216.

Part A over the telephone but who had failed to complete Parts B – D online were sent two reminder emails.

It is important to stress that there is probably a degree of self-selection in the findings of this survey. Despite the fact that we asked all companies in our sample to complete Part A regardless of whether or not they had a broad-based ESOP, it is likely that companies that had a broad-based ESOP or had an interest in this area were more willing to participate in the research project.

### 3.2. Data collection

Each of the companies was initially contacted by telephone by a research assistant. The research assistant explained the nature of the research and that it was being conducted by the University of Melbourne, and asked to speak with the person responsible for the company's employee share plan. If the person who answered the call was not sure who this was, or said the company did not have a plan, the research assistant asked to speak with the company secretary. The reason for this was that there is no standard location for the management of ESOPs within companies. They may be managed either by HR units or company secretaries, or sometimes by an external body.

If the relevant individual within the company agreed to participate, the respondent was asked to complete Part A via telephone at that time, or at another time more convenient to the respondent. If a respondent completed Part A of the survey on the telephone but did not have a broad-based employee share plan, the interview was complete. If the company at which the respondent worked did have a broad-based employee share plan, the respondent was given the option of completing the remainder of the survey over the telephone (at that time or at a more convenient time), online or as a paper survey which was mailed. The use of a mixed mode survey design (telephone, internet and mail out) has been recognised in the literature as potentially increasing response rates and lowering non-response biases.[25]

### 3.3. Survey content

The Employee Share Plan Survey was a structured survey, with a combination of closed questions and Likert scales. The survey asked a total of 47 questions and was divided into four parts (see the Appendix). Part A included 18 questions about general company characteristics, such as size and industry. The final four questions in Part A asked about the existence of narrow and broad-based employee share plans in the company. Respondents who indicated that their company did not have a broad-based employee share plan were asked to specify why they had abandoned a plan or, if they had never had one, to indicate the extent to which a range of factors were considered by the company in deciding not to have a broad-based plan. As noted above, respondents within companies that did not have a broad-based employee share plan completed the survey at the end of Part A.

Part B of the survey asked 17 questions about the employee share plan operating within the company. Part C included eight questions concerning employee involvement and participation in the decision to implement a broad-based employee share plan; the design and administration of the plan; and during the operation of the plan. Part D sought to elicit respondents' views as to the adequacy of the current regulatory framework.

Prior to administering the survey, the instrument was piloted with several company secretaries and other individuals responsible for administration of employee share plans within listed companies.[26] It was also circulated for comment among key stakeholding groups. A number of amendments to the survey were made based on feedback received.

### 3.4. Data analysis

We began our research with a list of basic hypotheses concerning the relationship between the presence of a plan and a number of company characteristics (discussed in Part 7). These hypotheses were drawn from existing studies both within Australia and overseas. Analysis was undertaken using the statistical and data management software package SPSS, with basic statistical tests performed: chi square for crosstabs and t-test for the comparison of means.

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[25] See, eg, G Woong Yun and C W Trumbo, 'Comparative Response to a Survey Executed by Post, E-Mail & Web Form' (2000) 6 *Journal of Computer-Mediated Communication* 1; and R Voogt and W E Saris, 'Mixed Mode Designs: Finding the Balance Between Non-response Bias and Mode Effects' (2005) 21 *Journal of Official Statistics* 367.

[26] We wish to thank those who piloted the survey for their time and helpful feedback: Sean Conlan (Macquarie Bank), Darryl Edwards (Perilya) and Mathew Reed (Computershare).

# 4. SAMPLE

Part A of the survey asked respondents a number of questions about the characteristics of the company. In this part of the report, we present the key characteristics of the companies in our sample. The characteristics of our sample group are important for understanding our findings in subsequent parts of this report.

## 4.1. Company size

The sample comprised a range of company sizes as measured by numbers of employees in Australia and annual turnover. Fifty-six percent of companies in the sample had 50 or fewer employees, just under one third of companies had between 51 and 1000 employees and nearly 12 percent of companies had over 1000 employees (see Figure 1).

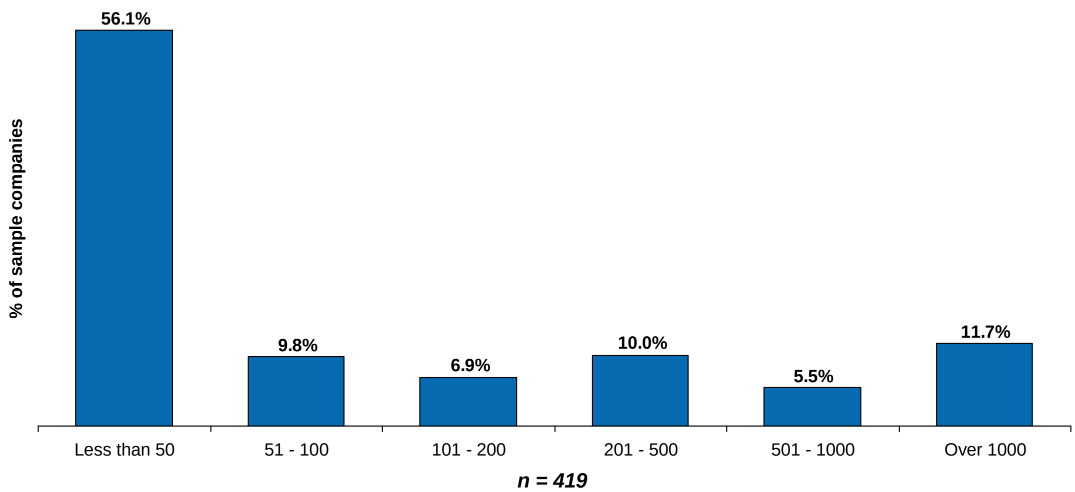


**Figure 1: Number of employees in Australia**

The majority of companies in our sample (56.5 percent) had an annual turnover of less than $20 million. Some 23.3 percent of companies had an annual turnover of $100 million or more (see Figure 2).

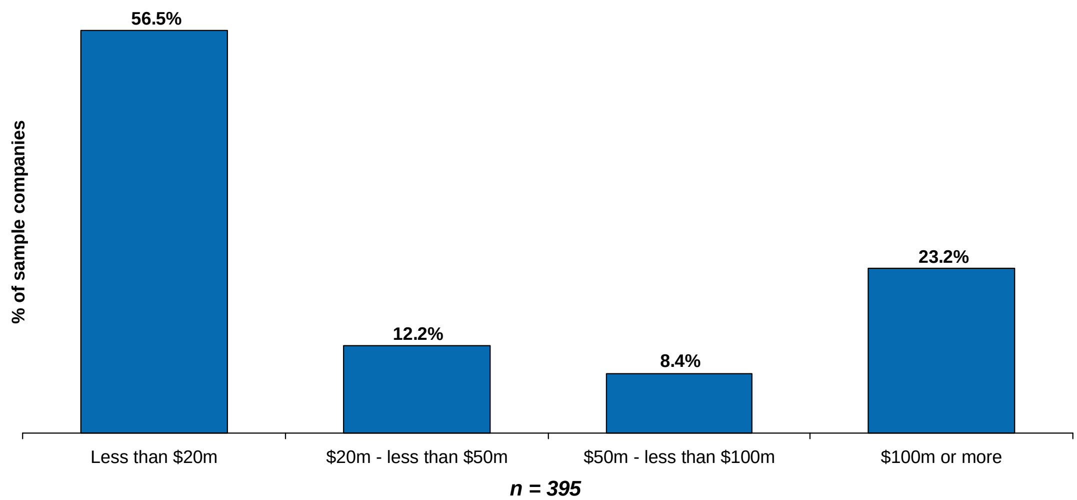


**Figure 2: Annual turnover**

Figures 1 and 2 indicate that a large proportion of the companies surveyed were small or medium-sized enterprises (SMEs), based on numbers of employees and annual turnover. This is consistent with the fact that SMEs account for approximately two-thirds of all ASX-listed companies.[27]

## 4.2. Company growth

The survey measured company growth based on changes to the number of employees and annual turnover over the past twelve months. Just over half of the companies in the sample (54 percent) reported that the number of employees in the company had increased over the past twelve months, reflecting the fact that we conducted the survey in a period of economic growth (see Figure 3). In 10.2 percent of companies, the number of employees had decreased and in just over one third of the sample (35.8 percent), the number of employees had remained the same over the past twelve months.

[27] ASX, 'SMEs Lead the Way in Market Capitalisation Growth!', ASX Email Newsletter, available at http://www.asx.com.au/resources/newsletters/listed_at_asx/20060321_smw_growth_far_in_excess.htm (last accessed 22 March 2009).

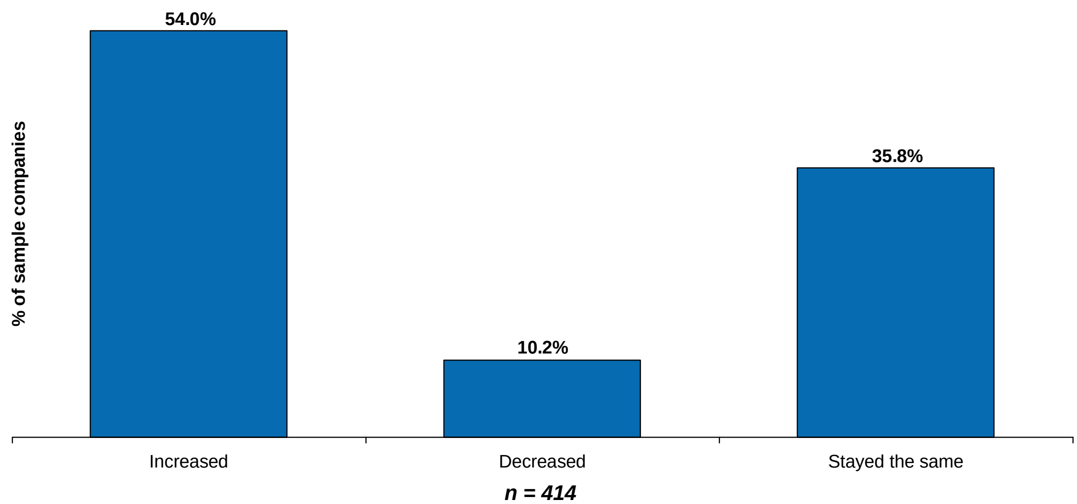


**Figure 3: Growth in number of employees**

As would be expected if employee numbers are increasing, of the companies in the sample, 52.7 percent reported an increase in annual turnover over the past twelve months, 12.3 percent of companies reported that annual turnover had decreased and just over a third of companies (35 percent) reported that annual turnover had remained constant over the past twelve months (see Figure 4).

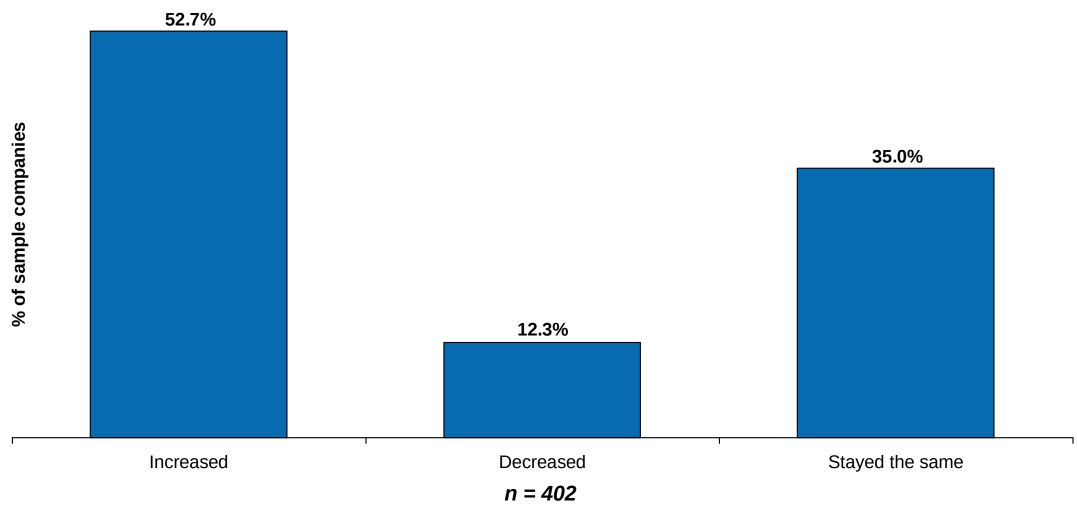


**Figure 4: Growth in annual turnover**

### 4.3. Presence of a centralised human resource function

The presence of a centralised HR management function is a well-accepted proxy for the sophistication of HR practices. Forty-seven percent of companies in the sample had a centralised HR management function and 53 percent did not ($n$ = 417). The proportion of companies with a centralised HR management function appears small given that the listed sector is generally known for its leadership in HR-related practices. However it may simply reflect the high proportion of SMEs in the sample group, as smaller companies are less likely to have a centralised HR function.

### 4.4. Extent of foreign ownership

The large majority of companies in the sample (96 percent) were not subsidiaries of overseas-based companies (0.7 percent were subsidiaries of US-based companies; 1.7 percent were subsidiaries of EU-based companies; and 1.2 percent were subsidiaries of companies from other countries).

### 4.5. Industry

Just over one third of respondent companies (34.5 percent) were in the mining industry (see Figure 5). Other common industries were finance and insurance (12.5 percent) and manufacturing (8.9 percent). The high proportion of mining companies in the sample reflects the ASX-listed population more broadly, in which listed mining companies represent about one third of all ASX listed companies.[28]

[28] See http://www.asx.com.au/investor/industry/mining/asx_involvement.htm

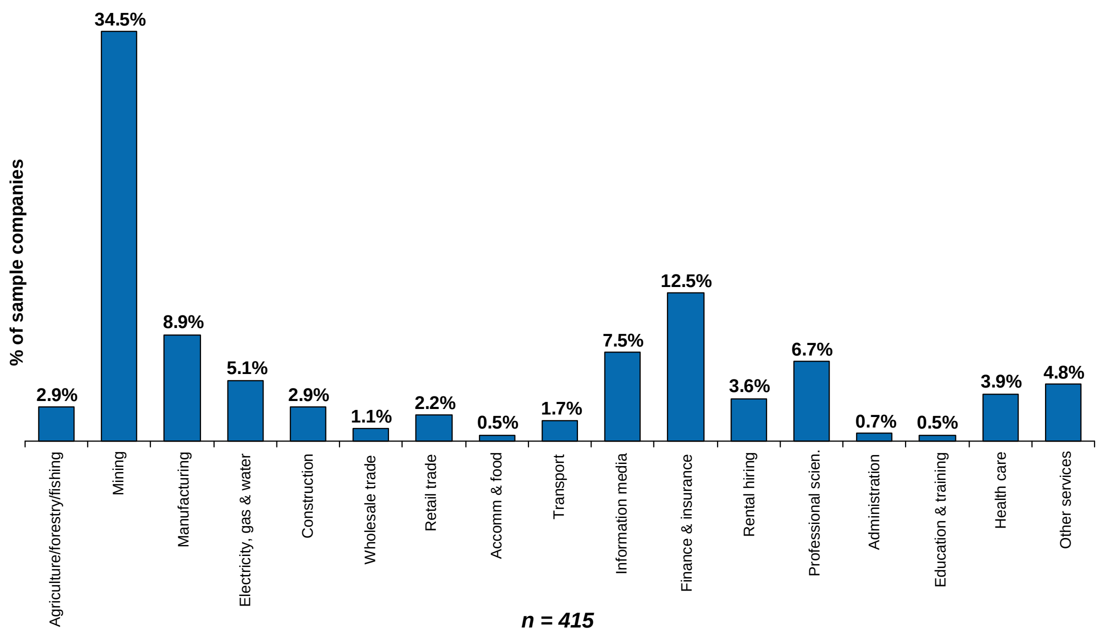


**Figure 5: Industry classification**

## 4.6. Type of industrial instrument

Respondents were asked to identify the main mechanism by which their company determined the terms and conditions of the majority of its non-managerial employees. The most common industrial instrument was individual common-law agreements, covering 73.4 percent of non-managerial employees (see Figure 6). This was followed by awards and Australian Workplace Agreements (both 7.3 percent), and union collective agreements (6.5 percent). In 3.1 percent of companies, the majority of non-managerial employees were covered by non-union collective agreements. The percentages of companies using Greenfield agreements and multiple business agreements were slight (1.3 percent and 1 percent respectively).

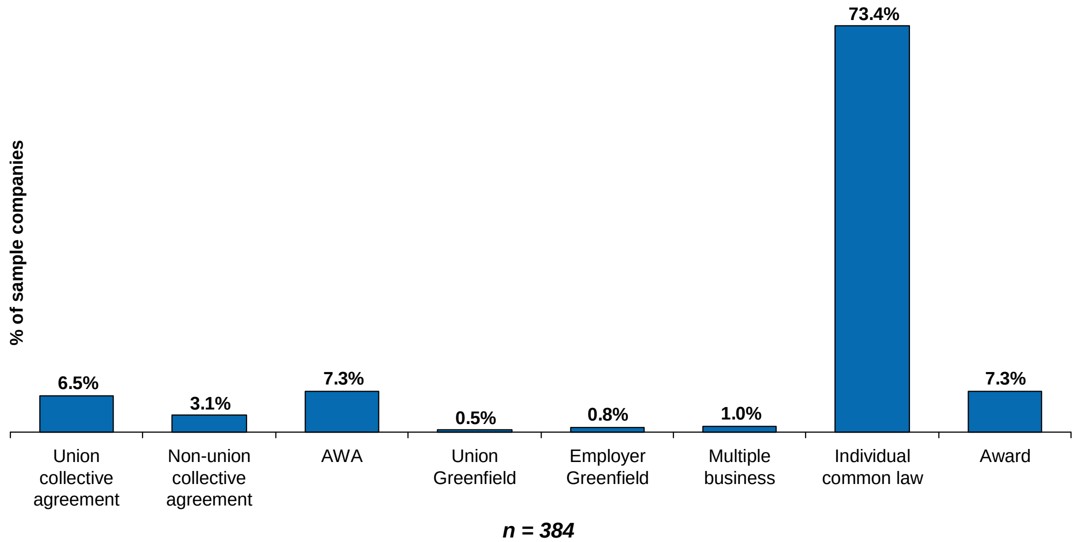


**Figure 6: Industrial instrument**

The high proportion of companies using individual common law contracts as the dominant form of industrial instrument is consistent with the use of industrial instruments within the broader Australian business population. However, beyond this, our data is very different to ABS statistics. According to the ABS, the most common method of setting pay among the private sector in 2006 was unregistered individual arrangement (39.0 percent). This is followed by collective agreements (28.1 percent), then awards (23.1 percent) and registered individual contracts (3.3 percent).[29] The coverage of awards and agreements in our sample appears very low when compared with the ABS data. It is often the case that a single employee is covered by several industrial instruments: for example an award and common law agreement. In addition, some inaccuracy may be a consequence of many of the respondents being company secretaries, who perhaps are not best-placed to answer HR-related questions.

## 4.7. Workforce profile

### *4.7.1. Employment status*

Respondents were asked to provide approximate percentages for full-time, part-time, casual and contract staff. The average percentage of full-time staff was around 80 percent; part-time staff around 5 percent; casual staff around 6 percent; and contractors around 8 percent (see Figure 7).[30]

[29] ABS, Employee Earnings and Hours, Australia, Cat. No. 6306, May 2006, 25.
[30] The figures provided by respondents did not consistently add up to one hundred percent. This is reflected in the aggregate data for this question.

Just over 60 percent of companies (60.6%) employed more than ninety percent of employees on a full-time basis.

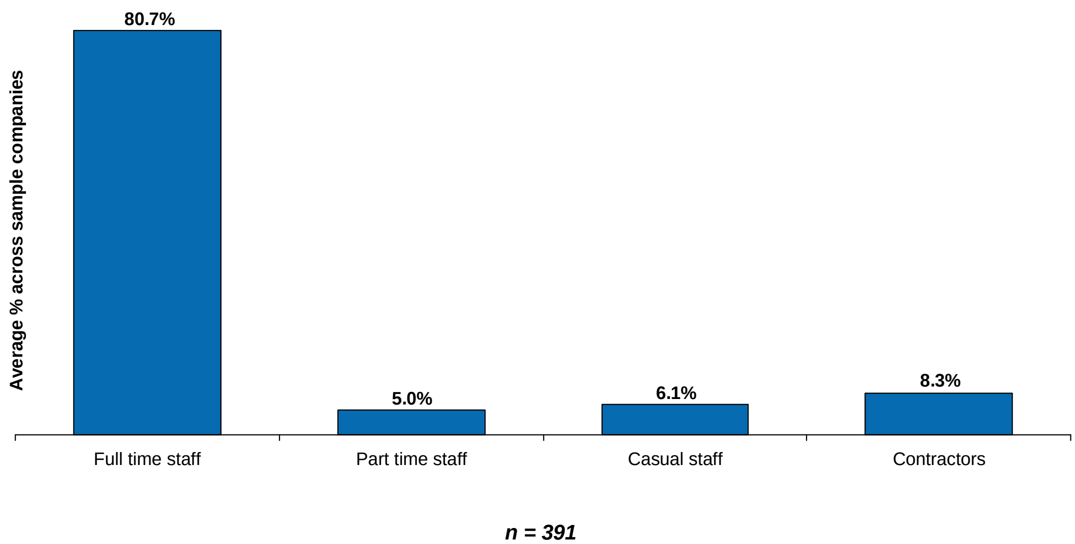


**Figure 7: Type of employment**

The proportion of casual employees in the companies sampled appears very low when compared to ABS statistics on the composition of the Australian workforce as a whole. Using the absence of paid leave entitlements as a proxy for casual status, ABS data indicates that around 25.9 percent of employees are employed on a casual basis.[31] Once possible explanation is that many casual employees work full time and therefore the respondents may have identified these as full time staff rather than casual staff.

