DESIGN YOUR ESPP FOR THE US AND THE WORLD

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Upcoming Events

- Webinar Series
  - All Things ESPP @ www.computershare.com/allthingsespp
  - All Things Equity Plans @ www.computershare.com/allthingsequityplans
- ESPP Day
  - November 8, 2018 in San Jose, CA
  - Sign up for alerts at www.computershare.com/esppday

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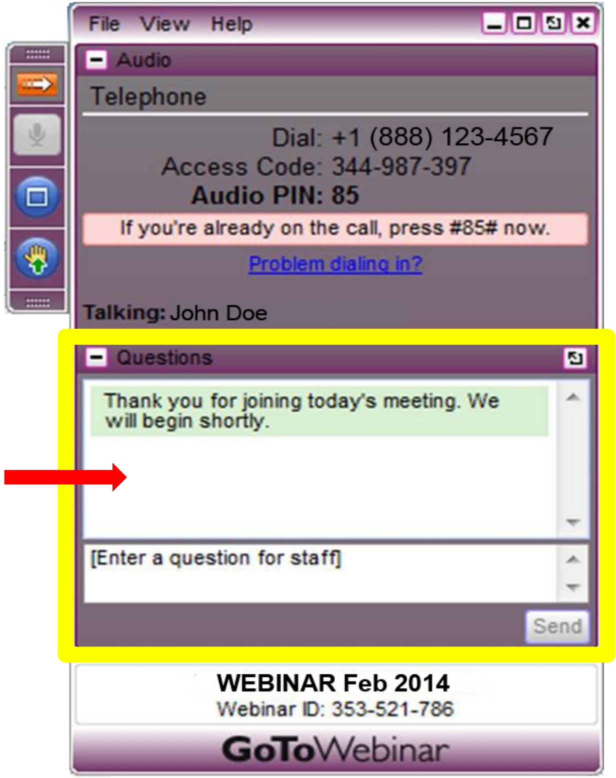

Housekeeping

- Presentation is being recorded
  - Email will be sent to all attendees with link to recording and presentation
- Presentation qualifies for one CEP credit
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Introductions

Barbara Klementz
Partner
Compensation
Baker McKenzie LLP

Barbara Klementz is the managing partner of Baker McKenzie's Los Angeles, Palo Alto and San Francisco offices in California. She is the chair of Baker McKenzie’s Compensation Sub Practice Group.

She has practiced in the area of global equity and executive compensation for seventeen years and currently serves on the Board of Directors of the Global Equity Organization.

Barbara has authored several articles on global equity issues for the BNA Executive Compensation Journal, Journal of Corporate Taxation and San Francisco and Los Angeles Daily Journal, among others, and she is the author of a blog on global equity related topics called the Global Equity Equation. She is also a frequent speaker on a variety of global equity topics.

Barbara has been recognized as a ranked practitioner by Chambers USA 2017. Chambers states that she "consistently delivers top-notch assistance and work product, and is a true expert in the field."

Barbara is admitted to private practice in California and Düsseldorf, Germany.

Introductions

Sinead Kelly
Partner
Compensation
Baker McKenzie LLP

Sinead Kelly is a partner in Baker McKenzie's Compensation practice in San Francisco. She advises on US executive compensation and global equity and has practiced in the compensation field for over 13 years.

In her practice, Sinead advises US and non-US public and private companies on all aspects of equity and executive compensation plans and arrangements, including plan design, administration, and global implementation, as well as compliance with US federal and state corporate, securities and tax laws, stock exchange rules, accounting rules, and non-US tax and regulatory requirements.

She has been recognized by Legal 500 as a leading lawyer for Executive Compensation and Employee Benefits and as "extremely knowledgeable."

She is a member of the State Bar of California and the Law Society of England and Wales. She has an LL.B. from Queen's University Belfast and an LL.M. from the University of California, Hastings College of the Law.

