Evolving Your Equity Compensation Strategy:

A Crash Course for Private Companies

OCTOBER 1, 2024

Today's speakers:

Jon Burg

Managing Director, Infinite Equity

jon@infiniteequity.com

Emily Cervino

Head of Industry Relationships and Thought Leadership, Fidelity

emily.cervino@fmr.com

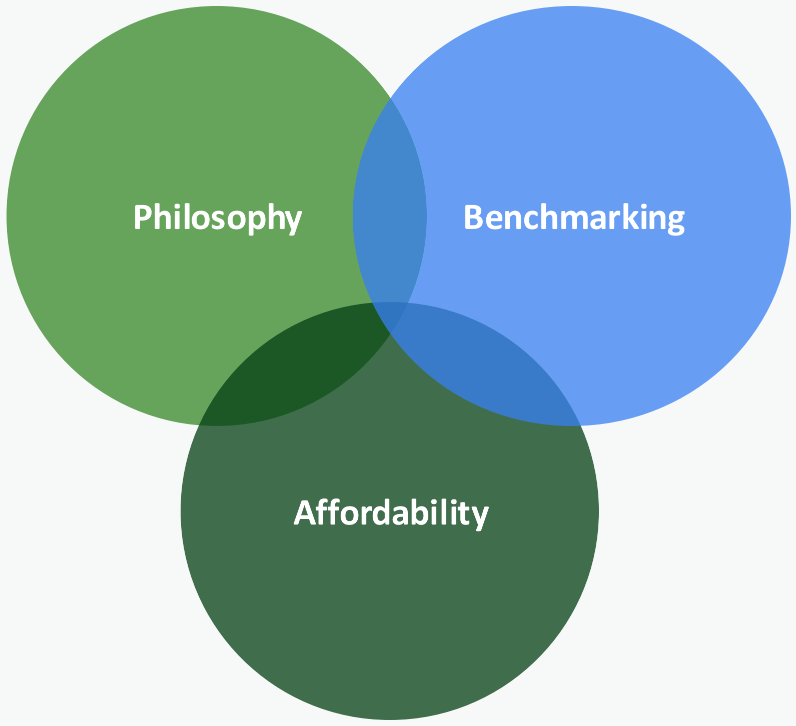
DeRonnie Pitts

VP, Business Partner Manager, Equity Compensation, Fidelity

deronnie.pitts@fmr.com

What is the importance of an equity compensation strategy?

Equity awards need to evolve and grow to balance equity philosophy, market benchmarks, and affordability, and may need attention due to changes in leadership, funding, and market volatility.



From Creative Designs to Streamlined Strategies:

How companies adjust their equity plans over time

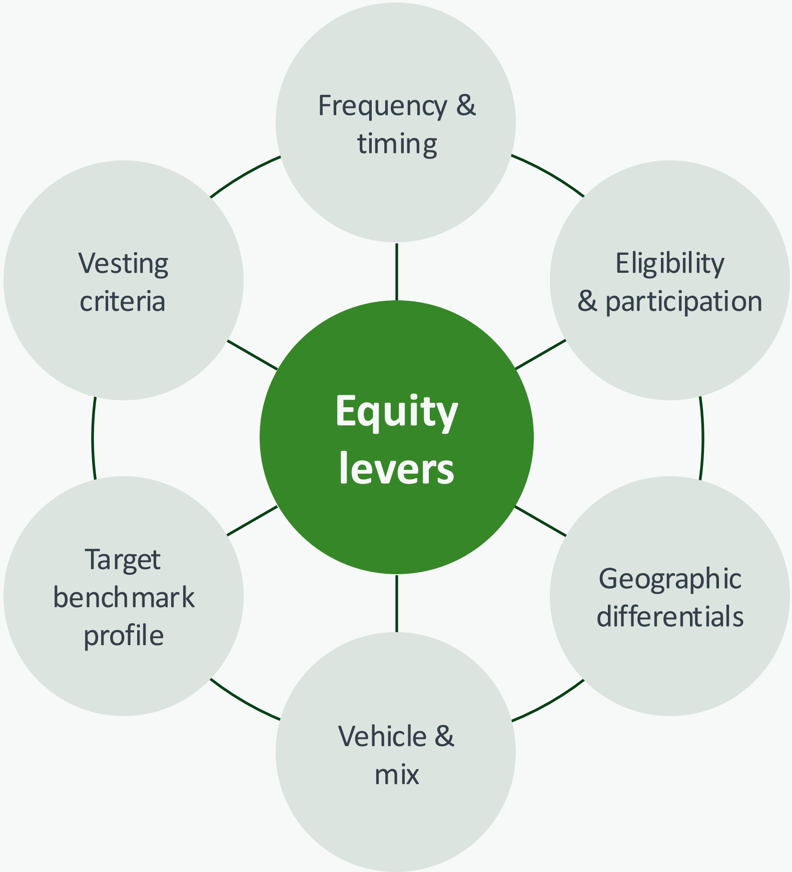
How companies evolve their strategies as they grow