### *4.7.2. Trade union density*

The average trade union density of companies was 4.4 percent (*n* = 306). Just over 81 percent of surveyed companies had no trade union members. Trade union density within this sample is considerably lower than trade union density within the private sector more broadly, where around 14 percent of employees are trade union members.[32] The low proportion of trade union members in our data could reflect the high proportion of SMEs in the sample, as larger companies tend to have higher trade union density. However, the accuracy of the data in this case is probably limited by the fact that many respondents to this survey were company secretaries who may not be very familiar with the industrial relations aspects of the company.

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[31] ABS, Employee Earnings, Benefits and Trade Union Membership, Australia, Cat. No. 6310.0, August 2007, 50.
[32] Ibid, 5.

### *4.7.3. Occupational groups*

Professional, technical and scientific constituted the largest average percentage of the workforce (57.2 percent), followed by clerical and secretarial (17.2 percent), craft and skilled manual (10.4 percent), sales and personal service (8.9 percent), and semi-skilled and unskilled manual (6.5 percent) (see Figure 8).

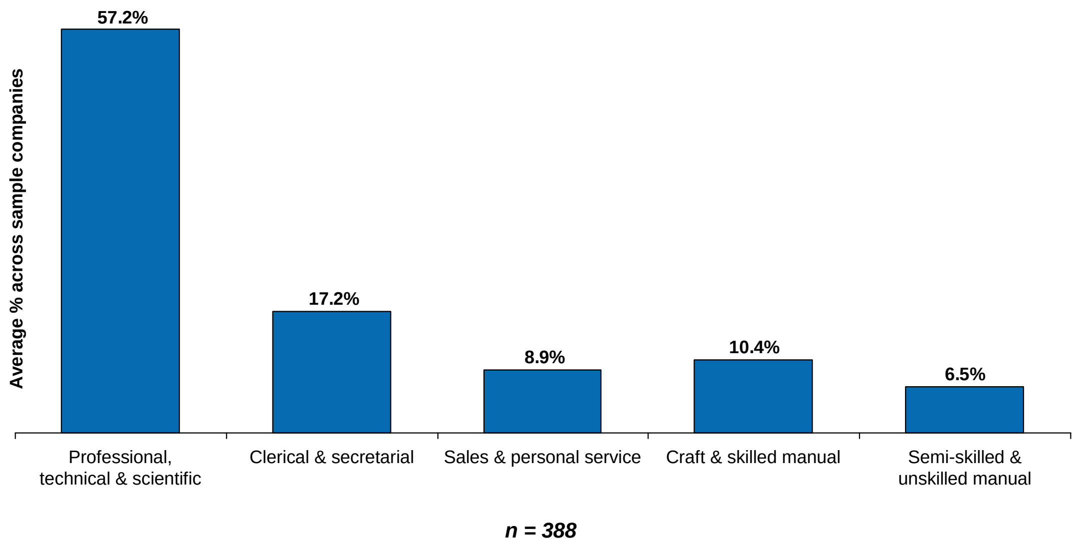


**Figure 8: Occupational groups**

## 4.8. Human resource practices

Because ESOPs are often linked with a range of other HR practices, we wished to discover what other kinds of HR management techniques are employed in respondent companies. The majority of companies in the sample (62.8 percent) had individual performance-related pay. Just under a quarter of the companies (24.1 percent) had group performance-related pay and just over a quarter (25.1 percent) of companies had a broad form of organisational performance-related pay. Just under a third of companies (31.3 percent) had none of these pay practices (see Figure 9). Note that, as respondents could answer affirmatively for more than one of the practices, the total percentage exceeds 100 percent.

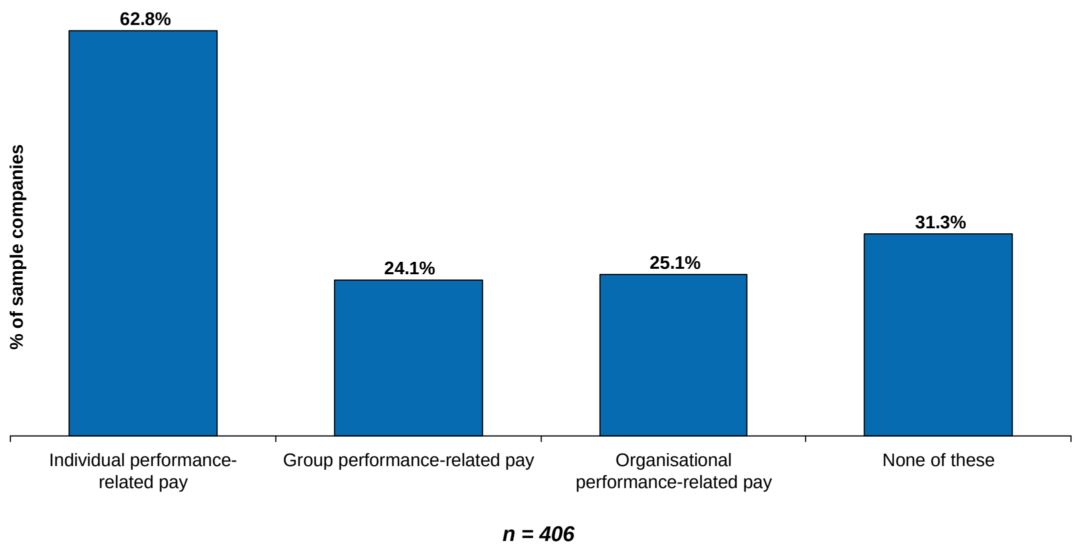


**Figure 9: Pay-practices for non-managerial employees**

The high incidence of individual performance-related pay compared with other pay systems appears broadly consistent with other studies conducted in Australia. Long and Shields, for example, found that 81 percent of Australian 'for-profit' firms used individual performance-related pay; 37 percent used some form of 'group' performance related pay; and 40 percent of firms used organisational performance pay plans.[33]

Respondents were also asked which of a number of employee participation practices were used within their company. Around 39 percent of companies had a formal structure for sharing company information with employees and 35 percent of companies had a formal structure for communication between all levels of employees and management (eg employee surveys) (see Figure 10). Over a quarter of companies (27.3 percent) reported that their company had a joint committee of managers and employees primarily concerned with consultation: for example, a joint consultative committee (JCC). Only 4.9 percent of companies in the sample offered business literacy training to their employees. Over a third of companies (37.2 percent) in the sample employed none of the above employee participation practices. Note that, as respondents could answer affirmatively for more than one of the practices, the total percentage exceeds 100 percent.

[33] Long and Shields, above n 7, 1793–5.

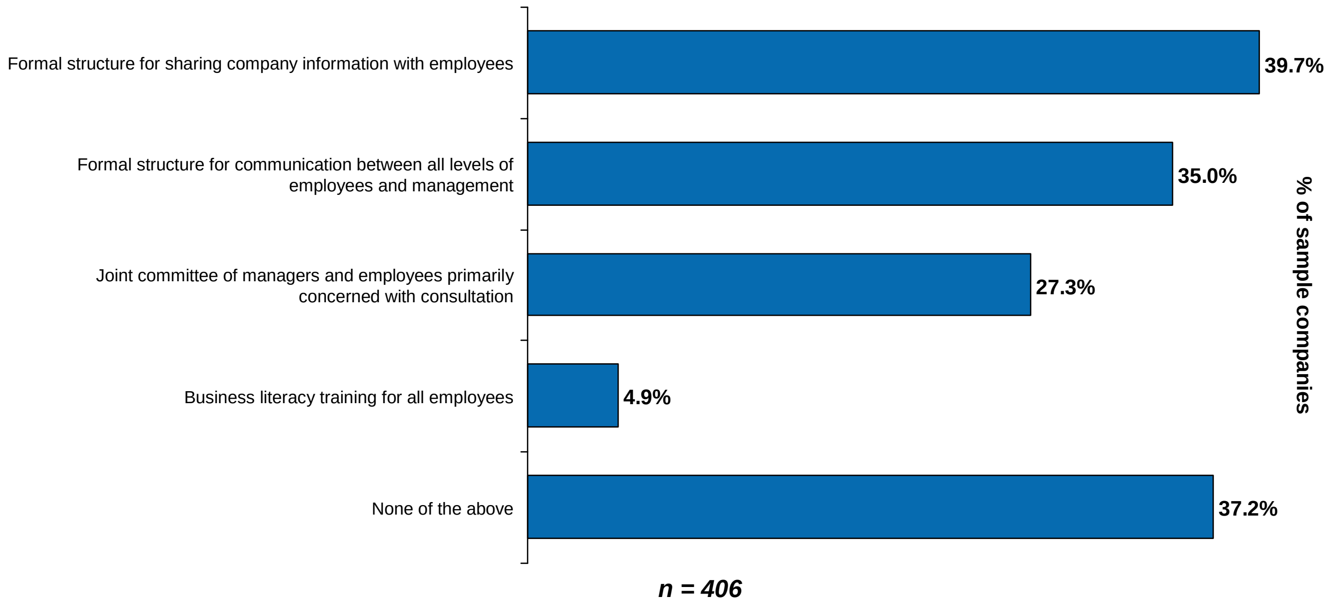


**Figure 10: Employee participation practices**

In Australia, employee consultative mechanisms are voluntary: they are generally not required by legislation (with the exception of specific topics such as occupational health and safety or large scale redundancies). The incidence of formal structures for consultation (JCCs) within our sample was lower than that revealed by previous studies. The Australian Workplace Industrial Relations Survey (AWIRS) 1995 revealed that since 1990, the incidence of JCCs had more than doubled, with the total number of committees in workplaces surveyed reaching 33 per cent.[34] The Victorian Workplace Industrial Relations Survey (VWIRS) 2003 found 62% of workplaces (both public and private) reported having a joint consultative and staff committee.[35]

It is important to note that, whilst our survey provides some evidence on the existence of these mechanisms, it does not provide any information as to their nature or quality. Forsyth, Korman and Marshall, for example, have emphasised that, because JCCs are the products of unilateral management initiative or of union/management agreement, rather than statute, they vary considerably in terms of composition, jurisdiction, powers and organisational level of operation.[36]

[34] Morehead et al, above n 12, 188.
[35] Industrial Relations Victoria, *Towards High Performance Workplaces*, State of Working Victoria Project, Information Paper No. 7, 2005, 8.
[36] A Forsyth, S Korman and S Marshall, 'Joint Consultative Committees in Australia: An Empirical Update', Paper presented to the 3rd Australian Labour Law Association National Conference, Brisbane, 22-23 September 2006, 2.

### 4.5. Shareholder influence

The survey also measured the influence of shareholders on company management. This indicator is relevant to one of the hypotheses in Part 7. The survey used a scale devised in research conducted in the US by Agle, Mitchell and Sonnenfield into which stakeholders mattered most to CEOs.[37] The scale was comprised of seven items: respondents were asked to rate the extent to which they agreed or disagreed with certain statement on a scale of one (strongly agree) to 5 (strongly disagree). This scale has recently been used in another study of Australian companies by Jones, Marshall, Mitchell and Ramsay and aims to promote nuanced insights on the nature of shareholder influence.[38] For instance the scale provides a sense of whether shareholders are 'active' and whether their demands are considered legitimate.

| ***Thinking about the relationship between the company and its shareholders over the past year…*** | **High Shareholder Influence (% agree#)** |
|---|---|
| Shareholders had the power to influence management | 76.7 |
| Shareholders were active in pursuing demands or wishes which they felt were important | 62.1 |
| Shareholders actively sought the attention of the management team | 69.2 |
| Shareholders urgently communicated their demands or wishes to our company | 49.1 |
| Shareholders demands or wishes were viewed by the management team as legitimate | 84.8 |
| Shareholders received a high degree of time and attention from our management team | 83.1 |
| Satisfying the demands or wishes of shareholders was important to the management team | 94.7 |
| *Average score for shareholder salience scale* | *3.83* |

# Includes 'agree' and 'strongly agree'

***n = 415***

**Figure 11: Shareholder influence**

[37] Derived from B R Agle, R K Mitchell and J A Sonnenfeld, 'Who Matters Most to CEOs? An Investigation of Stakeholder Attributes and Salience, Corporate Performance and CEO Values' (1999) 42 *The Academy of Management Journal* 507-525, Special Research Forum on Stakeholders, Social Responsibility and Performance Appendix, Table A (with minor modification – some of the items were removed because of duplication).
[38] Jones et al, above n 24.

The survey findings on this question can be broadly compared with the findings of Jones, Marshall, Mitchell and Ramsay regarding the influence of shareholders on company management. It is important to note, however, that these authors surveyed company directors and that their sample group was not restricted to companies listed on the ASX. Nonetheless, the average score for the shareholder salience scale in our survey (3.83) appears broadly consistent with their average score of 3.70.[39]

[39] Ibid.

## 5. RESULTS

### 5.1 Incidence of employee share plans

This part of the report outlines our findings as to the incidence of employee share plans. An important distinction exists between narrow based plans: that is, plans that are only open to executive/ managerial employees, and broad-based plans, that are open to the majority of non-managerial employees. Just over 40 percent of companies who responded to this survey had an employee share, option or rights plan that was only open to executives within the company.

Almost fifty seven percent of the companies who responded to this survey had a broad-based ESOP: that is, an ESOP open to the majority of employees within the company (see Figure 12). Of the 43.2 percent of companies that did not have an employee share plan open to non-managerial employees, 33.2 percent had never had one and 10 percent previously had one.

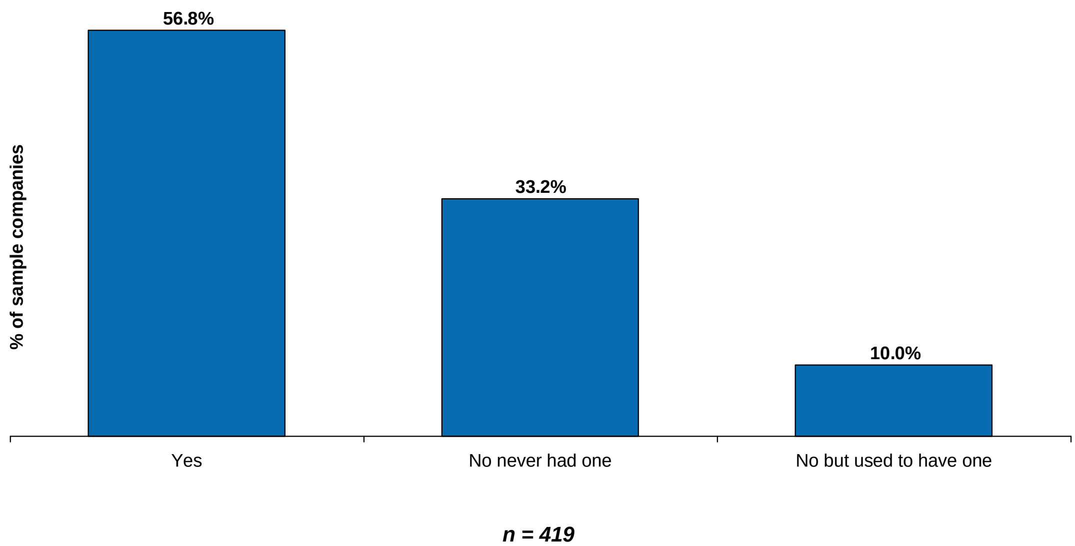


**Figure 12: Percentage of companies with a broad-based ESOP**

It is difficult to compare our findings with those of earlier studies on employee share ownership, as other surveys have either not grouped results according to company type; or have not distinguished between narrow and broad-based schemes. However, the findings of this study as to the incidence of broad-based ESOPs are broadly consistent with the ESODU research commissioned in 2004, in which 52% of public listed companies had an employee share ownership plan and there was a trend towards increased uptake of broad-based plans.[40]

There are several factors that may explain the relatively high incidence of plans in the listed sector. One important factor is clearly that the regulatory framework clearly favours listed entities. Listed companies generally tend to be larger and so have greater financial and administrative resources to implement plans. They also have structural advantages over unlisted companies due to their capacity to issue shares that can be traded on an open and liquid market. They may also have a greater incentive in implementing an employee share ownership plan to increase employee identification with the company, given that they may have large and spatially diffuse workforces.

The existence of fewer narrow-based, or executive-only, ESOPs in operation than broad-based ESOPs is highly surprising as it is generally thought that listed entities are more likely to have both broad and narrow-based plans in operation.. Earlier findings on the comparative incidence of broad-based vis-à-vis narrow-based schemes are conflicting. ESODU research in 2004 found that narrow or executive plans were the most common type of ESOP: six percent of all businesses surveyed had an executive plan, whereas only four percent of businesses had a broad-based plan. However, a 1998 KPMG survey of 750 Australian companies of all ownership types found that, of the 86 percent of companies with an employee share plan, 44 percent had a plan restricted to senior employees or executives, while 56 percent of the companies had a broad-based plan (the latter was defined as one that is open to more than 75% of employees).[41] There are a number of possible explanations for the differences in findings with respect to the incidence of narrow-based plans between the 2004 ESODU research and our own. First, as noted above, the ESODU surveyed businesses of all types, and it is possible that different trends are occurring in public listed companies. Second, the ESODU defined a broad-based plan as one open to 75% of employees within the company, whereas we defined it as a plan open to the majority of employees. Finally, as the ESODU research noted, the majority of plans implemented in the last year (63%) were open to all employees, indicating a shift towards broad-based plans. It is possible that, four years later, this shift is more pronounced.

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[40] ESODU research, above n 7. It is unclear from the Executive Summary of the ESODU research (the only publicly available report on the research) whether this figure was for all ESOPs or just broad-based ones.
[41] Ibid, 23

### *5.1.2 When Employee Share Plans Adopted*

Very few companies (1.5 percent) adopted a broad-based employee share plan before 1990 (see Figure 13). Just over 20 percent (21.4 percent) of companies adopted their broad-based ESOP in the 1990s. The majority of companies (77.1 percent) that have a broad-based ESOP in operation have adopted the plan since 2000.

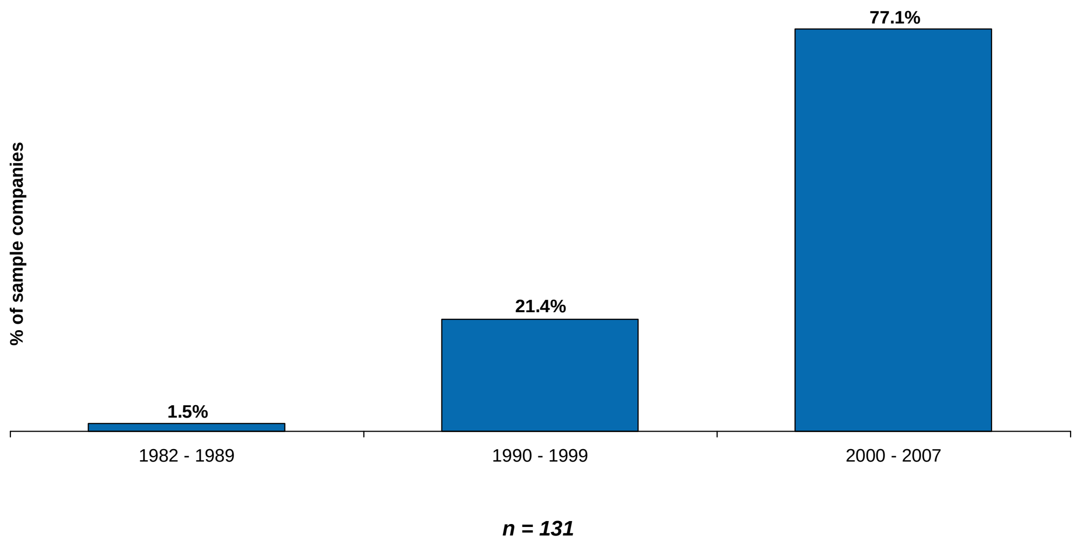


**Figure 13: When broad-based ESOP adopted**

Our findings suggest that broad-based employee share ownership plans are a recent trend in Australia. There are several factors that may explain the high rates of plan adoption of broad-based employee share ownership since 2000. One factor is that a number of companies took up the lead of their US counterparts in implementing such plans. Another factor appears to be the shift towards the determination of pay and conditions at the enterprise rather than at the industry level over the past two decades, giving companies greater remuneration flexibility and more scope to implement variable pay systems.[42] This period has also seen the rise of strategic human resource management (HRM), which emphasises the link between HR strategies (including remuneration) and business strategy. In particular, this trend has included the increased use of performance-related reward systems,[43] in which employee share ownership may be one of a bundle of incentive mechanisms.

[42] J Shields, 'Performance Related Pay in Australia' in M Brown and J Heywood (eds) *Paying for Performance: An International Comparison* (2002) 179.
[43] R Mitchell and J Fetter, 'Human Resource Management and Individualisation in Australian Labour Law' (2003) 45 *The Journal of Industrial Relations* 293, 294

Changes to the regulatory framework may also have had a positive effect on the take up of broad-based ESOPs. While the tax concessions in Div 13A of the ITAA 1936 were introduced in 1995, the exemption was doubled from $500 to $1000 in 1997. It is also worth noting that the prospectus requirements in the *Corporations Act* that apply to employee share schemes were relaxed in 1999.

Other explanations for the increased popularity of employee share ownership plans may lie in the strong performance of the Australian share market over the decade to 2008, and the promotion of broad-based employee share ownership under the former Coalition Government through the ESODU.

### *5.1.3 Number of plans*

Just over three quarters of those companies which had a broad-based ESOP (75.9 percent) had one such plan currently in operation (see Figure 14). Around 20 percent of companies (20.4 percent) had two plans operating concurrently. There was a low incidence of companies with more than two plans in operation (3.6 percent).

