Outline

- Introduction
- Compensation and Benefits Issues to Consider in the IPO Context
  - Compensation Philosophy
  - Stock Incentive Plans
  - Severance and Employment Agreements
  - Non-Employee Director Compensation
  - Corporate Governance
  - Financial and Wealth Transfer Planning
Introduction
• **Why Focus On Executive Compensation?**
  
  – Creation of a public market introduces a number of significant new legal and business factors that have a substantial impact on the appropriate design of a company's long-term compensation and benefits strategy including:
    
    – Increased value and liquidity of equity-based awards
    
    – Public disclosure of financial results
    
    – Public disclosure of executive compensation for “named executive officers”
    
    – Increased scrutiny of management performance and compensation decisions, “say-on-pay”
    
    – Shorter-term focus by investors

• **Investor Expectations Regarding Executive Compensation**
Compensation Philosophy
Establish a Post-IPO Compensation Philosophy That Accounts for these Material Changes

- Objectives of the compensation program
  - Driving Performance
  - Retention/Attraction of Executive Officers and Other Employees
- Reassess total pay mix
  - Cash vs. Equity-Based Compensation
  - Balance of Short-Term and Long-Term Incentives
  - Type of Equity Compensation Used
  - Limited Perquisites
Establish appropriate peer group and desired competitive market position
  – Market capitalization peers/direct competitors
  – Similar organizational structure or business model
  – Where is talent lost or recruited from

Keep in mind public disclosure requirements for “named executive officers”
  – Mandatory “say on pay” (except for EGCs)
  – Institutional investor preferences/“pay-for-performance”

Reassess approach to benefits and perquisites in public company environment

Consider engaging an outside compensation consultant to assist Board’s compensation committee
Stock Incentive Plans
Stock Incentive Plans

• Adoption of New or Amended “Omnibus” Stock Incentive Plan
  – All pre-IPO companies should adopt a new or amended stock incentive plan
  – Include full menu of stock awards, such as options, stock purchases, restricted stock bonuses, and stock appreciation rights
  – Single, unified pool for equity-based awards
  – Strongly consider “evergreen” share reserve
  – Post-IPO stockholder approval required to increase share reserve
  – Section 162(m) transition period and related issues
• Adoption of Employee Stock Purchase Plan
  – Allows eligible employees to purchase the company’s shares periodically throughout a year (offering periods can be as long as 27 months, although usually not longer than 6 months)
  – Shares are purchased with after-tax dollars withheld from payroll at the employees’ election
  – Plans can offer a discount of up to 15% of the trading price either at the beginning or end of the purchase period
  – May be more efficient than stock option or RSU awards in the US (under Section 423 of the IRC there is no immediate taxation on purchase at a discount)
  – Can include an evergreen reserve
Stock Incentive Plans

• Existing Employee Equity Awards
  – “Cheap stock” and Section 409A issues in lead up to IPO
  – Pre-IPO lack of liquidity
  – Increasing use of restricted stock units in lieu of stock options pre-IPO with service-based and liquidity restrictions (“Facebook” RSUs)

  – SEC registration (Form S-8)
  – Introduction of "Same-Day Sale" Program

  – Other post-IPO stock plan administration considerations (in-house vs. outsourcing)
Severance and Employment Agreements
Consider severance pay/retention arrangements

- Private companies may not have in place any severance or retention arrangements
- Executives with substantial stock holdings may become more of a retention risk post-IPO
- Public scrutiny of corporate financial performance and executive compensation may also increase need for retention incentives and executives’ desire for severance protection
- Severance/retention arrangements can be limited to senior management or broad-based
- Plan/policy vs. individual agreements (trend in recent years has been to use plans/policies)
Consider new or amended executive employment agreements

– Consider whether existing employment agreements are appropriate in a public company context

– SEC disclosure requirements for employment agreements with “named executive officers” and other “executive officers”

– Consider eliminating employment agreements in favor of a severance plan or policy
Non-Employee Director Compensation and Corporate Governance
Non-Employee Director Compensation Considerations

- Minimal cash compensation for directors pre-IPO
- New/independent board members are added in connection with IPO
- Compensation mix for non-employee directors post-IPO
- Automatic annual equity grants in addition to cash compensation
- Heightened scrutiny on compensation decisions regarding non-employee directors
- Consider separate shareholder-approved director equity plan and/or lower limits on director awards as compared to employee awards to manage threat of lawsuits alleging directors of self-dealing when compensating themselves
• Formalized compensation process
  – Public companies are subject to more stringent corporate governance rules regarding executive officer compensation
  – Stock exchange listing requirements relating to compensation committee duties and independence
  – Stock exchange listing requirements relating to compensation committee authority to engage consultants and advisors and related independence requirements
  – Securities laws (Section 16) require compensation committee approval of executive officer equity awards and transactions in connection therewith (i.e. share withholding)

• Obtain adequate Directors and Officer’s liability insurance
Financial and Wealth Transfer Planning
Financial and Wealth Transfer Planning

- Financial and Wealth Transfer Planning
  - Often overlooked by executives pre-IPO
  - Executives should consider the impact of an IPO on personal financial and estate planning
  - Tax-efficient approaches exist for achieving financial and estate planning objectives
  - Advance planning can prove very beneficial, especially from a tax perspective
Questions?
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