Global Shares

THE 6 MOST COMMON PITFALLS

of Stock Plan Management & How to **Avoid Them**

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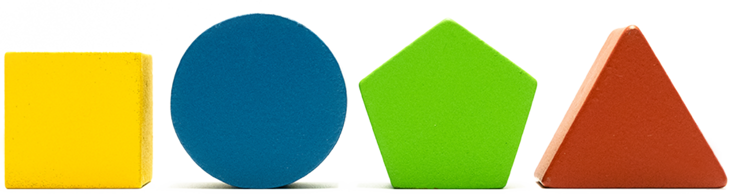


Introduction

The nature of business is such that you will have to adapt as new situations and opportunities arise. This could mean that people within your organization may find themselves stepping up, wearing different hats and performing tasks out of necessity and requirement, rather than due to any pre-existing skills or expertise.

Innovation is essential to meet new challenges and an abundance of passion and enthusiasm cannot be overlooked. Right from the early days in any business, through to when you're expanding, reaching into new markets, seeking fresh opportunities and even after becoming an established company, the need to make every dollar count, stretch and add value will inform a lot of decisions. This might mean that tasks which can potentially be performed inhouse, initially at least, generally will be. While your team will no doubt bring an eclectic blend of skills to the table, thereby ticking many of the necessary boxes, it may not be possible to cover all of the bases and as such there are bound to be knowledge gaps.

Versatility, of course, is absolutely essential in any successful business and a definite must if you want to thrive and survive. Equally an ability to acknowledge and identify where there are gaps, and to understand when it's best to bring in outside experts, is hugely important too.

Which brings us to the topic at hand – employee stock plans.

Creating and managing a stock plan will most likely not be within the wheelhouse of most people. While it might be possible to try and tackle it inhouse, maybe through keeping track of all relevant information on a spreadsheet, the more complicated a stock plan becomes the harder it will be to maintain 100% accurate information. The equity picture will become increasingly complex over time as staff inevitably join or leave the company, the administration burden will grow ever greater and the likelihood is that the plan itself will not be communicated effectively to employees, thereby diminishing the benefits to your company of even having such a plan in the first place.

This is just a flavor of the issues that can arise. There are many potential pitfalls associated with setting up and then managing an employee stock plan.

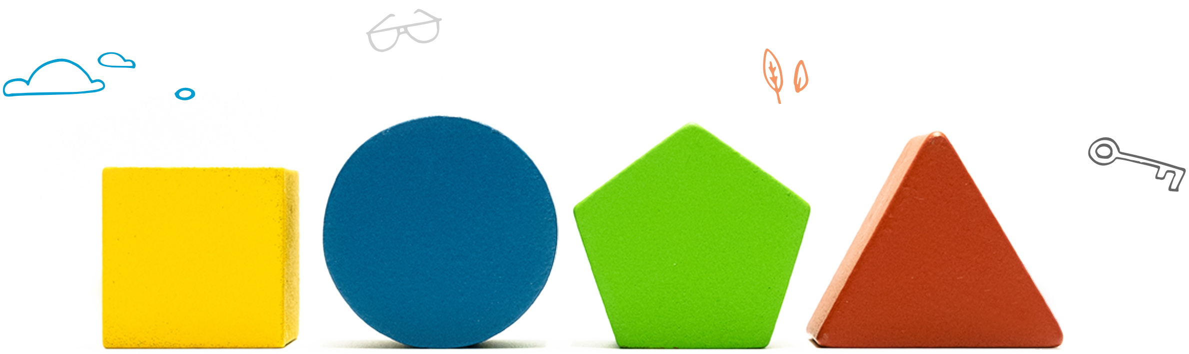
In this eBook, we will highlight some of the hurdles that can arise when a company decides to go it alone by setting up and managing its own stock plan:

- using spreadsheets,
- underestimating the administration burden,
- less than effective communication when trying to sell the plan to employees,
- not taking the time to understand the needs and priorities of your employees,
- not devoting sufficient thought to how to measure the success of the plan, and,
- not being sufficiently knowledgeable on the stock-related incentives available and the related regulatory obligations,

Some of these points are more problematic than others, but they share one thing in common – they are all avoidable. And at the risk of stating the obvious, the best way to deal with avoidable errors is to not make them in the first place.