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Introductions

Robyn Shutak, CEP

Equity Advisory Services Practice Leader
Computershare

Robyn Shutak is a practice leader for Computershare's US Plan Managers business and has more than 15 years of comprehensive experience with employee equity programs.

In her current role, Robyn helps increase the company's brand awareness in the US, cultivate new and existing relationships through content development and additional services, and as a subject matter expert, helps support Computershare's products, events, and initiatives.

Prior to joining Computershare, Robyn worked as a Senior Director at the Global Equity Organization (GEO) .

Robyn is a Certified Equity Professional (CEP). She has served on the Certification Counsel of the CEP Institute and the Curriculum Committee and has been regularly recognized by the CEP Institute with Volunteer Excellence awards.

She holds a BA in English from San Diego State University and a Paralegal Certificate (with honors) from the ABA Paralegal Program at the University of San Diego.

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Employee Stock Purchase Plans

Barbara Klementz & Sinead Kelly, Baker McKenzie LLP
Robyn Shutak, CEP, Computershare

August 14, 2018

Overview of Employee Share Purchase Plans

- ESPPs allow employees to contribute money over a set period of time in order to purchase company stock, usually at a favorable price.

Phase	Action Steps
Enrollment	Participant enrolls in plan and chooses how much they will contribute.
Offering Period	Deductions taken from each pay check and set aside until the purchase
Purchase	Accumulated deductions over entire offering period are used to buy company stock
Hold or Sell	Participant can hold shares and collect dividends or sell shares to realize value

Typical Section 423 ESPP Design

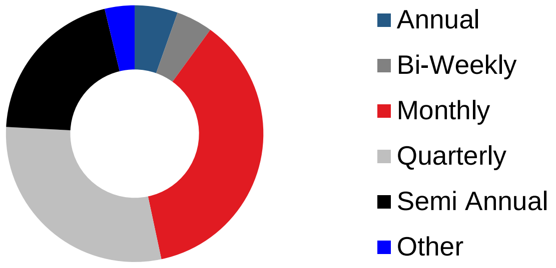
- Six-month purchase periods and/or offering periods of up to 24 months (often overlapping)
- 1-15% payroll deductions from employee's compensation
- 15% discount (with or without look-back feature); note 5% off market price at purchase is safe harbor (no compensatory expense)
- All employees of issuer and participating subsidiaries are eligible and have equal rights and privileges (but part-time/fixed-term employees and certain others may be excluded)
- $25,000 purchase limit for each year the option is outstanding (but can limit this to year is outstanding and exercisable)

ESPP Design Summary

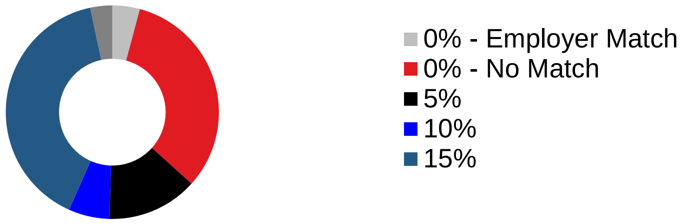
The plan design details of Computershare's data set is summarized below:

