United States General Accounting Office

GAO

Briefing Report
to the Honorable Russell B. Long
United States Senate

February 1986

EMPLOYEE STOCK OWNERSHIP PLANS

Interim Report on a Survey and Related Economic Trends

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UNITED STATES GENERAL ACCOUNTING OFFICE
WASHINGTON, D.C. 20548

PROGRAM EVALUATION
AND
METHODOLOGY DIVISION

February 7, 1986

B-220256

The Honorable Russell B. Long
United States Senate

Dear Senator Long:

This report is the second in a series responding to your request for information about employee stock ownership plans (ESOPs). The first report, "Initial Results of a Survey on Employee Stock Ownership Plans and Information on Related Economic Trends" (GAO/PEMD-85-11), included data from a survey of ESOPs and relevant background information.

In the present report, we provide additional information from our survey and from analyses of data provided by the Internal Revenue Service (IRS). Our major findings concern our census of ESOPs, the contribution of ESOPs to the goal of broadening the ownership of corporate stock, and the tax revenue losses associated with ESOPs. From our analyses, we estimate that in early 1985, 4,174 ESOPs were active, with more than 7 million participants and nearly $19 billion in assets. We find that tax credit ESOPs have more participants and hold larger amounts of assets than other types of ESOPs but that leveraged ESOPs provide the highest asset value per participant. We find also that the proportion of employees of ESOP-sponsoring firms participating in stock ownership through employer-sponsored ESOPs is more than three times the proportion of all U.S. families owning stock. Our estimate is that the corporate income tax revenue lost through incentives to promote ESOPs totaled $9.9 billion between 1977 and 1983, of which $8.9 billion was attributable to tax credit ESOPs. (These estimates assume that there would have been no substitution of other tax credits or deductions in the absence of ESOP tax incentives.)

In addition to these major findings, we report on the distribution of ESOPs among business sectors and geographic regions, the relative proportions of ESOPs and ESOP participants and assets in publicly traded and privately held companies, and the extent to which ESOPs hold stock that carries voting rights. Finally, we report on trends in the formation of ESOPs, in the number of ESOP participants, and in contributions to ESOPs over time.

To collect information for this report, we surveyed 2,004 employee benefit plans identified by IRS as possible ESOPs. We received responses on 1,616 (81 percent) of the plans we surveyed. For each plan in the sample, we have combined the information from the survey questionnaire with information maintained by IRS on computer files, to permit us to make a fuller analysis of the history and characteristics of the plans.

The data we report here are interim findings and subject to revision as we continue our analysis. Readers who compare some tables with corresponding tables in the first report will note some minor differences from the earlier estimates. They result from inquiries about a small number of plans.

As we arranged with your office, we are sending copies of this report to the Senate Committee on Finance and Committee on Labor and Human Resources, the House Committee on Ways and Means and Committee on Education and Labor, and the Joint Committee on Taxation. Copies will also be available to others who request them.

Sincerely yours,

Eleanor Chelimsky
Director

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2. CENSUS AND DESCRIPTION OF ESOPS

OVERVIEW

- The ESOP legislation has three goals:

  --broader ownership of corporate stock,

  --the provision of more funds for capital formation, and

  --improved performance of the sponsoring corporations.

- The Program Evaluation and Methodology Division (PEMD) of the U.S. General Accounting Office, at the request of Senator Russell B. Long, is conducting a study to determine whether ESOPs are achieving these goals. This study provides the largest available independent survey of ESOPs.

- In the first phase of this study, we surveyed corporate executives and plan administrators responsible for a representative sample of 2,004 plans identified through data that IRS provided us. The survey generated 1,616 responses (81 percent). In this report, we present the results of this survey, including information on the numbers and types of ESOPs; the growth in the number of ESOPs; the distribution of ESOPs by industry, region, and type of corporate ownership (whether public or private); the extent to which ESOPs hold stocks that carry voting rights; the numbers of participants in and amounts of assets held by ESOPs; the extent of employee participation in ESOPs; and the corporate tax savings associated with ESOPs.

- The first survey allowed us to identify 1,083 plans for a follow-up survey that will provide more detailed information on how ESOPs work, why corporations choose to establish and maintain or terminate them, and their effect on the sponsoring firms' operations. By December 18, 1985, 868 (80 percent) of the firms we surveyed had responded. The results of this follow-up work will be included in our final report.
- We are now collecting information from tax returns in order to assess from our sample of ESOPs the extent to which ESOPs improve the productivity and profitability of firms that sponsor them and to estimate whether these improvements result in tax revenues that reduce the net tax revenue losses attributable to ESOPs. For part of this study, we are collecting the same data on a matched sample of firms that do not have ESOPs.
- In addition, we have obtained background data on corporate stock ownership, the sources and uses of corporate funds, and trends in productivity and profitability.

ABBREVIATIONS

ERISA — Employee Retirement Income Security Act

ESOP — Employee stock ownership plan

PAYSOP — Payroll-based tax credit ESOP

TRASOP — Tax Reduction Act ESOP

1. OVERVIEW

SURVEY METHODS

- One objective of our study is to take a census of ESOPs. To do this efficiently, we surveyed a sample of plans selected from a list of 8,891 plans that IRS identified for us as having indicated on Form 5500 filed for 1979-83 that they had "ESOP features." Our survey was designed to estimate how many of these plans meet the legal definition of "employee stock ownership plan" and how many do not.
- We sorted these 8,891 plans into nine strata, each based on amount of assets and number of participants.
- We selected a stratified random sample of 2,004 of these plans, selecting a sufficient number of plans from each stratum to ensure that proportion estimates would represent the population of 8,891 within 5 percent at the 95-percent level of confidence.
- In January 1985, we mailed questionnaires to the sponsoring corporations, in order to determine how many of the 2,004 plans were ESOPs. The overall response rate was 81 percent, the individual strata varying from 70 to 98 percent. We are investigating differences that might introduce bias into our results.
- The responses we obtained allow us to generalize to a universe of 7,042 plans. The remaining 1,849 plans contain an unknown number of ESOPs to which our sample results cannot be extended.

THE CENSUS

- o We estimate from our survey that 4,174 of 7,042 plans are active ESOPs and that 719 ESOPs have been terminated, giving a total population of 4,893. The remaining 2,048 plans either are not ESOPs or cannot be identified without further information, which we are collecting. (See table 1
- o If the same pattern held for the nonrespondents, we would estimate that 5,188 of the original 8,891 plans were active ESOPs and 947 were terminated ESOPs, accounting for a total of 6,135 ESOPs.
- o These estimates omit ESOPs formed in 1984 and 1985 and all related stock bonus plans that were not identified as ESOPs on Form 5500. We are collecting data on these plans for ou final report.
- o Among the active ESOPs,

  --25.8 percent are tax credit ESOPs,

  --16.2 percent have used the leveraging provisions,

  --35.1 percent are leverageable but have not used this provision, and

  --22.4 percent are nonleveraged.
- o Nearly 40 percent of all terminated ESOPs were nonleveraged.
- o Leveraged ESOPs appear less likely than nonleveraged ESOPs t be terminated. Our second survey will allow us to examine the reasons for this difference, and we will report the findings in our final report.

Table 1

Estimates of the ESOPs Population

Type	Active		Terminated		Total	
	Number	Percent	Number	Percent	Number	Percent
Tax credit	1,078	25.8	166	23.1	1,244	25.4
Leveraged	676	16.2	58	8.1	733[a]	15.0
Leverageable	1,466	35.1	192	26.7	1,659[a]	33.9
Nonleveraged	933	22.4	287	39.9	1,221[a]	24.9
Other[b]	20	0.5	16	2.2	36	0.7
Total	4,174[a]	100.0	719	100.0	4,893	99.9[c]

[a]Weighted totals do not balance because of rounding.
[b]Includes ESOPs that cannot be placed in categories without further information; an attempt is being made to gather it.
[c]Does not add to 100.0 because of rounding.