Start Up	Series B/C	Late Stage	Pre-IPO	Public Co
Strategic considerations				
• Attract talent • Almost exclusively stock options • Possibly RSAs for founders and early employees	• Mostly options • Equity guidelines developed • C-suite benchmarked • Refresh and promotion strategy developed	• Guidelines refreshed • Global differentials • Refresh and promotion strategy refined • Buybacks and liquidity offering considered	• Guidelines refreshed • Comp. Committee formed and independent advisor hired • RSUs with liquidity trigger evaluated • Plans and agreements refreshed with evergreen provision • ESPP readied	• Guidelines refreshed every 2-3 years • RSUs primary vehicle below VP • Executives receive mix of RSUs, PSUs, and options • Burn rate and share reserve pressure • Employees stock purchase plans (ESPP) at 57%*
Practical/administrative considerations				
• Cap table decisions • Cap table owner • Support 83(b) elections	• Initial Section 409A valuation • Documentation practices	• Align solutions to public company needs	• Transfer Agent • Public company needs • ELR details. • Dual classes decisions • Automate data feeds • Establish tax withholding processes • Secure resources for public need	• Day 1 trading • Launch ESPP • Communication and education for employees • Monthly, quarterly, and annual reporting for internal stake holders.

*2024 Equity Incentives Design Survey, NASPP and Deloitte

Strategic Design Considerations

Equity strategy levers



Eligibility and participation should be considered as a company grows.

Guidelines should be benchmarked and targeted at the market 50th percentile.

Differentials and levers such as RSUs, stock options, performance awards, frequency, and vesting schedule can be utilized in equity strategy.

From Attraction to Retention

Understanding refresh strategies

Understanding refresh strategies

1

Developing a refresh strategy is critical for maintaining employee alignment in companies with longer exit timelines

2

Refresh awards can help retain key employees by offering new options with new vesting periods

3

Granting refresh awards sooner can potentially enhance retention by ensuring more tranches are unvested compared to those already earned

4

A new grant allows the company to introduce different vesting schedules, encouraging employees to stay longer and contribute to the company's ongoing growth.

Vesting Strategy

1 Traditional

Annual:

Year	1	2	3	4	5	6	7	8
New Hire	2,000							
Refresh 1			500					
Refresh 2				500				
Refresh 3					500			
Refresh 4						500		
Total	500	500	625	750	375	500	500	500

Every two years:

Year	1	2	3	4	5	6	7	8
New Hire	2,000							
Refresh 1			500					
Refresh 2					500			
Total	500	500	625	625	250	250	250*	250*

* If grants continue to stack it will reflect in shares vesting.

2 Boxcar

Annual:

Year	1	2	3	4	5	6	7	8
New Hire	2,000							
Refresh 1					500			
Refresh 2						500		
Refresh 3							500	
Refresh 4								500
Total	500	500	500	500	500	500	500	500

Every two years:

Year	1	2	3	4	5	6	7	8
New Hire	2,000							
Refresh 1					500			
Refresh 2							500	
Total	500	500	500	500	250	250	250	250

When is the right time to consider moving from stock options to RSUs?

RSUs may become more attractive to employees and employers as a company moves closer to an IPO.

Late-stage private companies often compete for talent with public companies, where RSUs are commonly granted below the Director level.

Transitioning to RSUs shouldn't be taken lightly. There are significant differences in tax treatment compared to stock options.

- NSOs are generally taxed at the time of exercise.
- ISOs are generally taxed upon the sale of the shares.
- RSUs are generally taxed when they vest.