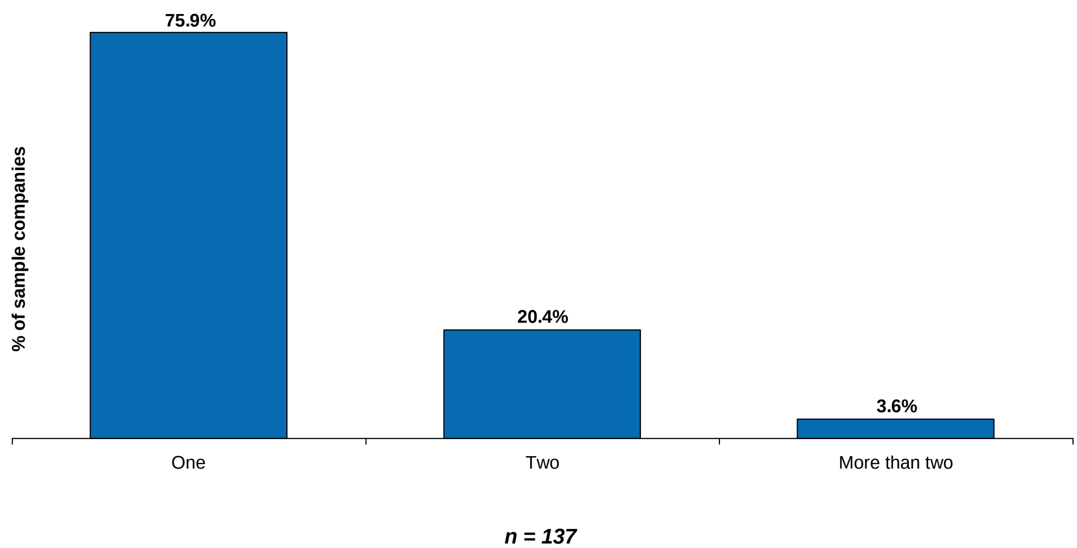


**Figure 14: Number of broad-based ESOPs**

## 5.2. Reasons for having or not having an employee share ownership plan

This part of the report includes an examination of the objectives of broad-based plans. It also presents findings on why companies choose not to have a plan, or to abandon a plan.

### *5.2.1. Employee share plan objectives*

Respondents who did have a plan were asked to select the extent to which they agreed or disagreed that the plan was implemented to achieve certain objectives. Of the fourteen objectives specified (see Figure 15), 97 percent of respondents either agreed or strongly agreed that the company sought to show employees that the company values them. Other common objectives were sharing financial success with employees (95.5 percent); aligning staff interests with shareholders interests (94.9 percent), retaining employees (92.0 percent) and attracting employees (81.8 percent). The three least common objectives for having the employee share plan were facilitating additional savings by employees for retirement (31.1 percent); raising capital (6.7 percent); and inhibiting takeovers (2.2 percent).

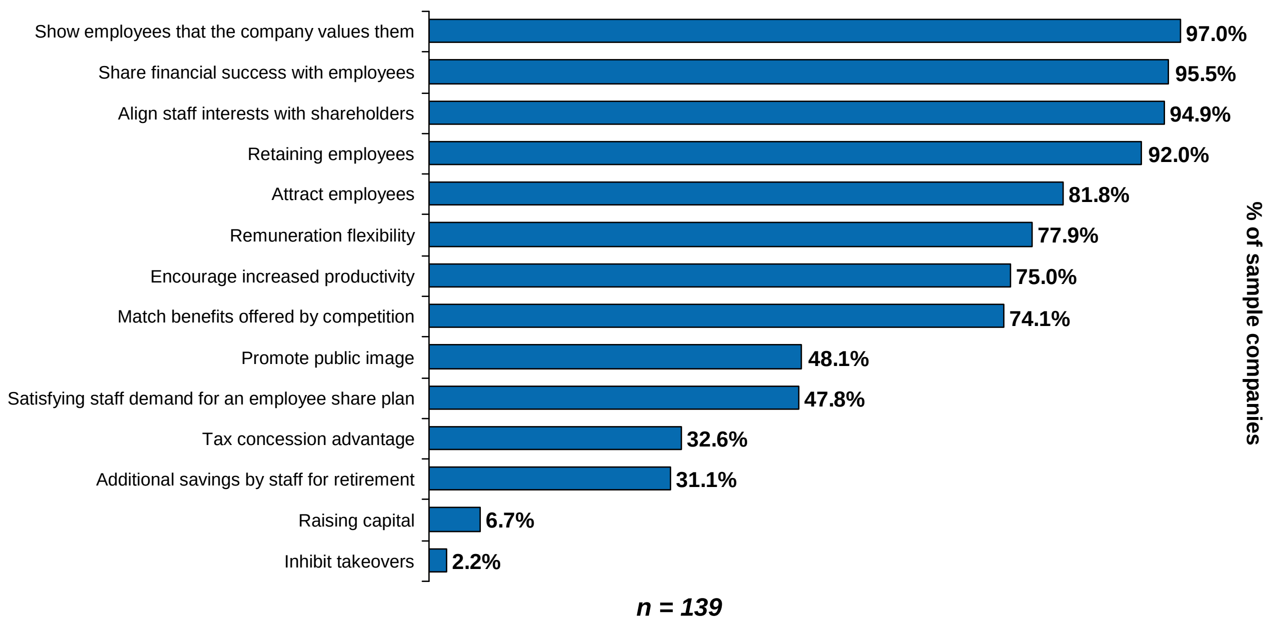


**Figure 15: Reasons for having a broad-based ESOP (percentage agreeing or strongly agreeing)**

It is clear from Figure 15 that the predominant objectives are based on human resource management (‘HRM’) rationales. Companies viewed ESOPs overwhelmingly as a mechanism for fostering identification between the company and the individual employee and aligning employees’ actions with employer interests. Using ESOPs to attract and retain employees also figured prominently, which probably reflects the tight labour market existing at the time this survey was conducted.

Three quarters of companies viewed ESOPs as a means of encouraging increased productivity. This is interesting given the absence of any convincing evidence of a direct link between broad-based

ESOPs and productivity.[44] This reflects the fact that responses to these types of questions are often vague.

Nearly 78 percent of companies identified increasing flexibility in remuneration as an objective for implementing a plan. Employee share ownership has been identified as a means through which companies may raise or lower remuneration in line with company performance without changing fixed wage levels:[45] as Kruse explains, 'when exogenous events lower company profitability, these plans automatically decrease employee compensation without the need for costly renegotiation of the hourly wage, or worker layoffs that may sacrifice firm–specific skills'.[46] If indeed companies are using ESOPs as a means of gaining more flexibility in remuneration, it is interesting to consider how this relates to our findings below showing that employees generally have little involvement in the design of these plans.

Less than a third of companies identified 'assisting employees generate additional savings for retirement' as an objective in implementing their ESOP. The potential contribution of ESOPs to employee savings was identified as a rationale for employee share schemes by the former Coalition Government, with former Prime Minister Howard noting the potential of ESOPs in 'fostering a more balanced approach to retirement planning'.[47] *Shared Endeavours* identified this as one of four public policy rationales for promoting ESOPs.[48] This policy rationale, however, does not appear to have much purchase at the company level. This is not particularly surprising given the $1000 tax exemption available. Objectives relating to raising capital and inhibiting takeovers received the least agreement by respondents. This is unsurprising, given the nature of ASX-listed companies and the very limited proportion of the company usually owned by employees (see further below).

Our findings as to company objectives for implementing an ESOP are similar to earlier studies. From their qualitative research conducted in 2005, Barnes et al reached the tentative conclusion that both management and employees adopt a 'nebulous' employee engagement rationale for the implementation of ESO schemes, rather than focusing on the potential for ESOPs to provide

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[44] The *Shared Endeavours* Minority Report, for example, noted that there was no clear and objective evidence to support the conclusion, however intuitive it may seem, that broad-based employee share plans fostered increased productivity: *Shared Endeavours*, above n 3, 290.
[45] See, eg, J Sesil, D Kruse and J Blasi, 'Sharing Ownership via Employee Stock Ownership' (Discussion Paper No. 25, World Institute for Development Economic Research, United Nations University, 2001) 8.
[46] D Kruse, 'Why Do Firms Adopt Profit-Sharing and Employee Ownership Plans?' (1996) 34 *British Journal of Industrial Relations* 515, 517.
[47] J Howard, 'Competence, Philosophy and Future Challenges', Address to the National Press Club, 2001.
[48] *Shared Endeavours*, above n 3, Recommendation 5.

incentives for specific kinds of behaviour.[49] In 2004, quantitative research commissioned by the ESODU found that businesses were more likely to agree that ESOPs provided benefits related to organisational culture and workplace relations/human resource strategies rather than rationales based on improved performance, a better working environment, competitive salary packaging or tax benefits for employees.[50]

### *5.2.2. Reasons for not having a broad-based employee share plan*

Where companies did not have a broad-based plan in operation, respondents were asked to indicate the influence of a number of factors in deciding not to have a plan.

Respondents were most likely to 'agree' or 'strongly agree' that high administration costs were a factor in deciding not to have a broad-based ESOP (see Figure 16). To implement an ESOP, companies must be willing to devote considerable time and resources to the design, preparation and ongoing operation of plans. The second most commonly identified reason for not having a plan was trade union opposition, with 29 percent of respondents either agreeing or strongly agreeing that this was a factor in their decision. This result appears anomalous, given that we know the vast majority of companies who responded to the survey (81.7 percent) reported having no trade union members. The third most commonly identified factor was share market volatility (27.5 percent). Where the price of the company's shares is volatile, companies may be reluctant to adopt an ESOP as the effects of participation in an ESOP on employees will be less predictable and there is a significant possibility that employees may lose money through participation in the plan. Cost of implementation was ranked equal fourth. This factor is often cited as highly significant and it may be that respondents were thinking of start-up costs when they chose high administration costs.

[49] A Barnes, T Josev, J Lenne, S Marshall, R Mitchell, I Ramsay and C Rider, 'Employee Share Ownership Schemes: Evaluating the Role of Tax and Other Factors Using Two Case Studies' (2007) 35 *Australian Business Law Review* 73.
[50] ESODU research, above n 7.

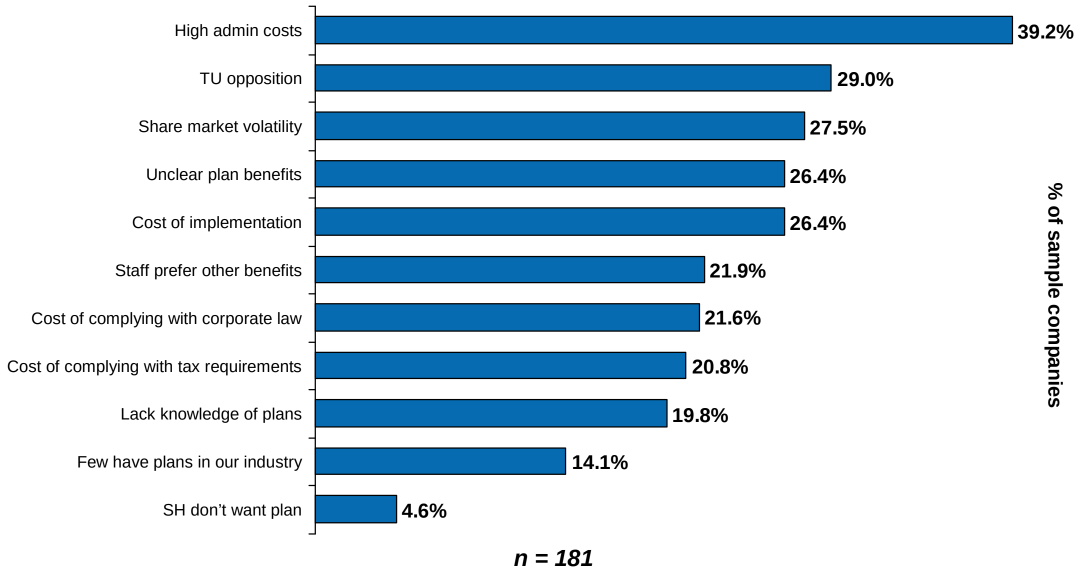


**Figure 16: Factors considered in not having a broad-based ESOP**

Overall, there was no one dominating reason why companies chose not to have an ESOP: that is, no one reason achieved over 40 percent agreement. This may suggest that many respondents have simply not considered ever having an ESOP or were apathetic towards the practice. Alternatively, reasons for not having a plan which had more purchase with respondents may not have been identified on the survey instrument.

It is possible to compare the findings of this survey with the 2004 ESODU research, which asked a similar question. It is important to note, however, that the ESODU survey was administered to companies of all types, not just listed companies. The ESODU reported that the four main barriers to increased implementation of ESOPs were: a perception of lack of relevance of employee share ownership to the business; practical issues regarding legal and tax complexities; employee resistance and expensive set up and maintenance costs.[51] Each of these considerations is also reflected in our results.

### *5.2.3. Reasons for abandoning a plan*

One in 10 companies surveyed indicated that they used to have a broad-based plan in operation but no longer did so. These respondents were asked why their company had abandoned the ESOP. This was an open-ended question. Reasons proffered for abandoning a plan can be broadly categorised into the following themes:

- Low participation rates;

- The company had been taken over and the new management did not want a plan;

- The plan was only intended to support an issue of shares to executives:

  *‘It was difficult to implement the share plan for directors without including it as part of a broad-based plan. This is why it was discontinued after issuing the original 'executive shares' because it was too costly to give shares to everyone.’*

- The company found that the costs of administering the plan were too high:

  *“Employee share plans are a nightmare to manage... you have people coming and going and we have to keep notifying the ASX every time we change anything... this adds complexity to our management that we just don't need."*

- The plan was not felt to have had its intended effects:

  *“It didn’t make any difference.”*

  *“It didn't make employees motivated to work harder.”*

  *“It didn't achieve the expectations which were for employees to take part in the growth of the company.”*

  *‘Management was disappointed that employees exercised their options plans within 6 months... This is why we discontinued the plan in 2001... Most of them just used the money to buy motorbikes.’*

  *“We had a share plan in place during the dot.com boom and some employees actually ended up losing money.”*

- The company wasn’t performing well:

  *‘When the company first floated we experienced a brief downturn, and the options were not exercised. We have preferred to focus on the bonus scheme rather than on short term share market gains.’*

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[51] Department of Employment and Workplace Relations, *Employee Share Ownership in Australia: Aligning Interests* (Executive Summary, Report prepared by TNS Social Research, 2004).

*'A very generous plan was introduced when the company was going through unprecedented growth - when things returned to normal, the plan was no longer thought appropriate for the time being.'*

Another reason that is often referred to is that the introduction of accounting standards in 2004 that required companies to expense options resulted in a number of companies abandoning plans or deciding not to proceed.

## 5.3 Employee share ownership plan structure

In this part of the report, we present our findings as to the type, and structure, of plans being utilised by the companies in our sample. As indicated in Part 4, many companies had more than one broad-based plan in operation. The survey instrument collected details on a maximum of two plans per company. Where a company had more than two broad-based plans (as was the case with 3.6 percent of companies), the respondent was asked to provide details of the two plans which had the most participants. It is important to note that in this part of the report, we draw upon the number of plans ($n$=165), rather than the number of companies ($n$=139).

### *5.3.1. Type of plan*

There are many different types of employee share plan in operation in Australia. They may be broadly categorised into those that fall within Division 13A of the ITAA 1936, through which participating employees may elect to access concessions, and those that do not. In our survey, respondents were asked to select which of five plan types their plan most closely resembled. The first two options – the tax exempt plan and tax deferred plan – refer to the two types of ESOPs that are designed to take advantage of the concessional regime in Division 13A. These types of ESOPs are explained in Part 2 of this report.

The survey instrument also sought information about a range of alternative possible plans including loan plans, replicator plans and 'other'. Loan plans were defined as plans that allow fully paid shares to be provided to employees, and the shares are paid for by a loan. Restrictions are often placed on the shares while loans are being repaid. These plans may involve the repayment of loans from dividends or salary deductions. Replicator plans were defined as plans that were structured to replicate a real employee share plan but without issuing real shares or rights. These have been described as employee share ownership ‘at a distance’, and may be useful in businesses that are unable to issue ordinary shares (such as partnerships).[52]

The most common type of plan was the tax-exempt plan (33.6 percent of all plans). This was closely followed by tax-deferred plans (31.5 percent). Only 7.4 percent of plans were loan-based, and 27.5 percent of plans were classified as ‘other’. Presumably this means that the plans were outside Div 13A, indicating that the benefit was provided other than by giving a discount to market price. This seems a very large percentage of plans that do not seek to obtain tax concessions. Whilst the category of ‘replicator plans’ was included in the survey question, no respondent identified this as a type of plan that they used. See Figure 17.

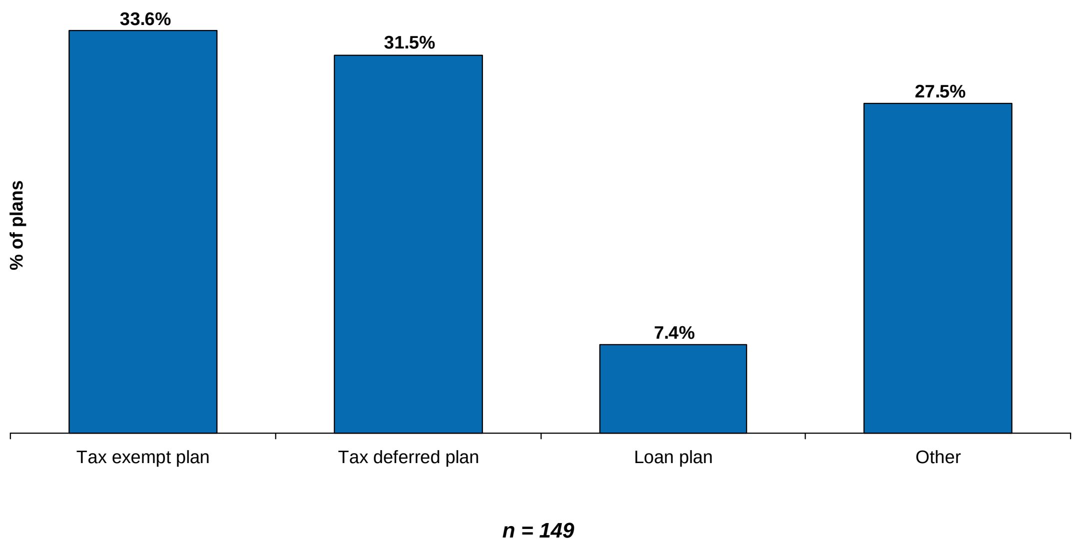


**Figure 17: Type of plan**

The two most common types of plans are those structured to take advantage of the tax concessions in Division 13A of the ITAA 1936. The dominance of tax exempt and tax deferred plans is unsurprising, and would appear to reflect the existence of taxation incentives. It has been widely thought that most broad-based plans have been structured as tax exempt plans so the almost equal split between tax exempt and tax deferred plans is somewhat surprising. It may be that the introduction of accounting standards in 2004 that require companies to expense the value of shares and options has pushed companies away from providing tax exempt benefits.

[52] J Lenne, R Mitchell and I Ramsay, ‘Employee Share Ownership Schemes in Australia: A Survey of Key Issues and Themes’ (2006) 14 *International Journal of Employment Studies* 1.

The absence of replicator plans among listed companies is to be expected, given that these plans are often designed and used by companies unable to issue shares. Where respondents indicated that they had a type of plan other than the four identified, the survey instrument did not ask respondents to provide further details.

### *5.3.2. Type of equity offered under the plan*

A range of types of equity can be offered through employee share plans. The survey instrument offered four alternatives: shares, options, rights and 'other'. A share is a type of claim in contract between the shareholder and the issuing company, as it comprises various rights and obligations on the part of both the shareholder and the company. The terms of the contract are contained in the *Corporations Act* and the company's constitution. An option gives an employee the right to acquire a share in the future at a predetermined price, subject to terms and conditions as set down in the offer. Rights are rights to acquire shares in the future. They differ from options in that there is no predetermined exercise price.

The most common form of equity offered under broad-based employee share plans was options (48.7 percent), followed by shares (46.7 percent). Only 3.3 percent of companies offered rights. A small number of companies (1.3 percent) offered 'other' forms of equity. Given that rights have become quite common in Australia, the low incidence of rights (3.3 percent) may be due to the fact that respondents were confused about the different categories and that some of the responses indicating shares are in fact rights. It is generally thought that larger listed entities are more likely to offer shares. Our sample group tended to be made up of smaller listed entities and this may partly explain the preference for options. Another point to note is that options will not be eligible for the exemption concession as they will not satisfy the condition relating to forfeiture. Given that approximately one-third of plans are exempt plans, the percentage for options may be overstated.

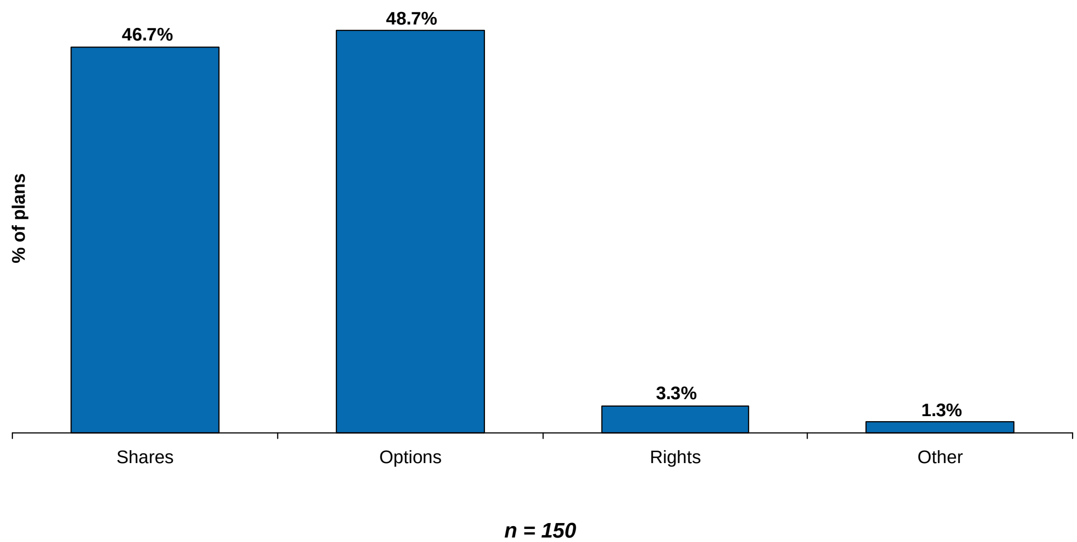


**Figure 18: Type of equity offered under plans**

Other surveys on employee share ownership in Australia have contradictory findings on the most common type of equity offered under plans, making comparison difficult. In 2003, KPMG reported that option and option-type schemes were the most popular type of equity-based compensation in Australia (constituting 49 percent of all employee share ownership plans). These were followed by tax-exempt plans (12 percent), deferred share plans (7 percent), and loan schemes (8 percent). In contrast, the ESODU's survey in 2004 found that 62 percent of businesses offered shares, 31 percent offered options and 7 percent offered units.