THE NUMBER OF ESOPS FORMED ANNUALLY

- Employee stock ownership plans are formed partly to take advantage of legislative provisions that allow new forms of capitalization (leveraging) or specific tax credits. Table 2 shows the distribution of ESOP types by year of formation from 1916 through 1983.
- The 2 years 1975 and 1976 were the period of the major formation of ESOPs. More than 700 ESOPs were formed during each of these years.
- The relatively large numbers of leverageable ESOPs formed in 1975 and leveraged ESOPs formed in 1975-76 may reflect an immediate response to the special leveraging provisions in the Employee Retirement Income Security Act of 1974 (ERISA).
- Similarly, the peak in the formation of tax credit ESOPs in 1976 may reflect the passage of TRASOP (or Tax Reduction Act ESOP) legislation in 1975.
- Nonleveraged ESOPs show the longest and most even period of formation from 1975 to 1980.
- The figures for 1916-73 in table 2 include all employee benefit plans formed in or before 1973, the year prior to the first major piece of ESOP legislation, that had been converted to ESOPs by the time of our survey. More generally, the year in which a plan was formed may differ from the year in which it became an ESOP. We will report on the incidence of conversion in our final report.

Table 2

The Number of ESOPs by Year of Formation

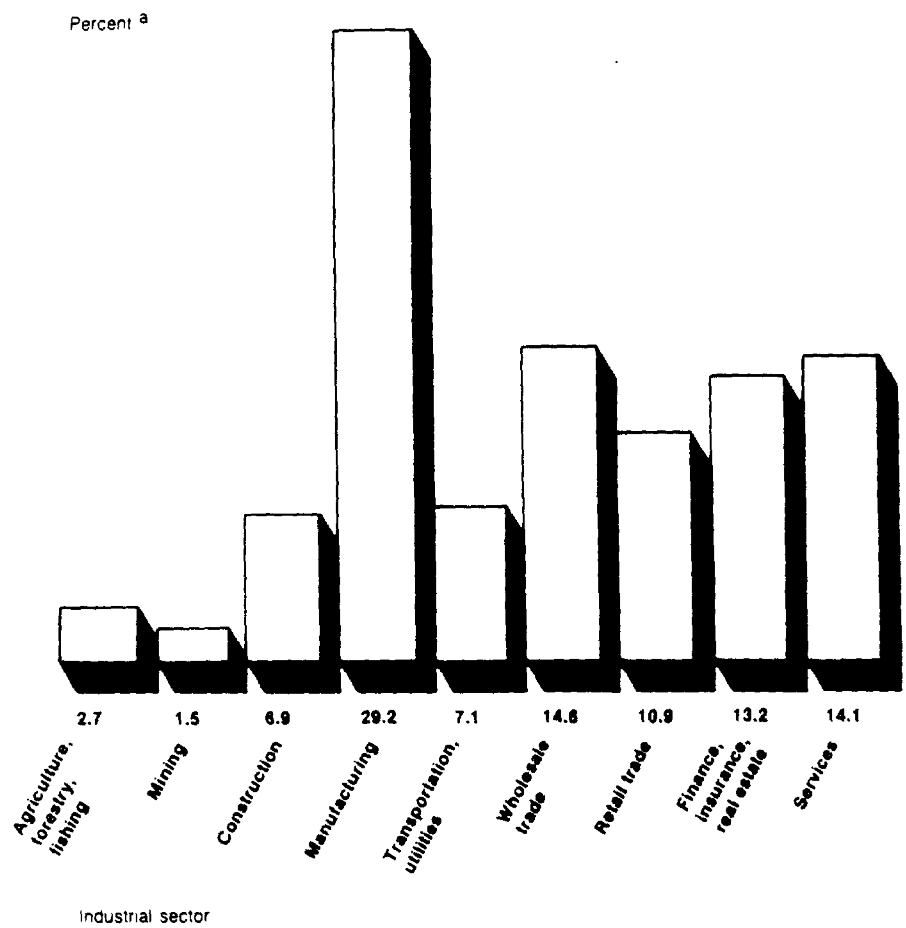
Type	1916-73	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	Total
Tax credit	135	29	176	250	92	109	92	117	82	77	86	1,244
Leveraged	106	51	114	124	67	36	58	52	47	50	28	733
Leverageable	285	122	269	152	94	144	171	130	152	105	34	1,659
Nonleveraged	207	80	163	174	114	159	106	90	83	37	7	1,221
Other	12	3	0	8	0	0	0	13	0	0	0	36
Total	746[a]	285	723[a]	708	367	449[a]	427	401[a]	363	270	155	4,893[a]

[a]Weighted totals do not balance because of rounding.

THE DISTRIBUTION OF ESOPS IN BUSINESS SECTORS

- The 29.2 percent of ESOPs in the manufacturing sector give it by far the largest share. (See figure 1.)
- Four other sectors follow manufacturing with roughly equal proportions: wholesale trade, 14.6 percent; services, 14.1 percent; finance, insurance, and real estate, 13.2 percent; and retail trade, 10.9 percent.
- The other sectors have smaller proportions: transportation and utilities, 7.1 percent; construction, 6.9 percent; agriculture, forestry, and fishing, 2.7 percent; and mining, 1.5 percent.

Figure 1: The Distribution of ESOPs by Major Industrial Sector



[a] Does not total to 100.0 percent because of rounding.

THE TYPES OF ESOPS IN BUSINESS SECTORS

- The distribution of types of ESOPs varies by business sector. For example, tax credit ESOPs are common in transportation and utilities (77.6 percent); mining (39.0 percent); and manufacturing (31.1 percent). (See table 3.)
- Only the finance, insurance, and real estate sector shows a high proportion of leveraged ESOPs (30.4 percent).
- High concentrations of leverageable ESOPs are found in agriculture, forestry, and fishing (62.8 percent); construction (50.1 percent); wholesale trade (49.2 percent); retail trade (39.3 percent); services (36.5 percent); and manufacturing (30.7 percent).

Table 3

The Types of ESOPs in Business Sectors

Sector	Type of ESOP						
	Tax credit	Leveraged	Leverageable	Nonleveraged	Other	Number	Total
Agriculture, forestry, fishing	4.4%	18.3%	62.8%	14.5%	0%	109	100.0%
Mining	39.0	19.8	16.0	25.3	0	60	100.1[a]
Construction	20.0	10.9	50.1	18.9	0	282	99.9[a]
Manufacturing	31.1	15.8	30.7	22.4	0	1,199	100.0
Transportation, utilities	77.6	2.2	16.6	2.6	1.0	291	100.0
Wholesale trade	11.6	10.2	49.2	29.0	0	598	100.0
Retail trade	15.5	16.4	39.3	28.8	0	448	100.0
Finance, insurance, real estate	24.0	30.4	23.9	18.5	3.1	543	99.9[a]
Services	17.8	19.2	36.5	26.5	0	579	100.0

[a]Totals do not add to 100.0 because of rounding.
[b]Data missing on 64 ESOPs.

THE GEOGRAPHIC DISTRIBUTION OF ACTIVE ESOPS

- Among all types of ESOPs, the highest absolute concentration is in the East North Central region, which has a total of 782, and the next is in the area of the Pacific states, which has a total of 766. The area with the fewest ESOPs is the East South Central region, with a total of 133; the New England states have a few more, with 177 ESOPs of all types. (See table 4.)
- In all sections of the United States except two--the Middle Atlantic and the East South Central states--the most common form is leverageable. In the Middle Atlantic states, the most common form is the tax credit ESOP, and in the East South Central region, nonleveraged ESOPs occur as frequently as leverageable ESOPs.

Table 4

The Distribution of Active ESOPs by Geographic Region

Region	Type OF ESOP: Tax credit	Leveraged	Leverageable	Nonleveraged	Other	Total	Percent
New England	45	41	62	29	0	177	4.3%
Middle Atlantic	147	85	120	66	0	418	10.0
East North Central	237	109	276	160	0	782	18.7
West North Central	145	88	213	156	0	601[a]	14.4
South Atlantic	140	83	164	72	8	468[a]	11.2
East South Central	29	29	38	38	0	133[a]	3.2
West South Central	112	63	164	142	0	481	11.5
Mountain	50	74	141	72	9	347[a]	8.3
Pacific	173	103	288	199	3	766	18.3
Total	1,078	676[a]	1,466	933[a]	20	4,174[a]	
Percent	25.8	16.2	35.1	22.4	0.5		100.0

[a]Weighted totals do not balance because of rounding.

