

## **What we have Here is a Failure to Communicate: Explaining Your Option Exchange to Your Employees**

The already challenging process of communicating about equity plans becomes even more difficult when your company decides to do an option exchange. Not only do you have to explain a challenging concept, but because most option exchanges are now considered Tender Offers, everything you communicate to your employees (written or verbal) must also be filed with the SEC. And yet, clear communication about your exchange is critical. The last thing you want is to spend all the money and effort implementing an exchange and end up with a low participation rate because employees didn't understand the value of the offer. This article summarizes just a few of the issues to keep in mind when communicating an exchange to your participants.

### **Legal Considerations**

As noted above, most option exchanges are considered a tender offer and are subject to Rule 13e-4 of the Exchange Act of 1934, which means – among other things – that for public companies all communications about the exchange must be filed with the SEC as part of your Schedule TO. In addition, your legal counsel will review all the communications before they are filed or distributed.

Why do option exchanges constitute tender offers? In most cases, the participant is being asked to make an investment decision. They are asked to “tender” one award in exchange for another with different terms (a different number of options or units, a different vesting schedule, etc.). Even if the exchange is a one-for-one exchange, if additional vesting or other changes to the terms are imposed, a tender offer is required.

Since your legal counsel has a great deal of say as to what is communicated and how it is communicated, bring them into the communication discussions early to get their input on methods and content. Avoid wasting time drafting documents or researching communication methods that legal doesn't feel are appropriate.

### **Which Communication Methods are Best?**

Which methods should you use to communicate with your employees about the exchange? Because of the Schedule TO requirements some of your regular communication approaches may be less practical for exchanges.

However, limiting your communication to (often lengthy and confusing) written documents may make it difficult for your employees to get the information they need about the exchange and make the right decision. We all know how likely we are to “read the manual” about new products we buy. The “manual” for your exchange is no different. So what other choices do you have?

Are phone calls permissible? Some legal counsels advise clients that no verbal communication be allowed to ensure that nothing outside the published text is communicated. But there are ways to make verbal communication acceptable as long as it is strictly controlled. Route your exchange “hot line” directly to a single individual, someone in legal or a senior stock plan manager who understands what may and may not be said to ensure that the message is consistent and “sticks to the script”. You may also want to consider using a recorded line, just in case any questions later arise.

Email communications for employee questions are an excellent alternative, since they are easily monitored and inexpensive to retain. We recommend that companies set up a special email address/inbox for your exchange, to easily track all incoming and outgoing messages (something such as exchange@demo.com). We also recommend any e-mail communications, no matter who they are signed by, are sent out of this e-mail box and replies are also directed there to strengthen your audit trail.

Both in-person employee meetings and live or recorded webcasts can work too. In these cases, you will need to file any slides and the transcript with the SEC.

Many of our clients have used a Tender Offer website, which requires a secure participant log in, to: distribute the communication materials; from PDFs to webcast recordings; collect elections; send commencement and reminder e-mails; and send confirmation e-mails after each participant election. A TO website can ease the administrative burden of an exchange, save time, reduce the risk of lost documents or elections, and improve your audit trail. Remember that you generally have only 20 business days to distribute materials and collect elections. If any materials must be distributed in hardcopy via interoffice or postal mail and then signed and returned in hardcopy, your participants have very little time to read and digest the information before they must make a decision. Obviously the problem is exacerbated when non-US locations and postal systems are involved. Even if a dedicated website is not feasible for your company, as long as your participants have e-mail and/or internet access, at least consider distributing your materials electronically to save time. If elections must be collected in hardcopy be very clear about the cutoff date, time and receipt location: "forms must be received in the office no later than midnight Pacific Time on June 15th" to minimize disputes about when forms were mailed.

A secure website also allows you to restrict who receives the information to just those eligible to participate in the exchange, limiting negative feelings about the exchange from non-participants. Though every communication is also filed with the SEC, participants who are not eligible seldom take the time to find and review the documents on the SEC website. We recommend that clients put the TO website site on the internet rather than the intranet so that participants can log on from home and review the decision with family members and print the documents to a private, rather than shared, printer.

### **Content of Communication**

As with other communications about your equity plans, you must be careful not to give advice. The communications cannot encourage participants to accept the offer. "Just the facts, Ma'am." Also try to ensure that your documents are in plain English, despite the legal tone that is required. It may sound obvious, but you'd be surprised how many companies fail to ask a third party, someone unfamiliar with options and exchange terminology, to read a draft of your documents and give feedback.

We recommend that you include a "projected payout" chart as part of your communication, showing what the payout would be at different price points of your stock if they accept the exchange as well as if they decline. Some legal groups do not allow this, saying that it treads too near the line of giving advice, but as long as the communication remains factual, your counsel may allow it and it really does seem to crystallize the impact of the exchange and reduce the number of questions you'll get.

A frequently-asked questions (FAQ) document is absolutely essential. We've helped clients with FAQs for many different projects and the content always varies greatly, due to differences in employee population, the structure of the exchange, the corporate culture, and the legal counsel involved. How do you compile the questions before the exchange has begun? Review sample documents on the NASPP website in the Underwater Options Portal and TO filings with the SEC to help design your FAQs. Also remember that amendments to Schedule TOs are common. No company we are aware of has managed to complete an option exchange without filing amendments to the schedule TO, so don't panic if you need to add a question to an FAQ after the offer has opened.

Be sure to include key dates for the exchange on all your communications in a large, bold font. And plan to send reminder communications as the date for the end of the offer draws near.

Customized communications are also crucial. Show the participant the before and after of the acceptance of the offer for their grants, grant-by-grant, don't rely on vague, generic descriptions of which grants will be eligible and how many shares will be issued if the offer is accepted. The election form (electronic or

paper) should also allow the participant to accept or reject the offer grant-by-grant. (Some companies have allowed participants to only exchange part of the outstanding shares of each grant, but we recommend against this as it makes communications more difficult with only limited benefit to the participants.)

### **Conclusion**

Communicating about exchanges is far from easy or straightforward, but taking the time and trouble to do it well will reap tangible results for your participants, your company and also ease the burden on the stock plans personnel.

Questions or comments? Please email us at [xtra@sos-team.com](mailto:xtra@sos-team.com)

### **About Stock & Option Solutions**

Stock & Option Solutions (SOS) has built a team of extremely qualified and dedicated professionals for the outsourced management or staffing of your stock plans and special projects. SOS's Stock Plan Outsourcing Solution is the most comprehensive outsourcing service in the marketplace, making the choice easy. Beyond our total outsourcing solutions, we are focused on helping companies like yours through challenging steps with temporary staffing, permanent placement, expert project resources, and high level project management. Call us today at 408.979.8700 to learn more or visit us online at [www.sos-team.com](http://www.sos-team.com).