Certain jobs require a definite skill set. Unless you're a trained electrician you're not going to tackle the rewiring of a premises yourself and if you do try it you're probably in line for a few shocks.

When it comes to setting up and then managing employee stock plans it's no different and the best way to avoid those potential pitfalls is to reach out to a stock plan specialist, like Global Shares, who can offer informed advice every step of the way, and, crucially, equip you with our award-winning software, which will allow you to be confident that the information at your fingertips will always be accurate, no matter how complex your stock incentive strategy may eventually become.



Pitfall 1

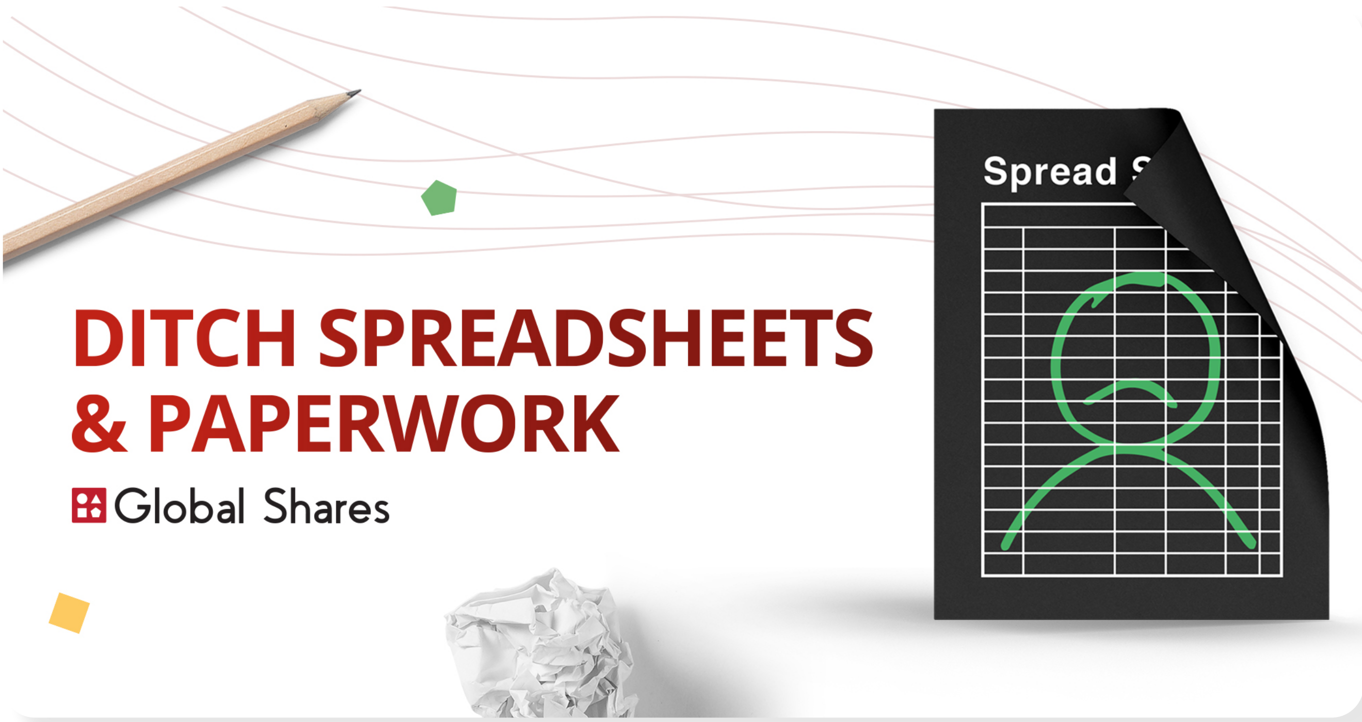
Spreadsheets & Stock Plans
- An accident waiting to happen

When you are launching your first employee stock plan, it might seem practical to manually input all relevant information on the participants and their awards into a spreadsheet.

Over time, though, the administration burden will become onerous. What seemed straightforward on day one will most likely become an increasingly complex, time consuming and convoluted task.

These inefficiencies aside a more serious issue is that relying on a manually updated spreadsheet to maintain what might be huge volumes of complex data is to risk inaccuracy. Not only does your stock plan data need to be accurate and up to date, you need to be confident that this is the case at all times. The more complex the plan, the harder it will be to guarantee that confidence if the data is managed through a spreadsheet.

