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2019 Domestic Stock Plan Design Survey

Presented by The National Association of Stock Plan Professionals and Deloitte Consulting LLP

Executive Summary

Introduction and methodology

The 2019 Domestic Stock Plan Design Survey was developed jointly by the National Association of Stock Plan Professionals (NASPP) and Deloitte Consulting LLP (Deloitte Consulting) and administered from January 2019 to April 2019 by Deloitte Consulting using their online survey tool, DeloitteDex. Members of NASPP and Deloitte Consulting clients were invited to participate.

Last published in 2016, this survey provides an in-depth look at equity compensation design practices of companies primarily headquartered in the United States that provide stock-based compensation to employees within the United States (US). The survey on administrative and communication practices, including employee stock purchase plans, stock ownership guidelines, and insider trading compliance will be released in 2020.

The 2019 Domestic Stock Plan Design survey includes more than 200 questions covering five areas and is one of the most comprehensive of its kind:

- Participant profile
- Plan Design
- Time Based Full Value Awards
- Performance Plans
- Time Based Stock Options (SOs) and Stock Appreciation Rights (SARs)

Guidelines for this year's survey include:

- Participants must have completed at least two sections of the survey to be included in the report. Multiple responses from the same company were eliminated; each company is presented in the database only once.
- We received 425 responses during the survey period (January 2019 to April 2019).
- The total number of companies that responded to each question is presented.
- Due to rounding, the total percentage of companies may not add up to exactly 100 percent for some questions.
- For some of the questions, we report the data by industry group or other demographic data (for example, number of employees).

Customized cuts of the data

Deloitte Consulting will make special cuts of the results available for an additional fee. If you are interested in your own customized cut of the data, please contact Joseph Rapanotti at jrapannoti@deloitte.com or Tara Tays at ttays@deloitte.com

Highlights of the 2019 survey

Participant responses reflect the most recent trends in domestic stock plans offered by US companies surveyed. Survey respondents represent a wide variety of industries, US regions, and company sizes (by revenue, market capitalization, and number of employees). In this year's survey, 65 percent of respondents were non-high-tech companies and 35 percent were high-tech companies. The five largest industries represented in the survey were technology services (10 percent), durable goods manufacturing (9 percent), high technology manufacturing (9 percent), financial services (9 percent), and retail/wholesale (8 percent). The majority of survey participants are publicly traded companies (96 percent) and listed on the New York Stock Exchange (65 percent).

Nearly all (91 percent) of surveyed companies averaged less than 15 percent overhang in the past three years. Seventy-eight percent of surveyed companies averaged less than 2.5 percent burn rate for the past three years, which is consistent with the results collected in the 2016 survey.

Full value awards have continued to surpass stock options in prevalence. Looking at the types of awards granted to employees, 92 percent of companies grant time based restricted stock/unit awards and 85 percent grant performance awards, while only 54 percent grant time-based stock options.

At the CEO, CFO, and other named executive officer level, 81 percent of companies grant time-based restricted stock/unit awards, 84 percent grant performance awards, and 51 percent grant time-based stock options. However, for employees below the senior management level, the prevalence of performance awards decline sharply, while the prevalence of time-based restricted stock/unit awards remains higher for middle management and Other exempt employees.

For example, only 23 percent of companies grant performance awards to middle managers whereas 81 percent grant time-based restricted stock/unit awards. It is not common for grants of any type to be issued to nonexempt employees, but where companies do issue grants at this level, restricted stock/unit awards (19 percent of respondents) are more common than performance awards and stock options.

Due to continued shareholder scrutiny of executive compensation arrangements, a number of companies have adopted shareholder friendly policies. For example, 72 percent of companies surveyed report that equity grants are subject to clawback provisions, a 5.9 percent increase since the 2016 survey and 20 percent increase over the 2013 survey. For companies that have adopted a clawback policy, it is most common to limit the provision to the CEO, CFO, and other Section 16 officers. Despite clawback provisions in place, 90 percent of companies report never enforcing them in the past 5 years (82 percent of companies report they haven't had any violations that would trigger enforcement). For equity vesting in connection with a change-in-control transaction, approximately 66 percent of companies report a double-trigger requirement for unvested awards compared to roughly 20 percent of companies using a single-trigger requirement for performance awards and restricted stock/units.

New for 2019 was a question on whether respondents grant "make-whole" or "buy-out" equity grants to new hires. Of the companies surveyed, 35 percent do not offer make-whole or buy-out equity grants, and 48 percent offer them on an exception basis only.

