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The Impact of Shareholder Activism on Financial Reporting and Compensation: The Case of Employee Stock Options Expensing

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Abstract

We examine the economic consequences of more than 150 shareholder proposals to expense employee stock options (ESO) submitted during the proxy seasons of 2003 and 2004, the first case in which the SEC allowed a shareholder vote on an accounting matter. Our results indicate that these proposals affected accounting and compensation choices. Specifically, (i) targeted firms were more likely to adopt ESO expensing relative to a control sample of S&P 500 firms, (ii) among targeted firms, the likelihood of adoption increased in the degree of voting support for the proposal, and (iii) non-targeted firms were more likely to adopt ESO expensing when a peer firm was targeted. Additionally, (i) CEO pay decreased in firms in which the proposal was approved relative to a control sample of S&P 500 firms, and (ii) among targeted firms, approval of the proposal was associated with decreases in CEO compensation and the use of ESO in CEO pay. Our findings reveal an increasing influence of shareholder proposals on governance practices.

Keywords: [shareholder activism](#); [shareholder votes](#); [Executive Compensation](#); [stock option expensing](#); [corporate governance](#); [financial reporting](#); [Executive Compensation](#); [Financial Reporting](#); [Employee Stock Ownership Plan](#); [Corporate Governance](#); [Business and Shareholder Relations](#); [Investment Activism](#);

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