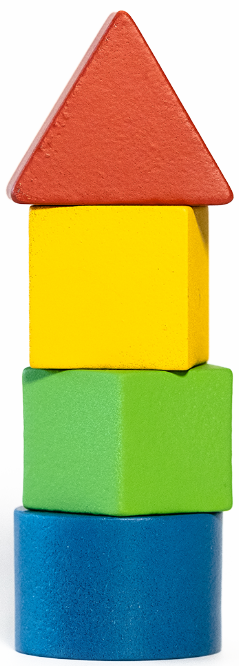
That snowball nearly always begins gathering pace from the company leadership. Committing to the ethos of employee ownership and demonstrating that commitment regularly is the only way to keep the ball rolling.



There are many reasons why it is unwise, bordering on reckless even, to maintain stock plan details this way, for example:

Human error

Manually maintained spreadsheets invite error. It is almost inevitable. With the best will in the world, one person staring at a sea of numbers on a screen is going to make a mistake at some point. This would be something to avoid in any circumstance, but the consequences can be grave when made in stock plan management. Errors can compound and create further inaccuracies meaning it can also prove quite difficult to track down that initial mistake.



Scalability

When there isn't a massive amount of information to keep track of, maintaining stock plan information on a spreadsheet might not seem like a misstep. However, over time, as your company grows, maintaining the specifics of your stock plan – or perhaps even multiple plans – will become more demanding as the document becomes more complex. You will need to constantly stay on top of stock plan changes arising from ongoing events such as issuing options, tracking vesting schedules, and categorizing multiple classes of shareholders. Attempting to do all of this on a continuous basis using a spreadsheet will eventually become problematic.

Version control

Spreadsheets are easy to copy and share.

This makes it likely that there may be multiple copies circulating among various personnel at any given moment, making it difficult to identify a "default" version. If, for example, three copies are bouncing around e-mail inboxes, it is possible that each might contain updates not saved in the others, thus creating an avoidable admin headache and undermining confidence in the reliability of a vital document.

Time and labor

Spreadsheets don't update automatically. That may not be a big deal on day one, but over the long haul it will create a massive amount of time-consuming work. Every relevant change will need to be manually logged – leavers, joiners, changes in share ownership etc. This brings with it the potential for human error, but even if it was possible to guarantee 100% accuracy at all times (and it isn't), you would still be left with an inefficient, time consuming process.

Once upon a time, spreadsheets represented the cutting edge of data organization technology, but those days are long behind us. Now we can do better. Global Shares offers an automated software solution that will enable you to neutralize all of the negatives associated with attempting to stay on top of all vital plan-related information using a spreadsheet.

Pitfall 2
Underestimating the administration burden

Whatever the size of your business, getting an employee stock plan up and running is only part of the battle. No matter how much time and effort are involved in reaching that point, there will be little opportunity for you and your team to pat each other on the back and clink glasses. Once your stock plan has been formally launched and initial options and/or stock has been awarded to participants – depending upon what type of plan you have decided best suits your interests and those of your employees – you will soon find yourself moving into the ongoing administration phase.

Doing it yourself is not going to save you time in the long run.

Essentially, choosing a plan and effectively selling it to your target audience – whether all employees or just senior executives – represents one challenge, while the job of maintaining it represents another. This will also involve considerable time and effort, as you will need to carefully maintain any stock plan for as long as it exists.

The information in your stock plan will be constantly changing so it's easy to imagine how this might prove problematic over time, particularly if you are managing your stock plan inhouse and on a spreadsheet.

Firstly, the effort involved in making the necessary updates can come to resemble an ongoing firefight. Merely ensuring that the flames are kept down might come to be regarded as success, but it shouldn't be a surprise to hear that this is not the best long-term strategy. Aside from anything else, the challenge of merely keeping up with updates, let alone simultaneously managing to avoid errors, will become so time consuming as to prevent you from taking a step back and assessing how well your plan is actually performing relative to whatever your competitors may be doing.

If you decide to handle this work inhouse, the admin burden will most likely fall to HR personnel whose plate will already be near to over-flowing, which is when issues with errors and oversights can creep in, with potentially serious negative consequences.