Stock/unit awards

While restricted stock/units are the most common equity award granted to all employee levels regardless of industry (92 percent), restricted stock units are the most common form of time-based full value awards granted (84 percent of companies that grant full value awards).

The most common vesting is graded vesting, in which awards vest in equal increments (73 percent). The most common vesting period is three years (60 percent), followed by four years (29 percent). Similar to our 2016 survey, the majority of all or a portion of companies surveyed (72 percent) do not allow deferrals of restricted stock units. In other words, once restricted stock units ("RSUs") vest, they are settled in shares and award holders are not able to defer the right to recognize income on their awards. Of the 28 percent of companies that allow deferred payouts, 78 percent do not allow re-deferrals.

Slightly below two-thirds (64 percent) of respondents provide for automatic or discretionary vesting of restricted stock/units in the event of normal retirement, either in the form of accelerated or continued vesting. It is very common to allow restricted stock/units to vest in the event of a termination due to disability (76 percent) or death (80 percent).

Share withholding is the most common tax payment method: 91 percent of companies surveyed report this tax payment method is used for a majority of executive transactions, and 87 percent for a majority of non-executive transactions. Fifty-three percent of the companies surveyed report employees are not provided a choice in tax payment methods.

Among dividend-paying companies, 64 percent provide for dividend payments on restricted stock (15 percent report that payment of dividends is not addressed in their plan—these companies may also pay dividends on their restricted stock awards) and 78 percent for restricted stock units. Dividends paid on restricted stock are most commonly paid out concurrently with dividend payments to shareholders (49 percent). Dividends paid on restricted stock units are most commonly paid out when the underlying award is paid, either in cash or in additional stock (35 percent).

Performance-based awards

The prevalence of performance-based full value awards (performance shares, performance cash, and performance stock options/SARs) has slightly increased compared to the 2016 survey results: 85 percent (83 percent in 2016) of companies surveyed currently have a plan that provides for the grant of performance awards. Three years continues to be the most common length of the performance period, which is consistent with the 2016 and 2013 surveys. It is also common for companies to grant performance awards with overlapping performance periods as reported by 74 percent of respondents.

Sixty-eight percent of companies surveyed use two or more performance metrics to determine award payouts. This year, value metrics are the most common category of metrics used in performance plans (65 percent), consistent with 2016. Fifty-four percent of companies use total shareholder return, slightly up from 2016 and up 11 percentage points from 2013. Following total shareholder return, earnings per share (EPS) and revenue are the two most prevalent metrics used (25 percent and 24 percent of respondents, respectively).

Sixty-two percent of companies report using relative performance compared to a peer group or index, a 10 percentage point increase from the 2013 survey results but only a 2 percentage point increase from the 2016 survey. For companies that use relative performance, 68 percent utilize a custom peer group and 21 percent utilize an index.

Sixty-six percent of companies report using different performance measures in their long-term incentive plan than the measures used in their annual incentive plan. Twenty-two percent of companies report using a combination of metrics in their annual and long-term performance plans.

Seventy percent of respondents provide for automatic or discretionary vesting of all or a portion of performance awards in the event of normal retirement. However, in most cases (57 percent), performance awards are paid in full or on a pro rata basis at the end of the performance period based on actual performance. Eighty percent of respondents provide for automatic or discretionary vesting of all or a portion of performance awards due to disability and 85 percent due to death.

Stock options/Stock appreciation rights

The number of companies that grant service-based stock options or stock appreciation rights appears to have increased slightly from the last edition of the survey. From 2007 to 2013, the percentage of respondents granting stock options dropped from 96 percent to 68 percent, and then dropped again to 51 percent in 2016. The slight increase to 54 percent of respondents may indicate that the decline of stock options has halted.

Of the companies that continue to grant stock options, nonqualified stock options (NQSOs) remain the most prevalent form of stock options (91 percent). The most common form of vesting is graded vesting (93 percent), while the most common vesting period is three years (48 percent) or four years (44 percent). Ten years continues to be the most common option term (82 percent), which is 4 percentage points higher than the 2016 survey results and 15 percentage points higher than the 2013 survey results.

Over half (62 percent) of respondents provide for accelerated or continued vesting of all or a portion of stock options in the event of normal retirement, and 46 percent of respondents provide retirees with 12 months or longer to exercise their vested stock options, while 24 percent allow for the remaining term of the stock option. It is also common for vesting of stock options to be accelerated or continued upon disability (68 percent) or death (70 percent).