THE TRADING STATUS OF STOCK IN ESOPS

- Nearly 76 percent of active ESOPs are sponsored by privately held rather than publicly traded corporations. (See table 5.)
- Tax credit ESOPs differ from leveraged, leverageable, and nonleveraged ESOPs in that nearly 65 percent of them are sponsored by employers whose stock is publicly traded rather than privately held.

Table 5

The Trading Status of Stock in Active ESOP Trusts

Type	Privately held	Publicly traded	Total
Tax credit	35.4%	64.6%	1,064
Leveraged	84.7	15.3	676
Leverageable	94.4	5.6	1,462
Nonleveraged	86.3	13.7	911
Other	--	100.0	12
Total	75.5%	24.5%	4,124[a]

[a]Data missing on 49 ESOPs. Weighted total does not balance because of rounding.

VOTING RIGHTS IN ACTIVE ESOPS

- Overall, 69.5 percent of all ESOPs hold stock of sponsoring corporations that carries voting rights, including 93.6 percent of those sponsored by publicly traded and 61.7 percent of those sponsored by privately held firms. (See table 6.)
- For each type of ESOP, publicly traded corporations are more likely than privately held corporations to have ESOPs that hold stock of the sponsoring corporation that carries voting rights.
- According to our respondents, practically all tax credit and leveraged ESOPs sponsored by publicly traded firms have stock with voting rights. Publicly traded firms are required by law to contribute stock that carries voting rights to the tax credit or leveraged ESOPs they sponsor.
- Among privately held firms, a higher percentage of leveraged ESOPs than tax credit ESOPs hold stock of sponsoring firms that carries voting rights.
- Nevertheless, stock with voting rights is more prevalent among all tax credit ESOPs than among all leveraged ESOPs, because a much higher percentage of tax credit ESOPs are sponsored by publicly traded firms, which almost invariably contribute stock that carries voting rights. (See table 5.)
- Among publicly traded and privately held sponsors, nonleveraged ESOPs have the lowest rate of stock that carries voting rights.

Table 6

The Percentage of Active ESOPs Providing Stock with Voting Rights

Type	Publicly traded	Privately held	All corporations
Tax credit	98.3%	55.4%	82.8%
Leveraged	99.0	72.5	76.6
Leverageable	88.4	67.8	69.0
Nonleveraged	66.5	45.9	48.7
Other	100.0	--	100.0
Total	93.6%	61.7%	69.5%[a]

[a]Data missing on 73 ESOPs.

THE NUMBER OF PARTICIPANTS IN AND AMOUNTS OF ASSETS OF ACTIVE ESOPS

- Overall, 90.1 percent of all ESOP participants (6,391,029 of 7,082,789) are in tax credit ESOPs. (See table 7.)
- The median tax credit ESOP has 430 participants, many more than other types.
- Overall, 79.3 percent of the assets held by ESOP trusts ($14.8 billion of $18.7 billion in 1983) are held by tax credit ESOPs.
- The median tax credit ESOP holds much larger amounts of assets than other types.
- But tax credit ESOPs have fewer assets per participant than leveraged, leverageable, and nonleveraged ESOPs. Leveraged ESOPs have the most assets per participant, at $8,660.
- Tax credit ESOPs rank lower than other types of ESOPs in assets per participant but higher in total assets, perhaps because some tax credit ESOPs appear to have been formed in very large firms. When these large amounts of assets are allocated to many participants, tax credit ESOPs provide limited assets per participant.
- In summary, tax credit ESOPs typically have more participants and hold more gross assets than the other types of ESOPs, but leveraged ESOPs have the highest asset value per participant.

Table 7

Estimates of the Participants in and Assets of Active ESOPs[a]

	Participants			Assets[b]			
Type	Number	Percent	Median per plan	Total (million)	Percent	Median per plan	Median per participant
Tax credit	6,391,029	90.1	430	$14,800	79.3	$864,446	$2,952
Leveraged	158,238	2.2	54	1,450	7.8	444,708	8,660
Leverageable	293,274	4.1	37	1,445	7.7	272,663	7,149
Nonleveraged	238,406	3.4	40	961	5.2	209,397	5,098
Other	1,842	c	10	1	c	0	0
Total	7,082,789	99.8[d]	54	$18,660	100.0	$334,606	$5,226

[a]Based on plans active in 1983, the last year for which complete data are available.
[b]In constant 1983 dollars.
[c]Less than 0.05.
[d]Total does not equal 100.0 because of rounding.

PARTICIPANTS AND ASSETS IN PRIVATELY HELD AND PUBLICLY TRADED FIRMS

- Although the majority of ESOPs are sponsored by privately held companies, about 93 percent of the participants and 83 percent of the assets in active ESOPs are in plans sponsored by publicly traded corporations. (See table 8.)
- For the four main categories, the median number of participants in ESOPs is larger in publicly traded than in privately held firms.
- The median value of assets is also larger in publicly traded than in privately held corporations for tax credit, leveraged, and leverageable ESOPs.

Table 8

ESOP Participants and Assets by the Trading Status of Their Stock[a]

	Privately held	Publicly traded	Total[b]
Total participants	495,757	6,574,833	7,070,590
Median number of participants	39	631	54
Total assets[c]	$3,109,983	$15,488,434	$18,598,417
Median value of assets[c]	$277	$1,464	$337

[a]Based on plans active in 1983, the last year for which complete data are available.
[b]Excludes 81 ESOPs for which trading status data were not ascertained.
[c]In thousands of 1983 dollars.

TRENDS IN THE NUMBER OF PARTICIPANTS

- The number of participants in ESOPs increased each year 1975 through 1983. In 1975, there were 756,523; in 1983, there were 7,082,789. (See table 9.)
- The same pattern of annual growth occurred consistently for the four main types of ESOPs during 1975-82.
- The early years of ESOPs showed the largest rate of growth in the number of participants, the number in 1975 more than doubling in 1976 and the number in 1976 almost doubling again in 1977.
- Tax credit ESOPs were mainly responsible for the rapid overall growth in the early years, but the number of participants in 1975 approximately tripled in both leveraged and leverageable ESOPs in 1976.
- Leveraged and leverageable ESOPs increased rapidly in number of participants in 1980-82.
- Nonleveraged ESOPs, which do not take advantage of the special tax provisions for ESOPs, do not follow the growth patterns of the other types. The major increase in number of participants (both absolutely and proportionally) occurred in 1979-80.

Table 9

The Numbers of ESOP Participants in 1975-83

Type	1975	1976	1977	1978	1979	1980	1981	1982	1983
Tax credit	708,354	1,517,863	3,081,350	3,262,655	4,296,566	4,600,799	4,836,478	5,464,778	6,391,029
Leveraged	17,325	52,020	63,985	71,054	81,855	93,665	119,235	145,994	158,238
Leverageable	7,077	20,657	41,460	56,174	66,531	99,775	284,218	313,974	293,274
Nonleveraged	23,767	29,048	41,741	54,026	63,587	165,567	204,992	206,730	238,406
Other	0	117	114	116	116	715	1,792	1,458	1,842
Total	756,523	1,619,705	3,228,650	3,444,025	4,508,655	4,960,521	5,446,715	6,132,934	7,082,789

CONTRIBUTIONS TO ESOPS

- Contributions of cash and stocks to ESOPs totaled $12.4 billion over the 7-year period 1977-83, rising from about $997 million in 1977 to more than $2.4 billion in 1983. (See table 10.)
- Of total contributions, nearly 83 percent ($10.3 billion) went to tax credit ESOPs. This pattern is reflected in the high proportion of assets in tax credit ESOP trusts (see table 7).
- In most years, the amounts contributed to leveraged, leverageable, and nonleveraged ESOPs were similar, and the totals in 1977-83 for these three types were in a relatively narrow range (about $569 million for nonleveraged ESOPs to nearly $849 million for leverageable ESOPs).