And it's not just about keeping track of what changes occur – it's also about understanding prior to launch what needs to be done and keeping track of those points over time. For example, you'll need to ensure that a proper vesting schedule is in place on day one and then keep track of that. So whether it is cliff or graded, you must implement the vesting schedule as specified at the outset as participants need to know that the vesting process will proceed along specified lines. If you are using graded vesting, any administrative oversights can be very damaging to the credibility of the plan in the eyes of your employees. Remember, one of the purposes of your plan in the first place will be to encourage retention, but if participants have a negative experience in a cliff vesting scenario, then they might become less likely to stick around for the full term of the plan.

And if any of that confused you or didn't make sense then that's why you need to seek professional help with your stock plan.

If relying on manual processes amounts to doing it the hard way, then embracing a more streamlined solution represents the easy way. In fact, when you move away from manually updating spreadsheets and go with an automated method you not only eliminate the admin burden, but you reduce the potential for human error and the chances of mistakes creeping in, as the dedicated software involved handles those day-to-day admin-related tasks and issues.

The Global Shares stock plan management platform can provide you with that solution. This automated software can handle all types of grants, awards, and plans, whether for a small group of senior executives or all employees. This fully automated software is configured to the client's needs and therefore gives you peace of mind, while also reducing your workload and costs.

Pitfall 3

Not selling the plan to your employees as well as you could

So you've done your research and eventually settle on a stock plan that you believe best meets the needs of both the company and its employees. So far so good. But then comes a potentially difficult challenge – selling that plan to your employees and convincing them that it is in their interests to sign up and become participants.

You and those around you may know the key elements of what is being proposed and why it will benefit your employees, but failing to transmit that information to your target audience can undermine what you are trying to accomplish even before one piece of stock or a single option has been assigned.

Communication is key. More specifically, effective communication can be the difference between your employee stock plan securing the level of participation you want or failing to connect with the target audience.

Your communications strategy needs to be carefully thought out and pitched in a way that will allow employees to highlight the benefits of what is being proposed, hitting that sweet spot between not providing enough information and potentially overwhelming them with unnecessary facts and details, with either extreme likely to hinder understanding.

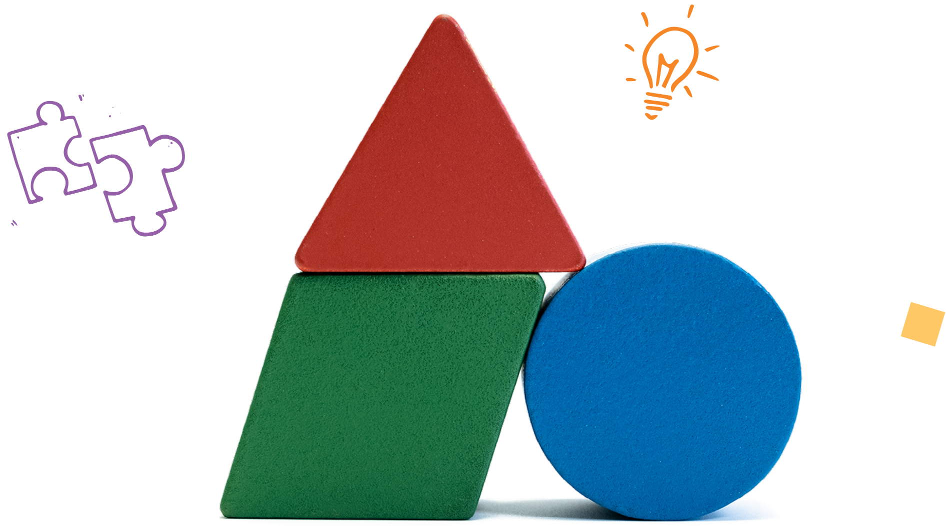
Depending upon the industry in which a given company operates, the concept of stock options and why they are attractive may be alien to at least part of your workforce. So, at the start of the communications process, some or even many of your target audience may not fully understand what is being proposed and why they should be interested. And if prospective participants do not understand the proposition, they will be less likely to sign up to the plan.

Remember, you only get one chance to make a good first impression. If your message or how you deliver that message isn't clear or doesn't land with your employees, you will either be left needing to recover the situation or see your plan fail to take off.
This is another example of a task that a company might decide to keep inhouse, but if your team doesn't possess sufficient experience or expertise, then potentially costly mistakes may be made.

