

**AMENDMENT IN THE NATURE OF A SUBSTITUTE  
TO H.R. 3574  
OFFERED BY MR. OXLEY**

Strike all after the enacting clause and insert the following:

**1 SECTION 1. SHORT TITLE.**

2 This Act may be cited as the “Stock Option Account-  
3 ing Reform Act”.

**4 SEC. 2. MANDATORY EXPENSING OF STOCK OPTIONS HELD  
5 BY HIGHLY COMPENSATED OFFICERS.**

6 Section 13 of the Securities Exchange Act of 1934  
7 (15 U.S.C. 78m) is amended by adding at the end the  
8 following:

9 “(m) MANDATORY EXPENSING OF STOCK OP-  
10 TIONS.—

11 “(1) NAMED EXECUTIVE OFFICER.—As used in  
12 this subsection, the term ‘named executive officer’  
13 means—

14 “(A) all individuals serving as the chief ex-  
15 ecutive officer of an issuer, or acting in a simi-  
16 lar capacity, during the most recent fiscal year,  
17 regardless of compensation level; and



1           “(B) the 4 most highly compensated execu-  
2           tive officers, other than an individual identified  
3           under subparagraph (A), that were serving as  
4           executive officers of an issuer at the end of the  
5           most recent fiscal year.

6           “(2) IN GENERAL.—Subject to paragraph (4),  
7           every issuer of a security registered pursuant to sec-  
8           tion 12 shall show as an expense in the annual re-  
9           port of such issuer filed under subsection (a)(2), the  
10          fair value of all options to purchase the stock of the  
11          issuer granted after December 31, 2004, to a named  
12          executive officer of the issuer.

13          “(3) FAIR VALUE.—

14                 “(A) IN GENERAL.—The fair value of an  
15                 option to purchase the stock of the issuer that  
16                 is subject to paragraph (2) shall be—

17                         “(i) equal to the value that would be  
18                         agreed upon by a willing buyer and seller  
19                         of such option, who are not under any  
20                         compulsion to buy or sell such option; and

21                         “(ii) shall take into account all of the  
22                         characteristics and restrictions imposed  
23                         upon the option.

24                 “(B) PRICING MODEL.—To the extent that  
25                 an option pricing model, such as the Black-



1 Scholes method or a binomial model, is used to  
2 determine the fair value of an option, the as-  
3 sumed volatility of the underlying stock shall be  
4 zero.

5 “(4) EXEMPTIONS.—

6 “(A) SMALL BUSINESS ISSUERS.—This  
7 subsection shall not apply to an issuer, if—

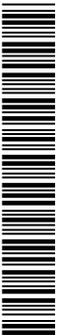
8 “(i) the issuer has annual revenues of  
9 less than \$25,000,000;

10 “(ii) the issuer is organized under the  
11 laws of the United States, Canada, or Mex-  
12 ico;

13 “(iii) the issuer is not an investment  
14 company (as such term is defined under  
15 section 3 of the Investment Company Act  
16 of 1940 (15 U.S.C. 80a-3));

17 “(iv) the aggregate value of the out-  
18 standing voting and non-voting common  
19 equity securities of the issuer held by non-  
20 affiliated parties is less than \$25,000,000;  
21 and

22 “(v) in the case of an issuer that  
23 meets the criteria in clauses (i) through  
24 (iv) and is a majority owned subsidiary,



1 the parent of the issuer meets the require-  
2 ments of this paragraph.

3 “(B) NON-REGISTRANTS.—An issuer  
4 whose securities are not registered pursuant to  
5 section 12 shall not be required to expense any  
6 option to purchase the stock of such issuer  
7 issued to its employees or members of its board  
8 of directors.

9 “(C) DELAYED EFFECTIVENESS.—The re-  
10 quirements of this subsection shall not apply to  
11 an issuer before the end of the 3-year period  
12 beginning on the date of the completion of the  
13 initial public offering of the securities of the  
14 issuer, and shall only apply to an option to pur-  
15 chase the stock of an issuer granted after such  
16 date.”.

17 **SEC. 3. PROHIBITION ON EXPENSING AND ECONOMIC IM-**  
18 **PACT STUDY.**

19 (a) PROHIBITION.—Section 19(b) of the Securities  
20 Act of 1933 is amended by adding at the end the fol-  
21 lowing:

22 “(3) PROHIBITION ON EXPENSING STAND-  
23 ARDS.—

24 “(A) IN GENERAL.—The Commission shall  
25 not recognize as ‘generally accepted’ any ac-



1 counting principle relating to the expensing of  
2 stock options unless—

3 “(i) it complies with the requirements  
4 of subparagraph (B); and

5 “(ii) the economic impact study re-  
6 quired under section 3(b) of the Stock Op-  
7 tion Accounting Reform Act of 2003 has  
8 been completed.