Table 10

Contributions to ESOPs in 1977-83[a]

Type	1977	1978	1979	1980	1981	1982	1983	Total
Tax credit	925,542	1,051,756	1,195,278	1,361,370	1,714,237	2,021,584	1,998,115	10,267,882
Leveraged	29,136	69,079	81,603	102,581	111,145	199,637	141,262	734,443
Leverageable	26,653	71,375	94,033	109,261	184,213	199,159	164,031	848,725
Nonleveraged	16,090	62,523	68,944	93,449	103,456	106,472	118,127	569,061
Other	0	0	117	0	235	144	292	788
Total	997,421	1,254,733	1,439,975	1,666,661	2,113,286	2,526,996	2,421,827	12,420,899

[a]Current dollars in thousands.

3. ESOPS AND THE DISTRIBUTION OF STOCK OWNERSHIP

THE BREADTH OF STOCK OWNERSHIP IN FIRMS WITH ESOPS

- As we noted in section 1, an important goal of the ESOP legislation is to broaden the ownership of corporate stock by fostering broad participation in ESOPs. By opening stock ownership to workers who might otherwise never invest in stocks, ESOPs are expected to strengthen support for the U.S. economic system and to provide a source of income from capital accumulation and dividends in addition to salaries or wages. The Congress legislated the ESOP leveraging provisions of the tax code as a method of financing the purchase of stock through either transfers of ownership or the issuance of corporate treasury stock to the ESOP trust. Examining evidence on the extent to which employees have participated in stock ownership, we found the following:
- The median percentages of employees participating in all types of ESOPs are quite similar, although the median for tax credit ESOPs is somewhat lower than for the other types. (See table 11.)
- The ownership of stock is much more prevalent among employees of ESOP-sponsoring corporations than among other stock-owning members of the U.S. population. The median percentage of employees participating in stock ownership through ESOPs in 1983 was more than three times higher than the percentage of U.S. families owning stock. (Compare figure 2 on page 34.)

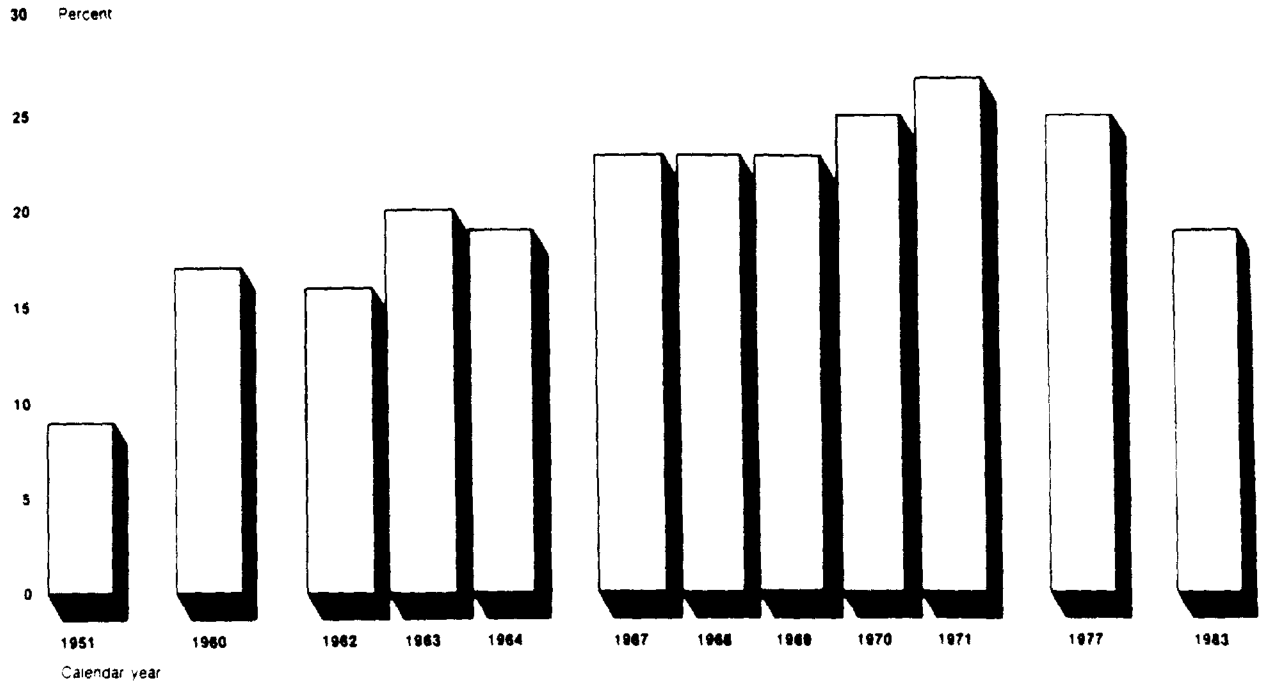
Table 11

The Number of Employees Participating in ESOPs in 1983[a]

Type	Total employees	Total employees participating	Median participating
Tax credit	12,097,769	6,135,833	62.8%
Leveraged	255,667	135,706	71.2
Leverageable	503,134	263,819	74.3
Nonleveraged	274,604	189,393	73.9
Other	2,607	1,712	78.7
Total	13,133,782[b]	6,726,462[b]	70.6

[a]Excludes ESOPs on which data were missing.
[b]Weighted totals do not balance because of rounding.

Figure 2. Percentage of All Families Owning Stock in Selected Years 1951-83a



[a]Includes publicly and privately held companies and mutual funds. Where there were discrepancies between statistics published in different years, we used the number in the most recent survey. No discrepancy was greater than 2 percentage points.

Source: Surveys of Consumer Finances. Survey Research Center, Institute for Social Research, University of Michigan, Ann Arbor, Mich.

STOCK OWNERSHIP BY U.S FAMILIES GENERALLY

o To compare the breadth of ownership of stock in ESOP corporations to the extent to which U.S. families own stock generally, we looked at a variety of studies on stock ownership. Using periodic surveys of consumer finances from the University of Michigan Survey Research Center, we found that

--the percentage of U.S. families that own stock increased steadily between 1964 and 1971 and then declined,

--the percentage of families owning stock in 1983 was equivalent to the percentage that owned stock 19 years earlier, in 1964, and

--the families that owned stock were fewer than 30 percent of all U.S. families in the years shown in figure 2 (the average was about 20 percent).

o These figures apply only to directly owned shares of stock and holdings in mutual funds. Families may also own shares indirectly through pensions or other accounts.

STOCK OWNERSHIP BY TOP ASSET HOLDERS

- o Tax incentives for ESOPs are based on the premise that a wide diffusion of stock ownership will provide support for the economic system and produce asset-based income for workers and their families. Several studies indicate that stockholding is not widely dispersed. We have already noted that a minority of families own stock directly.
- o We compared stock ownership to the ownership of all assets. The University of Michigan Survey Research Center has estimated asset holdings for 1958-76, and IRS has produced similar estimates for 1981. Both used the estate-multiplier technique, which estimates the population's wealth from estate tax returns and mortality tables. (See table 12.)
- o The value of stock is much more concentrated than the value of total assets.
- o The proportional difference between the concentration of stock ownership and the ownership of total assets has persisted, despite a decline in both over time.
- o Unpublished figures from the Federal Reserve Board based on the Survey of Consumer Finances and an augmented sample of high-income families show that the families that were ranked among the top 0.5 percent in income in 1983 owned 41 percent of all publicly traded stock. These figures are not directly comparable to those in table 12 because they are based on income rather than wealth and because they are limited to publicly traded stock, but they reinforce the conclusion that stock ownership is highly concentrated.