In essence, you need to know who you are talking to, what their needs are, how to calibrate your message to appeal to those needs, and also how to communicate that message. It most likely won't be a one-size-fits-all solution, and failure to recognize that may stymie your efforts to get your stock plan off the ground. The content and delivery of your pitch should be different when looking to reach different audiences, such as senior executives or factory floor workers. While e-mail communications and online presentations might prove effective with senior executives, postering in warehouses and in-the-flesh meetings might be necessary with factory workers.

There is more to think about than first glance might suggest, which is why experience in this area is so important. Better to work with professionals who have been down this track before than to acquire that experience yourself the hard way.

At Global Shares, we have the necessary experience. Our dedicated team know what is involved in designing a communications strategy geared towards you achieving your goal – maximizing participation in your stock plan.



Pitfall 4

Not being plugged in to the needs of your target audience

This is somewhat related to the previous point on communication, but sufficiently distinct as to merit being dealt with under its own heading.

The key point here being don't make the mistake of losing sight of your audience.

There is no point looking around at what stock plans you might consider introducing in your company without already having the basic demographics of your potential participants in mind.

Is it an incentive plan for senior executives only? Or do you want to introduce an offering with most or all of your workforce in mind? These are key questions. And even when you answer them, you must then avoid the potential pitfall of allowing yourself to focus too much on the needs of the company. Any plan should have significant upsides for both the company and employees, because if it ultimately proves to be a hard sell with potential participants, then it won't matter how much it may suit the company's sense of its own needs. A plan which doesn't resonate with the target audience will not succeed in achieving your goals, which presumably will be around recruitment, retention, and improved worker performance.

For example, if you are debating the merits of plans centered around stock awards or focused on the granting of options, the composition of your workforce should be one of the factors that informs your decision-making process, and the failure to do so could ultimately undermine your efforts.

At the outset, among the points to consider on this front will be the age profile of your workforce and also their knowledge of stock plans, as you may need to educate them on the benefits of stock ownership at the outset?

If your employees are not knowledgeable about the world of stocks then your communications strategy will need to be designed with this in mind. Assumed knowledge can be a pitfall in business, but it may be fatal when looking to sell a stock plan to employees if a significant proportion of that audience have had little exposure to or reason to think about such matters previously.

If you are looking at introducing a plan for all or most employees and that target population isn't particularly "stock literate", then direct stock awards might prove to be an easier sell than an options plan, even if the terms offered with the latter are particularly generous. Why? The idea of being given stock is more straightforward than being presented the opportunity to purchase stock in the future at an agreed price which may or may not lead to making a substantial profit. The idea of receiving a direct award now feels tangible and more real than a hypothetical "if this, then that, at point X" scenario. Options aren't complicated when you understand them but can seem mysterious and arcane when you don't. Failing to bear this in mind when devising your employee stock plan strategy could backfire on you.

Similarly, if you have a multi-generational workforce, that too needs to be borne in mind. So, if you are looking to introduce a plan revolving around offering employees stock at a discounted rate, building up the purchase pot based on payroll deductions over a number of years, that may or may not prove attractive, depending upon the age profile of your workforce. Young employees often don't have a lot of disposal income and may not be swayed by the prospect of financial benefits down the line if that means losing even a small chunk of their salary in the here and now. Alternatively, if your workforce skews older, those individuals may be looking toward retirement and may be disinterested in signing on to long-term plans.

The point in raising all of the above is to highlight how much thinking needs to go into the process of selecting the type of plan you want to establish and then looking to secure participants for an employee stock plan. When you haven't been down this road before, it is possible you will underestimate what is required to get to where you want to go.

Better to go with dedicated professionals, like Global Shares, who have been down this path multiple times rather than going it alone and risking making avoidable mistakes and then having to deal with whatever headaches come from that.