The Black-Scholes valuation model continues to be the most widely used model to determine stock option fair value under Accounting Standards Codification (ASC) Topic 718. Seventy-six percent of companies surveyed use historical stock prices to determine volatility, and daily stock prices (78 percent) continue to be the most common approach used to determine stock price volatility. These results are consistent with the 2016 and 2013 survey findings. To calculate the fair value of stock options, 36 percent of companies use third-party software, 27 percent use Excel spreadsheets (up 4 percentage points or 23 percent from 2016), 22 percent use an outside valuation consultant, and 11 percent use a third-party administrator.

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Section 2: Plan design

Overview of findings

1. **Performance awards are typically granted only to senior management and above.**
   - Senior management generally receive a mix of performance awards and time-vested stock/unit awards. At all other levels, time-based stock/unit awards are the most common type of award.
2. **The vast majority of organizations establish grant guidelines.**
   - Eighty-one percent of respondents have grant guidelines for determining plan eligibility, award size, and types of awards. The most common minimum criteria for participation are job level, compensation, and job group. Very few companies (no more than 11 percent) offer awards to all employees.
3. **Grant sizes may be based on either absolute or subjective criteria.**
   - The vast majority of respondents, 70 percent, do not have a minimum number of shares that are required to be granted. The number of shares granted are typically determined by job level, manager discretion, and/or individual performance.
4. **Competitive information, value, and costs influence stock grant guidelines the most.**
   - When setting grant guidelines, 85 percent of companies consider surveys and other market data to determine eligibility and award size. The value of the award is also a consideration, as noted by 63 percent of respondents.
5. **Most companies establish stock grant guidelines based on value not number of shares.**
   - Eighty-seven percent of respondents base stock grant guidelines on the value of shares/options, while only twenty-four percent use number of shares. Very few companies use percentage of outstanding shares to determine grant guidelines, consistent with findings in 2016. Similarly, sixty-five percent of respondents use the fair market value on the day of grant to determine value of shares/options.
6. **"Make whole" or "buy-out" equity grants for new hires are frequently used, but most often on an exception basis or above a certain level rather than for all employees.**
   - Sixty-five percent of respondents offer "make whole" or "buy-out" equity grants, but only 2 percent of respondents offer them for all employees. Most respondents that offer make-whole grants do so on an exception basis (48 percent) while 15 percent offer these grants only to employees over a certain level.
7. **One-half of respondents report less than 5 percent overhang.**
   - For 50 percent of respondents, average overhang during the past three fiscal years has been below 5 percent. For 17 percent of respondents, average overhang range from 5 percent to 7.49 percent, and for 11 percent of respondents reported overhang range from 7.5 percent to 9.99 percent.
8. **Over 75 percent of respondents have a three-year average burn rate below 2.49 percent.**
   - During the previous three fiscal years, 78 percent of respondents reported an average burn rate of less than 2.49 percent. Only 13 percent of respondents reported a three-year average burn rate of 4 percent or more.
9. **The trend in adopting a clawback provision continues to grow.**
   - The majority of survey respondents (72 percent) subject grants to a clawback forfeiture provision.
   - The provision is typically applied to senior management and above. However, 44 percent of survey respondents also noted that they apply a clawback to middle management, as well, with 29 percent applying the provision to Other exempt employees.
10. **Double trigger is the most common change of control provision.**
    - Upon change of control, the most common vesting acceleration provision is double trigger (employees' awards vest upon a change in control and termination of employment). Sixty-six percent of all respondents use double trigger, while single trigger is used by fewer than 20 percent of respondents. Approximately 13 percent of companies reported vesting is at the discretion of the board of directors or compensation committee, a 5 point reduction from 2016.
11. **Under double trigger provisions, upon a change in control, it is common for awards to be converted to time-based awards based on target or actual performance.**
    - Thirty-six percent of respondents reported that upon a change of control, unvested shares are converted to time-vested RSUs based on target performance, while 26 percent base the value on actual performance. Nine percent of respondents use the greater of the prior two determinations.
12. **Retirement eligibility typically requires attainment of both a defined minimum age and years of service.**
    - For options/stock awards to qualify for retirement vesting treatment, the majority of respondents (54 percent) require employees to meet both minimum age and years of service requirements. For those respondents that specify a minimum age, 50-55 years is the most common requirement (63 percent). For those that specify a minimum service requirement, 10 years is most common (48 percent).