Table 12

The Percentage of Corporate Stock Value and Total Assets Held by Top Asset Holders[a]

Year	Top 0.5% Value	Top 0.5% Assets	Top 0.8% Value	Top 0.8% Assets	Top 1% Value	Top 1% Assets
1958	60.8%	20.2%			68.8%	25.2%
1962	53.7	21.2			62.4	26.8
1965	58.6	23.4			67.4	29.0
1969	50.1	20.4			57.9	25.8
1972	54.8	20.5			62.7	26.0
1976	38.3	13.8			46.0	18.3
1981			41.0%	20.0%		

[a]Based on gross value of total assets. Corporate stock value (or "value") includes the value of all common and preferred stock in domestic or foreign firms, whether publicly traded or privately held, plus the value of certificates and shares of building and loan and savings and loan associations, Federal Land Bank stock, and other instruments representing equity interest in an enterprise. Total assets (or "assets") include the value of corporate stock, real estate, bonds, cash, debt instruments, life insurance, trusts, and miscellaneous holdings (such as consumer durables, personal effects, mineral rights, and business assets other than real estate).

Source: 1958-76 data from James D. Smith, "Recent Trends in the Distribution of Wealth: Data, Research Problems and Prospects," paper presented at the C. V. Starr Center Conference on International Comparisons of the Distribution of Household Wealth, New York, 1983; unpublished 1981 data from Marvin Schwartz, "Trends in Personal Wealth, 1976-1981," Internal Revenue Service, Washington, D.C.

STOCK OWNERSHIP BY INDIVIDUALS AND INSTITUTIONS

- Corporate stocks are held by individual and institutional investors. The Federal Reserve Board flow of funds accounts show the distribution of corporate stock among individual and institutional investors in 1960-83. The figures in table 13 show the market value of common and preferred corporate stock, including investment company shares but not the stock of privately held firms.
- Households owned the majority of corporate stock value. (The household category consists predominantly of individuals but includes personal trusts and nonprofit organizations.) This group held more than 68 percent of all stock value in each year shown. This estimate is conservative. Substantial portions of stock held by mutual funds and life insurance companies are owned by individuals, but there is no accurate way of estimating them.
- The portion of stock value held directly by households, however, decreased, falling from 87.7 percent in 1960 to 68.1 percent in 1983.
- The portion of stock value held by pension funds and other institutional investors rose nearly continuously. Self-administered private pension funds held 3.7 percent of all stock value in 1960 and 14.2 percent in 1983.
- The portion of stock held by foreign investors more than doubled between 1960 and 1983, rising from 2.1 percent to 4.5 percent.

Table 13

The Distribution and Market Value of Corporate Equities in Selected Years 1960-83[a]

	1960	1965	1970	1975	1980	1981	1982	1983
Total stock outstanding	$451.0	$749.0	$906.2	$892.5	$1,635.6	$1,568.5	$1,810.5	$2,151.5
Held by								
Households	87.7%	84.9%	80.4%	72.5%	72.6%	72.3%	70.4%	68.1%
Private pension funds (self-administered)	3.7	5.4	7.4	11.4	12.8	12.5	13.7	14.2
State and local government retirement funds	0.1	0.3	1.1	2.7	2.7	3.0	3.3	4.2
Mutual funds	3.3	4.1	4.4	3.8	2.6	2.4	2.7	3.4
Brokers and dealers	0.1	0.2	0.2	0.4	0.2	0.4	0.2	0.1
Life insurance companies	1.1	1.2	1.7	3.1	2.9	3.0	3.1	3.0
Other insurance	1.7	1.6	1.5	1.6	2.0	2.1	2.1	2.2
Commercial banking[b]								
Mutual savings banks	0.3	0.3	0.3	0.5	0.3	0.2	0.2	0.2
Foreign owners	2.1	1.9	3.0	4.0	3.9	4.1	4.2	4.5

[a]Current dollars in billions.
[b]Less than 0.05 percent.

Source: Assets and liabilities outstanding 1960-83, Flow of Funds Section, Federal Reserve Board, Washington, D.C.

4. CORPORATE TAX SAVINGS ON CONTRIBUTIONS TO ESOPS

CORPORATE INCOME TAX COSTS

FOR CONTRIBUTIONS

- The major tax incentives for corporate contributions to ESOPs are the tax credits for contributions to TRASOPs, effective in 1975-82, and PAYSOPs (payroll-based tax credit ESOPs), effective since 1983, and the deductions from corporate income for contributions to other types of ESOPs. For the period 1977-83, we estimate that these provisions of the tax code may have resulted in revenue costs to the federal treasury of nearly $9.9 billion. (See table 14.)
- This estimate assumes that corporate contributors claimed all applicable tax credits and income deductions, that tax credits and deductions were claimed in the year the contributions were made, and that in the absence of ESOP incentives, corporate sponsors would not have changed their behavior to take advantage of other tax incentives (for example, by contributing to pension plans).
- Of the $9.9 billion in lost revenue, $8.9 billion (90 percent) are accounted for by tax credit ESOPs. This reflects the facts that most of the money contributed to ESOPs goes to tax credit ESOPs and that credits imply a dollar-for-dollar reduction in taxes, whereas the value of deductions depends on the marginal tax rate (46-48 percent, in this instance).
- Our estimates do not include increases in revenue that could have been generated if ESOPs stimulated increased corporate income through productivity or profitability gains. We will estimate these in our final report.

Table 14

Corporate Income Tax Costs for Employer Contributions to ESOPs in 1977-83[a]

Type	1977	1978	1979	1980	1981	1982	1983	Total
Tax credit[b]	925,542	1,051,756	1,195,278	1,361,370	1,713,713	1,433,128	1,235,604	8,916,391[c]
Leveraged[d]	13,985	33,158	37,537	47,187	51,127	89,783	63,154	335,931
Leverageable[d]	12,794	34,260	43,255	50,260	84,738	87,998	71,311	384,616
Nonleveraged[d]	7,723	30,011	31,715	42,987	47,590	47,945	49,614	257,585
Other[d]	0	0	54	0	108	66	134	362
Total	960,044	1,149,185	1,307,839	1,501,804	1,897,276	1,658,920	1,419,817	9,894,885

[a]Current dollars in thousands.
[b]Assuming all employer contributions were claimed as credits in the year of contribution.
[c]The difference between our estimate of the cost of ESOP tax credits, $8.9 billion, and the IRS estimate in table 15, $6.8 billion, is explained by three factors: (1) our data cover 1977-83 and the IRS data cover 1975-82 (for 1977-82, years covered in both tables, our estimate of tax credit cost is $7.7 billion and the IRS estimate is $6.3 billion); (2) we assume that all contributions were claimed in the year of contribution, whereas IRS includes only the amounts actually claimed in each year (there are carryover provisions for the credits); and (3) different sampling frames were used in drawing the two samples, which may therefore represent somewhat different populations.
[d]Assuming all employer contributions were deducted in the year of contribution and applying marginal tax rates of 48 percent for 1977 and 1978 and 46 percent for subsequent years.

INVESTMENT TAX CREDITS AND DEPRECIATION DEDUCTIONS

- A number of tax code provisions, including those related to ESOPs, affect cash flow to corporations in order to encourage new or replacement investment in productive assets. The most important of these provisions are the investment tax credit and the depreciation allowance. Data from IRS statistics of income show that

  --the allowed investment credit totaled about $105.5 billion between 1975 and 1982 and

  --the tentative investment credit, before limitations and carryovers, totaled about $142.3 billion in the same period.

- Of this amount, the 7-percent and 10-percent investment credits accounted for approximately $135.3 billion, 95 percent of the total tentative investment credit, and the ESOPs portion of the credit totaled about $6.8 billion, less than 5 percent of the total tentative investment credit. (This sum is derived by combining the amounts shown in table 15 for the 1-percent and 0.5-percent ESOP tax credits.)

- We estimate that corporate savings from the depreciation deduction against taxable income totaled about $515.6 billion, approximately 3-1/2 times the amount of the tentative investment credit.

5. ESOPS AND ECONOMIC PERFORMANCE: FINANCING CORPORATE GROWTH

SOURCES OF CORPORATE FUNDS

- o Corporations finance capital formation and increases in financial assets through external and internal (primarily retained earnings and depreciation) sources of funds. An important goal of ESOP legislation is to provide corporations with a financing mechanism that permits workers to share in equity ownership. The Flow of Funds Section of the Federal Reserve Board collects data on the sources of corporate funds from the U.S. Department of Commerce, making some supplementary adjustments for the nonfarm, nonfinancial corporate sector. We show the following data in table 16.
- o Internal sources of funds have supplied and continue to supply the majority of corporate funds.
- o Capital consumption allowance, or depreciation, provides a substantial proportion of total sources of funds by increasing cash flow. This item alone provided more than half of all corporate funds in 7 of the 11 years shown in the table.
- o New equity issues constituted up to 6.5 percent of total sources of funds in the years shown here.
- o Debt provided a higher proportion of corporate funds than new equity issues in each of the years shown and, for most of them, accounted for the majority of the externally raised funds.