There are a number of considerations that may explain our survey findings in terms of the popularity of option-based plans. First, options would appear to present employees with a lower level of risk than shares. Employees can make a profit by converting their options to shares when the market rate is higher than the exercise price. If the market price goes below the agreed exercise price, the option holder would normally not exercise the option and it would lapse. In the latter case, the employee only bears the loss of any nominal amount paid to acquire the options. Options would thus appear to reduce the risk for employees and the necessity to pay upfront for the shares. Because of the deferred nature of options (employees can only convert their options after a certain period of time), options may also be an effective means of encouraging employees to remain with the company.

The use of options to foster a sense of ownership among employees, however, appears somewhat counter-intuitive. Prior to converting the options into shares, the employee does not enjoy the ownership rights that attach to shares, such as voting. It is these ownership rights that would appear to be the means through which a sense of involvement in the company among employees is fostered. Moreover, employees may simply decide never to convert their options into shares.

### *5.3.3. Value of securities*

Respondents were asked whether, under their plans, the securities were offered to employees at or below market value. The majority of plans (68 percent) provided securities to employees at market value. See Figure 19.

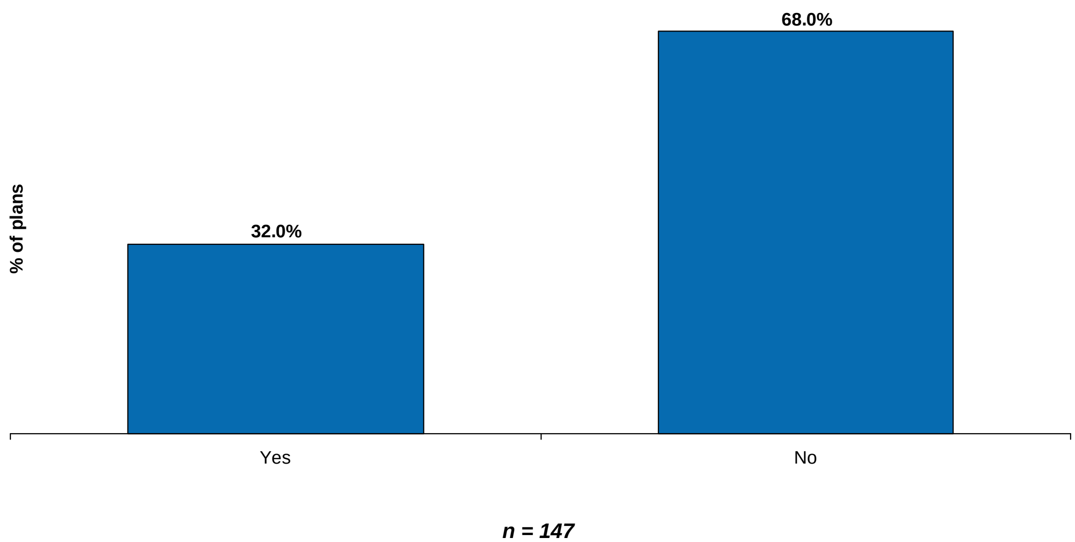


**Figure 19: Securities offered at less than market value**

This data may reflect the fact that listed companies have large numbers of non-employee shareholders and are reluctant to offer shares to employees below market value. It may also be that the "benefit" is provided in some other way, for example, by salary sacrificing or the provision of a loan. It is also possible that the provision of options at the current market value may be seen as a benefit to employees because, if the market value increases, there will be a discount on exercise of the option. It may be that respondents were not clear whether they were being asked about the value of the securities at the date of issue or the price that they had to pay.

### *5.3.4. Company contribution to the value of employee securities*

Respondents were asked the extent to which the company contributed to the value of the securities offered to employees. Companies appear to fund the plans in a range of ways (see Figure 20). In almost half of the plans (47.7 percent), the company did not contribute to the value of the securities.

It seems likely that this would arise in the context of a salary sacrificing arrangement ie the employees were contributing the whole amount but from pre-tax income. In 33.6 percent of plans, the company contributed 100 percent of the value: in other words, the securities were offered to the employee as a ‘gift’. Companies were much less likely to make a partial contribution to the cost of the securities. In 3.4 percent of plans, the company contributed a fixed dollar amount to the value of securities per employee. In 1.3 percent of cases, the company ‘matched’ every security purchased by the employee with a free share. In 14.1 percent of cases, companies had ‘other’ arrangements (not specified).

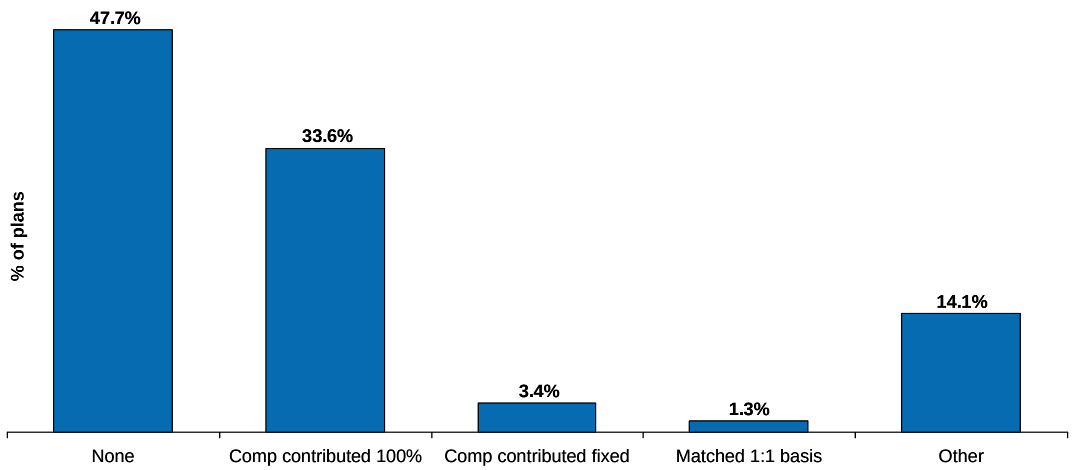


**Figure 20: Company contribution to value of securities**

It is interesting to note that around two-thirds of plans required participating employees to contribute some of their own money to the purchase of the securities. On one hand, this would appear consistent with the notion of employee share plans as a means of sharing both reward and risk with employees. On the other hand, it raises policy considerations over the extent to which employees are exposed to risk in the case of their employer experiencing financial difficulties. In such cases, employees are exposed to risk both as *employees* (e.g. risk to job security and wages) and to risks as *investors* (e.g. to loss of savings).

The findings above also raise the question of why employees participate in ESOPs where they are required to contribute 100 percent of the value of the securities. Why wouldn’t employees simply purchase securities in other perhaps better performing companies through the stock exchange? One possible explanation is the influence of the tax concessional regime. The two forms of concession available have the effect of providing a financial rationale to take up shares in the employer rather than in other companies. Another possible explanation lies in more subjective motivations of employees: for example, employees may participate in an ESOP to show their loyalty to the company. These two sets of motivations are of course not mutually exclusive.[53]

### *5.3.5. Form of employee contribution*

Of the 109 plans in which employees were required to make contributions to the plan, 47.7 percent of plans provided for employee contributions from post-tax salary. Just over one quarter (26.6 percent) of companies provided for employees to contribute to the value of securities through salary sacrifice mechanisms. In 2.8 percent of plans, employees could opt to contribute their bonus to the purchase of securities under the plan and in 3.7 percent of cases, employees could use money received through profit-share arrangements to participate in the plan. Finally, in 19.3 percent of cases, companies provided for 'other' forms of employee contribution. See Figure 21.

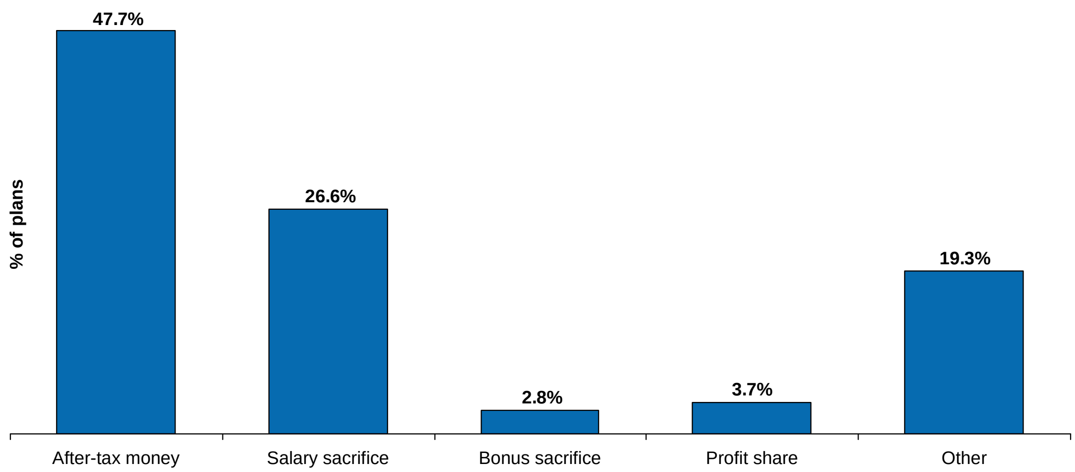


**Figure 21: Form of employee contribution**

Contributions can be either from after-tax income or pre-tax income. Contributions by way of salary sacrifice allow employees to obtain shares from pre-tax income and so there is clearly a tax saving in respect of the acquisition. What is surprising about these results is that almost 20 per cent of plans require other contributions that are not described as coming from after-tax income or from salary or bonus sacrifice or profit share. It may be that these types of plans offer some other benefit such as a loan arrangement.

The availability of salary sacrifice to purchase shares may have the effect of making participation in the ESOP more appealing to employees. Similarly, using profit share to fund participation in an

[53] See M Brown, I Landau, R Mitchell, A O'Connell and I Ramsay, 'Why do Employees Participate in Employee Share Plans? A Conceptual Framework' (2008) 18 *Labor & Industry* 45.

ESOP would also presumably increase participation rates as employees may be more willing to forego profit share bonuses than a proportion of their regular salary.

### *5.3.6. Maximum employee contribution*

Just over half the plans that provided for employee contributions (53.2 percent) capped employee contributions at $1000 per year (see Figure 22). This is consistent with the maximum tax exemption concession available, and would suggest that the available concessional regime is having a powerful effect in shaping and constraining the extent of employee contributions to plans in Australia.

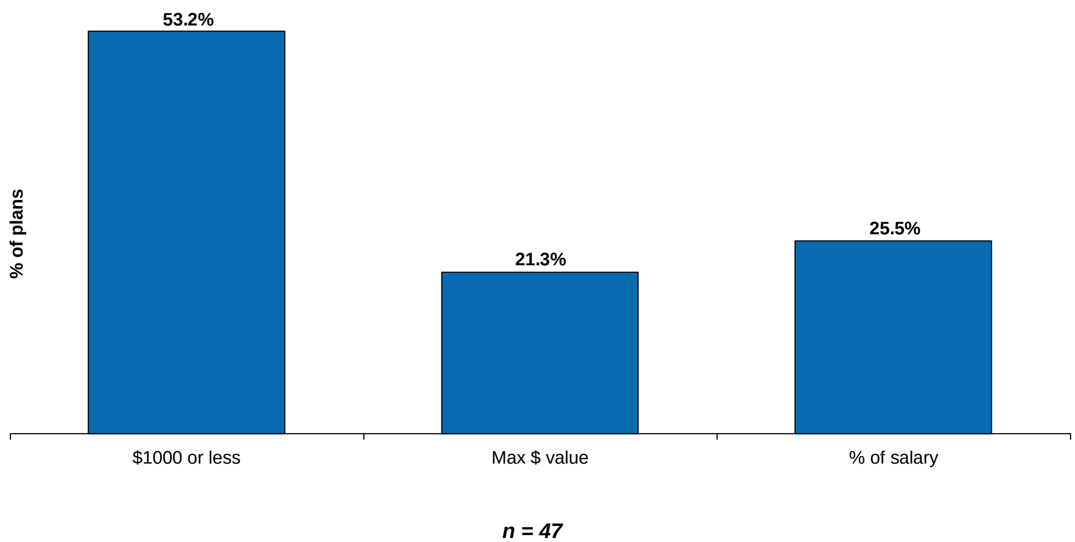


**Figure 22: Maximum employee contribution**

Around twenty-two percent of plans requiring employee contributions provided a maximum dollar value for employee securities per year. Of the 10 plans that capped employee contributions at a maximum dollar value, the average amount was $8082.50. Within these 10 companies, 2 companies capped employee contributions at $125.00 per year and 2 companies capped employee contributions at $15,000 per year. The other 6 companies capped employee contributions at $700, $875, $4000, $5000, $10,000 and $30,000.

Around a quarter of plans requiring employee contributions imposed a cap on employee contributions per year based on a percentage of salary. The average maximum percentage of salary was 36.2 percent. Of these 14 companies, three companies set the maximum percentage of salary at 10 percent and 2 companies at 20 percent. Other common maximum caps were 30 percent of salary (2 companies) and 50 percent of salary (3 companies).

### *5.3.7. Eligible employees*

The overwhelming majority of plans (94.7 percent) were open to permanent full-time employees. Around sixty-two percent of plans were also open to permanent part-time employees. Around thirteen percent of plans were open to independent contractors and around 10 percent of plans were open to casual employees (see Figure 23).

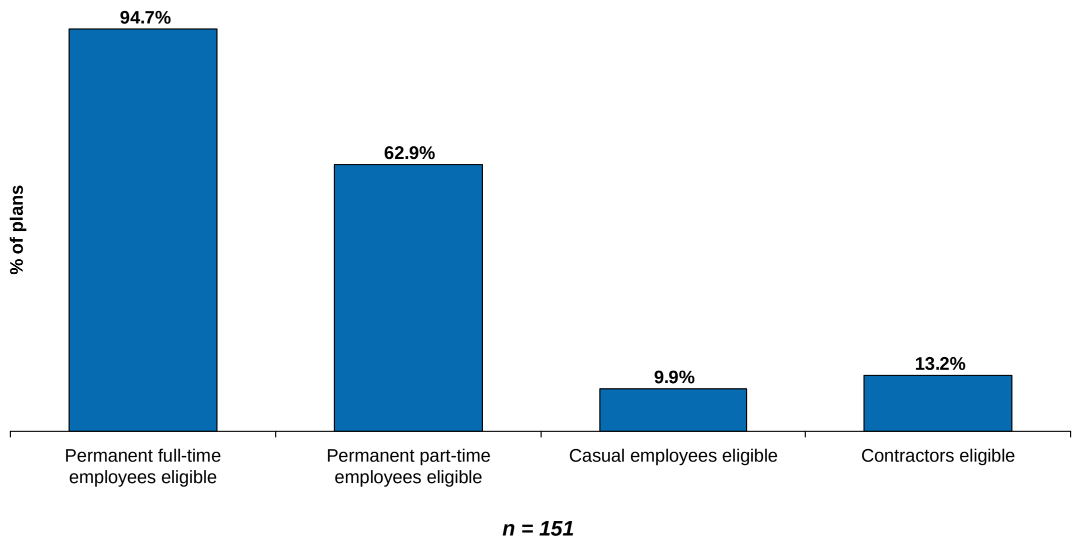


**Figure 23: Employee eligibility**

There is a range of possible explanations for the findings above. The most significant is likely to be that the tax concessions and disclosure relief rules are restricted to employee relationships and do not apply where the relationship is that of independent contractor. [54] It may also be that companies are most concerned with fostering identification and commitment among their ‘core’ workforce: that is, permanent full and part-time employees. Offering equity to these types of employees may also make more sense where the equity is options or where there is a minimum retaining period on the securities that contractors or casuals (who may be involved with the company for a shorter period of time) may not often meet.

The exclusion of casual workers raises equity considerations. The effect is to reinforce benefits to the ‘core’ workforce that enjoys better pay and conditions and more benefits than the ‘non-core’

[54] ASIC will consider extending relief to offers made to casual employees or contractors on a case-by-case basis, see Part 2 above.

workforce. There is also an important gender dimension to the exclusion of part-time and casual workers, as women tend to be over-represented in these forms of work.[55]

### *5.3.8. Minimum period of employment requirement*

Companies may impose a qualifying period of employment before an employee is eligible to participate in the plan. More than half of all plans (58 percent) imposed a minimum period of employment requirement before an employee is eligible to participate in the plan. See Figure 24.

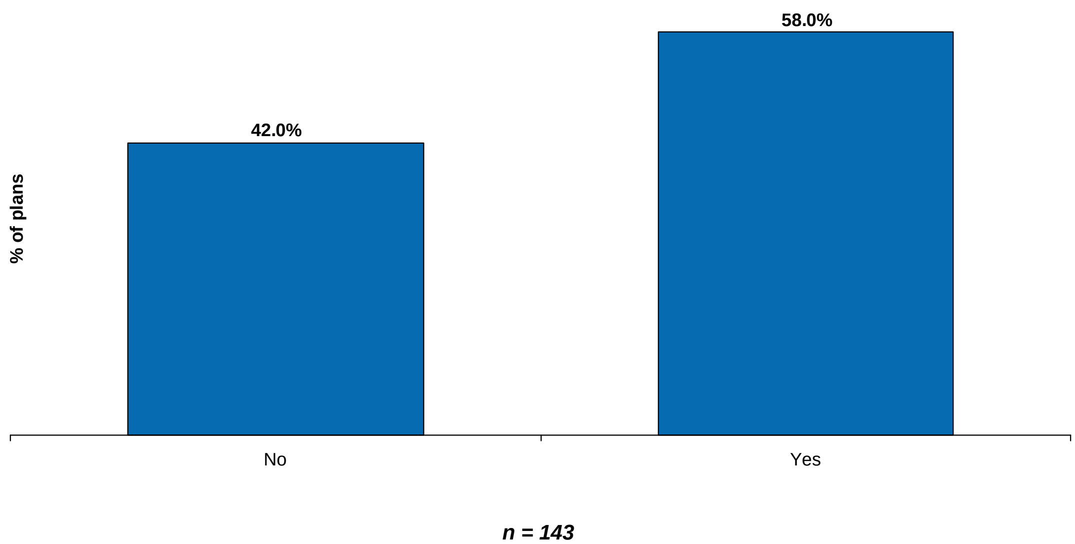


Figure 24: Minimum period of employment requirement

Again, these findings would appear to reflect the impact of the regulatory framework. To access concessions in tax and corporate law, the ESOP must be open to at least 75 percent of permanent employees, defined as full-time or part-time employees with at least 36 months prior employment.

There may also be other economic considerations for imposing a minimum qualifying period. If a company has implemented an ESOP with the objective of providing an incentive to employees to increase effort and productivity, for example, qualifying periods may be desirable in that they prevent new employees from 'free riding' on the performance improvements achieved as a result of existing employees' efforts.[56]

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[55] ABS, 'Table 1: Work, National Summary 1997-2007', Australian Social Trends, Data Cube. Cat. No. 4102.0, August 2008.

[56] J McCartney, 'Financial Participation in the EU: Indicators for Benchmarking' (Report prepared for the European Foundation for the Improvement of Living and Working Conditions, Luxembourg, 2004) 9.

### *5.3.9. Link with performance hurdles*

The majority of plans (around 57 percent) did not make the grant of securities to employees under the plan contingent upon the employee or the company achieving certain performance hurdles (see Figure 25). Only around 14 percent of plans linked the grant to the company achieving certain performance targets; around 10 percent of plans linked the grant of securities to the employee completing a satisfactory performance review; and around 7 percent linked the grant to the employee remaining with the company for a specific period of time. Around 11 percent of plans linked the grant to 'other' conditions.

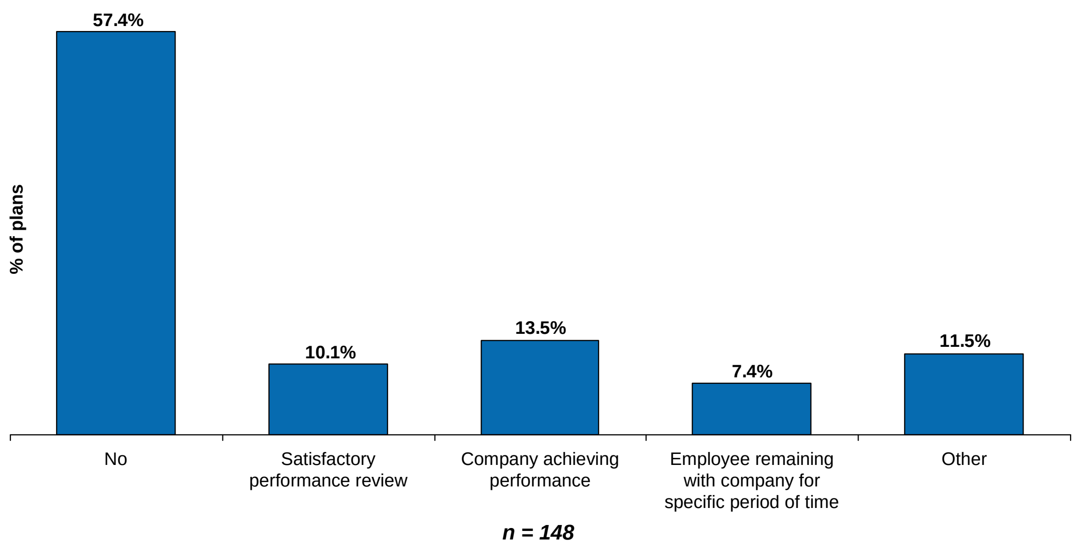


**Figure 25: Link with performance**

These findings suggest that ESOPs, as they are structured in many companies, do not have a role to play in terms of performance enhancement and reward: that is, there is little direct relationship between an individual's efforts and any reward they may enjoy through participation in an ESOP. It is interesting to consider this data against the earlier finding that around three quarters of companies surveyed either agreed or strongly agreed that, in implementing an ESOP, their company was seeking to encourage employees to increase productivity. It would appear that companies are seeking to increase employee productivity indirectly rather than directly: that is, through rewarding employees and fostering greater identification between the employee and the company.