Section 3: Time-based full value awards

Overview of findings

1. **Use of time-based stock/units grants remains high.**
   - The percentage of companies issuing stock/unit awards increased by 3 percent since our last survey (up from 89 percent in 2016 to 92 percent in 2019).
2. **Time-based stock/unit awards are the equity vehicle most frequently granted to all levels of employees below the middle management employees.**
   - Stock/unit awards are the most common equity vehicles granted to middle management and lower-level employees.
3. **Restricted stock units are the vehicle of choice among various types of time-based full-value awards.**
   - Respondents continued to shift away from restricted stock awards. Respondents reporting they grant restricted stock awards[1] dropped from 31 percent in 2016 to 26 percent in 2019.
4. **Awards are most commonly granted on an annual basis.**
   - The overwhelming majority of companies grant awards annually (ranging from 96 percent of respondents for CEOs, CFOs, and other named executives to 69 percent of respondents for nonexempt employees).
5. **Awards are typically approved at the board level, even for non-Section 16 officers.**
   - At a majority of respondents, grants of stock/units issued to non-Section 16 officers are approved at the board level, either by a committee of the board (68 percent) or the full board (6 percent). Twenty percent of respondents have delegated authority to approve non-Section 16 officer grants to the CEO.
6. **Accelerated or continued vesting is common in the event of retirement, disability, or death.**
   - Sixty percent of respondents provide for accelerated or continued vesting upon normal retirement, up from 58 percent in 2016. Acceleration or continuation of vesting is also common for terminations due to disability (72 percent of respondents) and death (76 percent).
   - Full acceleration of vesting is the predominant practice in both death and disability cases (59 percent and 47 percent of respondents, respectively).
7. **Dividend-paying companies pay dividends on restricted stock and unit awards, most often when the underlying award is paid out.**
   - For restricted stock, practices favor paying the dividends concurrently with those paid to shareholders (49 percent) followed paying dividends when the underlying award pays out 28 percent). For restricted stock units, 70 percent of respondents pay dividends out with the underlying award. These respondents are equally split between paying the dividends in cash or paying them in stock. Once awards have vested and have been paid out to employees, automatic enrollment in the reinvestment program is still limited; only 14 percent of respondents note that vested shares are automatically enrolled in the dividend reinvestment program.
8. **Share withholding is the predominant method of covering taxes on restricted stock/unit awards.**
   - Share withholding continues to be the most popular method of covering taxes due on restricted stock/unit awards, with a substantial majority of respondents reporting that this is the tax payment method used on more than 75 percent of award transactions. Sell-to-cover is a distant second, with just 25 percent of respondents reporting this tax payment method for over 75 percent of executive transactions (12 percent of respondents for non-executive transactions). For those companies that use share withholding, 81 percent round the shares withheld up to the nearest whole share and only 21 percent issue a Form 1099-B for the shares withheld.
9. **Deferral of restricted stock units is still not a common practice.**
   - Deferral of award payouts continues to be uncommon, with only 27 percent of respondents indicating a deferral feature is offered, down slightly from 33 percent in 2016.

[1] Awards not in lieu of cash.

Section 4: Performance plans

Overview of findings

1. **Performance shares are by far the most common type of performance-based award granted to named executive officers.**
   - Ninety-five percent of respondents granted performance shares, while 16 percent granted performance cash/units and 6 percent granted performance options/SARs.
2. **Three-year performance periods are typical, with overlapping performance cycles.**
   - Three years is the most common performance period among respondents. The majority of respondents (74 percent) have overlapping performance periods as performance awards are granted annually. For the majority of respondents (84 percent), additional years of service are not required after the performance condition has been met.
3. **Most companies use one or two performance metrics for performance-based awards.**
   - Awards are typically tied to one or two performance metrics: 46 percent of respondents use two metrics and 32 percent use one metric. Just over 20 percent use three or more metrics. Most respondents (66 percent, up 6 percent from 2016) use performance metrics that are not the same as those in the annual incentive plan, as a matter of good governance.
4. **Value metrics are the preferred category of performance metric, followed closely by revenue/profit metrics.**
   - Sixty-five percent of companies use value metrics, while 58 percent use revenue/profit metrics, 43 percent use return/margin metrics (compared with 33 percent in 2016), and 13 percent use strategic metrics.
5. **Total shareholder return ("TSR") is the most frequently used performance metric.**
   - Fifty-four percent of respondents utilize TSR to measure performance, while earnings per share and revenue are the next most commonly used metrics (25 percent and 24 percent, respectively). Over sixty percent percent of companies evaluate performance relative to a peer group and 79 percent of companies who use TSR apply a payout cap to awards. More than 80 percent of respondents pay out awards even if TSR is negative as long as the company outperformed its peers.
6. **Performance-based awards are typically tied to overall corporate performance as an incentive for delivering impact across the organization.**
   - The vast majority of respondents (90 percent) measure performance exclusively at the corporate level, with only three percent measuring at the division/sector level, and seven percent measuring a combination of division/sector performance and corporate performance.
7. **Continued vesting after retirement is common for performance awards.**
   - When performance award holders retire, close to 60 percent of respondents allow vesting to continue. Payouts to retirees are commonly pro-rated for time of service and achievement of performance. Vesting on either an accelerated or continued basis is also common for termination due to death or disability. Performance awards are typically forfeited for other types of termination events.