Table 16

The Sources of Funds for Nonfarm, Nonfinancial Corporations in Selected Years 1955-85[a]

	1955	1960	1965	1970	1975	1980	1981	1982	1983	1984	1985
Total	$52,660	$48,622	$91,840	$102,344	$156,953	$335,231	$364,155	$309,360	$436,349	$482,597	$449,520
Internal	55.9%	72.8%	63.7%	60.4%	76.2%	56.5%	63.3%	75.7%	64.3%	69.4%	79.0%
Retained earnings	22.4	16.5	20.8	7.4	21.7	14.6	12.6	3.3	4.3	7.1	5.5
Capital consumption allowance	36.1	54.8	35.4	50.6	59.8	50.1	52.0	66.9	49.3	47.3	53.1
Iva and cca[b]	-7.1	-4.7	2.7	-4.0	-13.5	-17.1	-8.1	-1.8	5.0	10.2	15.2
Foreign earnings	4.5	6.2	4.8	6.4	8.3	8.9	6.7	7.2	5.7	4.8	5.2
External	44.1%	27.2%	36.3%	39.6%	23.8%	43.5%	36.7%	24.3%	35.7%	30.6%	21.0%
New equity issues	3.3	2.8	[c]	5.6	6.3	3.8	-3.1[d]	3.7	6.5	-16.0[d]	-18.9[d]
Debt	16.0	22.0	20.0	28.9	13.3	23.3	28.3	22.6	13.6	36.4	31.8
Other	24.8	2.4	16.1	5.2	4.2	16.3	11.6	-2.1	15.6	10.2	8.2

[a]Dollars current in millions, adjusted seasonally but not annually for inflation. All figures based on quarterly estimates, except 1985 based on first-quarter estimates only.
[b]iva = inventory valuation adjustment; cca = capital consumption adjustment.
[c]Less than 0.05 percent.
[d]Indicates firms bought more stock than they issued.

Source: Flow of Funds Section, Federal Reserve Board, Washington, D.C.

USES OF CORPORATE FUNDS

- The Flow of Funds Section of the Federal Reserve Board also collects data on the uses of corporate funds. Table 17 shows nonfarm, nonfinancial corporate expenditures for capital investment and increases in financial assets in selected years 1955-85:

  --the use of the majority of corporate funds was for capital expenditures rather than financial assets (this pattern held for intervening years not shown in the table) and

  --the portion of corporate funds used for capital expenditures varied from the low of 66.4 percent to the high of 90.5 percent for the years in the table, with no consistent increase or decrease.

Table 17

The Use of Funds by Nonfarm, Nonfinancial Corporations in Selected Years 1955-85[a]

	1955	1960	1965	1970	1975	1980	1981	1982	1984	1985
Total	$49,121	$41,409	$82,729	$198,726	$150,912	$317,627	$334,179	$258,013	$439,373	$413,592
Capital expenditures	66.4%	90.5%	73.7%	81.0%	72.7%	69.6%	81.2%	89.0%	83.7%	89.9%
Financial assets	33.6	9.5	26.3	19.0	27.3	30.4	18.8	11.0	16.3	10.1

[a]Current dollars in millions, adjusted seasonally but not annually for inflation. All figures based on quarterly estimates, except 1985 based on first-quarter estimates only.

Source: Flow of Funds Section, Federal Reserve Board, Washington, D.C.

6. ESOPS AND ECONOMIC PERFORMANCE: PRODUCTIVITY AND PROFITABILITY

THE ECONOMIC PERFORMANCE OF CORPORATIONS

Finally, an important goal of the ESOP legislation is to improve the economic performance of sponsoring corporations. Proponents of ESOPs cite two ways in which ESOPs can aid the economic performance of sponsoring companies:

--workers might be more motivated and, therefore, more productive when they acquire ownership in the company for which they work and

--as a method of corporate finance, ESOPs can provide capital for expansion.

- We are examining the effects of ESOPs on the economic performance of firms. In the present report, we include only background data on national trends in productivity, noting first the results of our search for and review of relevant studies. Despite methodological weaknesses, the research provides some evidence, though mixed, that ESOPs aid the economic performance of sponsoring firms.
- The productivity growth rate of a sample of about 125 ESOP firms was greater in 1975-79 than the national rate for their industries.[1]
- However, 10 matched firms had productivity as high as or higher than 10 ESOP firms in the same industry in 1978-81.[2]

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[1]Thomas Marsh and Dale McAllister, "ESOPs Tables: A Survey of Companies with Employee Stock Ownership Plans," Journal of Corporation Law, 6 (Spring 1981), 521-623.

[2]Harold Hamilton, The Effects of Employee Stock Ownership Plans on the Financial Performance of the Electrical and Electronic Machinery, Equipment, and Supplies Industry (Ann Arbor, Mich.: University Microfilms International, 1983).

- A sample of majority employee-owned firms, some of which had ESOPs, had greater employment growth than conventionally structured firms.[3]
- Ten ESOP firms were not significantly more profitable than 10 matched firms on three measures of profitability (the ratios of net profits to net sales, to net worth, and to net working capital) but outperformed the non-ESOP firms for 2 years during 1978-81 on a fourth measure (the ratio of net sales to net worth).[4]
- A sample of employee-owned firms had 50-percent higher profits than the average for their industries.[5]
- An elaboration of this study with a matched comparison of firms found no difference in the profitability of employee-owned and non-employee-owned firms.[6]

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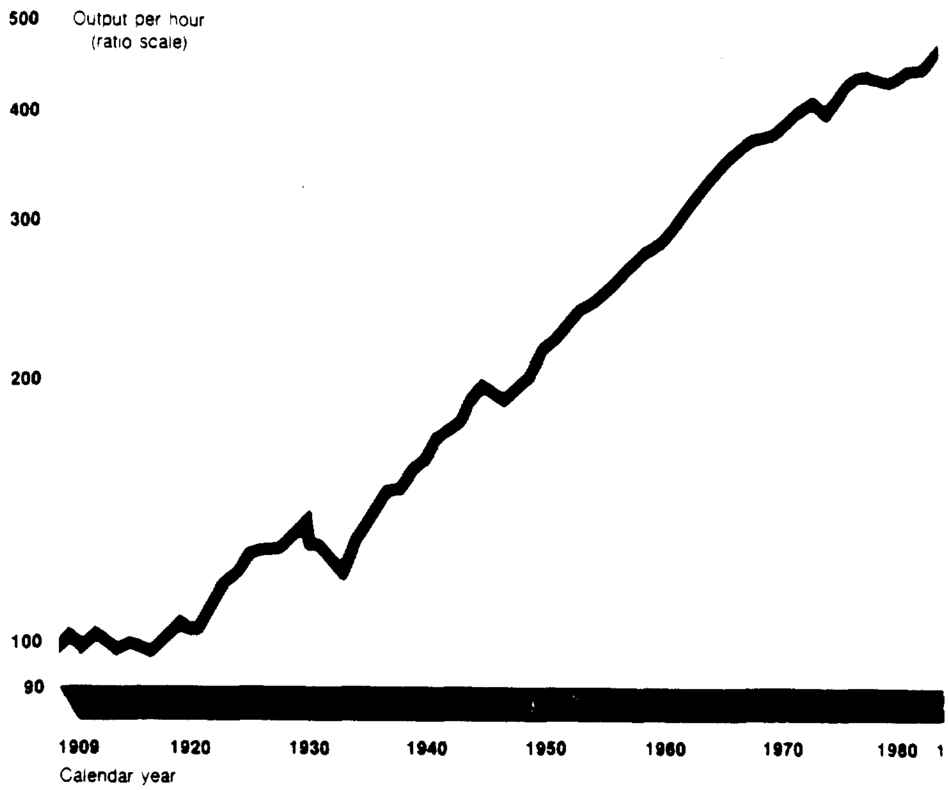
[3]Hamilton.