Plan Type

Length of Purchase Period



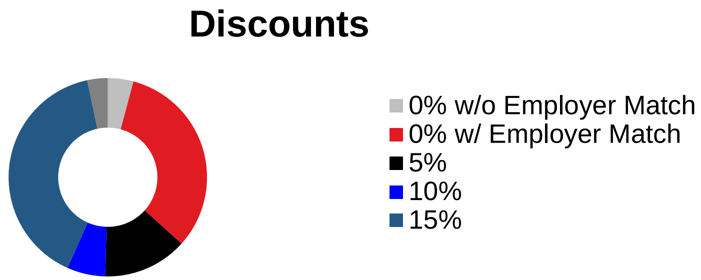
Discounts

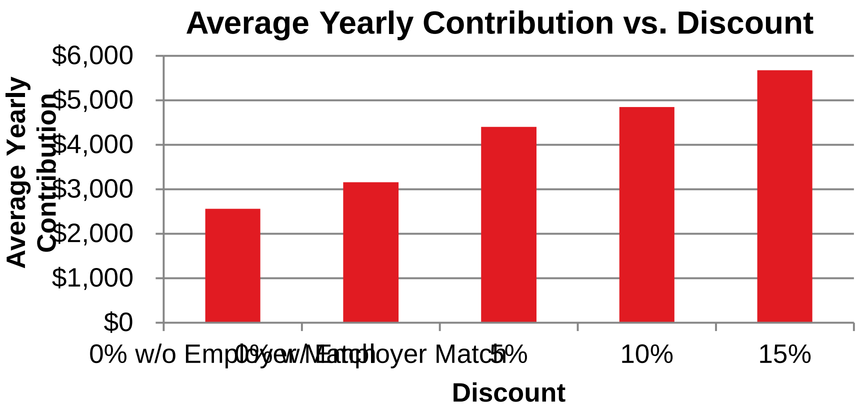


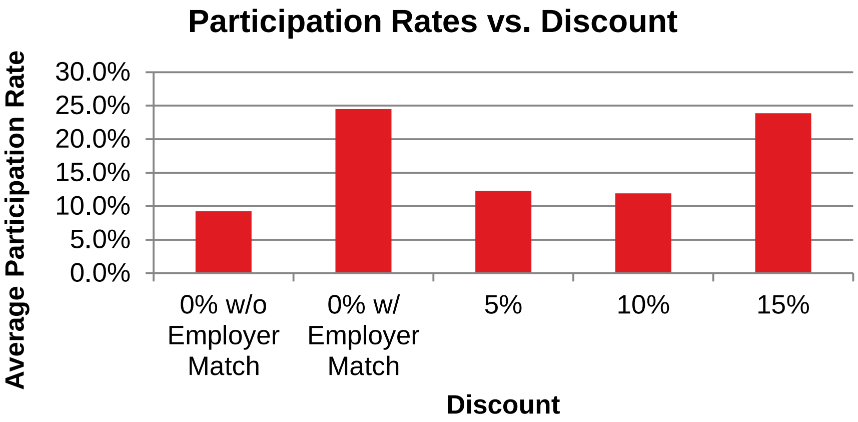
Look-Back

Discount

Larger discounts lead to higher contribution rates and participation rates

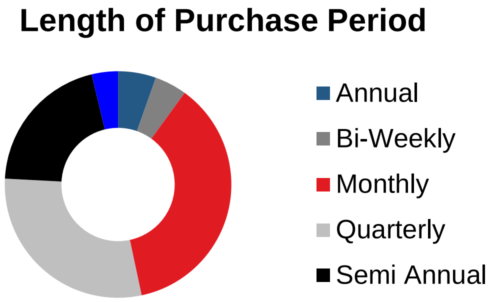


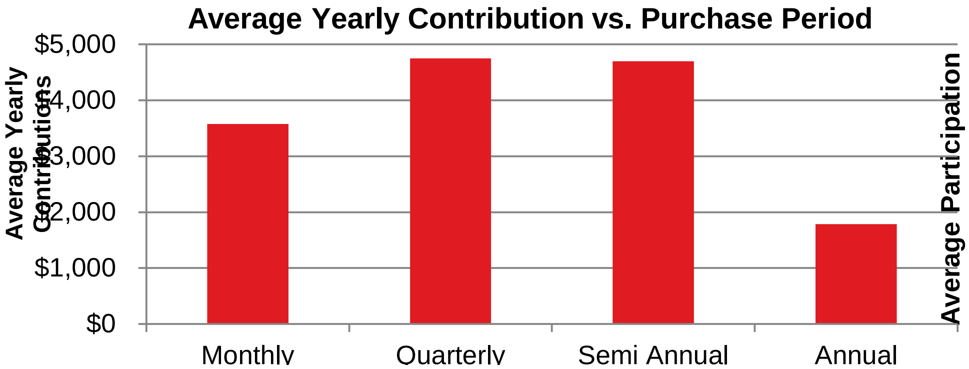


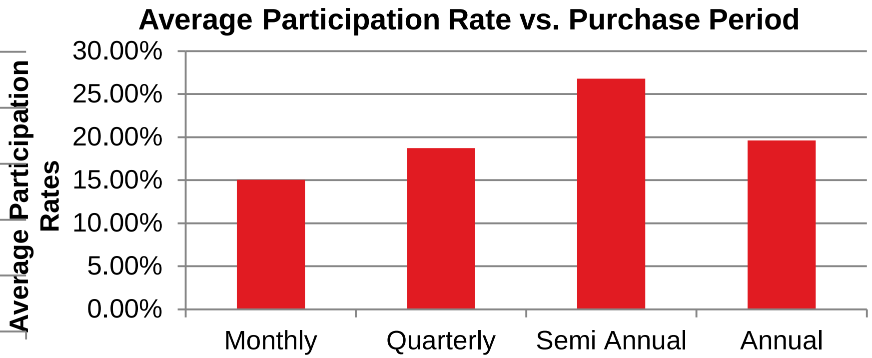


Length of Purchase Period

