Recommended Steps to Successful Equity Plan Approval – (Part 1: Steps 1-8)

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There was a time when seeking shareholder approval of an equity compensation plan was a fairly simple process. Management would discuss a share increase with the board of directors, and the company would include a brief discussion of the proposal in the proxy. Those days are long gone.

Companies that are planning to submit an equity plan for shareholder approval in 2016 should start the process early and consider a wide range of issues, from shareholder perspectives to future needs for equity grants to evolving case law. In this two-part blog series, we outline 15 steps to be considered when submitting an equity plan for shareholder approval in 2016.

1. Review your shareholder base to determine whether the shareholders follow Institutional Shareholder Services, Inc. (ISS) or Glass Lewis recommendations.

2. If your shareholders follow ISS recommendations, consider subscribing to ISS’s proxy review services.

3. Review any internal guidelines published by your shareholders for approval of equity plans.

4. Whether or not you subscribe to ISS’s services, sign up for the ISS Equity Plan Data Verification portal (no charge) If you sign up for this portal, ISS will send a confirmation of the data on which their recommendation will be based. Upon receipt of the ISS data confirmation, you will have two business days to verify the data or request modifications if the data is incorrect.

5. When considering share authorization, review share overhang (outstanding equity grants as compared to outstanding shares), burn rate (share usage) over the past several years (usually three years), the company’s projected need for shares over the next several years (usually three to four years), and, if applicable, ISS’s assessment of the allowable share authorization.

6. ISS’s current methodology for reviewing equity plans, the Equity Plan Scorecard, gives “points” based on plan cost (share authorization), plan features, and grant practices. ISS reviews share authorization two ways: (1) taking into consideration outstanding equity grants and (2) without including outstanding equity grants. This approach is helpful for companies with a large number of outstanding equity grants, such as unexercised stock options, that create a high overhang percentage.

7. Under the Equity Plan Scorecard, ISS’s “points” for plan features take into account, among other factors, whether or not the plan has:
   - Double trigger vesting
   - Minimum vesting requirements
• Prohibition against discretionary vesting (except upon death, disability or change in control)

• Liberal share counting (e.g. adding back to the plan reserve shares that are withheld for taxes or for the exercise price of options).

In determining whether to include ISS’s favored plan terms, it is important to balance the need to maximize the share authorization against the importance to the company of retaining flexibility, especially with respect to vesting.

8. Update the plan to reflect current best practices and legal requirements, and, if applicable, ISS requirements. ISS may recommend against an equity plan if it:

• Has a liberal change in control definition

• Permits repricings or cash buyouts of underwater options or stock appreciation rights without shareholder approval

• Is a vehicle for problematic pay practices or has a pay-for-performance disconnect

• Features other provisions or practices that are considered detrimental to shareholder interests, such as tax gross-ups.

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