Section 5: Time-based Stock Options & Stock Appreciation Rights (SARs)

Overview of findings

1. **Use of stock options remains stable.**
   - The prevalence of stock options remains stable in our 2019 survey, with only 54 percent of respondents indicating that they have a plan that provides for the grant of options or SARs. This is consistent from 2016 and down from 100 percent in the pre-ASC 718 era (in the 2000 survey, all 345 respondents to the survey indicated they had an option plan and currently granted options).
2. **Broad usage of stock-settled SARs still has not materialized.**
   - Despite predictions of widespread usage of stock-settled SARs at the time FAS 123(R) (now ASC 718) was adopted, fifteen years later this practice has still not materialized: Only 7 percent of respondents that grant stock options/SARs do so in the form of SARs payable in stock. The majority of respondents that award stock options grant NQSOs, while only 17 percent grant ISOs.
3. **Annual vesting is most prevalent, although a small but notable percentage of tech companies have shifted to vesting with a one-year cliff and then monthly thereafter.**
   - The prevalence of graded vesting for options/SARs increased to 93 percent, up from 90 percent of respondents in the 2016 survey. For awards that are subject to graded vesting, three to four years are the most common vesting periods (46 percent and 45 percent, respectively). For respondents that use cliff vesting, three years is the most common period (75 percent of respondents). While annual vesting continues to be most common increment (82 percent of respondents, down from 83 percent in 2016), the survey indicates a small shift to a one-year cliff with monthly vesting thereafter among high-tech companies (22 percent of high-tech companies, up from 21 percent in 2016).
4. **The most frequently used option term is 10 years.**
   - Eighty-two percent of respondents who offer options utilize a term of 10 years; the next most frequent term length is 7 years at 12 percent.
5. **Option/SAR grants are most commonly issued on an annual frequency.**
   - The majority of companies that grant stock options and SARs do so on an annual basis (ranging from 93 percent of respondents for CEOs, CFOs, and other named executives to 83 percent of respondents for nonexempt employees).
6. **Grants are typically approved at the board level, even for non-Section 16 officers.**
   - At a majority of respondents, grants of options/SARs issued to non-Section 16 officers are approved at the board level, either by a committee of the board (67 percent) or the full board (6 percent). Twenty-one percent of respondents have delegated authority to approve non-Section 16 officer grants to the CEO.
7. **Continued reliance on third party software for fair-value calculation.**
   - The most common approach to determining the option fair value is still a third-party software (36 percent of respondents, up just slightly from 33 percent in 2016). The percentage of respondents that rely on an Excel spreadsheet to perform fair value option valuations rose to 27 percent (from 23 percent in 2016). Reliance on valuation consultants stayed about the same (22 percent, down from 25 percent in 2016). Most respondents (87 percent) use the Black-Scholes model to value service-based stock options.
8. **Accelerated or continued vesting is common in the event of retirement, disability, or death.**
   - Fifty-eight percent of respondents provide for automatic accelerated or continued vesting upon normal retirement, up from 56 percent in 2016. Full continued vesting is most common (29 percent of respondents), followed by full acceleration of vesting (15 percent). Acceleration or continuation of vesting for disability and death is also common for terminations due to disability (65 percent of respondents) and death (67 percent). Full acceleration of vesting is the predominant practice in both cases (48 percent and 56 percent respectively).
9. **Options are typically exercisable for three months following normal resignation, longer for other types of terminations.**
   - In the event of the normal resignation of an employee, 60 percent of respondents indicate that options are exercisable for three months (or 90 days), 12 percent indicate that options are exercisable for one month (30 days), and 11 percent indicate that options are immediately forfeited. In the event of normal retirement, 46 percent of respondents indicate that options are exercisable one year or longer and another 24 percent indicate that options are exercisable for their remaining term.

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