Longer purchase periods lead to higher contributions and participation up to a point (semi-annual), after which longer periods lead to lower contributions and participation



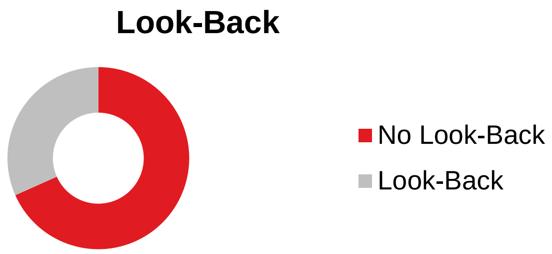


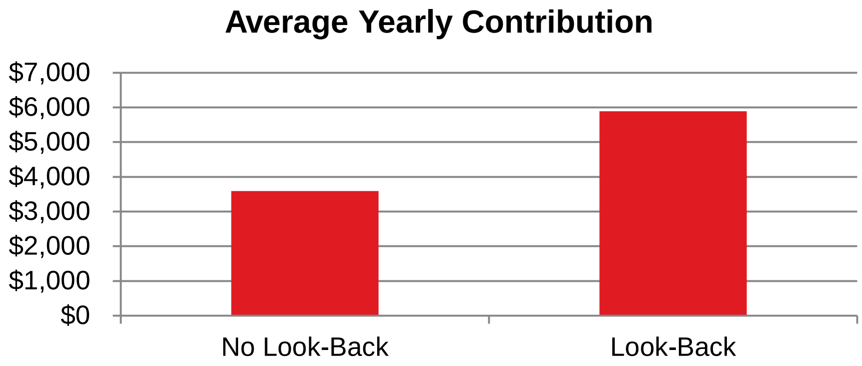


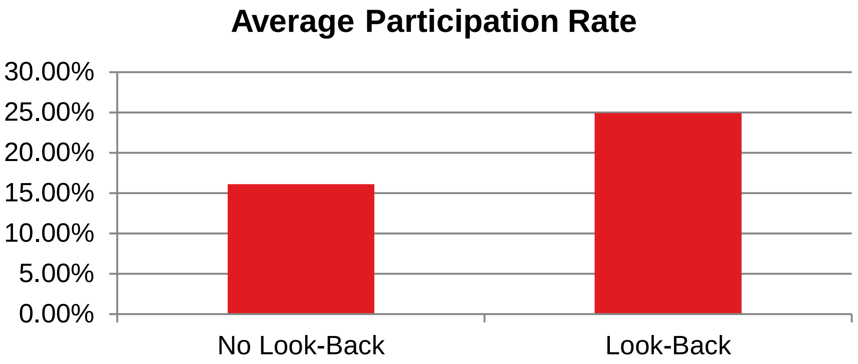
Look-Back

Approximately 32% of companies offer a plan with a Look-Back feature

Companies who offer plans with a Look-Back period see higher average contributions and participation rates