[4]Corey Rosen and Katherine Klein, "Job Creating Performance of Employer-Owned Firms," Monthly Labor Review, 106 (August 1983), 15-19.

[5]Michael Conte and Arnold Tannenbaum, "Employer Owned Companies: Is a Difference Measurable?" Monthly Labor Review, 101 (July 1978), 23-28.

[6]Arnold Tannenbaum, Harold Cook, and Jack Lohmann, The Relationship of Employee Ownership to the Technological Adaptiveness and Performance of Companies (Ann Arbor, Mich.: Institute for Social Research, 1984).

Figure 3: The Hourly Output of All Persons in the U.S. Private Business Economy in 1909-84[a]



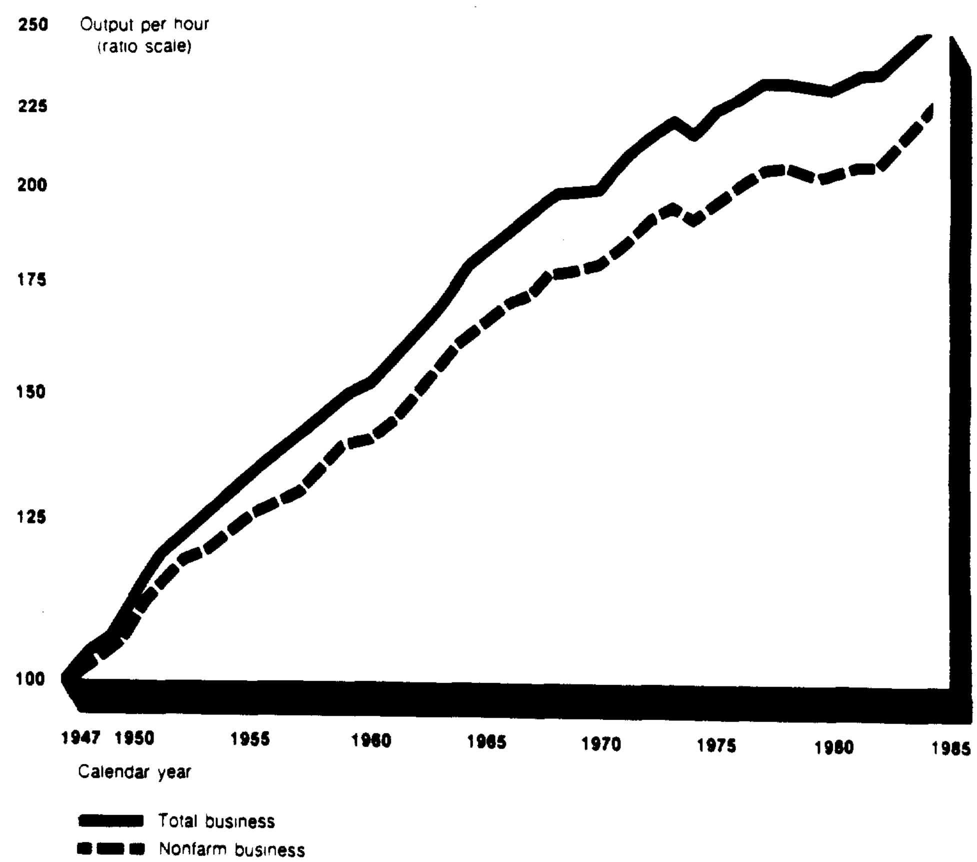
[a]1909 = 100.

Source: U.S. Bureau of Labor Statistics, Washington, D.C. 1983.

TRENDS IN U.S. PRODUCTIVITY

- The Bureau of Labor Statistics computes U.S. productivity fro data for establishments and from measures of compensation and output provided by the U.S. Department of Commerce and the Federal Reserve Board. Output per hour of all persons is a measure of labor productivity based on the value of goods and services in constant dollars produced per hour of labor. The following data are shown in figures 3 and 4.
- U.S. productivity has generally risen in the 20th century, counting from 1909 through 1984.

Figure 4: The Hourly Output of All Persons in the Total U.S. Business and Nonfarm Business Economies 1947-82[a]

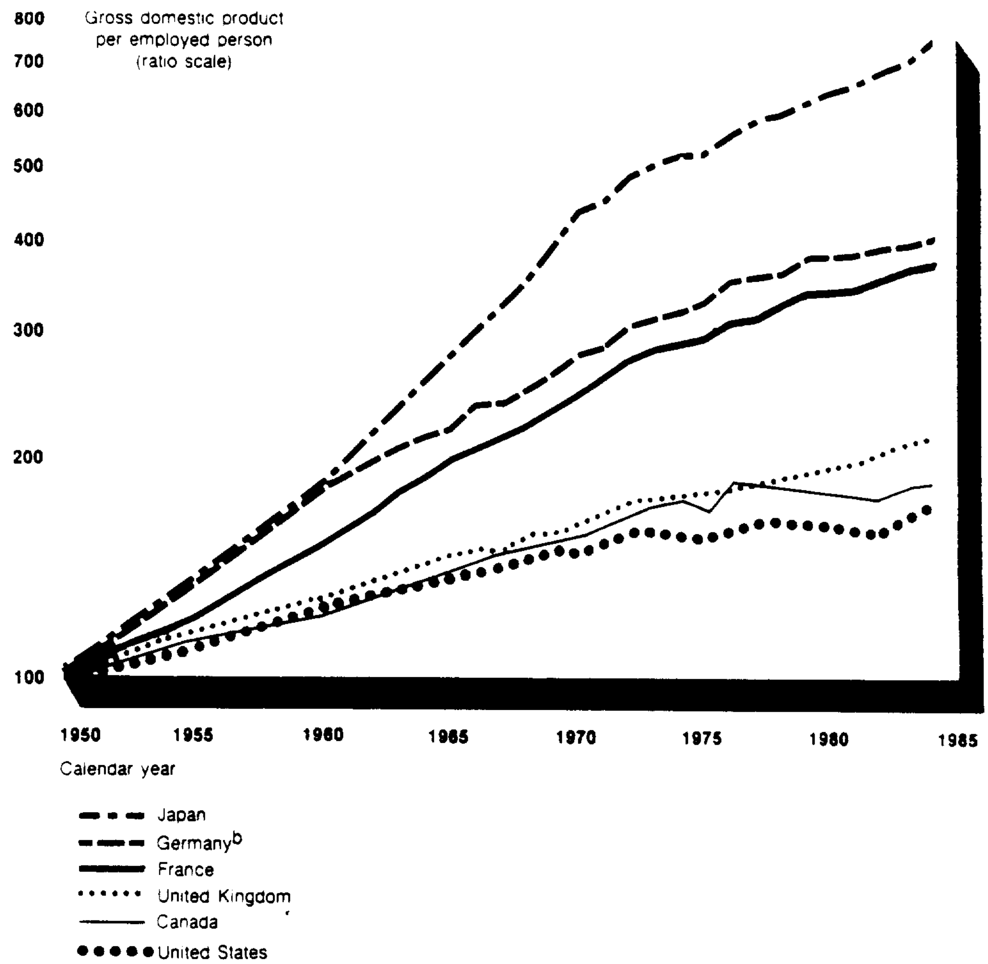


[a]1947 = 100.

Source: U.S. Bureau of Labor Statistics, Washington, D.C., 1983.

- Between 1977 and 1982, productivity growth was slight, and it declined in 1979 and 1980.
- Data for 1983 and 1984 suggest there was renewed growth in productivity, but the average for the first two quarters of 1985 (not shown here) is only slightly higher than the 1984 annual average and lower than the fourth-quarter figure for 1984.
- Overall productivity growth has slowed since 1965.

Figure 5: Trends in Real Gross Domestic Product per Employed Person in Selected Countries and Years 1950-84[a]



[a]1950 = 100. Data for the latest year are based on preliminary estimates.

