

**American Benefits Council:
Executive Compensation Webinar #2:
Stock Plans and Awards**

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About our Panel

- Lynn Dudley, American Benefits Council
- Mark Poerio, Paul Hastings
- Brigen Winters, Groom Law Group
- Erik Lundgren, Winston & Strawn
- Elizabeth Drigotas, Deloitte Tax LLP

Life Cycle of Stock Plans

- Adoption by board of directors
- Shareholder approval
- SEC registration of plan shares
- Administration of Plan
 - Granting of awards
 - Grant-making procedures
 - Interpreting Plan
- Modification of Awards
- Plan amendment and termination

Stock Awards Overview

- Types of Awards
 - Appreciation (*Options/SARS*) vs. Full Value (*RS/RSUs/PSUs*)
 - Promise vs. Property
 - Time Vesting vs. Performance Vesting
- Many Important Considerations – requires Team Effort
 - Governance – Board and compensation committee
 - Tax – individual and company (Sections 83, 162(m), 409A, etc.)
 - Finance and accounting
 - SEC – registration, disclosure and reporting
 - HR and Payroll – design, implementation and administration
 - Shareholder/investor relations

Stock Option Basics

Key Terms

- Incentive stock options
- Non-statutory (nonqualified) stock options
- Grant Date
- Exercise Price and Fair Market Value
- Vesting and Exercise
- In-the-money Value ... and Synonyms
- Term and Expiration Date
- Termination of Employment

Stock Options – Tax vs. Financial

Example:

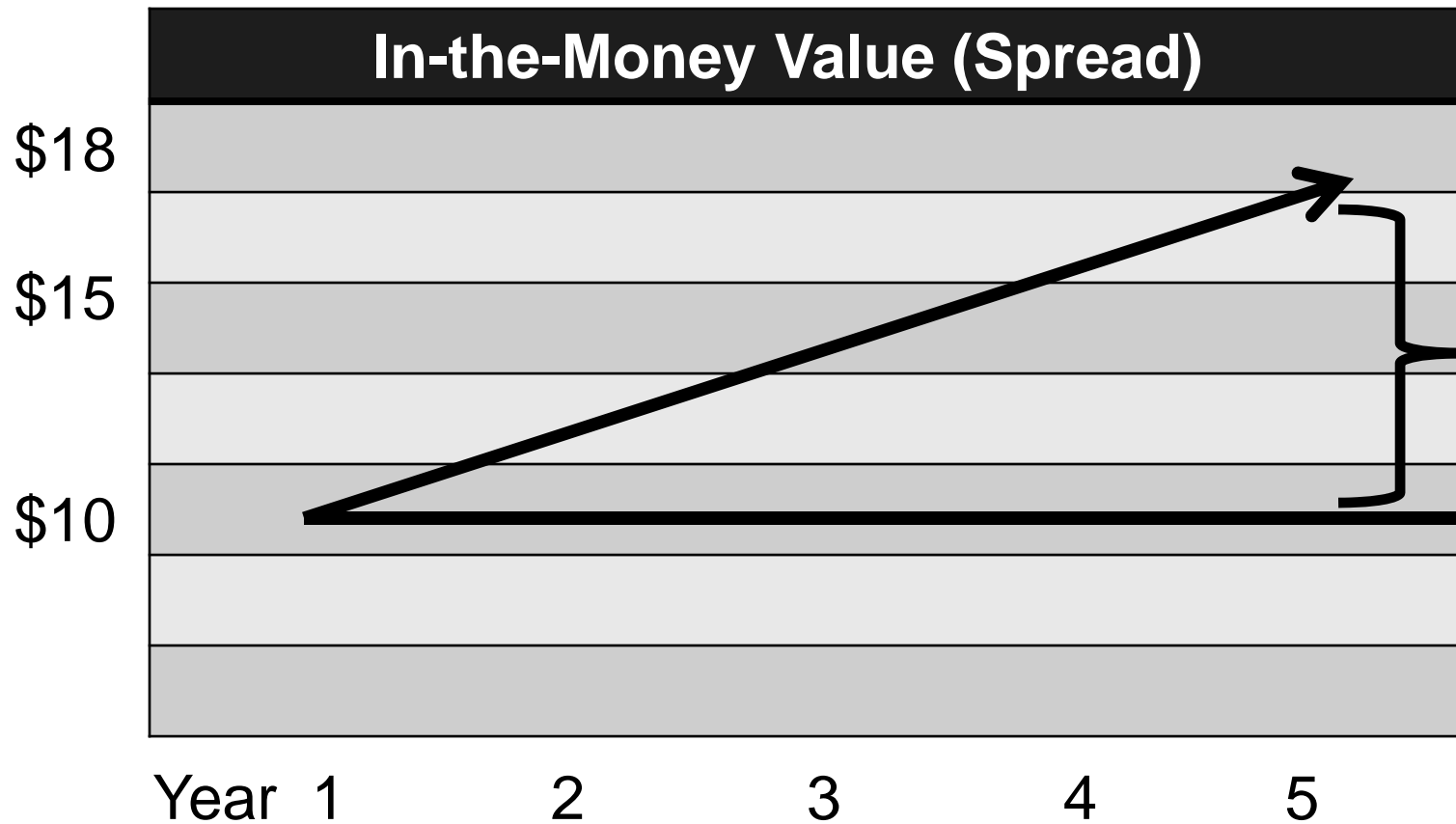
- Grant Date – 100 shares at FMV = \$10/share
- Vesting – 50% year 1; 50% year 2
- Exercise Yr 3 – 100 shares at FMV = \$15/share
- Sale Yr 5 – 100 shares at FMV = \$18/share