The IRS does not take shares for tax payments, so vesting illiquid stock can be counterproductive.

Companies may need to settle tax withholding with cash or consider granting double-trigger vested RSUs.

When is the right time to consider a liquidity program?

Private company liquidity programs provide cash liquidity to employees without them having to find their own buyers in a secondary market.

Sponsored liquidity programs involve the company providing the liquidity or allowing a third party to facilitate the transaction.

Liquidity programs can be implemented at different times, such as when early investors or employees request liquidity or a new round of financing is received.

A well-structured liquidity program can be a strategic move that demonstrates a company's commitment to creating shareholder value and managing its capital effectively.

We are running out of shares. Now what?

Equity compensation plan reserves can be replenished through funding rounds to attract new talent, replenish existing equity, and incentivize employees for milestones.

Companies should regularly review their share plans and consider increasing the pool if necessary to stay competitive.

Regulations and governance standards must be met before adding shares to the plan, including seeking shareholder approval and adhering to securities laws.

Upgrade, Please!

When to upgrade administrative solutions?

When is the right time to upgrade administrative solutions?

Public company equity compensation program administration is complex with increased regulatory compliance and disclosure.

Timing depends on complexity and risk. Often companies start to rally in this area 12–18 months in advance of IPO.

With a trend towards nontraditional lock-up provisions, private companies can no longer count on the lock-up as a haven to upgrade systems and staff.

Focus on selecting a provider with experience in managing restricted securities and in meeting the needs of established public companies.

What's an early lockup release?

A lock-up is a period after an IPO where employees are prohibited from selling shares to stabilize the stock price.

An early lockup release (ELR) can be negotiated by the company with its lead underwriter to allow employees to sell shares.

Approaching IPO:
Should an ESPP Be Part of Your Equity Strategy?

ESPP basics

- Most common way for public companies to share ownership on a broad basis.
- Broad based, voluntary plans, funded through payroll contributions to purchase stock on favorable terms
- Section 423 tax qualified and NQ plans
- Require shareholder approval. Generally easy as a public company. Even easier when closely held.
- Pre IPO approval can enable an evergreen provision and an IPO launch

ESPP prevalence

- ESPP interest is increasing, with 57% of companies offering [1]
- For IPOs since 2021, 44% have launched an ESPP, with others currently working towards launching ESPPs that were approved pre-IPO.[2]
- The most common ESPPs offer a 15% discount and a lookback pricing feature.
- NQ ESPPs can offer share or dollar match arrangements.

[1] 2024 Equity Incentives Design Survey, NASPP and Deloitte

[2] Fidelity Internal Data Analysis as of 8/2024 on 48 full administration clients that IPO'd since 1/2021.

ESPP design considerations

- Understand market practice and prevalence of ESPPs.
- Non-qualified ESPPs offer design flexibility and creative solutioning.
- Considerations such as automatic enrollment with opt out or change periods should be discussed with company counsel.
- Launching an ESPP in conjunction with IPO is a significant undertaking, and a lookback is generally considered most valuable.

Spotlight employee education and communication

Supporting employee needs

Understanding how registration and security restrictions may affect their ability to sell shares.

How/when RSUs that vest contingent on IPO are taxed.

How Incentive Stock Option holding periods work for preferential tax treatment.

Now what?

Managing and evolving equity compensation strategy and plans is significant and amplified by the activity at a private company driving towards IPO.

We hope this session provided helpful insights. Our whitepaper is also available as a reference when needed.

It’s a lot. We are here to help. We’ve ferried many others safely across what may feel like tumultuous waters.

We're here to support you!

Fidelity Private SharesSM is committed to supporting the startup and venture capital ecosystem. We help companies prepare for their next round of funding with our cap table management and data room platform and offer educational content, events, and opportunities for community connections.
No matter where you are in your journey – from idea to exit, and beyond – Fidelity has the solutions to support you.

FidelityPrivateShares.com

Founded in 2019, Infinite Equity is a leader in its field, providing professional advice and technology-enabled solutions that allow businesses to create and support a prosperous ownership culture. Infinite Equity is known for its success in assisting companies to increase the effectiveness and return of their equity programs, believing that equity compensation drives performance and fuels success. To learn more about Infinite Equity's employee ownership solutions visit

https://www.infiniteequity.com/