

Frederic W. Cook & Co., Inc.

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**Stock Plan Dilution and Negative  
Shareholder Votes - Update for 2000 Results**

Investor Responsibility Research Center (IRRC) has updated its study of dilution from equity plans at the S&P Super 1,500<sup>1</sup> and reports that average dilution for the full S&P Super 1,500 has increased from 11.6% in 1997<sup>2</sup> (the first time they studied the full S&P Super 1,500) to 14.6% in 2000.

**Total Potential Dilution:**

IRRC calculates dilution on a non-diluted basis and defines total potential dilution as:

$$\frac{\text{Stock Options Outstanding} + \text{Shares Available To be Granted} + \text{New Share Request}}{\text{Shares Outstanding}^3}$$

Potential dilution is higher in all of the sub-groups of the S&P Super 1,500 than in 1997 with the larger companies having a slightly higher increase. The 2000 dilution levels compared to 1997 are:

	<b>Average Total Potential Dilution from Stock Plans</b>		
	<b>1997</b>	<b>2000</b>	<b>% Change</b>
S&P 500	10.0%	13.1%	31.0%
S&P MidCap 400	10.5	13.9	32.4
S&P SmallCap 600	<u>13.8</u>	<u>16.8</u>	<u>21.7</u>
Total Super 1,500	11.6%	14.6%	25.9%

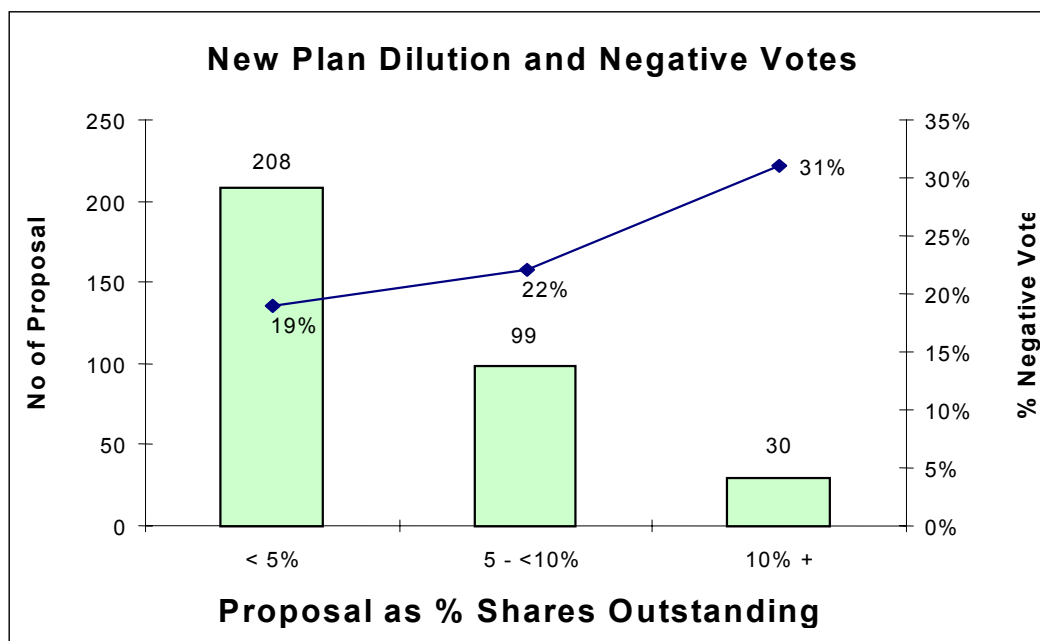
<sup>1</sup> Potential Dilution, 2000. Potential Dilution from Stock Plans at S&P Super 1,500 Companies, by Annick Siegl, Investor Responsibility Research Center

<sup>2</sup> See our letter of July 8, 1998

<sup>3</sup> For companies with more than one class of stock, the calculation is based on voting power, i.e. shares times their relative voting power

## Votes on New Plans

A total of 337 proposals for new or amended plans were presented to shareholders in 2000. Most share requests were for authorizations below 5% of shares outstanding; those above 10% received significant negative votes<sup>4</sup>. Average negative votes on all plans in 2000 was 20.7% versus 17.4% in 1997:



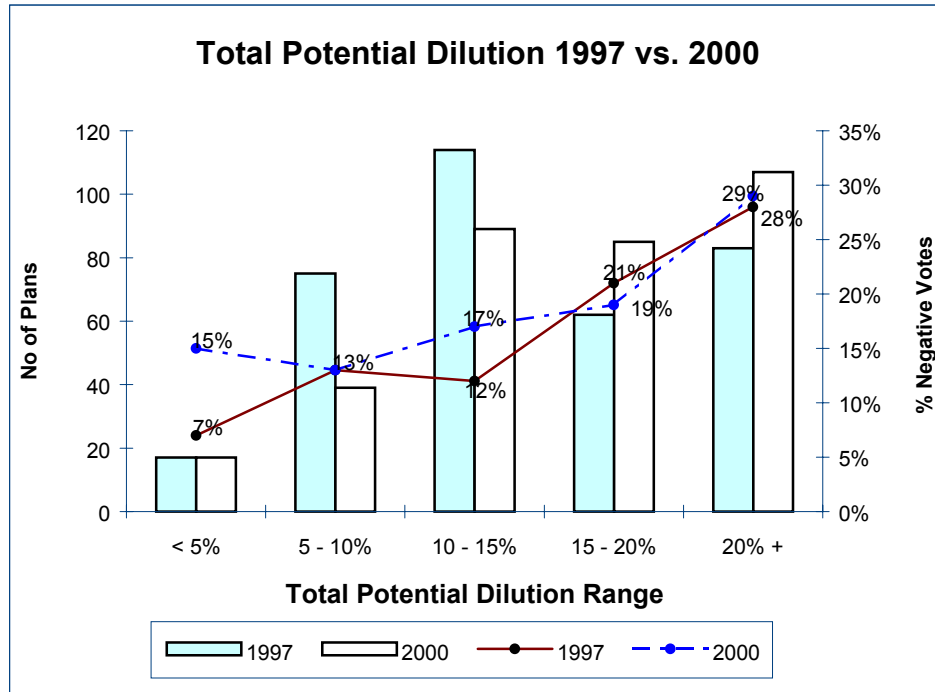
## Total Potential Dilution

Of these 337 proposals, 192, or 57%, would have resulting total potential dilution of more than 15% compared to 42% of the proposals presented to shareholders in 1997.

Total Potential Dilution	1997		2000		
	# of Plans	% of Total	# of Plans	% of Total	
<5%	17	5%	17	5%	
5-10%	75	21	39	12	
10-15%	114	32	89	26	
15-20%	62	18	85	25	} 57%
20%+	83	24	107	32	
	351	100%	337	100%	

<sup>4</sup> Percent negative vote is negative votes divided by total votes cast, including abstentions

The graph below illustrates the correlation between total potential dilution and negative shareholder vote. The patterns for the two years studied are similar, although the average negative votes in 2000 are higher for proposals resulting in relatively low potential dilution. It appears that stock plan proposals are drawing more negative votes, regardless of the dilution level.



**High Dilution Levels:**

The number of companies in the S&P Super 1,500 with very high potential dilution has increased since 1997. In 1997, only 13 companies had total potential dilution above 40%; in 2000, 21 do.

Total Potential Dilution	No. of Companies	
	1997	2000
40%-50%	9	10
50%-60%	2	4
60%-70%	1	2
70% or above	<u>1</u>	<u>5</u>
Total	13	21

**Plan Failure:**

Not surprisingly, with the increased dilution levels, six plans IRRC studied during the year actually failed in 2000 versus three in 1997. High dilution may not be the only reason that plans fail but it is a primary consideration in voting decisions. And, the number of failures may be understated because companies often test the water first and withdraw plans that might fail.

**Future:**

Even after the market decline, we expect to see continued high interest in stock compensation. However, many companies are reviewing their equity grant practices so dilution levels may have already peaked, or soon will, peak.

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Questions on this letter may be addressed to Beverly Aisenbrey in the New York Office (212) 986-6330. Copies of this letter and other published materials are available on our website, [www.fwcook.com](http://www.fwcook.com).