Pitfall 5

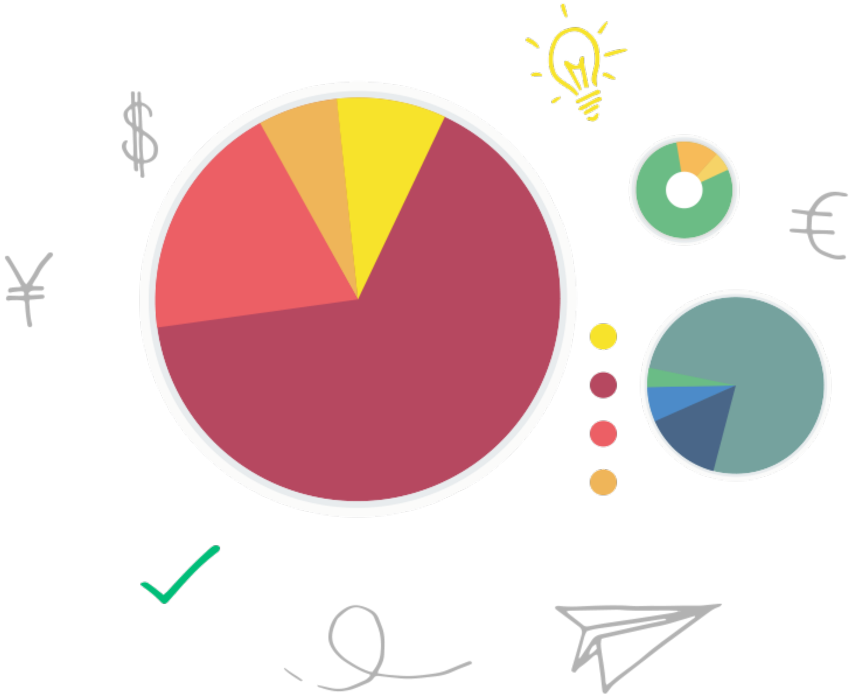
Not knowing what success looks like

Deciding to embrace the principle of employee ownership for your company is a landmark moment, but it is merely one step on a journey rather than an end in itself and there will be many questions you must ask and answer before committing to a definitive strategy. Not least, you need to be clear on what you want to achieve from your stock plan. Who are you targeting? What will success look like? How do you measure that success? And all this even before a single participant has signed up.

The answers to questions such as these will guide you towards the plan that will be the best fit for you and your employees, and if you do not take the time to properly address these questions prior to establishing that plan, then, at the very least, you will hinder the ability of your business to maximize the benefits that can arise from it.

We cannot over-emphasize the importance of being able to assess the impact of your plan once it is up and running. As with so much else we've highlighted here, trying to figure it out as you go might work but a point will come when you are going to be relying more on good luck than solid planning – and fortune tends to favor those who take the time to fully prepare.

How you measure the success of your plan will, of course, be influenced by what you hope to achieve with it. Typical objectives include improving employee engagement and seeing greater retention rates.



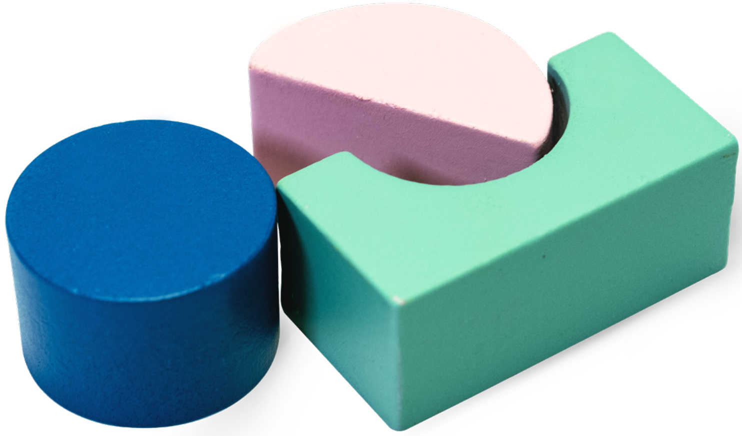
If those are your objectives, then, even before your stock plan is put in place, you need to consider how to measure its performance on those key metrics.

Assessing how successful your stock plan is in terms of employee retention is relatively straightforward. If you see reduced staff turnover rates among participants over time, then it is reasonable to conclude that your stock plan is encouraging those individuals to stick with the company.

However, it can be a little trickier to measure changes in employee engagement. Among the ways you could consider are:

Track absenteeism: Everyone gets sick and misses work at one time or another, but absenteeism rates across the board can offer a glimpse into the general mood and disposition of a workforce. So, for example, if absenteeism rates in a company are higher than they “should” be over a calendar year, then that may point to an issue with morale and engagement.

Comparing absenteeism rates before and after the introduction of an employee stock plan may offer up interesting results. If the plan has the desired effect, it will make participants more invested in the business, they will draw a firm connection between their own efforts and the success of the company, and, in turn, this should impact positively on both motivation and engagement.



