Dispositions Tracking & Reporting – Drudgery or Delight?

If your company has a qualified Employee Stock Purchase Plan (ESPP) or grants Incentive Stock Options (ISO), disposition tracking is likely already on your list of year-end headaches. It's been on our minds here at SOS lately as well, since a client recently requested we build them a website to do their surveys electronically. They had recently switched from one service provider to another and realized, part way through the conversion, that ESPP shares could not be transferred in bulk between the brokerage firms (service providers vary in what they can do in terms of bulk transfers). They were faced with the prospect of sending paper surveys to literally thousands of participants every year *and* potentially losing hundreds of thousands of dollars in tax deductions for the company, since participants are notoriously reluctant to complete paper surveys and send them back.

Remember that for ESPP shares, ordinary income from *qualifying* dispositions must be reported on the employee's W-2 in addition to disqualifying dispositions, so in theory you are supposed to track and report on the shares for the rest of the employee's (or former employee's) life!

Disposition surveys are painful, but you can get creative about solutions without a big budget. The most common way to avoid these surveys is to have your service provider do the work for you. The majority of brokerage firms that deal in stock plans now have automated ways for you to get reports of who has sold ESPP or ISO shares and all the information you need about the transaction in order to do your W-2 reporting. My perfect solution is to require the employee to hold the shares at the designated brokerage firm. For ESPPs my recommendation is that the shares be restricted from transfer *forever* (even after termination). For ISOs we recommend transfer be restricted for 2 years + 1 day from the grant date and 1 year + 1 day from the exercise date. Many stock plan professionals gasp when we get to the "forever" part of that recommendation, but remember, that a) this is an employee benefit that they received as an employee of the company and b) you're not keeping them from their rightful gains, they can *sell* the shares at any time, just not *transfer* them away from the designated broker.

In the NASPP / Deloitte survey from 2011 31% of respondents disallowed transfer of shares away from the designated broker. That's certainly not a majority, but when the idea of disallowing transfer was first introduced, years ago, and the service provided started enhancing their platforms to support the restrictions, the most common reaction we received to the idea of restricted transfers was "What?! We would never do that! That's not employee friendly!". As companies clearly understand and can quantify what's at stake (huge company tax deduction, correct tax report for employees), more and more are likely to jump on the restriction of transfer bandwagon.

Of course this does not solve the issue if you change service providers, and it's definitely something to consider as part of your decision to change providers. Don't let the issue catch you unaware. Plan ahead!

In the ongoing movement away from paper and postal mail, we believe we will see more and more email surveys and online surveys developed and implemented by service providers, consulting firms and even in-house IT groups. In the NASPP/Deloitte survey 20% of companies distributed surveys electronically and 17% had an online survey. I'll bet we see a jump in that number the next time the NASPP includes ESPP in its survey.

Even if you are still tasked with paper surveys (whether to your whole participant base or only terminated employees), consider this inexpensive way to reduce the *number* of surveys you have to send : for those employees you have an email address for, send them an online survey asking if they've sold (or plan to sell) any company stock this year. If they answer no, that is one less paper survey to send.

However if you are doing your surveys, how do you increase response rates? Consider offering an entry in a raffle for a prize or two, or a cash reward for each form returned. Even something as small as a $25 gift card for a ubiquitous coffee shop can really drive participation. (Note that some legal counsel will have concerns about this approach, so do get with legal before spending too much time pursuing this route and, depending on the size of the prize, you may have to report the prize as part of the winning employees' income on their W-2. Another wrinkle here is non-employees, again, the size of the prize may drive whether it's reportable income or not.)

Another possible way to improve return rates on paper or electronic surveys is to educate employees on the benefit to them. ("Yes, it's good for the company, but what's in it for *me*?") Having an accurate W-2 is certainly a boon when they are struggling with their tax forms or software on April 14th.

Regardless of how you are currently tracking dispositions, keep in mind that all your efforts really do pay off for the company, not only in accurate tax reporting, but also in that glorious tax deduction. And keeping an eye open for new ideas and creative ways to track, survey and incent responses, can only pay off in the long run.

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