



A Stock Option Exchange Update – Shareholder-Approved Exchanges

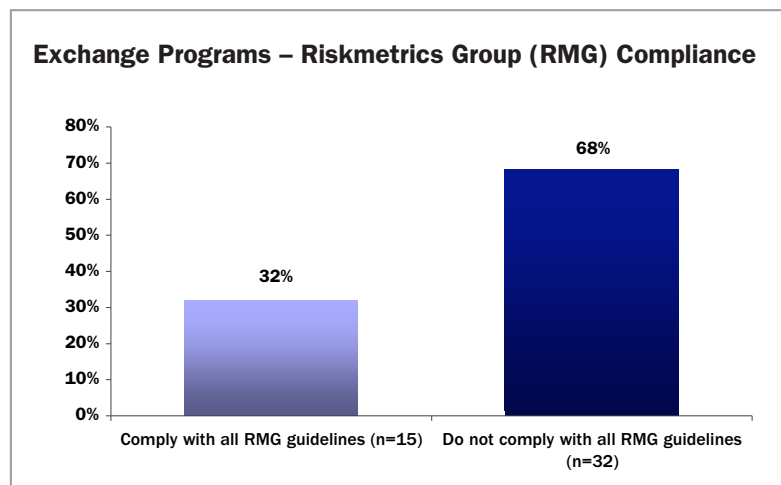
With the stock market in turmoil, a significant number of companies are implementing stock option exchange programs. As of the end of February, we have identified (and compiled data on the terms and conditions of) over 130 option exchange programs since the adoption of Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment (SFAS123(R)) in 2004. To date, 47 of these programs had been submitted to shareholders for approval.

Typically, companies that seek shareholder approval of an option exchange program are required to do so under the terms of their employee stock plan. However, a small group of companies with the ability to implement an exchange program solely with Board of Directors' authorization have sought shareholder approval as a matter of good corporate governance.

Depending on the composition of your shareholder base, designing a meaningful option exchange program that will be approved by shareholders can be a daunting task. RiskMetrics Group ("RMG"), other proxy advisory firms, and many institutional shareholders require that the program satisfy a number of specific conditions or "guidelines" before they will support it. Many of these guidelines limit a company's flexibility to set the terms and conditions of the program. For example, generally RMG will not support an exchange program unless it reflects the following characteristics:

- Excludes named executive officers and non-employee directors
- Is "value-neutral" for financial reporting purposes
- Imposes new vesting restrictions on the awards received
- Excludes certain "underwater" stock options (for example, options granted within one-three years of the proposed exchange date or options priced below the 52-week market price of the company's common stock at the time of the proposed exchange), so that the program is not perceived to be an overreaction to a short-term market drop,

Satisfying these conditions (as well as any other applicable guidelines for an option exchange) may undermine your desired objectives or reasons for pursuing an exchange program. For example, a company may not be able to significantly enhance employee retention and reduce excessive and unproductive "overhang" if the majority of underwater options are





THOUGHTFUL PAY ALERT

A Stock Option Exchange Update – Shareholder-Approved Exchanges (continued)

deemed to be ineligible for exchange in the program. Consequently, a surprisingly significant number of companies (32 of 47) which were required to obtain shareholder approval of their option exchange program elected to do so without complying with all of the RMG guidelines.

As of the end of February 2009, of the 15 companies that structured their option exchange programs to comply with all of the RMG guidelines, 12 had been approved by shareholders and 3 were pending approval.

The following chart identifies the specific RMG guidelines that the other 32 companies that sought shareholder approval of their option exchange programs did not appear to comply with (categories are not mutually exclusive).

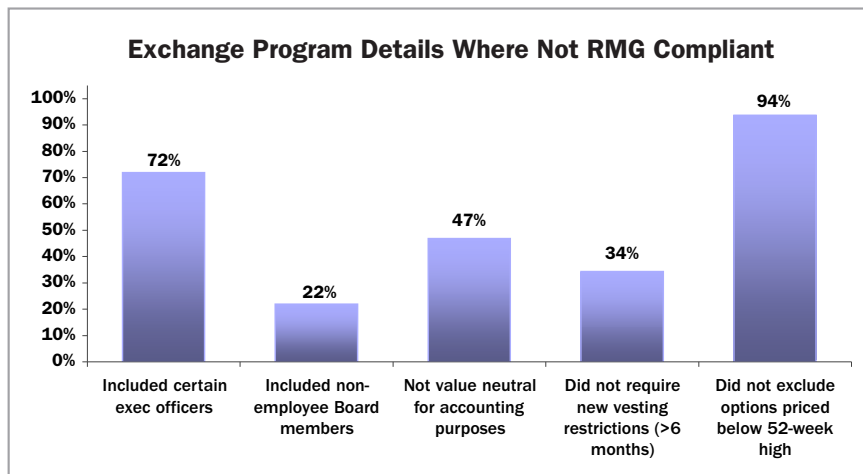
Of these 32 programs, 69% were approved by shareholders, 6% failed to receive shareholder approval, 6% were withdrawn prior to the formal vote, and 19% were pending approval.

From these results, it is becoming increasingly clear that, where shareholder approval is required, it is critical that you understand not only RMG's guidelines, but also the policies and concerns of your shareholder base so that an option exchange program that best meets your objectives will still be supported by your shareholders.

Need Assistance?

Compensia has significant experience in designing stock option exchange programs. In addition to being one of the top compensation advisers to technology and life science companies, we have advised numerous technology and life science companies regarding option exchanges in the past several years. Several of our partners have legal backgrounds and have extensive experience advising companies on all aspects of the exchange. If you have any questions on option exchanges or evaluating the advantages and disadvantages of seeking shareholder approval

for an option exchange program, please feel free to contact us. Our contact information is included at the end of this article. ■





THOUGHTFUL PAY ALERT

Compensia

A Stock Option Exchange Update – Shareholder-Approved Exchanges (continued)

About Compensia

Compensia, Inc. is a management consulting firm that provides executive compensation advisory services to Compensation Committees and senior management.

San Francisco

770 Tamalpais Drive
Suite 207
Corte Madera, CA 94925
415.462.2990

Mark H. Edwards, Chairman
medwards@compensia.com
415.462.2985

Michael Benkowitz
mbenkowitz@compensia.com
415.462.2996

Mark A. Borges
mborges@compensia.com
415.462.2995

Southern California

Anna-Lisa Espinoza
alespinoza@compensia.com
858.509.1179

Silicon Valley

1731 Technology Drive
Suite 810
San Jose, CA 95110
408.876.4025

Timothy J. Sparks, President
tsparks@compensia.com
408.876.4024

Thomas G. Brown
tbrown@compensia.com
408.876.4023

Susan Gellen
sgellen@compensia.com
408.907.4302

Tom LaWer
tlawer@compensia.com
408.907.4309