While this won't eliminate absenteeism – people will still get sick, after all – it should help to minimize days lost where absences are due more to poor morale and a lack of engagement than actual sickness.

And most importantly it's measurable.

KPI performance: Related to the above, if your stock plan helps to make participants more motivated and engaged, it stands to reason that this will also lead to improved performance on the job.

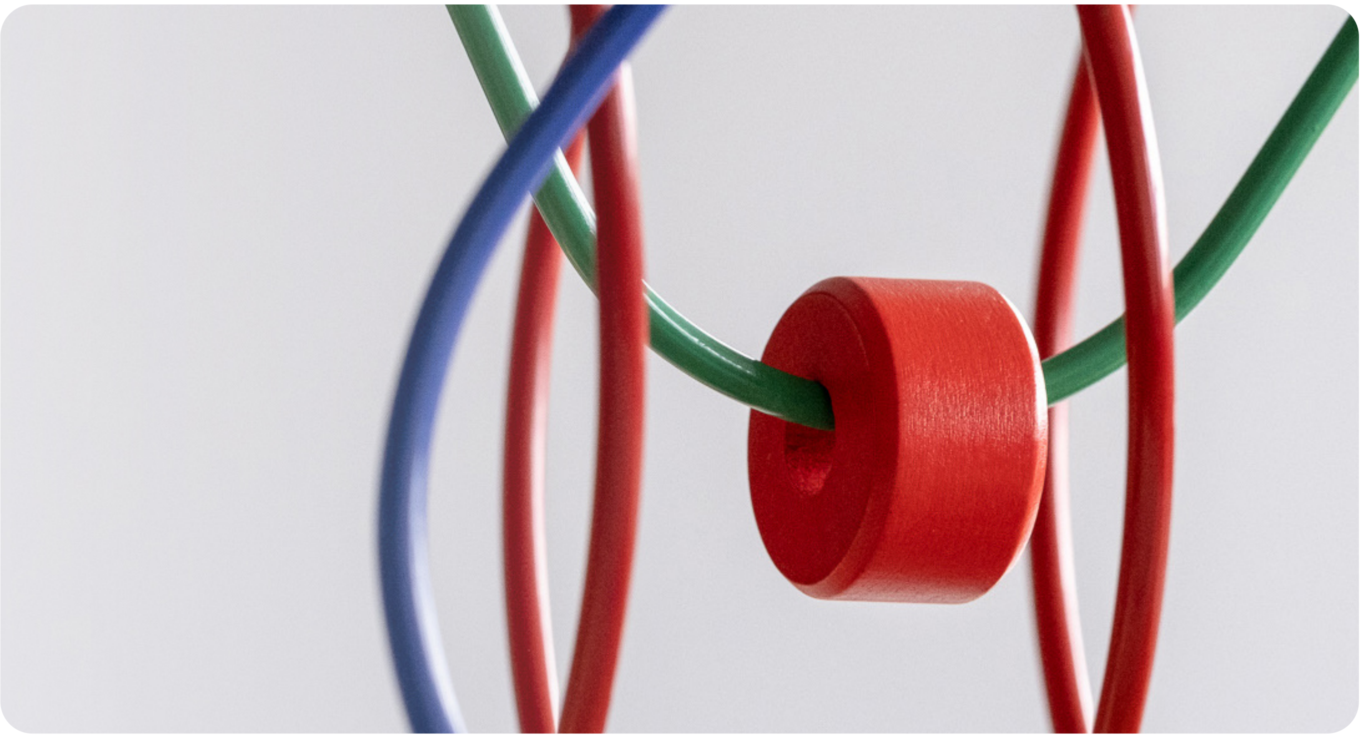
So, as well as measuring absenteeism rates over time, you can also look at how plan participants are faring on their KPIs, and ideally be able to compare their performance with that of co-workers who did not sign up.

Depending upon the industry, KPIs will look very different, but you will hopefully be able to see a noticeable improvement over time among plan participants. If you are able to detect such a pattern and also find lower rates of absenteeism among those employees, then these two data points would offer compelling testimony towards the success of your stock plan.