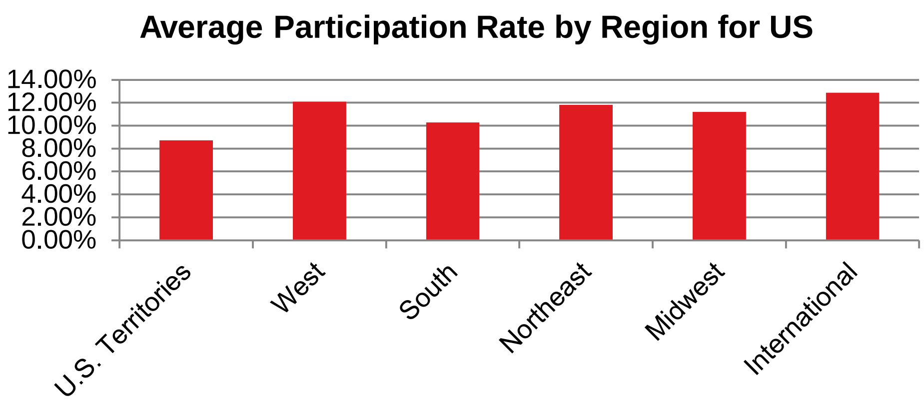


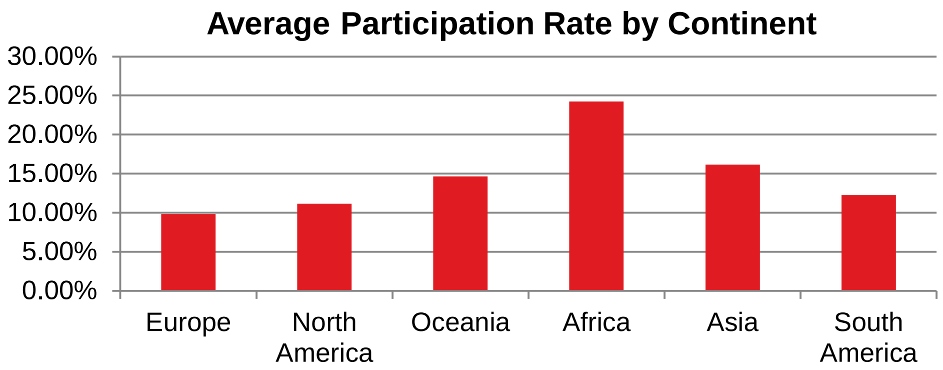




Weighted Average Participation Rate by Region & Continent

- The participation rate of eligible participants is fairly consistent throughout the US and Internationally
- The overall average participation across all Domiciles is 11.32%.
- Europe and North America have lower participation rates compared to the other continental regions across the world.





Additional ESPP Information

- 2017 ESPP Design and Participation Analysis (Computershare and Aon)
- ESPP Day: www.computershare.com/esppday

Session 1

ESPP

- General US and § 423 Challenges and Considerations

Excluding Eligible Employees

- <u>General rule</u>: All eligible employees of issuer and each participating subsidiary must be allowed to participate
- Certain employees may be excluded (*e.g.*, less than 2 years, part-time employees, highly compensated employees)
- ***Q****: Can you exclude union employees?*
- **Q:** *Can you exclude interns?*
- ***Q****: Can you exclude employees of a (US or non-US) branch of the issuer or a participating subsidiary?*
- ***Q****: What about employees who are excluded because of lost enrollment forms?*

Designating Participating Entities

- General rule: The board/committee must designate the subsidiaries which may participate in the ESPP
- Be mindful of corporate as well as tax structure of entities

- **Q:** *What are the consequences of not properly designating subsidiaries as participating subsidiaries?*

- **Q:** *Are automatic designations a good idea?*

- **Q:** *Can the authority to designate participating subsidiaries be delegated to an officer?*