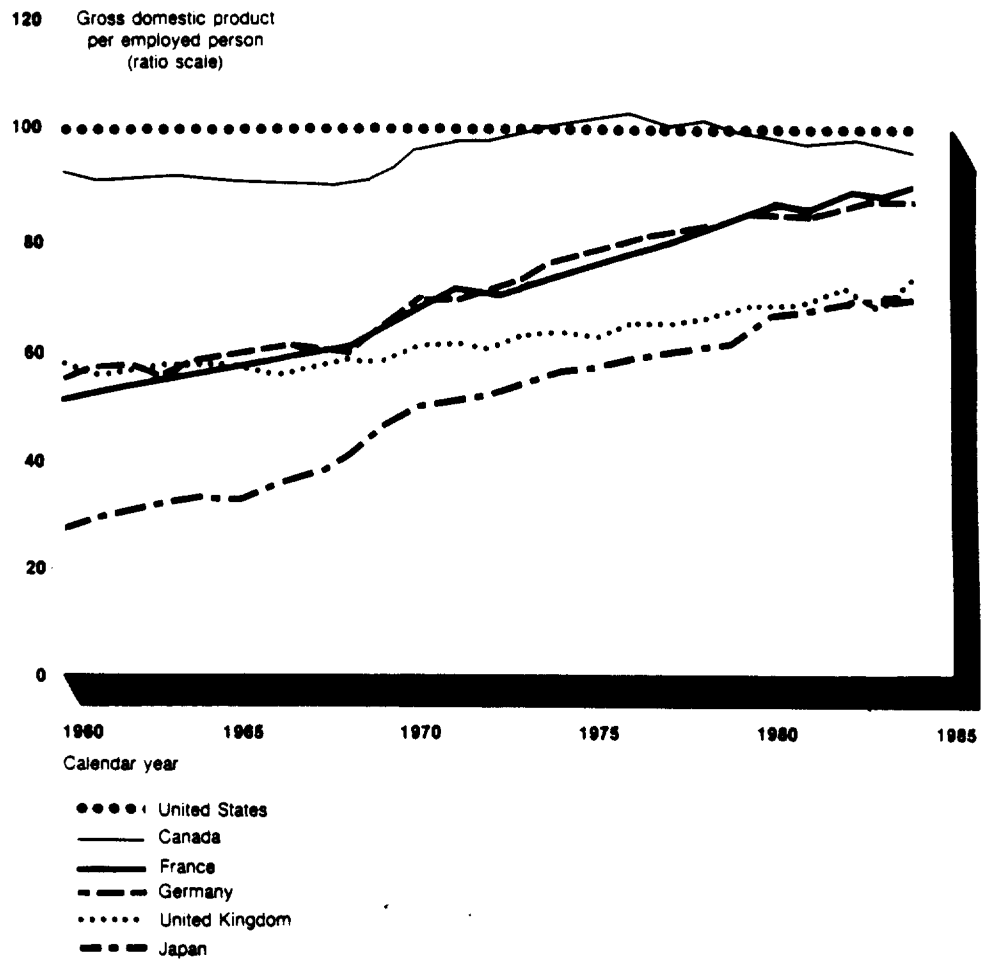
[b]Excludes Saar and West Berlin in 1950 and 1955.

Source: Unpublished data, U.S. Bureau of Labor Statistics, Washington, D.C.

TRENDS IN PRODUCTIVITY IN THE UNITED STATES AND SELECTED OTHER COUNTRIES

o The Bureau of Labor Statistics presents international comparisons of productivity in terms of gross domestic product per employed person. The following data are shown in figures 5 and 6.

Figure 6: The Relative Levels in Real Gross Domestic Product per Employed Person in Selected Countries and Years 1960-84[a]



[a]United States = 100. Data for the latest year are based on preliminary estimates.

Source: Unpublished data, U.S. Bureau of Labor Statistics, Washington, D.C.

- U.S. productivity growth has lagged behind that of some other industrial countries.
- The level of U.S. productivity remains superior to that of other major industrial countries.
- However, the international edge of the United States has diminished since 1960 because productivity growth rates have been greater in some other industrial countries.

7. THE GAO STUDY OF PRODUCTIVITY AND PROFITABILITY IN ESOP FIRMS

DESIGN AND METHODOLOGY

- We are conducting a study of the effect of ESOPs on the productivity and profitability of corporations that sponsor ESOPs. Unlike some previous studies relevant to the effect of ESOPs on economic performance, our study uses a relatively large sample of ESOP corporations and does not include other types of employee-owned firms as an ESOP-like sample. Our sample consists of firms that established ESOPs in tax years 1976 through 1979.
- Our study is designed to compare the economic performance of a matched sample of ESOP and non-ESOP firms for several years before and after the companies sponsored ESOPs. This allows a more definitive interpretation of findings than a design without a comparison group or a comparative study using data from a single year. The matched comparison group of non-ESOPs is necessary to differentiate the effects of cyclical changes in the economy from the effects of ESOPs on the economic performance of ESOP firms.
- If ESOP firms do tend to outperform non-ESOP firms, the data before and after the formation of ESOPs allow us to distinguish between two possible explanations: either more prosperous firms tend to sponsor ESOPs or firms tend to become more prosperous after sponsoring ESOPs.
- We are gathering financial data about the corporations from corporate tax returns and employee plan data from IRS computer files and questionnaires to corporations.

QUESTIONS ON PRODUCTIVITY

- After collecting and analyzing the data from our current study, we expect to report on four major questions about the effect of ESOPs on economic performance:

  1. Do companies with ESOPs experience an improvement in productivity? We expect to report whether ESOP firms that began to sponsor ESOPs in 1976-79 experienced an improvement on a measure of productivity relative to similar firms.

  2. Do companies with ESOPs experience an improvement in profitability? We expect to report whether ESOP firms that began to sponsor ESOPs in 1976-79 improved in profitability relative to similar firms.

  3. What factors related to ESOPs influence the effects of ESOPs on productivity and profitability? We plan to report which of a variety of factors are associated with changes in rates of productivity and profitability.

  4. What is the relationship, if any, between the establishment and continuation of ESOPs and the level of employees' compensation and benefits from the sponsoring corporation? To the extent possible, we will report on whether employees' compensation and benefit levels tend to be diminished, unaffected, or increased with the establishment of ESOPs.

8. GLOSSARY

GLOSSARY

Capital consumption adjustment. An adjustment in the estimates of the capital consumption allowance, or book depreciation, to reconcile these figures with actual economic depreciation.

Employee stock ownership plan (ESOP). A trust established to receive stock of an employer and other assets for allocation to the individual accounts of participating employees.

ERISA. The Employee Retirement Income Security Act of 1974, which first permitted the leveraging of qualified ESOPs.

Inventory valuation adjustment. An adjustment made in the valuation of inventories to account for differences between historical and current costs of inventories.

Leverageable ESOP. An ESOP that is permitted to leverage under the terms of the plan documents but has not done so by a given date.

Leveraged ESOP. An ESOP in which money is borrowed by the ESOP trust for the purpose of buying stock of the employer. The stock is normally held as security by the lender and released for allocation to participant accounts as the loan is paid off.

Nonleveraged ESOP. An ESOP other than a tax credit ESOP that is not permitted to leverage under the terms of the plan documents. Although these plans do not take advantage of the special tax credit or leveraging provisions of the tax code, employers may establish them to take advantage of the higher limits on deductions for contributions under section 415 of the code. Also, some employers may be unaware that they may establish and maintain a stock bonus plan that is not an ESOP.

PAYSOP. An ESOP eligible for tax credits based on employee payroll; replaced TRASOPs in 1983.

Tax credit ESOP. An ESOP originating in the Tax Reduction Act of 1975, which allows employers to claim a tax credit for contributions to an ESOP. From 1975 through 1982, the credit was based on an employer's eligible investment; a 1-percent credit could be claimed for contributions up to that amount, and an additional 0.5 percent could be claimed for contributions that matched employees' contributions up to that amount. Since 1983, a credit of 0.5 percent of employee payroll has been allowed.

TRASOP. An ESOP eligible for tax credits based on the investment tax credit provisions of the Tax Reduction Act of 1975.

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