

Employee Stock Plan Proposals at the Bay Area 150

2013 was another busy year for employee stock plan proposals among the 150 largest publicly-traded technology and life sciences companies headquartered in the San Francisco Bay Area (“the Bay Area 150”). Once again, we have compiled information about the voting results from the 2013 proxy season of proposals to either adopt a new employee stock plan or increase the share reserve for an existing plan.

This Thoughtful Pay Alert summarizes these results for the past 12 months, based on the information disclosed in the companies’ proxy statement filings with the Securities and Exchange Commission.

Number of Employee Stock Plan Proposals Remained Robust in 2013

Nearly one-third of the Bay Area 150 submitted proposals to their shareholders to either adopt a new employee stock plan or increase the share reserve for an existing plan during the past 12 months (based on a review of proxy statements filed for companies with fiscal year ends during the period from June 1, 2012 through May 31, 2013). This figure is consistent with the number of proposals submitted for shareholder action in each of the prior three years.

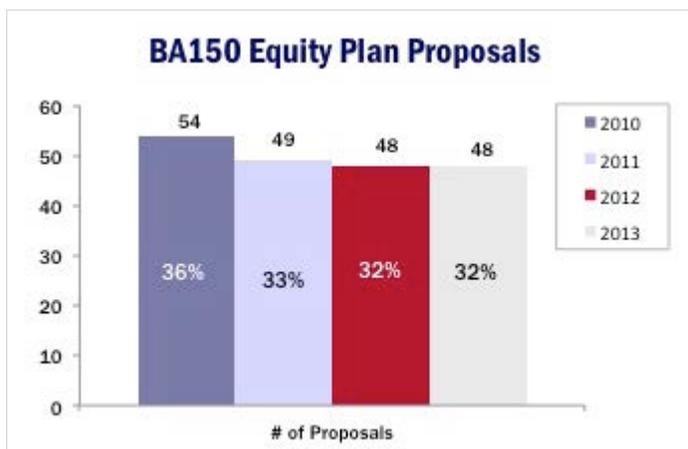
This pattern over the last four years reflects the typical life cycle for many employee stock plans. Mature public compa-

nies generally seek to replenish their employee stock plan share reserve, or adopt a new plan, approximately every two to three years. The data suggests that, in any given year, approximately one-third of the Bay Area 150 is going through the process – and attendant scrutiny – of seeking shareholder approval for an employee stock plan. This pattern also reflects, in part, the dilution policies of the major proxy advisory firms, such as Institutional Shareholder Services (“ISS”), and some institutional investors, which typically limit the number of shares that they will authorize at any given time for purposes of making equity awards.

Notable exceptions do exist, however. These include companies that, for corporate governance or consistency purposes, seek approval of a share reserve increase for an existing employee stock plan on an annual basis (such as Intel Corporation and Maxim Integrated). On the flip side, most recently-public companies that are new to the Bay Area 150 have an “evergreen” provision in their employee stock plan that provides for annual share replenishments without shareholder approval for up to 10 years. In addition, other companies have favorable shareholder bases that permit more aggressive, longer-term share reserve requests.

Size of Share Reserve Requests Increased in 2013

Among the 48 Bay Area 150 companies that sought shareholder approval of a new or amended employee stock plan in 2013, the average share reserve request (as a percentage of the company’s outstanding shares) was up 14% (5.17% in 2013 compared to 4.53% in 2012). Further, the median share reserve request was up 12% (4.57% in 2013 compared to 4.10% in 2012). Four Bay Area 150 companies (Echelon, Nanometrics, Ultra Clean, and WageWorks) sought an increase of more than 10% of their outstanding shares to add to an existing plan share reserve. No such share reserve increases were sought in 2012. Including the shares remaining available for grant in existing share reserves at the time of the proposal, only 31% (15 of 48) of the companies had total share reserves in



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Equity Plan Reserves

	June 2011 to May 2012 (n=48)			June 2012 to May 2013 (n=48)		
	New Shares as %	Current Shares as %	Total Shares as %	New Shares as %	Current Shares as %	Total Shares as %
Market 75th	5.68%	4.90%	9.69%	7.22%	4.50%	11.39%
Market 50th	4.10%	3.61%	7.89%	4.57%	3.28%	8.41%
Average	4.53%	3.75%	8.28%	5.17%	4.52%	9.69%
Market 25th	2.47%	2.35%	6.04%	2.96%	1.75%	6.45%

excess of 10% of their outstanding shares (assuming the proposal was approved by shareholders).