### *5.3.10. Manner of determining allocations to individual employees*

Plans displayed a high level of variation in the manner in which allocations of securities to individual employees were determined (see Figure 26). In just under one third of companies, all employees were entitled to receive the same value of securities. Twenty percent of plans determined allocations by reference to the employee's job grade and around 19 percent of plans linked allocations to individual performance. Around 11 percent of plans linked allocations to salary level and around 16 percent of plans linked 'other' (not specified) methods to determine allocations to individual employees.

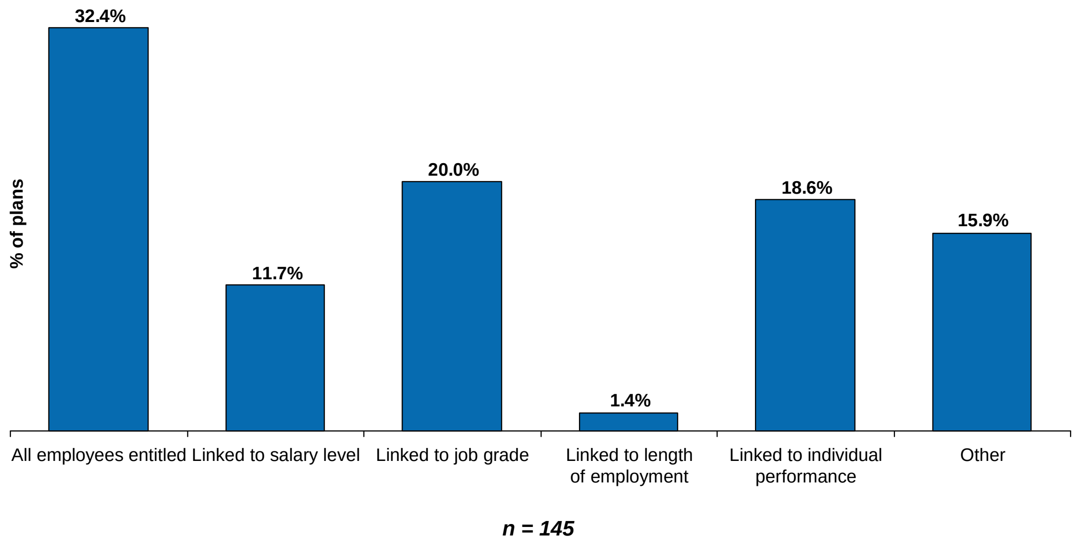


**Figure 26: Allocation of securities**

### *5.3.11. Restrictions imposed on entitlements*

Respondents were asked what, if any, restrictions were imposed on the employee securities once vested (ie relating to entitlement). It was possible for respondents to select more than one of the following options.

The vast majority of plans did not impose restrictions on entitlements in relation to the employee securities once vested. Four percent of plans imposed restrictions on voting rights, 1.3 percent restricted dividend entitlements and two percent placed restrictions on bonus issues. Around 12 percent of plans imposed 'other' restrictions. See Figure 27.

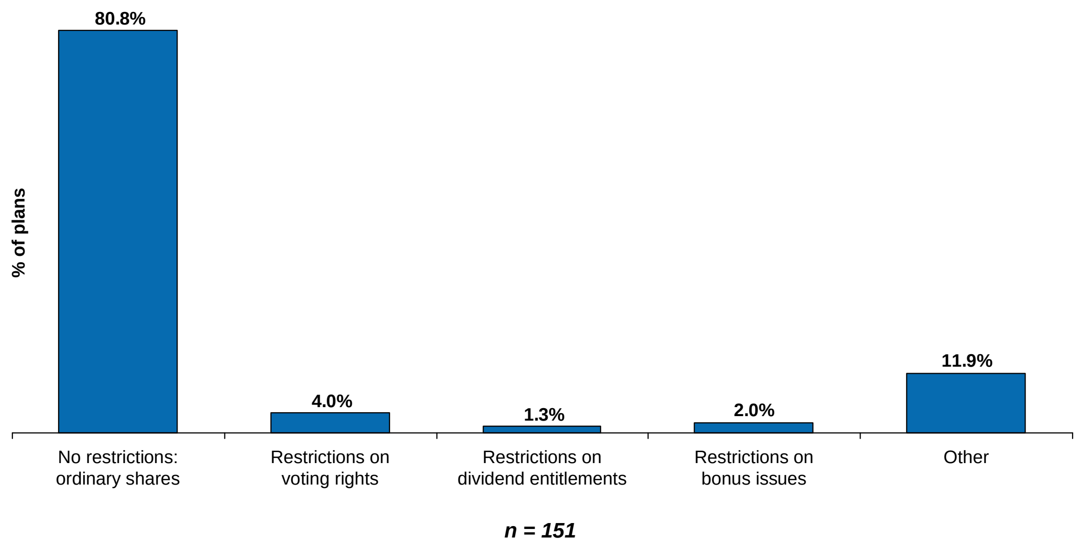


**Figure 27: restrictions imposed on securities once vested**

The absence of restrictions on entitlements may reflect the existing regulations. To access either of the two concessions in Division 13A of the ITAA 1936, for example, a company must issue ordinary shares or options to acquire ordinary shares.[57] Ordinary shares would not have any restrictions on voting rights or dividend entitlements. The tax legislation also imposes restrictions on disposal in certain cases and this is discussed below.

### *5.3.12. Restrictions imposed on the disposal of employee securities*

Just over half of all plans (51.7 percent) did not impose restrictions on the disposal of securities (see Figure 28). A quarter of plans (25.8 percent) restricted trade to ‘trading windows’. In 16.6 percent of the plans there was a minimum holding period and in 5.3 percent of plans, disposal was only available when the employee left the company. The tax exemption concession does require a restriction on disposal for a minimum of 3 years, and so it might have been thought that more plans would impose a restriction (see Fig 17 re type of plan offered). However, plans may impose forfeiture conditions and this will have a similar effect to imposing a restriction.

[57] Section 139CD(4) of the ITAA.

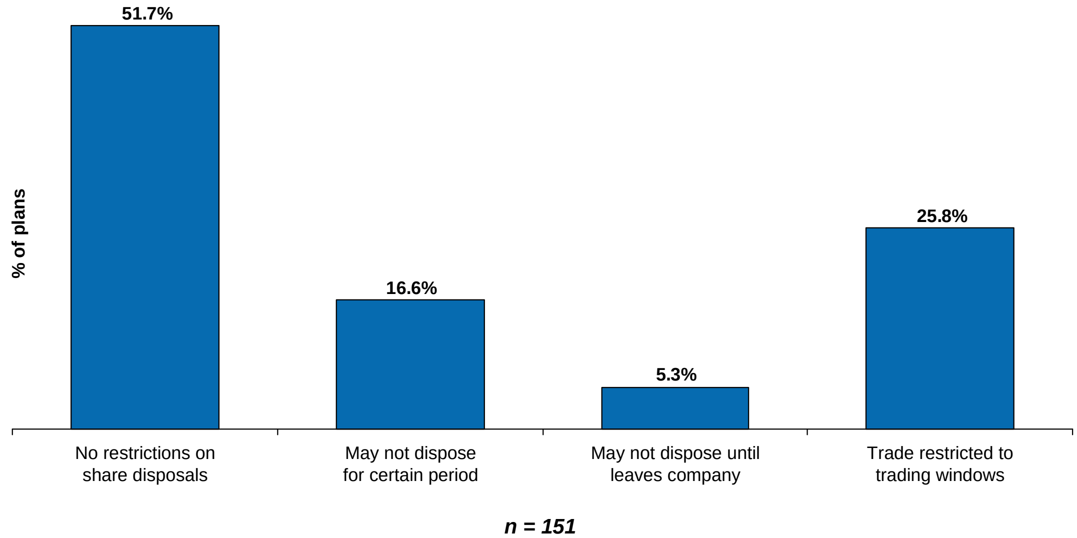


**Figure 28: Restrictions imposed on the disposal of employee securitites**

### *5.3.13 Minimum holding period*

The minimum holding period refers to the length of time an employee must retain securities under the employee share plan before he or she is able to dispose of them.

Just over half of the plans did not impose any minimum holding period (see Figure 29). Many of these plans may have been plans that provided options, where they will be 'held' through their vesting period.

Eleven percent of companies imposed a one year holding period, and around 5 percent of companies imposed a two year holding period. Approximately 21 percent of companies imposed a minimum holding period of 3 years. These are presumably those companies who are taking advantage of the available exemption concession within Division 13A as, to access this concession, shares or rights must not be disposed of for a minimum of three years (unless employment ceases earlier).[58] Figure 29 suggests that many companies who are designing plans to access the exemption concession are complying with the bare minimum holding period: there appears to be relatively fewer companies choosing to impose longer holding periods. This may be because long holding periods would discourage participation.[59] Further where there is high labour market mobility, it may be impractical to require employees to hold their shares for longer than 3 years.

[58] Section 139CE of the ITAA.
[59] McCartney, above n 57, 15.

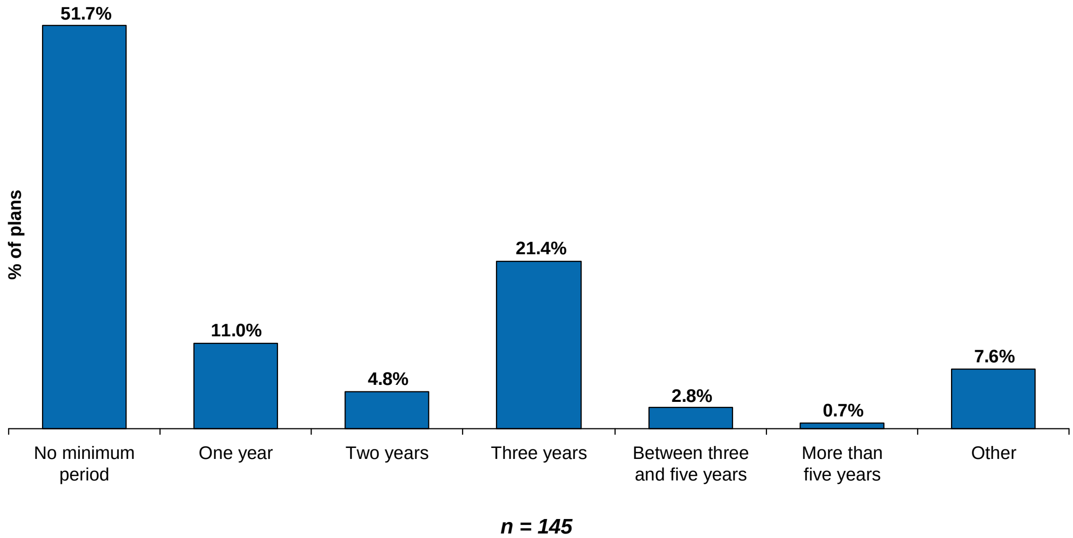


**Figure 29**: **Minimum holding period**

### *5.3.14. Maximum holding period*

Just over 70 percent of plans did not set a limit on the amount of time that an employee could hold their securities in an ESOP (see Figure 30). Around 14 percent of plans imposed maximum holding periods between 3 and 5 years.

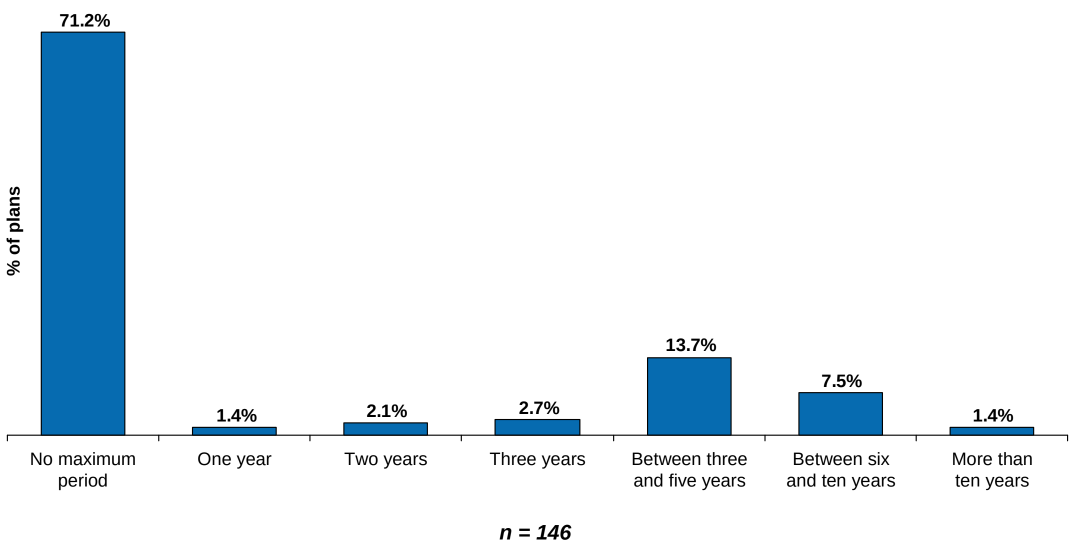


**Figure 30: Maximum holding period**

### *5.3.15. Use of trust structure*

Only 29.5 percent of plans were administered through a trust structure. The majority of plans (70.5 percent) were not administered through a trust structure. This result is surprising. Unlisted entities are more likely to use trust structures to administer an ESOP as such a structure can be used to buy-back shares from departing employees.[60] However, many listed companies also use trusts to enforce disposal and forfeiture conditions. This may not be the case in our sample which tended to be made up of smaller listed entities.

## 5.4. Employee involvement and participation

Part C of the survey examined the nature and extent of employee involvement and participation in the design and administration of employee share plans. This part of the survey used a number of questions derived from a survey of employee financial participation in listed firms in Europe.[61]

### *5.4.1. Introduction of plan*

The overwhelming majority of plans were introduced as a board or management decision only, without the formal agreement of employees and/or their representatives (see Figure 31). In only 4 percent of companies was a plan introduced as part of a formal agreement with trade unions or other employee representatives. In 4.8 percent of cases, respondents chose ‘other’ (not-specified).

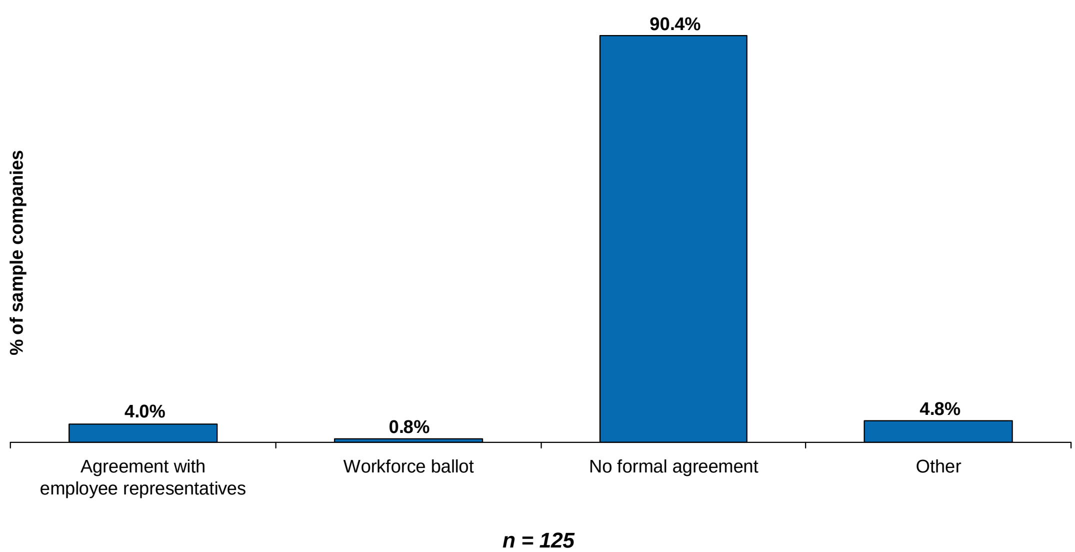


**Figure 31: Employee involvement in introduction of plan**

[60] See A O’Connell, ‘Employee Share Ownership in Unlisted Entities: Objectives, Current Practices and Regulatory Reform’ (Research Report, Employee Share Ownership Project, Melbourne Law School, The University of Melbourne, December 2008) 26.

[61] E Poutsma (ed), ‘Changing Patterns of Financial Participation in Europe: A Survey among Listed Firms in Six European States’ (Final Report, Nijmegen School of Management, January 2006).

There do not appear to be any existing studies on the extent to which employees and/ or their representatives are involved in the design and administration of ESOPs in Australia with which to compare our findings. Qualitative interviews conducted on the project to date, however, suggest that the plans are overwhelmingly a management initiated phenomenon, with little or no input from the potential participants. Overseas studies appear to have reached similar conclusions.[62]

### *5.4.2. Extent of employee involvement in design and administration of plan*

Respondents were asked to indicate the extent to which employees or their representatives were involved in various aspects of the design and administration of the employee share plan. As Figures 32, 33, 34, 35 and 36 illustrate, employees (or their representatives) are rarely involved in making decisions on the funding rules of the plan, the eligibility criteria, the plan rules, plan administration, and changes to the plan.

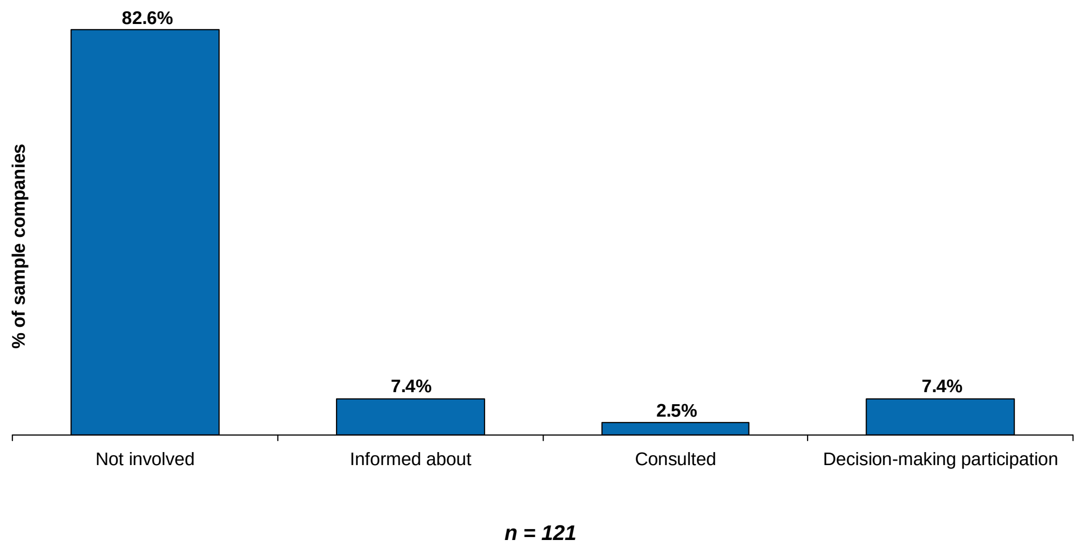


**Figure 32: Extent of employee involvement in funding decisions**

[62] In the UK, for example, Baddon has found that less than 10 percent of companies with employee share ownership stated that employees had been consulted prior to, or during, the implementation of the plan: L Baddon, *People's Capitalism?: A Critical Analysis of Profit-Sharing and Employee Share Ownership* (1989) 72.