Separate Offerings

- General rule: Under the “equal rights and privileges” requirement, all participants in an offering must participate on the same basis
- But separate legal entities may be designated as participating in separate offerings that may be subject to different terms

- **Q**: *Can you offer a discount of 15% for employees of a business unit based in California and 10% for employees of a business unit of the same subsidiary located in Nebraska?*

- **Q**: *What if the participants were employed by two different subsidiaries?*

Failure to Designate Participant Offering Maximum (1)

- General rule: To treat the first day of the offering as the "grant" date, you must designate a maximum number of shares that may be purchased by each participant in any offering

- Why is it important to treat the first day of the offering as the grant date?
  - To use a purchase price "look-back" -- the discount can be applied to the FMV on first date of the offering
  - The holding period starts on the grant date

- Otherwise, the purchase date is considered to be the grant date

Failure to Designate Participant Offering Maximum (2)

- **Participant Offering Limit Formulations**
  - Can designate a flat maximum number of shares that may be purchased by each participant – OR
  - Establish a formula that on the first day of the offering allows for the maximum number of shares to be purchased by each participant to be calculated
- Monitor to make sure that do not exceed limit – otherwise, purchase will be non-qualified (taxed at purchase)

Refunding ESPP Contributions Upon 401(k) Hardship

- General rule: A participant who takes a hardship withdrawal under a 401(k) plan may not contribute to any other plan of his or her employer for 6 months after the withdrawal (safe harbor rule)
- Note – 6 month suspension following hardship distribution is likely *optional* for 401(k) plan years starting after December 31, 2018 (Bipartisan Budget Act of 2018)

- **Q**: *Can company prohibit an ESPP participant from making further contributions if this prohibition is not contained in the ESPP?*
- **Q**: *Can the company force accrued contributions to be refunded preventing the participant from purchasing with the accrued contributions?*
- **Q**: *What if the refund requirement is included in the ESPP terms?*

Carry Over of Unused Payroll Contributions

- General rule: Cannot carry over unused payroll contributions that are not applied to the purchase of whole shares to a subsequent *offering* period
- If ESPP allows unused payroll contributions to carry over to the next offering period, it must allow other participants to make direct payment of an equal amount to avoid violating equal rights & privileges

- **Q**: *Can a fractional share amount be carried over?*

- **Q**: *Can a fractional share amount be cashed out?*

Reporting Dispositions

- General rule: Required to track both disqualifying and qualifying dispositions
  - Applies to current and former employees
- Without reporting, company is not entitled to corporate deduction for disqualifying disposition
- "Reasonable efforts" standard for qualifying dispositions?
- **Tracking methods**
  - Captive broker (required to hold shares with company-designated broker)
  - Require employees to notify company of sale
  - Survey employees (including former employees)

Insider Trading Violation Considerations

- General Rule: Purchases (or investments) in company securities are generally covered by (prohibited under) a company's insider trading policies

- **Q**: *Does enrolling in an ESPP involve an "investment election"?*
- **Q**: *Are participation changes considered investment elections?*
- **Q**: *What about purchases occurring during black-out periods?*

- Challenging for companies with extended black-out periods or employees exposed to non-public information on a regular basis
- Potential solution is to extend duration of enrollment period

Session 2

ESPP

- Non-US Challenges and Considerations

Equal Rights & Privileges Dilemma (1)

- Country-specific requirements may conflict with “typical” ESPP provisions and/or require different terms of offer than in US
  - ESPP may exclude part-time and fixed-term employees, but local law may require their participation
  - Payroll deductions may be illegal (under local law) or not feasible (*e.g.*, employees on leaves of absence who are not on payroll and who are permitted to participate in ESPP)
  - Local law may restrict amount of payroll deductions / percentage of salary that may be contributed to a lower amount than provided under ESPP

Equal Rights & Privileges Dilemma (2)