9 “(B) REQUIREMENTS.—A standard re-  
10 ferred to in subparagraph (A) shall require  
11 that—

12 “(i) if an option to purchase the stock  
13 of an issuer that is subject to the require-  
14 ments of section 13(m) of the Securities  
15 Exchange Act of 1934 is exercised—

16 “(I) any expense that had been  
17 reported under that section 13(m)  
18 with respect to such option shall be  
19 recomputed as of the date of exercise  
20 and shall be equal to the difference  
21 between the price of the underlying  
22 stock and the exercise price; and

23 “(II) to the extent the recom-  
24 puted amount differs from the  
25 amount previously reported under sec-



1                   tion 13(m) with respect to such op-  
2                   tion, the difference shall be reported  
3                   in the fiscal year in which the option  
4                   is exercised as a reduction or increase,  
5                   as the case may be, of the total ex-  
6                   pense required to be reported under  
7                   that section 13(m) during that fiscal  
8                   year;

9                   “(ii) if an option to purchase the  
10                  stock of an issuer that is subject to the re-  
11                  quirements of section 13(m) of the Securi-  
12                  ties Exchange Act of 1934 is forfeited or  
13                  expires unexercised, any expense that had  
14                  been reported under that section 13(m)  
15                  with respect to such option shall be re-  
16                  ported in the fiscal year in which the op-  
17                  tion expires or is forfeited as a reduction  
18                  of the total expense required to be reported  
19                  under that section 13(m) during that fiscal  
20                  year; and

21                  “(iii) to the extent that any reduction  
22                  required under clause (i) or (ii) exceeds  
23                  total option expenses for any fiscal year,  
24                  such excess shall be reported as income



1 with respect to options to purchase the  
2 stock of the issuer.”.

3 (b) **ECONOMIC IMPACT STUDY.**—The Secretary of  
4 Commerce and the Secretary of Labor shall conduct and  
5 complete a joint study on the economic impact of the man-  
6 datory expensing of all employee stock options, including  
7 the impact upon—

8 (1) the use of broad-based stock option plans in  
9 expanding employee corporate ownership to workers  
10 at a wide range of income levels, with particular  
11 focus upon non-executive employees;

12 (2) the role of such plans in the recruitment  
13 and retention of skilled workers;

14 (3) the role of such plans in stimulating re-  
15 search and innovation;

16 (4) the effect of such plans in stimulating the  
17 economic growth of the United States; and

18 (5) the role of such plans in strengthening the  
19 international competitiveness of businesses organized  
20 under the laws of the United States.

21 **SEC. 4. IMPROVED EMPLOYEE STOCK OPTION TRANS-**  
22 **PARENCY AND REPORTING DISCLOSURES.**

23 (a) **ENHANCED DISCLOSURES REQUIRED.**—Not later  
24 than 180 days after the date of enactment of this Act,  
25 the Commission shall, by rule, require each issuer filing



1 a periodic report under section 13(a) or 15(d) of the Secu-  
2 rities Exchange Act of 1934 (15 U.S.C. 78m, 78o(d)) to  
3 include in such report more detailed information regarding  
4 stock option plans, stock purchase plans, and other ar-  
5 rangements involving an employee acquisition of an equity  
6 interest in the company. Such information shall include—

7 (1) a discussion, written in “plain English”, in  
8 accordance with the Plain English Handbook pub-  
9 lished by the Office of Investor Education and As-  
10 sistance of the Commission, of the dilutive effect of  
11 stock option plans, including tables or graphic illus-  
12 trations of such dilutive effects;

13 (2) expanded disclosure of the dilutive effect of  
14 employee stock options on the issuer’s earnings per  
15 share;

16 (3) prominent placement and increased com-  
17 parability and uniformity of all stock option related  
18 information;

19 (4) the number of outstanding stock options;

20 (5) the weighted average exercise price of all  
21 outstanding stock options; and

22 (6) the estimated number of stock options out-  
23 standing that will vest in each year.

24 (b) DEFINITIONS.—As used in this section:



1           (1) COMMISSION.—The term “Commission”  
2 means the Securities and Exchange Commission.

3           (2) ISSUER.—The term “issuer” has the mean-  
4 ing provided in section 2(a)(7) of the Sarbanes-  
5 Oxley Act of 2002 (15 U.S.C. 7201(a)(7)).

6           (3) EQUITY INTEREST.—The term “equity in-  
7 terest” includes common stock, preferred stock,  
8 stock appreciation rights, phantom stock, and any  
9 other security that replicates the investment charac-  
10 teristics of such securities, and any right or option  
11 to acquire any such security.