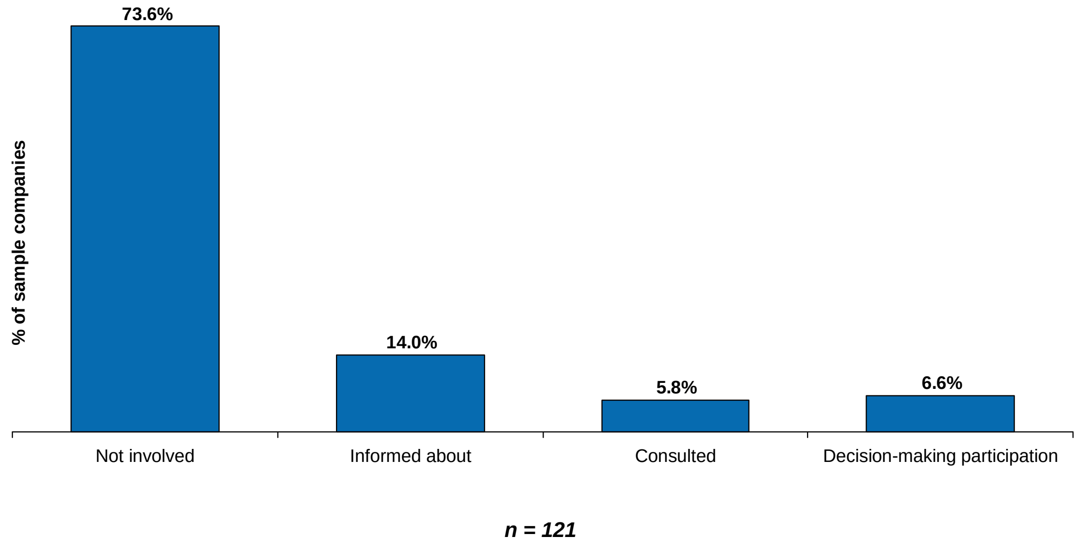


**Figure 33: Extent of employee involvement in setting eligibility criteria**

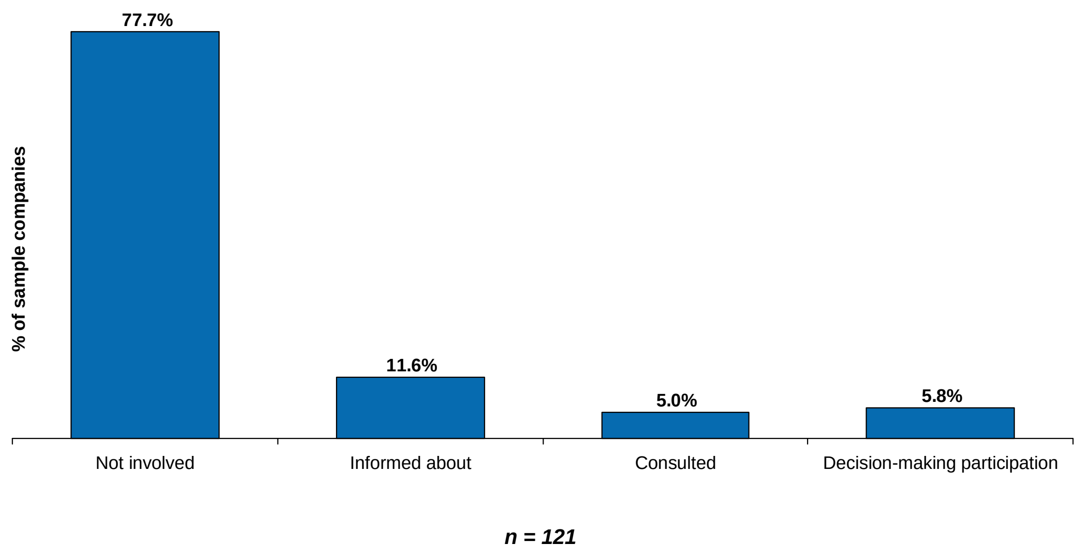


**Figure 34: Extent of employee involvement in drafting plan rules**

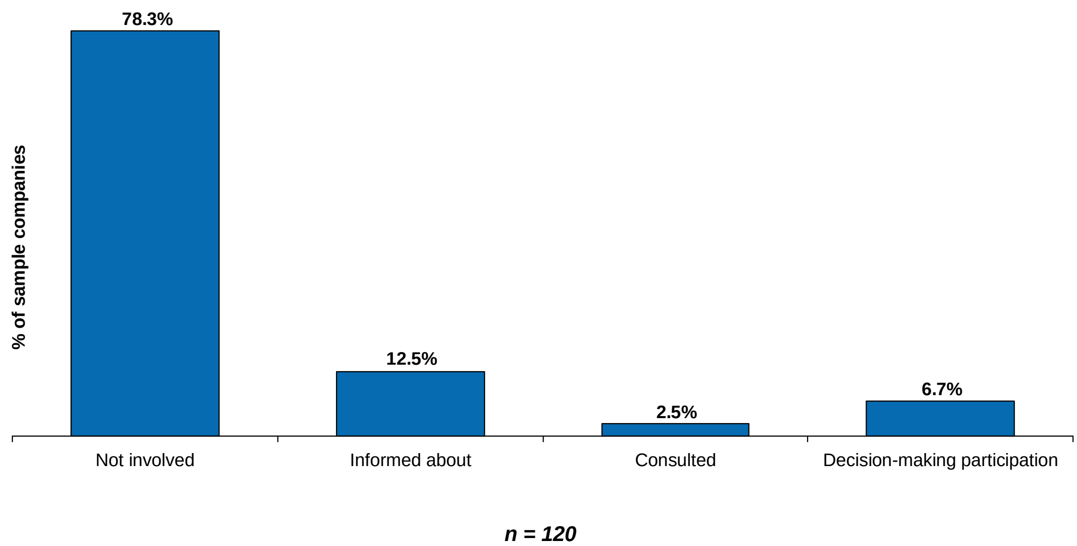


**Figure 35: Extent of employee involvement in plan administration**

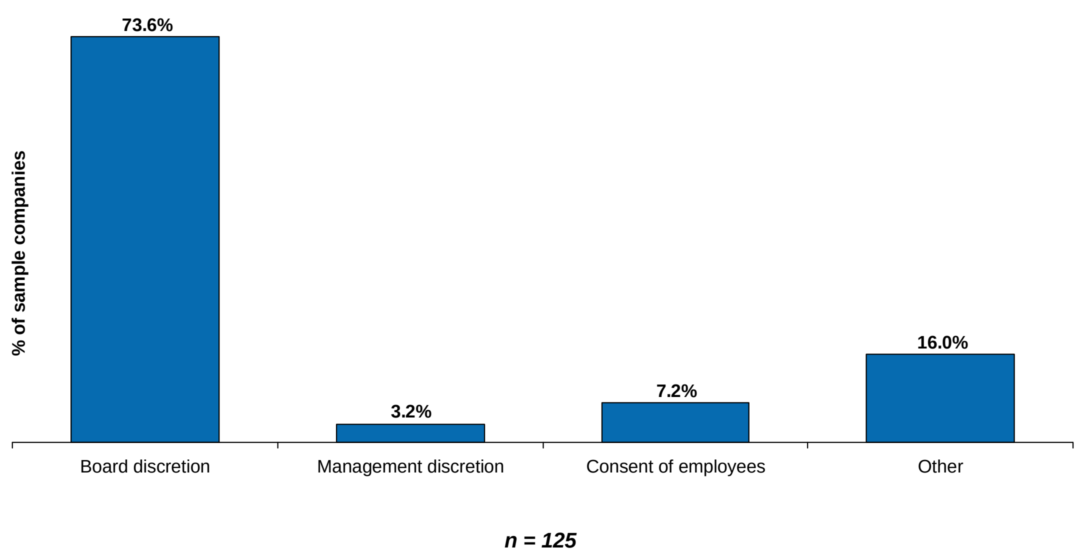


**Figure 36: How plan rules can be altered**

It is clear from the findings above that employees are rarely involved in the decision to implement a broad-based ESOP, or in how such plans are structured and administered. This raises a number of considerations in light of the increasing popularity of such plans and the potential for employees to make significant contributions of their own funds to such plans. Employee involvement in the design and implementation of ESOPs may help to protect employees from the risks associated with financial participation.[63] It has also been argued that employee involvement may increase employee participation in the ESOP. As Lawler observes of pay systems, 'understanding and acceptance of the system tend to be quite high when they participate in designing it, allowing for a rapid start-up of the system and a commitment to its survival'.[64]

### *5.4.3. Maximum percentage of equity available to non-managerial employees*

Companies were asked to specify the maximum percentage of company equity available under their broad-based ESOP(s). This was an open-ended question. The average percentage of equity available to non-managerial employees through employee share ownership plans was 6.4 percent. Of those companies that set a maximum percentage of equity available through their ESOP(s), around 69.4 percent set this maximum at 5 percent. Figure 37 provides a breakdown of the maximum percentage of equity available.

| Maximum percentage of equity available | Number of companies |
|---|---|
| 1.00 | 9 |
| 2.00 | 1 |
| 3.00 | 2 |
| 5.00 | 68 |
| 10.00 | 5 |
| 12.00 | 2 |
| 15.00 | 6 |
| 20.00 | 4 |
| 30.00 | 1 |

***n* = 98**

**Figure 37: Maximum percentage of equity available to non-managerial employees**

### *5.4.4. Percentage of equity currently owned by non-managerial employees*

Companies were also asked to specify the percentage of company equity currently owned through their ESOP(s). This was an open-ended question. The average percentage of equity currently owned by non-managerial employees was 2.7 percent. Figure 38 provides a breakdown of the percentage of equity currently owned by non-managerial employees.

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[63] See, eg, E Heery, 'Risk, Representation and the New Pay' (1996) 25 *Personnel Review* 54.
[64] E Lawler, 'The New Pay: A Strategic Approach' (1995) *Compensation and Benefits Review* 14, 20.

| Percentage of equity currently owned | Number of companies |
| --- | --- |
| 1.00 | 39 |
| 2.00 | 18 |
| 3.00 | 7 |
| 4.00 | 4 |
| 5.00 | 6 |
| 8.00 | 2 |
| 10.00 | 2 |
| 15.00 | 1 |
| 20.00 | 1 |

***n* = 80**

**Figure 38: Percentage of equity currently owned by non-managerial employees**

### *5.4.5. Percentage of non-managerial employees participating in the plans*

The existence of a broad-based employee share plan alone tells us little about the extent of employee participation in the plan. Respondents were asked to indicate approximately what percentage of employees eligible to participate in the plan actually did so.

In over a third of plans (38.5 percent), more than 90 percent of employees participate in the plan. These plans with very high participation rates may be those plans which provide shares or options to employees as a ‘gift’, without requiring employee contributions. Below the 90 to 100 percent mark, however, there is a wide variation in participation rates among companies (see Figure 39).

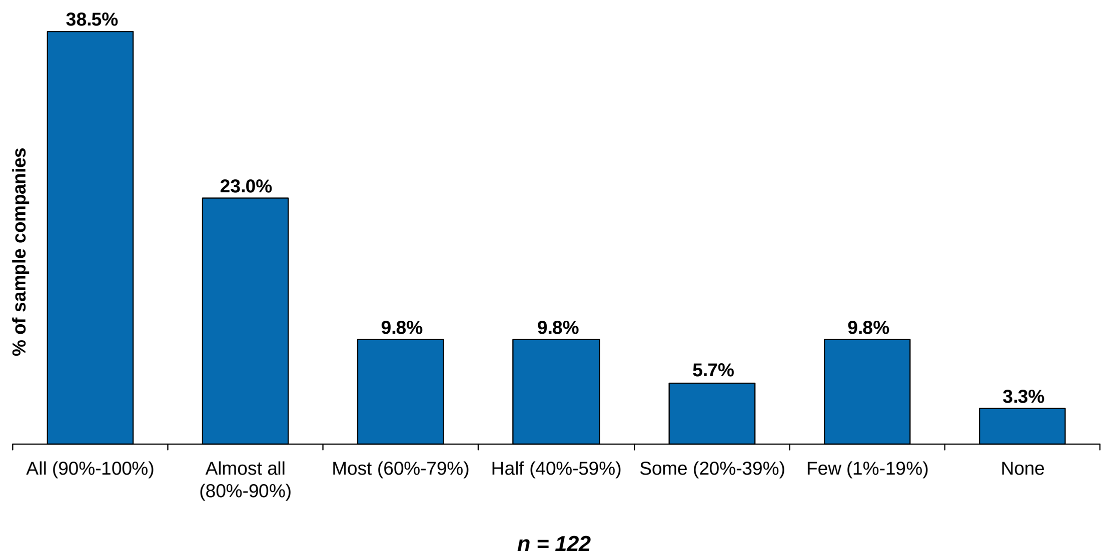


**Figure 39: Extent of employee participation in plans**

### *5.4.6. Employee involvement in corporate decision-making*

Respondents were asked to indicate the extent to which employee shareholders were involved in corporate decision-making. In the majority of companies (72.4 percent), employee shareholders enjoyed the same voting rights as ordinary shareholders (see Figure 40). Very few companies showed any form of innovation in terms of collective representation of employee shareholders via indirect voting rights or employee board representation. Just over 17 percent of companies indicated that employee shareholders were involved in corporate decision-making through 'other' mechanisms. The survey instrument did not provide them with an opportunity to specify what 'other' mechanisms these included.

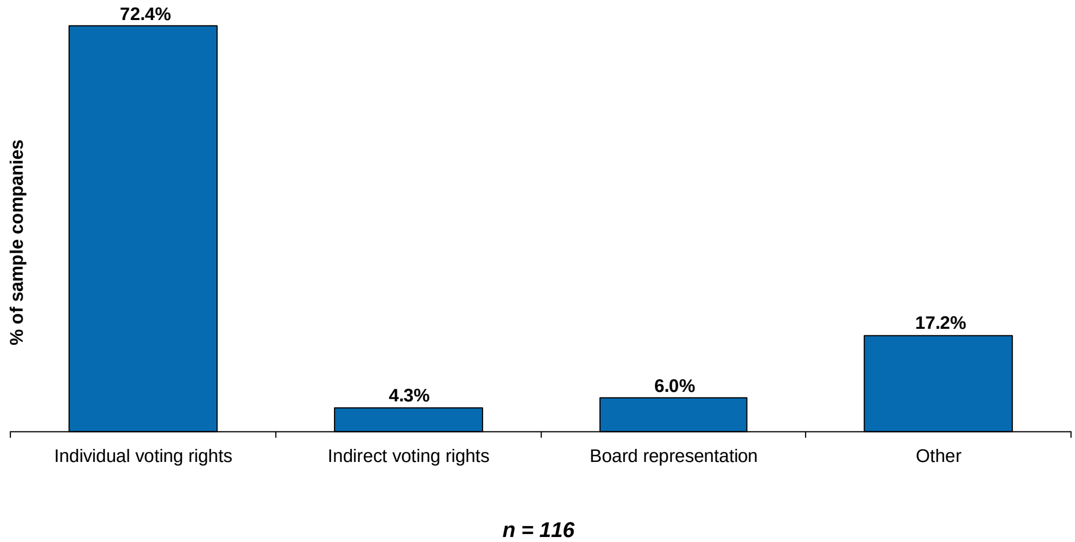


**Figure 40: Employee shareholder involvement in corporate decision-making**

Our findings suggest that the existence of an ESOP does not automatically lead to increased employee participation at the level of corporate decision-making. Writing on ESOPs in the UK, Pendleton has observed that there is little evidence to suggest that companies with employee share schemes develop mechanisms for employee participation in decision-making.[65] This observation would appear to apply equally in Australia.

[65] A Pendleton, 'Employee Share Ownership, Employment Relationships and Corporate Governance,' in B Harley et al (eds), *Participation and Democracy at Work: Essays in Honour of Harvie Ramsay* (2005) 75, 119.

## 6. COMPANY VIEWS ON THE REGULATORY FRAMEWORK

The final part of our survey sought to examine the relationship between company practice and the regulatory framework in corporate and taxation law. This was done in two principal ways. First, we asked respondents to indicate the extent to which they thought the concessions available for broad-based employee share plans influenced the decision to implement, and the design of, the broad-based plan. This was asked in relation to the concessions offered through Division 13A of the ITAA 1936 and concessions to disclosure, fundraising and licensing under the *Corporations Act* offered by ASIC. Second, we sought to elicit respondents' views on the adequacy of the current regulatory regime for employee share plans, in corporate and taxation law.

### 6.1. The perceived impact of the regulatory concessions

Respondents were asked to indicate the extent to which they agreed with key statements on a scale from 1 (strongly agree) to 5 (strongly disagree). Over one third of respondents (35.4 percent) either agreed or strongly agreed that the availability of tax concessions influenced their decision to introduce a broad-based employee share plan (see Figure 41). More respondents (44.9 percent) either agreed or strongly agreed that the availability of tax concessions influenced the *design* of their broad-based plan. In contrast, only 24.6 percent of respondents either agreed or strongly agreed that the availability of relief from disclosure and fundraising requirements offered by ASIC influenced their decision to implement a plan and 25.4 percent either agreed or strongly agreed that the availability of this relief influenced the design of the plan. Note that, as respondents were able to select more than one of the following options, the total percentage in Figure 40 exceeds 100.

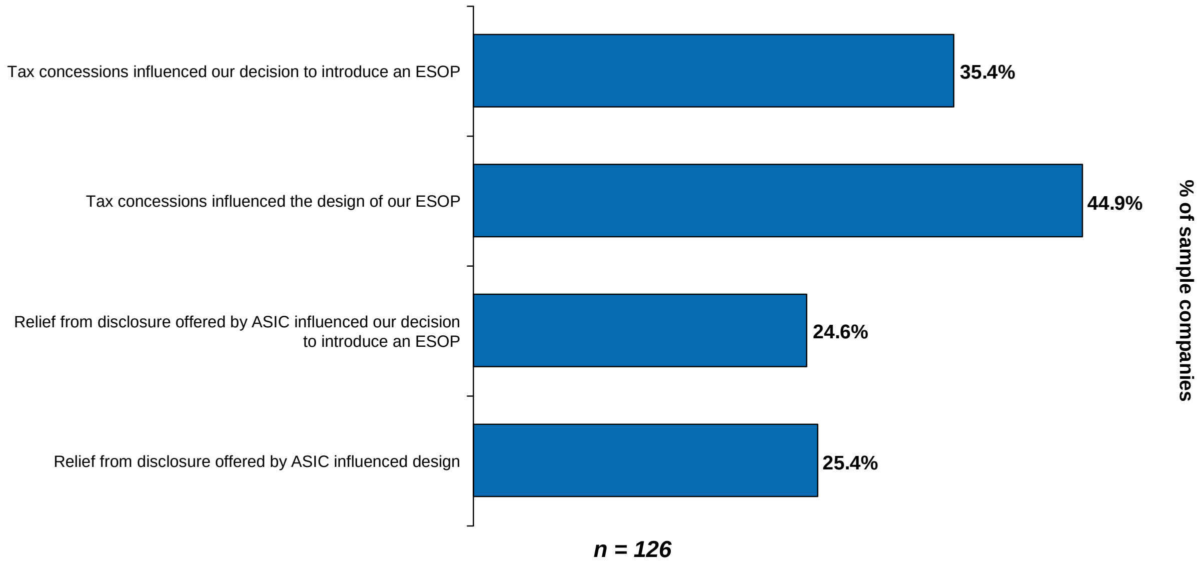


**Figure 41: Influence of tax incentives and disclosure relief**

The incidence of respondents who believed the availability of tax concessions influenced their decision to implement a plan is broadly consistent with the data in Figure 15, in which 32.6 percent of respondents either agreed or strongly agreed that taking advantage of the tax concessions was an objective of the company in implementing an employee share plan.

The survey findings would appear to suggest that a significant majority of companies would pursue employee share ownership in the absence of tax concessions. However, the findings also suggest that the concessional regimes are important in shaping company practice: that is, the features of the plan.

## 6.2. Views on regulatory reform

The final question of the survey asked respondents to indicate the extent to which they agreed with a number of statements concerning potential reforms to the existing regulatory framework. These statements were based on key recommendations identified in the Majority Report of the Standing Committee on Employment, Education and Workplace Relations' Inquiry into Employee Share Ownership in Australian Enterprises.[66]

The regulatory framework governing employee share ownership in Australia has changed little over the past decade, in contrast to considerable changes in labour market conditions and HRM practices

[66] See *Shared Endeavours*, above n 3.

within companies. The static nature of employee share ownership regulation suggests that we may find an increased disjuncture between the regulatory framework and objectives and views in this area. Note that, as respondents were able to select more than one of the following options, the total percentage in Figure 42 exceeds 100.

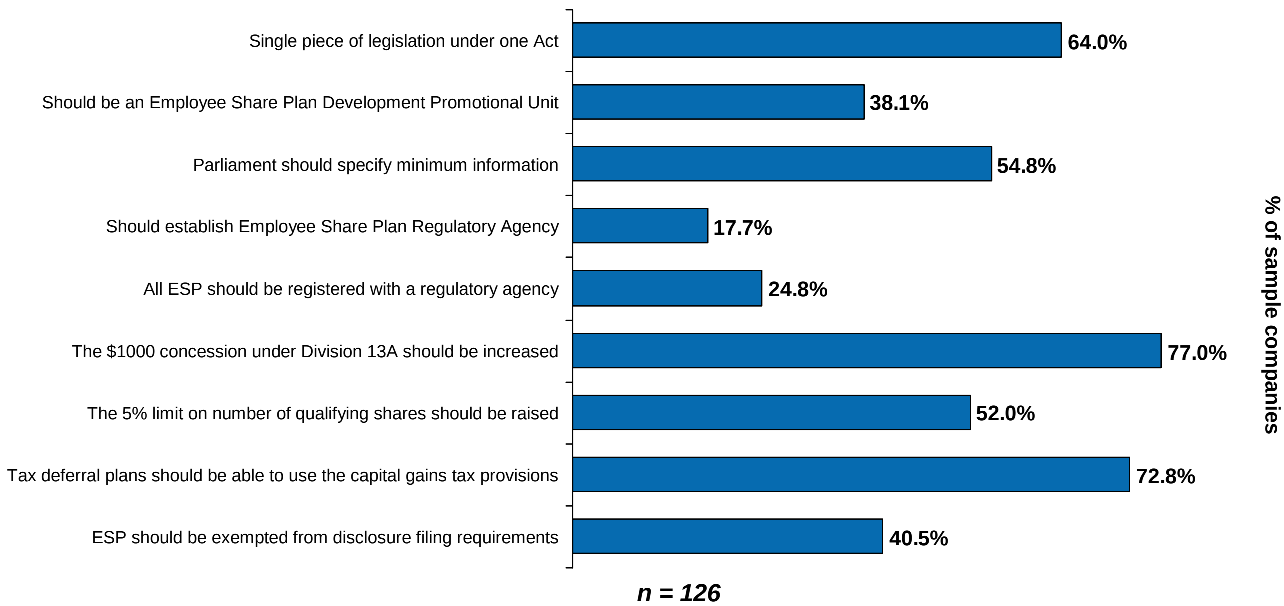


**Figure 42: Company views on regulatory framework**

Figure 42 demonstrates that there was strong support for the proposition that the $1000 tax exemption should be raised (77 percent of respondents); and that tax deferral plans should, like exempt plans, attract capital gains tax (CGT) treatment (72.8 percent of respondents).

There was also support for reducing the complexity of the current regulation. Sixty four percent of respondents agreed that there should be one single piece of legislation governing employee share ownership plans. Over half of all respondents agreed that Parliament should specify the minimum information companies are required to give to employees prior to the offer of securities as part of an ESOP.

These findings suggest that most listed companies who have broad-based ESOPs find the existing regulatory framework constraining.

Overall, our findings appear to reflect a tension between the desire of respondents for greater guidance and clarity in relation to employee share plans, while at the same time, a general reluctance to encourage more business regulation.

# 7. HYPOTHESES

In this part of the report, we present our findings relating to a number of hypotheses concerning company characteristics and the presence of an employee share plan.

Authors in Australia and internationally have sought to identify the characteristics of companies that adopt broad-based ESOPs. These explanations can be broadly categorised into two sets of factors: *structural* factors, such as size, ownership, industry and workforce composition; and *strategic* or *action* factors, which focus on the particular HRM strategies and styles adopted within the company.[67] Drawing upon the existing literature in Australia and other countries, we hypothesised that a number of company-level characteristics would be associated with the presence of an ESOP.