High Prevalence of Fungible Share Provisions

The size of the share reserve requests noted above are based on total shares as a percentage of each company's outstanding shares (basic) of common stock. Notably, many of these employee stock plans contain a "fungible share" provision that limits the amount of full-value equity awards (such as restricted stock unit and performance share awards) that may be granted from the share reserve. Under a fungible share provision, full-value awards are counted at a higher rate for reserve depletion purposes to effectively neutralize their impact on a plan's share reserve relative to appreciation-based equity awards (such as stock options and stock appreciation rights). For example, if the employee stock plan provides that, for share reserve depletion purposes, full-value awards count as two shares for every one share granted, then one restricted share granted will count the same as two option shares granted under the plan.

In 2013, 67% (32 of 48) of the Bay Area 150 companies that submitted proposals for new or amended employee stock plans had a fungible share provision in their plan (while two other companies had specified full-value share limits in their plans). Looking solely at these companies, the size of their total share reserve requests was slightly higher at the median than in the case of the proposals at companies without fungible share provisions. Generally, the fungible

share ratios ranged between 1.5:1 to 2.0:1 and, in most cases, were specifically derived for each company from the relative fair value of a full-value award compared to the fair value of an appreciation-based award (based, in many cases, on ISS' notion of "fair value").

All Employee Stock Plan Proposals Approved in 2013

As was the case in 2012, each of the 48 Bay Area 150 companies with an employee stock plan proposal in 2013 saw its proposal approved by its shareholders. The average level of support was 79.8% of the votes cast (which was largely consistent with the average level of support in 2012 – 78.6%). Notably, 15% (7 of 48) of the Bay Area 150 companies registered vote totals in favor of their proposals which represented 50% or less of their total outstanding shares. We note that these situations have become more common in recent years as a result of the Dodd-Frank Act provision which prohibits companies from taking broker non-votes into consideration when calculating the votes cast on an employee stock plan proposal.

Observations

Shareholder support of employee stock plan proposals in 2013 was up somewhat from 2012 and the average size of

Equity Plan Reserves (FYE June 2012 to May 2013) (n=48)

	Fungible Plans (n=34)			
	New Shares as %	Current Shares as %	Total Shares as %	Plan Fungible Ratio
Market 75th	7.92%	4.44%	11.45%	2.00
Market 50th	5.07%	3.99%	8.75%	1.76
Average	5.53%	3.41%	8.94%	1.99
Market 25th	3.25%	2.09%	7.15%	1.53

Employee Stock Plan Proposals at the Bay Area 150 (continued)

these share reserve requests also increased slightly. Only 29% (14 of 48) of the Bay Area 150 companies conducting an employee stock plan votes received less than 75% support based on the number of votes cast. Both the consistent level of support and the slight increase in the size of the share reserve requests likely reflect that companies continue to comply with ISS' equity plan dilution limits to ensure a successful outcome on their proposal.

When compared to the broader market, the experience of the Bay Area 150 companies was not unusual. Generally, looking at public companies submitting a new employee stock plan or proposal for a share reserve increase during the first half of 2013, less than one-third received an unfavorable vote recommendation from one or more of the major proxy advisory firms and just a handful failed to

see their plan proposal or share reserve request approved by shareholders.

Need Assistance?

Compensia has extensive experience in assisting companies in formulating employee stock plan proposals and developing effective strategies for obtaining shareholder approval of such proposals. If you would like assistance in analyzing your equity compensation strategy or negotiating the various pressure points in implementing an employee stock plan or a share reserve increase, or if you have any questions on the subjects addressed in this Thoughtful Pay Alert, please feel free to contact Jason Borrevik at 408.876.4035 or Mark A. Borges at 415.462.2995. ■

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