- Country-specific requirements (cont'd):
  - Payroll deductions may need to be segregated in separate bank account
  - Payment of interest on ESPP payroll deductions may be required
  - Holding periods may be beneficial in certain countries (*e.g.*, to obtain tax benefits)
  - Immediate sale requirements may need to be imposed to address securities or exchange control restrictions
  - Shorter offering periods may be desirable
    - Minimize exposure in countries with entitlement risks
    - Contain employer social contributions in countries with high rates

Equal Rights & Privileges Dilemma (3)

- Solutions for complying with "equal rights and privileges" requirement despite different country requirements and considerations
  - Exception for foreign residents if terms are required to comply with foreign law and are less favorable than for US residents (rarely applicable)
  - **Separate Offering (under 423 Plan)**
    - Allows different terms for different legal entities (but same terms must apply within offering)
  - **Non-423 Plan Component**
    - Allows exclusion of unwanted countries and different treatment of employees at same legal entity
    - Also, enables offers to employees at entities that do not meet parent or subsidiary definitions under Code Section 424

Omnibus Plan Structure

- Strongly recommended to set up ESPP as omnibus plan with 423 and non-423 component to ensure maximum flexibility for offerings outside the US (and to minimize risk for Section 423 qualification in the US)
- Easier to administer than:
  - US ESPP and International ESPP
  - US ESPP with non-423 sub-plans
- Can use same share reserve
- Complete one Form S-8 filing
- Entity designations to be reviewed for each offering to ensure properly designated as participating in respective component

Transfers from 423 Plan to Non-423 Plan

- Fact Pattern: During an offering period, an employee participating in a 423 component of an ESPP transfers employment from US parent to a subsidiary that participates in the non-423 component of the ESPP

- **Q**: *May the participant purchase shares on a qualified basis for US tax purposes?*

- **Q**: *Would it make a difference if the purchase occurs within 3 months of the transfer?*

Compliance/Tax Considerations

- **Review compliance requirements in each country**
  - Securities Laws
  - Exchange Controls
  - Labor Laws
- **Evaluate feasibility of offering ESPP in light of headcounts and compliance burdens**
  - Consider minimum headcount in country before ESPP is offered
- **Taxable event in most countries is at purchase**
  - Tax withholding / reporting and social insurance contributions may apply

Operational Considerations

- **Coordination with payroll for deductions**
  - Process for countries where payroll deductions not permitted
- **Conversion of funds from local currency to USD**
  - *e.g.*, Spot rate at purchase or average rate over purchase period?
- **Remittance of funds**
  - Intercompany transfers may not be permitted in all countries

Challenging Jurisdictions (1)

- **European Union**
  - Under EU Prospectus Directive, prospectus required for ESPP offers unless exemption or exclusion applies
    - Small Offering Exemption (less than 150 persons)
    - €5 million Exclusion (consideration paid for securities is less than €5 million in 12-month period – or such other threshold as of July 21, 2018)
    - Employee Share Plan Exemption (currently only available to companies with registered seat in EU or shares listed on EU-regulated exchange)
  - EU Prospectus Regulation (expected effectiveness July 21, 2019)
    - Employee Share Plan Exemption more broadly available
      - Requires short Information Statement to be provided to offerees

Challenging Jurisdictions (2)

- **China**
  - Exchange control (SAFE) requirements apply
    - ESPP must be registered with SAFE
    - Annual quota must be approved for outbound funds
    - All funds must flow between dedicated account in China and broker
    - Non-PRC nationals do not need to be included in SAFE registration (per local SAFE office practices), but may be difficult to get their funds in and out of China if not included

Challenging Jurisdictions (3)

- **Japan**
  - Securities registration requirements apply unless exemption applies
    - Small offering exemption (less than 50 persons, ¥10 million or less)
    - Employee share plan exemption (depends on corporate structure)
    - RSUs now considered a “parallel offering” and may require additional disclosure if filing is made for ESPP
- **Vietnam**
  - Previously, ESPP could not be offered due to exchange control requirements
    - Since 2016, ESPP can be offered but requires exchange control approval and compliance with various ongoing requirements
    - Few (if any) companies actually operating ESPP in Vietnam

Questions?

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