## 7.1. Hypothesis 1

**Companies that are large, measured by number of employees and annual turnover, will be more likely to have a broad-based employee share plan**

Overseas studies have found company size to be a strong predictor of the presence of an ESOP.[68] Traditionally, this has been a benchmark factor in predicting the presence of organisational performance pay.[69] Larger companies generally have greater resources and greater administrative and financial expertise to introduce and administer an ESOP.[70] They are also better able to spread the fixed costs of plan development and administration across a larger workforce.[71]

Company size has also been the focus of authors who hypothesise that employee share ownership is used to reduce agency costs. In this context, company size is used as proxy for underlying economic

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[67] M Poole and G Jenkins, 'Human Resource Management and the Theory of Rewards: Evidence from a National Survey' (1998) 36 *British Journal of Industrial Relations* 227, 229-30.

[68] See, eg, D L Kruse, 'Why Do Firms Adopt Profit-Sharing and Employee Ownership Plans?' (1996) 34 *British Journal of Industrial Relations* 515; R J Long, 'The Incidence and Nature of Employee Profit Sharing and Share Ownership in Canada' (1992) 47 *Industrial Relations* 712; A Pendleton, E Poutsma, J Van Ommeren and C Brewster, 'Employee Share Ownership and Profit-Sharing in the European Union' (European Foundation for the Improvement of Living and Working Conditions, 2001) 48.

[69] C Brown, 'Firms' Choice of Method of Pay' (1990) 43 *Industrial and Labour Relations Review* 143; Long and Shields, above n 7, 1783; Kruse, above n 69; Long, above n 69; M Festing, Y Groening, R Kabst and W Weber, 'Financial Participation in Europe - Determinants and Outcomes' (1999) 20 *Economic and Industrial Democracy* 295; Pendleton et al, 'The Incidence and Determinants of Employee Share Ownership and Profit Sharing in Europe', above n 7; and Baddon, above n 63, 250-275.

[70] Brown, above n 70.

[71] Ibid.

processes and relationships such as the cost of monitoring work performance and the need to enhance employee cooperation.[72] Drawing upon agency theory, scholars have reasoned that, as companies grow larger, it becomes increasingly difficult and costly for management to monitor employees.[73] Employee share ownership is used as a means of ameliorating the 'free-rider' problem. The use of company size as a proxy for employee monitoring costs, however, does have some problems, as it is impossible to determine whether a higher incidence of ESOPs in larger companies does indeed reflect employee monitoring costs or whether these companies are simply implementing ESOPs because they face lower administrative costs in doing so.[74]

Other empirical studies in Australia have found size to be a strong predictor of organisational performance pay,[75] and employee share ownership plans more specifically.[76] The ESODU, for example, found that businesses with over 100 employees, more than 50 offices in Australia and an annual turnover of over $50 million were more likely to have an ESOP.[77] Similar findings have been produced overseas.[78]

While the weight of previous studies suggests a positive correlation between company size and the presence of an ESOP, this study neither affirmed nor disaffirmed this hypothesis. There was no statistically significant correlation between company size and the presence of a broad-based employee share plan in the survey results. Whilst larger companies were more likely than smaller companies to have an ESOP, the difference was not statistically significant. It is possible that the incidence of employee share plans is in fact higher in larger employers, but that our sample size (which contained a high incidence of SMEs) was not sufficient to demonstrate the existence of a significant correlation.

[72] See, eg, Kruse, above n 69; E Poutsma, P Ligthart and R Schouteten, 'Employee Share Schemes in Europe: the Influence of US Multinationals' (2005) 16 *Management Revue: The International Review of Management Studies* 99; and Pendleton et al, 'The Incidence and Determinants of Employee Share Ownership and profit Sharing in Europe', above n 7.

[73] See, eg, Pendleton et al, 'The Incidence and Determinants of Employee Share Ownership and profit Sharing in Europe', above n 7; and J Core and W Guay, 'Stock Option Plans for Non-Executive Employees' (2001) 61 *Journal of Financial Economics* 253.

[74] Pendleton et al, 'The Incidence and Determinants of Employee Share Ownership and profit Sharing in Europe', above n 7.

[75] Long and Shields, above n 7. The Australian phase involved a mail-out survey to 542 for-profit firms, with a final sample of 70 firms, of which 37.7% were publicly-traded firms: at 1795.

[76] ESODU research, above n 7, 14.

[77] Ibid.

[78] See, eg, Long, above n 69; Festing et al, above n 70; M Tremblay and D Chenevert, 'The Effectiveness of Compensation Strategies in International Technology Intensive Firms' (2004) 10 *International Journal of Technology Management* 1; Pendleton et al, 'The Incidence and Determinants of Employee Share Ownership and profit Sharing in Europe', above n 7; and Kruse, above n 69.

Other Australian studies also have a high proportion of SMEs in the Australian market.[79] Given that the Australian market is, itself, relatively small when compared with international markets it is not unexpected that the findings in the present study demonstrate only a marginal correlation between company size and the presence of a broad-based employee share plan. The present findings do not contradict earlier studies, they simply show that Australian market is distinctive.

### 7.2. Hypothesis 2

**Companies that have experienced growth over the past twelve months, measured by turnover and increased numbers of employees, will be more likely to have a broad-based employee share plan**

Companies with high rates of growth may be more likely to use ESOPs as this enables them to attract and retain employees while at the same time retaining the capital needed to fund continued expansion.[80] Company growth may also influence whether a company maintains an employee share plan: companies with lower rates of growth may choose to discontinue their plans because they are an unnecessary expense and/or because employees are dissatisfied with the performance of the plan.

The empirical evidence on the impact of company growth rates on ESOP adoption is ambiguous. In their study of British firms, Poole and Jenkins found that expanding companies with high levels of profitability were more likely to have an ESOP.[81] However, studies in Australia, Canada and the European Union have found no significant relationship between employee share ownership and company growth.[82]

We hypothesised that companies that have experienced growth over the past twelve months, measured by turnover and increases in employee numbers, will be more likely to have a broad-based ESOP. Conversely, companies that have experienced negative growth will be more likely to have abandoned an ESOP or not have implemented one.

This hypothesis was partly confirmed. We found that companies who had experienced growth over the past twelve months with respect to the number of employees were significantly more likely (at the five percent level) to have a broad-based ESOP. With respect to growth in annual turnover,

[79] Long and Shields, above n 7, 1789.
[80] Ibid.
[81] M Poole and G Jenkins, 'Human Resource Management and the Theory of Rewards: Evidence from a National Survey' (1998) 36 *British Journal of Industrial Relations* 227.

however, the results were not statistically significant. However, the results are suggestive of a correlation in that 60.8 percent of companies that reported an increase in annual turnover over the past twelve months had a broad-based ESOP, while only 48.8 percent of companies reporting a decrease in annual turnover over the past twelve months had a broad-based ESOP.

### 7.3. Hypothesis 3

**Companies with a centralised HR function will be more likely to have an ESOP**

We hypothesised that there would be a significant correlation between the existence of a centralised HR function and the presence of an employee share plan. Employee share ownership is regarded as a sophisticated HR practice, and is often used in conjunction with a range of other HRM strategies. Moreover, a relatively developed HR function is necessary to develop and administer an employee share ownership plan. Overseas research has found that companies without a written HR strategy are significantly less likely to have an employee share ownership scheme.[83]

This hypothesis was confirmed. Companies with a centralised HR function were significantly more likely (at the one percent level) to have a broad-based employee share plan.

### 7.4. Hypothesis 4

**There will be significant industry or sectoral differences in the incidence of ESOPs**

The industry sector in which the company is located may also influence whether or not it has an employee share plan. Quantitative studies in Australia have found that companies in the construction, mining, manufacturing, finance and insurance and the communication industries are more likely to have an ESOP. In 2004, ESODU research found that manufacturing had the highest incidence of employee share ownership (22 percent), followed by finance and insurance (19 percent) and communication services (15 percent).[84] The ESODU research also found that broad-based plans were more likely to be found in construction (84 percent of plans); manufacturing (92 percent) and least likely in retail (14 percent) and property and business services (20 percent). In the following year Australian Bureau of Statistics research found that the finance and insurance

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[82] See Long and Shields, above n 7; and Pendleton et al, 'The Incidence and Determinants of Employee Share Ownership and profit Sharing in Europe', above n 7, 16.
[83] Ibid, 78.
[84] ESODU Research, above n 7, 23.

industry had the highest proportion of employees holding shares in the company in which they were employed (32 percent). While only 4 percent of employees worked in finance and insurance, this industry accounted for 21 percent of all employees who received shares as an employment benefit. The ABS research found that the finance industry was followed by mining (16 percent) and communication services (16 percent).[85] Studies have consistently found that ESOPs will be more likely in certain industry sectors, such as manufacturing and finance and insurance. It should be noted that in both the ESODU[86] and ABS[87] findings, there was a high representation by the finance and insurance industry. The inclusion of employee share ownership provisions in enterprise bargaining agreements in the major banks was a very strong influence on the results. In its research, the ABS noted that the industries with high levels of employee share ownership tended to reflect the influence of a small number of very large companies in those industries.

The reasons for the high incidence of ESOPs in some industries but not others are not always clear. The popularity of ESOPs in the finance sector has been explained by the fact that employers and employees in this industry have a greater knowledge of how these schemes work.

It has also been hypothesised that broad-based ESOPs are more common in industries with a higher concentration of non-manual workers, as these workers are more likely to be inclined towards non-cash forms of savings.[88]

Long and Shields observe that companies in industries where activity is focused on producing physical output (such as manufacturing) may be more likely to use incentives based on individual or group results, whereas those in industries characterised by revenue volatility (that is, where there are significant fluctuations in industry output each year) may favour profit sharing, as this is more closely linked to ‘capacity to pay’. These include industries such as resources and retailing.[89]

Differences between industries may also be explained by fashion or benchmarking, as companies within an industry seek to imitate each other. Companies may also find it necessary to implement an ESOP to compete for employee recruitment and retention within an industry.

Unfortunately, the low sample sizes for most industry groups in our survey results rendered it impossible to determine what industries were statistically more likely to have broad-based ESOPs.

[85] ABS, ‘Spotlight: Employee Share Schemes,’ Australian Labour Market Statistics, Cat.No.6105.0, 2005.
[86] ESODU Research, above n 7.
[87] ABS, ‘Spotlight: Employee Share Schemes, Australian Labour Market Statistics’, above n 86.
[88] Pendleton et al, ‘The Incidence and Determinants of Employee Share Ownership and profit Sharing in Europe’, above n 7, 53.

### 7.5. Hypothesis 5

**Companies within the same industry will tend to have similar types of plans**

We hypothesised that companies in the same industry would tend to have similar types of plans. This is based largely on the reasoning that companies will tend to imitate other companies who are direct competitors in their industry. Unfortunately, as was the case for hypothesis 4 above, our sample sizes in different industries were too small to draw any conclusions.

### 7.6 Hypothesis 6

**Companies which have a majority of professional, technical and scientific workers will be more likely to have a plan**

The composition of a company's workforce may influence remuneration strategies, including the use of employee share plans.[90] A more highly educated workforce may be more motivated by employee share plans as they are more likely to understand them and may have a greater potential to influence performance results.[91]

This hypothesis was not confirmed by the results. Companies with higher percentages of professional, technical and scientific workers were no more likely to have an employee share ownership plan than companies with higher percentages of other categories of workers.

### 7.7. Hypothesis 7

**Companies which have a majority of professional, technical and scientific workers will be more likely to have ESOPs that give employees choice as to how they wish to invest in the plan, and to have a tax deferred rather than a tax-exempt plan**

We hypothesised that companies with educated and skilled workforces might be more likely to provide their employees with choice in the nature of their investment. This would involve providing a tax deferred rather than a tax exempt plan as the latter is limited to discounts of up to $1000 per year. We reasoned that these employees would be more likely to be familiar with how employee

[89] Long and Shields, above n 7, 1789.
[90] Ibid.
[91] Ibid.

share plans operated and to desire greater choice and control with regards to the nature and extent of their participation.

This hypothesis was not confirmed. The data did show, however, that companies with a high percentage of professional, technical and scientific workers were significantly less likely (at the one percent level) to have a broad-based plan that issued shares and significantly more likely (at the one percent level) to have a plan that used options.

### 7.8. Hypothesis 8

**The more part-time and casual employees a company has, the less likely it will be that it has a plan**

We hypothesised that companies with more part-time and casual employees would be less likely to implement an ESOP. This is because ESOPs tend to rely on employees being with the company for a significant period of time, and they are often directed at fostering long-term commitment to the company. For these reasons, we would anticipate that ESOPs would be more likely to be present in companies with a larger 'core' workforce of full-time employees. Another reason informing this hypothesis is the structure of the regulatory framework, which promotes employee share ownership participation among full time and long term part-time employees.

The existing evidence on this association is ambiguous. Long and Shields found to their surprise that companies in Australia with a higher proportion of part-time and casual employees were more likely to have forms of group-based performance pay.[92] In the UK, however, analysis of the 2004 national Workplace Employment Relations Survey (WERS) revealed no relationship between workforce composition and the presence of an employee share plan.[93]

Our study confirmed this hypothesis. Companies with a higher proportion of full-time employees were significantly more likely (at the 5 percent level) to have a broad-based employee share plan.

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[92] Ibid.
[93] A Pendleton, Presentation to the Australian Employee Ownership Association, 2007, on file with authors.

### 7.9. Hypothesis 9

**Companies with a higher union density will be less likely to have a broad-based ESOP**

We hypothesised that companies with a higher union density would be less likely to have a plan. Unions have traditionally been hostile or apathetic to employee share plans where they require employee contribution or are used as a substitute rather than a complement to fixed/standard wages.[94] This would suggest that companies with higher rates of union density would be less likely to have an ESOP. There is little empirical data on this question in Australia. Long and Shields found no significant relationship between unionisation and employee share plans in Australia.[95] The overseas evidence is equivocal. From their analysis of financial participation in four European countries, Festing et al found a negative relationship between employee share ownership and union density.[96] Another pan-European study found a weak relationship between union density and broad-based equity plans, though union density was inversely related to the presence of a narrow-based ESOP.[97]

In the UK, Baddon et al found that employee share plans were more common in workplaces with union representation and collective bargaining.[98] A recent study, based on the UK Workplace Employee Relations Survey 1998, found that unions had no influence, either positively or negatively, on the use of share plans. [99] In the US, Kruse concluded from his analysis of 500 publicly listed firms, that there was no significant relationship between union density and the presence of an ESOP.[100] In 2006, Kroumova and Sesil found that there was a negative correlation between unions and the presence of broad-based stock options plans.[101]

Our data did not reveal any significant correlation between union density and the presence or absence of a plan. However, our capacity to test this hypothesis was very limited given the low numbers of companies in the sample with trade union members.

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[94] Finance Sector Union of Australia, Submission no. 29; The Australian Manufacturing Worker's Union, Submission no. 12; and the Australian Council of Trade Unions, Submission no. 27, to the House of Representatives Standing Committee on Employment, Education and Workplace Relations' Inquiry into Employee Share Ownership in Australian Enterprises, September 2000.
[95] Long and Shields, above n 7.
[96] Festing et al, above n 70.
[97] Pendleton et al, 'The Incidence and Determinants of Employee Share Ownership and profit Sharing in Europe', above n 7, 164.
[98] Baddon et al, above n 63.
[99] A Pendleton, 'Incentives, Monitoring, and Employee Stock Ownership Plans: New Evidence and Interpretations' (2006) 45 *Industrial Relation*s 753.
[100] Kruse, above n 69.

### 7.10. Hypothesis 10

**Companies with a higher shareholder influence orientation will be more likely to have a broad-based ESOP**

Some authors have hypothesised that employee share ownership is more likely to be found in companies with higher shareholder influence or 'shareholder value orientations'.[102] In a European study, Kurdelbusch found a strong correlation between the flexibility of remuneration schemes for non-managerial employees and shareholder value orientation in large German companies.[103] There appear to be several possible explanations for why companies with a higher shareholder value orientation would have an ESOP. First, there is the 'trickle down' effect: performance-related pay for executives is a key characteristic of a high shareholder orientation company[104] and companies may then implement broader-based ESOPs to appear 'fairer' on their own/in response to employee demands.[105] Employee share ownership plans may also signal to employees the importance of financial results and investor returns.[106]

This hypothesis was not confirmed: there was no statistically significant relationship between high shareholder influence and the presence of a broad-based ESOP. However we found that companies with higher shareholder influence were significantly more likely (at the five percent level) to have some type of organisation level performance-based pay.

### 7.11. Hypothesis 11

**Companies with broad-based ESOPs will be more likely to have other forms of direct employee participation and communication**

While this survey did not explore the nature of companies' HRM practices in depth, we included a question which sought to tentatively explore the relationship between the presence of a broad-based ESOP and other forms of direct employee participation. This question inquired into the presence within the company of four common forms of direct employee participation: a joint committee of managers and employees primarily concerned with consultation (e.g. a joint consultative committee

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[101] M K Kroumova, and J C Sesil, 'Intellectual Capital, Monitoring and Risk: What predicts the Adoption of Employee Stock Options?' (2006) 45 *Industrial Relations* 734.
[102] A Kurdelbusch, 'Multinationals and the Rise of Variable Pay in Germany' (2002) 8 *European Journal of Industrial Relations* 325, 338–40.
[103] Ibid.
[104] Ibid, 338.
[105] Ibid, 339.

or JCC); a formal structure for sharing company information with employees (e.g. information on company finances and business strategy); a formal structure for communications between all levels of employees and management (e.g. quality circles, regular employee surveys, suggestion schemes); and business literacy training for all employees.

Our hypothesis – that companies with ESOPs would be more likely to have other forms of direct employee participation - is informed by a number of considerations. First, these practices tend to be directed at the same objective: that is, to foster a sense of employee involvement in, and cooperation with, the company. Second, authors have theorised that financial participation (including through ESOPs) and direct forms of employee participation are complementary, in that they work together to foster greater employee identification with the company and cooperation. They also tend to be intertwined in that financial participation may be seen as a reward for involving oneself in direct forms of participation, and involvement in a financial participation scheme may foster a greater desire to be aware of, and involved in, company decisions.[107] This reasoning is supported by empirical evidence indicating that companies with ESOPs also tend to have a range of mechanisms to facilitate employee involvement.[108] However, as Pendleton notes, the forms of employee involvement adopted alongside ESOPs rarely provide rights to employees to influence what are regarded as management decisions: rather, they are designed to promote information sharing and to foster a sense of engagement and involvement in the company.[109]

We found that companies with broad-based ESOPs were significantly more likely to have structures directed at communicating with employees: that is, a formal structure for sharing information and a formal structure for communicating with employees (both at the one percent level).

In Europe, Pendleton et al have also found that businesses with broad-based ESOPs are more likely to have various forms of employee communications.[110] They identify three main explanations for this relationship. First, businesses may view ESOPs (which operate in the business rather than the employment stream of the company) as complements to employment-related initiatives (such as

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[106] B Black, H Gospel and A Pendleton, ‘Finance, Corporate Governance and the Employment Relationship’ (2007) 46 *Industrial Relations* 643, 645.

[107] Pendleton et al, ‘The Incidence and Determinants of Employee Share Ownership and profit Sharing in Europe’, above n 7.

[108] Pendleton, above n 37, 33. See also A Pendleton et al, ‘Employee Share Ownership and Profit-Sharing in the European Union’, above n 69, 18; and M Poole, ‘Factors affecting the Development of Employee Financial Participation in Contemporary Britain: Evidence from a National Survey’ (1988) 26 *British Journal of Industrial Relations* 21.

[109] Pendleton, above n 37.

employee communications) and so implement both. Second, both broad-based ESOPs and company initiatives directed at communicating with employees may simply reflect a sophisticated HR function: that is, they are not viewed as related. Finally, Pendleton et al posit that implementation and administration of ESOPs requires extensive communication with employees and this necessitates the establishment and maintenance of forms of communication.

[110] Pendleton et al, 'Employee Share Ownership and Profit Sharing in the European Union', above n 69, 68.

## 8. CONCLUSION

This research report presents findings from a survey of employee share ownership practice in ASX-listed companies. Our findings suggest that broad-based ESOPs have become an increasingly popular form of remuneration benefit since 2000. Over half of all companies who responded to the survey reported having at least one broad-based ESOP in operation.

There appears to be significant variation in how companies are structuring their ESOPs. While it is not possible to draw conclusive observations from this survey, our findings suggest that the existing regulatory framework is having a significant influence in shaping the structure of ESOPs. For example, over half of plans capped employee contributions at $1000 per year and the overwhelming majority of plans restricted eligibility to participate to permanent full-time and part-time employees. Both these characteristics reflect structural requirements for accessing the taxation concessions. Around 45 percent of respondents agreed or strongly agreed that the tax concessions influenced the design of their company's broad-based ESOP.

To our knowledge, this study is the first to examine the extent of employee involvement in the design and administration of ESOPs in Australia. The study found that broad-based employee share ownership in ASX-listed companies is overwhelmingly a management initiated and driven phenomenon. Employees and/or their representatives are rarely involved in decisions relating to the introduction of a plan or its design and administration.

In this research, we also sought to elicit company views on the adequacy of the existing regulatory framework for broad-based employee share ownership in corporate and taxation law. The majority of respondents believed that the current regulations were too complex and constraining.  There was strong support for the propositions that the $1000 tax concession be increased and that the CGT tax provisions should be extended to tax deferral plans. Over sixty percent of respondents agreed or strongly agreed that all ESOP regulation should be in a single piece of legislation.

Finally, this survey provided us with an opportunity to test some of the commonly identified determinants of ESOPs in the Australian context. Three structural variables were found to have a significant and positive relationship with the presence of an ESOP: company growth over the past twelve months (measured by increases in number of employees); a centralised HR function; and the composition of a company's workforce (the proportion of full time employees).

While our findings in Part 7 were limited due to our sample size, the results also suggest that the conventional single variants did not provide a clear indication of the presence or effect of ESOPs in Australia. Studies in the future may benefit from testing multiple variants, or from focusing less on structural variables and more on the relationship between employee share ownership and company HR strategy.