Tax Result: Non-ISO vs ISO?

409A: Exception for non-discounted awards

Accounting -- Black-Scholes at Grant Date - \$3/share

Stock Options – Financial Picture



Stock Appreciation Rights

Key Terms

- Net Settlement
- Cash vs. Shares

Differences from Stock Options

- Tax
- Accounting

Historical Perspective RE: Little Use

409A: Exception for certain awards

Post-Grant Issues

Underwater ... Out-of-the-Money

Sample Facts:

- Grant Date FMV – 100sh @ \$10
- FMV at end Year 1 -- \$4/share

Business Challenge???

- Repricing?
- History – Acctg Changes
- Exchange Offer

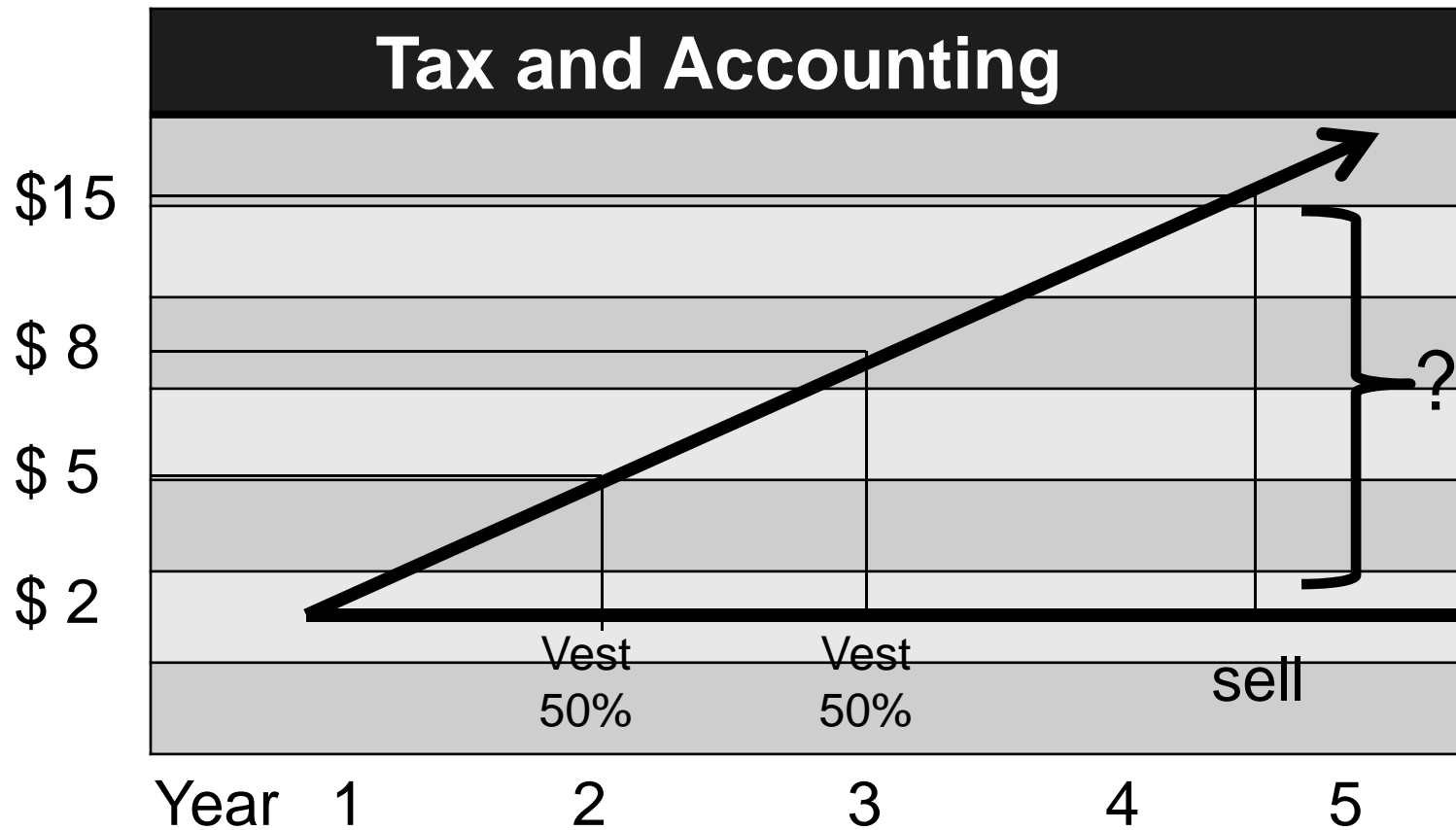


Restricted Stock - Basics

Key Terms

- Nature of Award
- General Tax and Accounting Rules
- Code Section 83(b)
 - Basic Rule
 - Circumstances when utilized
- Administration – stock issuance; legend
- 409A exemption

Restricted Stock – Financial



Restricted Stock – Tax and Fin'l

Example:

- Grant Date – 100 shares at FMV = \$2/share
- Vesting – 50% year 1 @ \$5/share
50% year 2 @ \$8/share

Accounting Result? \$___ expense per year

Tax Result:

- With 83(b) Election: income = \$___ at ___ (when?)
- Normal Rule: income = \$___ at ___ (when?)

Restricted Stock – Net Tax Settlement

Assume Net Settlement for 50 shares vesting at FMV \$5 per share at end of year one.

- Assume 25% withholding rate on supp income.
- How many shares withheld for taxes? ____
- What happens to those shares? Their \$ value?
- How many shares issued to employee? ____

Restricted Stock Units (RSUs)

- Nature of Award
 - Administration
- Tax Timing Alternatives
 - Tax on Vesting
 - Deferral permitted?
 - Code Section 83(b)?
 - Code section 409A
- Financial Accounting

Restricted Stock vs RSUs

Restricted Stock	RSUs
Unvested shares issued, and then replaced with vested	Only vested shares issued >>> <i>easier administration</i>
Voting of unvested shares	No voting until vesting
U.S. Section 83(b) election allowed	Ineligible for Section 83(b) election
Tax deferral not allowed post-vesting	Tax deferral possible
Dividends paid or reinvested	Same as restricted stock

Performance-based awards

- A. Performance shares
- B. Performance units
- C. Performance-based Amount
- D. Performance-based Vesting
 - Service-based Vesting

Other Types of Awards - Terms

- DSUs -- how different from RSUs?
- Phantom Stock
- Phantom SARs
- ESPPs and Section 423 plans
- DRIPs

Conclusion

- Questions?