# APPENDIX: EMPLOYEE SHARE PLAN SURVEY

## PART A: ABOUT YOUR COMPANY

**1. How many employees does your company have in Australia?**

☐ Less than 50
☐ 201 – 500
☐ 51 – 100
☐ 501 – 1000
☐ 101 – 200
☐ Over 1000

**2. Has the number of employees in your company increased, decreased or stayed the same over the past twelve months?**

☐ Increased
☐ Stayed the same
☐ Decreased

**3. What was the annual turnover of your company in the past twelve months?**

☐ Less than $20M
☐ $50M – less than $100M
☐ $20M – less than $50M
☐ $100M or more

**4. Has the annual turnover of your company increased, decreased or stayed the same over the past twelve months?**

☐ Increased
☐ Stayed the same
☐ Decreased

**5. Does your company have a centralised human resource management function?**

☐ Yes
☐ No

**6. Is this company a subsidiary of an overseas-based company?**

☐ No

☐ Yes, a subsidiary of a US-based company

☐ Yes, a subsidiary of a EU-based company

☐ Yes, other. Please specify: ____________________

7. **What type of industrial instrument are the majority of <u>non-managerial</u> employees at this company covered by:**

☐ A union collective workplace agreement

☐ A non-union collective workplace agreement

☐ Australian Workplace Agreements (AWAs)

☐ A union Greenfield agreement

☐ An employer Greenfield agreement

☐ A multiple business agreement

☐ Individual common law agreements

☐ An award

☐ An unregistered collective common law agreement

8. **What percentage of the total workers engaged by your company are:**

Full-time permanent? ____%

Part-time permanent? ____%

Casual ?____%

Contractors ____%

9. **Approximately, what percentage of this company's Australian employees are trade union members?**

______ %

10. **Approximately, what percentage of workers engaged (either as employees or contractors) by your company fall within the following occupational groups?**

Professional, technical and scientific ____%

Clerical and secretarial ____%

Sales and personal service ____%

Craft and skilled manual ____%

Semi-skilled and unskilled manual ____%

11. **Which of the following best describes the industry in which your company operates?**

☐ Agriculture, Forestry and Fishing

☐ Manufacturing

☐ Mining

☐ Electricity, Gas, Water and Waste services

☐ Construction

☐ Wholesale Trade

☐ Retail Trade

☐ Accommodation and Food Services

☐ Transport, Postal and Warehousing

☐ Information Media and Telecommunications

☐ Financial and Insurance Services

☐ Rental, Hiring and Real Estate Services

☐ Professional, Scientific and Technical Services

☐ Administrative and Support Services

☐ Public Administration and Safety

☐ Education and Training

☐ Health Care and Social Assistance

☐ Arts and Recreation Services

☐ Other Services

12. **Thinking about the relationship between the company and its <u>shareholders</u> over the past year, please indicate the extent to which you agree or disagree with the following statements. If your company has a large number of shareholders, your response need not be true of every shareholder. It is sufficient if it is only true of a particular shareholder or group of shareholders.**

    *Please circle the number which accurately reflects your position.*

    **1 = Strongly agree 2 = Agree 3 = Unsure 4 = Disagree 5 = Strongly disagree**

| **a) Shareholders had the power to influence management** | **1** | **2** | **3** | **4** | **5** |
|---|---|---|---|---|---|
| b) Shareholders were active in pursuing demands or wishes which they felt were important | 1 | 2 | 3 | 4 | 5 |
| c) Shareholders actively sought the attention of the management team | 1 | 2 | 3 | 4 | 5 |
| d) Shareholders urgently communicated their demands or wishes to our company | 1 | 2 | 3 | 4 | 5 |
| e) Shareholders demands or wishes were viewed by the management team as legitimate | 1 | 2 | 3 | 4 | 5 |
| f) Shareholders received a high degree of time and attention from our management team | 1 | 2 | 3 | 4 | 5 |
| g) Satisfying the demands or wishes of shareholders was important to the management team | 1 | 2 | 3 | 4 | 5 |

13. **Which of the following pay practices for <u>non-managerial</u> employees are there in your company?**

    *More than one answer is possible.*

☐ Individual performance-related pay

☐ Group performance-related pay

☐ Organisational performance-related pay

☐ None of the above pay practices

**14. Which of the following practices are there in your company?**

***More than one answer is possible.***

☐ A joint committee of managers and employees primarily concerned with consultation (e.g. a joint consultative committee)

☐ A formal structure for sharing company information with employees (e.g. information on company finances and business strategy)

☐ A formal structure for communication between all levels of employees and management (e.g. quality circles, regular employee surveys, suggestion schemes)

☐ Business literacy training for all employees

☐ None of the above practices

**15. Does your company currently have an employee share, option or rights plan that is open to <u>executive/ managerial employees</u> only (that is, a 'narrow-based' plan)?**

☐ Yes ☐ No

**16. Does your company currently have an employee share, option or rights plan that is open to the majority of <u>non-managerial employees</u> (that is, a 'broad-based' plan)?**

☐ Yes

☐ No, this company has never had one

☐ No, this company used to have one

**If you answered 'yes' to the above question, please proceed to Part B. If you answered 'no', please continue to the next question.**

**17. If you have discontinued a broad-based employee share plan, please specify why it was discontinued:**

______________________________________________________________________________
______________________________________________________________________________
____________________________

18. **To what extent have the following factors been a consideration of the company in deciding not to have a <u>broad-based</u> employee share plan?**

    ***Please circle the number which accurately reflects your position.***

    **1 = To a large extent  2 = To some extent  3 = Unsure  4 = To a small extent  5 = Definitely not**

| | | | | | |
|---|---|---|---|---|---|
| **a) The cost of compliance with tax requirements** | **1** | **2** | **3** | **4** | **5** |
| b) The cost of implementation | 1 | 2 | 3 | 4 | 5 |
| b) Few other companies in our industry have plans | 1 | 2 | 3 | 4 | 5 |
| c) Existing shareholders do not want employees to hold shares in the company | 1 | 2 | 3 | 4 | 5 |
| d) Trade unions are opposed to plans | 1 | 2 | 3 | 4 | 5 |
| e) The benefits of having a plan are not clear | 1 | 2 | 3 | 4 | 5 |
| f) Plan administration costs are high | 1 | 2 | 3 | 4 | 5 |
| g) Employees prefer other benefits/ rewards | 1 | 2 | 3 | 4 | 5 |
| h) The cost of compliance with corporate law requirements | 1 | 2 | 3 | 4 | 5 |
| i) Lack of knowledge on employee share plans | 1 | 2 | 3 | 4 | 5 |
| j) Share market volatility | 1 | 2 | 3 | 4 | 5 |
| k) Expensing the benefits provided under employee share plans in accordance with new accounting standard AASB 2 is too costly | 1 | 2 | 3 | 4 | 5 |

**Thank you for your participation. Please return this survey in the reply paid envelope provided.**

## PART B: ABOUT THE EMPLOYEE SHARE PLAN AT YOUR COMPANY

19. **In what year did your company introduce its first <u>broad-based</u> employee share plan?** *A 'broad-based' plan is one that is open to the majority of non-managerial employees within the company.*

    __________

20. **Which of the following objectives is your company seeking to achieve through the employee share plan?**

    *Please circle the number which accurately reflects your position.*

    **1 = Strongly agree  2 = Agree  3 = Unsure  4 = Disagree  5 = Strongly disagree**

| | | | | | |
|---|---|---|---|---|---|
| **Attracting employees** | **1** | **2** | **3** | **4** | **5** |

| | | | | | |
|---|---|---|---|---|---|
| Raising capital | 1 | 2 | 3 | 4 | 5 |
| Showing employees that the company values them | 1 | 2 | 3 | 4 | 5 |
| Aligning employee interests with shareholder interests | 1 | 2 | 3 | 4 | 5 |
| Increasing flexibility in remuneration | 1 | 2 | 3 | 4 | 5 |
| Retaining employees | 1 | 2 | 3 | 4 | 5 |
| Satisfying employee demand for an employee share plan | 1 | 2 | 3 | 4 | 5 |
| Inhibiting takeovers of the company | 1 | 2 | 3 | 4 | 5 |
| Encouraging employees to increase productivity | 1 | 2 | 3 | 4 | 5 |
| Facilitating additional savings by employees: eg for retirement | 1 | 2 | 3 | 4 | 5 |
| Sharing financial success with employees | 1 | 2 | 3 | 4 | 5 |
| Ensuring that the benefits packages offered by your company matches those offered by competitors | 1 | 2 | 3 | 4 | 5 |
| To take advantage of tax concessions | 1 | 2 | 3 | 4 | 5 |
| Promoting a public image of the company as a progressive corporate citizen | 1 | 2 | 3 | 4 | 5 |
| Other, please specify: | | | | | |

**21. How many employee share plans that are open to non-managerial employees currently operate within your company?**

☐ 1

☐ 2

☐ More than 2.

*If you have one plan only, please complete the first column below. If you have two plans, please complete Plan A and Plan B. If you have more than two plans in operation, please provide details of the two plans which have the highest numbers of participants.*

**PLAN A**

**22A. Which of the following best describes the broad-based plan offered by your company?**

☐ Tax exempt plan

**PLAN B**

**22B. Which of the following best describes the broad-based plan offered by your company?**

☐ Tax exempt plan

*Under this type of plan, designed to take advantage of the tax exemption available under Division 13A of the Income Tax Assessment Act 1936 (Cth), employees may receive up to $1000 worth of shares or rights tax free each year.*

☐ Tax deferred plan

*Under this type of plan, designed to take advantage of the deferred share benefit available under Division 13A of the Income Tax Assessment Act 1936 (Cth), employees may defer tax on the discount of the shares or rights for a maximum of 10 years.*

☐ Loan plan

*Loan plans allow fully paid shares to be provided to employees and the shares are paid for by the use of a loan. Restrictions are often placed on the shares while loans are being repaid.*

☐ Replicator plan

*This type of plan is structured to replicate a real employee share plan but it does not issue real shares or rights.*

☐ Other

**23A. What type of security is issued under the plan?**

☐ Shares

☐ Options

☐ Rights

☐ Other

**24A. Are the securities offered to employees at less than market value?**

☐ Yes

☐ No

**25A. What is the company contribution to the value of the securities?**

☐ None. Employee contributes 100%.

☐ Company contributes 100% of the  value of the

*Under this type of plan, designed to take advantage of the tax exemption available under Division 13A of the Income Tax Assessment Act 1936 (Cth), employees may receive up to $1000 worth of shares or rights tax free each year.*

☐ Tax deferred plan

*Under this type of plan, designed to take advantage of the deferred share benefit available under Division 13A of the Income Tax Assessment Act 1936 (Cth), employees may defer tax on the discount of the shares or rights for a maximum of 10 years.*

☐ Loan plan

*Loan plans allow fully paid shares to be provided to employees and the shares are paid for by the use of a loan. Restrictions are often placed on the shares while loans are being repaid.*

☐ Replicator plan

*This type of plan is structured to replicate a real employee share plan but it does not issue real shares or rights.*

☐ Other

**23B. What type of security is issued under the plan?**

☐ Shares

☐ Options

☐ Rights

☐ Other

**24B. Are the securities offered to employees at less than market value?**

☐ Yes

☐ No

**25B. What is the company contribution to the value of the securities?**

☐ None. Employee contributes 100%.

☐ Company contributes 100% of the value of the securities. Go to Q28A.

☐ Company contributes fixed dollar amount per employee

☐ Company matches employee contribution on a 1:1 basis

☐ Other, please specify (eg company matching on 1:2 basis): ____________

____________________________________

**26A. How is the <u>employee contribution</u> to the value of the securities made?**

☐ After-tax money

☐ Salary sacrifice

☐ Bonus sacrifice

☐ Profit share

☐ Other, please specify:_______

**27A. What, if any, is the maximum contribution an employee can make under the share plan each year?**

☐ $1000 or less

☐ Maximum value of $____

☐ Percentage of salary, please specify: ______%

☐ Percentage of bonus, please specify: _____%

**28A. Which groups of employees are eligible to participate in the plan?**

*More than one answer is possible.*

☐ Permanent full-time employees

☐ Permanent part-time employees

☐ Casual employees

☐ Contractors

☐ Other, please specify: ________

securities Go to Q28B.

☐ Company contributes fixed dollar amount per employee

☐ Company matches employee contribution on a 1:1 basis

☐ Other, please specify (eg company matching on 1:2 basis):______________

______________________________________

**26B. How is the <u>employee contribution</u> to the value of the securities made?**

☐ After-tax money

☐ Salary sacrifice

☐ Bonus sacrifice

☐ Profit share

☐ Other, please specify:_______

**27B. What, if any, is the maximum contribution an employee can make under the share plan each year?**

☐ $1000 or less

☐ Maximum value of $____

☐ Percentage of salary, please specify: ______%

☐ Percentage of bonus, please specify: _____%

**28B. Which groups of employees are eligible to participate in the plan?**

*More than one answer is possible.*

☐ Permanent full-time employees

☐ Permanent part-time employees

☐ Casual employees

☐ Contractors

☐ Other, please specify: ________

**29A. Is there a minimum period of service requirement before an employee is eligible to participate in the plan?**

☐ No

☐ Yes, please specify: ______________________________

**30A. Is the grant of securities to employees under the plan contingent upon the employee or the company achieving certain performance hurdles?**

☐ No

☐ Yes, employee completing satisfactory performance review

☐ Yes, company achieving certain performance targets

☐ Yes, employee remaining with company for specific period of time.

☐ Yes, other, please specify: ______

______________________________

**31A. How are allocations to individual employees determined under the plan?**

☐ All employees are entitled to receive the same value of securities

☐ Linked to salary level

☐ Linked to job grade or position

☐ Linked to length of employment

☐ Linked to individual performance

☐ Other, please specify: __________

**32A. What, if any, restrictions on the securities are imposed once vested?**

*More than one answer is possible*

☐ No restrictions. Ordinary shares

**29B. Is there a minimum period of service requirement before an employee is eligible to participate in the plan?**

☐ No

☐ Yes, please specify: ______________________________

**30B. Is the grant of securities to employees under the plan contingent upon the employee or the company achieving certain performance hurdles?**

☐ No

☐ Yes, employee completing satisfactory performance review

☐ Yes, company achieving certain performance targets

☐ Yes, employee remaining with company for specific period of time

☐ Yes, other, please specify: ______

______________________________

**31B. How are allocations to individual employees determined under the plan?**

☐ All employees are entitled to receive the same value of securities

☐ Linked to salary level

☐ Linked to job grade or position

☐ Linked to length of employment

☐ Linked to individual performance

☐ Other, please specify: __________

**32B. What, if any, restrictions on the securities are imposed once vested?**

*More than one answer is possible*

☐ No restrictions. Ordinary shares

☐ Restrictions on voting rights

☐ Restrictions on entitlements to dividends

☐ Restrictions on bonus issues

☐ Other, please specify: _____

**33A. What, if any, restrictions are imposed on the disposal of shares once vested?**

*More than one answer is possible*

☐ No restrictions.

☐ Employees may not dispose of shares (or certain proportion of shares) for certain period

☐ Employees may not dispose of shares until he or she leaves the company

☐ Trading restricted to trading windows

☐ Other, please specify: ________

**34A. What, if any, is the minimum holding period?**

☐ No minimum holding period

☐ One year

☐ Two years

☐ Three years

☐ Between three and five years

☐ More than five years

☐ Other, please specify: ________

**35A. What, if any, is the maximum holding period?**

☐ No maximum holding period

☐ One year

☐ Two years

☐ Three years

☐ Restrictions on voting rights

☐ Restrictions on entitlements to dividends

☐ Restrictions on bonus issues

☐ Other, please specify: _____

**33B. What, if any, restrictions are imposed on the disposal of shares once vested**?

*More than one answer is possible*

☐ No restrictions.

☐ Employees may not dispose of shares (or certain proportion of shares) for certain period

☐ Employees may not dispose of shares until he or she leaves the company

☐ Trading restricted to trading windows

☐ Other, please specify: ________

**34B. What, if any, is the minimum holding period?**

☐ No minimum holding period

☐ One year

☐ Two years

☐ Three years

☐ Between three and five years

☐ More than five years

☐ Other, please specify: ________

**35B. What, if any, is the maximum holding period?**

☐ No maximum holding period

☐ One year

☐ Two years

☐ Three years

☐ Three – five years

☐ Six – ten years

☐ More than ten years.

**36A. Is the share plan administered through a trust?**

☐ Yes

☐ No

☐ Three – five years

☐ Six – ten years

☐ More than ten years.

**36B. Is the share plan administered through a trust?**

☐ Yes

☐ No

## PART C: EMPLOYEE INVOLVEMENT AND PARTICIPATION

**37. Was the employee share plan(s) introduced as part of a formal agreement with employees or their representatives?**

☐ Agreement with trade union representatives

☐ Agreement with other employee representatives

☐ Ballot of the workforce

☐ No formal agreement – board or management decision only

☐ Other, please specify: _______________________________

**38. To what extent have employees or their representatives been involved in the following:**

*Please circle the number which accurately reflects your position.*

**1 = Not involved 2 = Informed about 3 = Consulted (asked their opinion)**

**4 = Took part in decision-making**

| **The funding of the plan** | **1** | **2** | **3** | **4** |
|---|---|---|---|---|
| Determining the eligibility criteria | 1 | 2 | 3 | 4 |
| Drafting the plan rules | 1 | 2 | 3 | 4 |
| Plan administration | 1 | 2 | 3 | 4 |
| Other, please specify: | | | | |

**39. How can the rules governing the employee share plan(s) be altered?**

☐ At any time, at the discretion of the board

☐ At any time, at the discretion of management

☐ Only with the consent of employee shareholders (or a proportion thereof)

☐ Other, please specify: _______

**40. If the plan(s) is administered through a trust, who selects the share plan trustees?**

☐ The company board

☐ Employee shareholders or their representatives

☐ Both of the above

☐ Other, please specify: _____

**41. What is the maximum percentage of your company's total equity made available to non-managerial employees through employee share plan(s)?**

______%

**42. What percentage of your company's total equity is currently owned by non-managerial employees?**

______ %

**43. What percentage of eligible non-managerial employees participate in the employee share plan(s)**

☐ All

☐ Almost all (80 – 90%)

☐ Most (60 – 79%)

☐ Around half (40 – 59%)

☐ Some (20 – 39%)

☐ Just a few (1 – 19%)

☐ None (0%)

**44. To what extent are employee shareholders or their representatives involved in corporate decision-making?**

☐ Employee shareholders have individual voting rights

☐ Employee shareholders have indirect voting rights via collective representation

☐ Employee shareholders are represented on the board

☐ Other, please specify: _______________

## PART D: YOUR VIEWS ON THE REGULATORY FRAMEWORK

**45. The Australian government offers a number of incentives for companies to introduce employee share plans. These include tax concessions (offered through Division 13A of the *Income Tax Assessment Act 1936* (Cth)) and disclosure, fundraising and licensing concessions under the *Corporations Act 2001* (Cth) and ASIC Class Order 03/184. We are interested in the extent to which these incentives have influenced your decision to implement a plan and the design of the plan. Please indicate the extent to which you agree or disagree with the following statements.**

*Please circle the number which accurately reflects your position*

**1 = Strongly agree  2 = Agree  3 = Unsure  4 = Disagree  5 = Strongly disagree**

| **a) The availability of tax concessions influenced our decision to introduce a broad-based employee share plan** | **1** | **2** | **3** | **4** | **5** |
|---|---|---|---|---|---|
| b) The availability of tax concessions influenced the design of our broad-based employee share plan | 1 | 2 | 3 | 4 | 5 |
| c) The availability of relief from disclosure and fundraising requirements offered by ASIC influenced our decision to introduce a broad-based employee share plan | 1 | 2 | 3 | 4 | 5 |
| d) The availability of relief from disclosure requirements (offered by ASIC) influenced the design of our broad-based employee share plan | 1 | 2 | 3 | 4 | 5 |

**46. In 2000, a parliamentary inquiry into employee share ownership identified a number of areas in which the current regulatory framework for employee share plans could be improved. We are interested in your views on some of these recommendations. Please indicate the extent to which you agree or disagree with the following statements.**

*Please circle the number which accurately reflects your position.*

**1 = Strongly agree  2 = Agree  3 = Unsure  4 = Disagree  5 = Strongly disagree**

| **a) Parliament should enact a single piece of legislation, bringing under one Act all laws governing employee share plans** | **1** | **2** | **3** | **4** | **5** |
|---|---|---|---|---|---|
| b) There should be an Employee Share Plan Development Promotional Unit within the Department of Workplace Relations, responsible for promoting employee share ownership and providing assistance to employers and employees | 1 | 2 | 3 | 4 | 5 |
| c) Parliament should specify, within legislation, the minimum information that all companies must provide to employees in relation to an employee share plan | 1 | 2 | 3 | 4 | 5 |
| d) The government should establish an Employee Share Plan Regulatory Agency, whose responsibilities would include administering share plan legislation, monitoring the operation of plans and advising the government as to potential reforms. | 1 | 2 | 3 | 4 | 5 |
| e) All employee share plans operating in Australia should be registered with a regulatory agency. This would enable, among other things, data to be collected and published regularly on current practice in employee share plans | 1 | 2 | 3 | 4 | 5 |

| | | | | | |
|---|---|---|---|---|---|
| f) The $1000 concession available to share plans operating under Division 13A should be increased | 1 | 2 | 3 | 4 | 5 |
| g) The 5% limit on the number of qualifying shares or rights that can be issued under an employee share plan should be raised. | 1 | 2 | 3 | 4 | 5 |
| h) Tax deferral plans should attract capital gains tax treatment | 1 | 2 | 3 | 4 | 5 |
| j) Employee share plans should be exempted from disclosure filing requirements under the *Corporations Act* | 1 | 2 | 3 | 4 | 5 |

**47. If there is anything we didn't cover that you think would help our research, please use the space below to record your suggestions:**

______________________________________________________________________________

______________________________________________________________________________

______________________________________________________________________________

______________________________________________________________________________

________________________________________________________

**Thank you for taking the time to complete this survey.**

**Please return it in the reply paid envelope provided.**