To reiterate a point made elsewhere in this eBook, know-how and experience can make a difference when faced with this issue. Being able to reliably measure success is vital, and rather than having to figure it out inhouse, you can save a lot of time and effort by reaching out to potential partners with the experience and expertise to advise you at every step along the way, including this one. Global Shares can be that partner for you, offering you the benefit of our passion for employee stock plans and a track record in assisting companies like yours on their own journeys.

Pitfall 6

Not being sufficiently aware of stock-related issues



All the stumbling blocks and potential issues raised in this eBook point to the need for know-how and pre-planning when it comes to selecting, launching, and then assessing the effectiveness of your employee stock plan.

But perhaps the area where experience and expertise are most needed relates to the stock itself, where serious errors, once made, can be extremely difficult to recover from.

Recognize that not all stock-based incentives are the same: This might sound obvious, but it is important to be clear on the type of stock you are using. There are many different options that can be offered, and each will need to be handled in its own distinct ways.

The most common types of stock issued are incentive stock options (ISOs), non-qualified stock options (NSOs), or restricted stock units (RSUs), and they differ depending on who they are designed for and how and when taxes are paid.

For example, ISOs are for employees, whereas NSOs can be issued not only to employees, but also to directors, consultants, advisors, and contractors.

ISOs tend to be more popular with employees due to the possibility of receiving more favorable tax treatment. Assuming specified vesting schedules are adhered to, tax is deferred until stock is sold, and even then participants will only pay capital gains tax. With NSOs, on the other hand, tax falls due both at the point that options are exercised and when stock is sold.

RSUs meanwhile are regarded as being most suitable for established companies, as opposed to startups. With ISOs and NSOs participants receive options, while with RSUs individuals are given stock, but with conditions attached, e.g., vesting linked to staying with the company for a specified period of time and/or achieving performance goals. RSUs can be popular with employees because there is less risk attached to them and the process is straightforward, i.e. achieve the specified goals and/or stay with the company for X years and then the agreed amount of stock is released to the participant.

You will either need to be clear on the differences between the various types of stock or else work with an outside partner who has expert knowledge in the area and the ability to guide you and frame the information in the context of what you want to achieve with your employee stock plan before you will be able to make an informed decision on whether ISOs, NSOs, or RSUs best suit your needs.

Be aware of your exercise price obligations: It is important to be aware of the process around which you will set the strike price for options assigned under the terms of your plan. There are legal obligations involved and any mistakes made could expose you and your employees to tax penalties.

As a private company, you are obliged to get a 409A valuation and let that guide you towards a fair market value (FMV) for your common stock. One way to go about getting that valuation is to enlist the services of a third-party appraiser. Once the FMV has been formally determined, it creates a boundary for the strike price, meaning it is not permissible to set the price below that level. If you were to do so, you could be exposing your plan's participants to potential penalties.

Also, it is important to note that securing a 409A valuation is not a one-off obligation. As long as you are granting options you will need to have your stock valued approximately every 12 months, to ensure that your strike price continues to be in synch with FMV.

These are merely two of the stock-related factors that require knowledge and expertise to be handled effectively. Missteps can prove particularly costly, so attempting to handle all of this inhouse if you are not fully equipped to do so constitutes an unnecessary risk.

As with all other potential pitfalls detailed in this eBook, problems on this front are entirely avoidable. The best way forward for you and your business is clear – partner with a third-party company with a proven track record in assisting clients in creating, implementing, and maintaining successful employee stock plans. Global Shares can be that partner for you.

Conclusion

This eBook has highlighted a number of potential pitfalls that can complicate or even derail the process of setting up and the ongoing overseeing of your employee stock plan.

- Choosing to rely on spreadsheets and therefore risking human error and inefficiency.
- Underestimating the admin burden involved.
- Not devoting enough attention to selling the plan effectively to your employees.
- Not recognizing the needs and priorities of your employees.
- Not giving enough thought to how you will go about measuring the success of your plan.
- Not recognizing the range of different stock-related incentives that exist and related regulatory obligations.

While the extent of the potential negative implications associated with each of the above will vary, they share one common point – whatever problems can arise are entirely avoidable.

When you choose to engage with an outside specialist you are also investing in peace of mind.

Global Shares specializes in working with companies at all stages of setting up and then maintaining employee stock plans so you can be confident that when you partner with us, you get the benefit of our years of experience and expertise.

Our automated software is designed by experts who understand stock plan administration and work to ensure that the final product is user-friendly for both administrators and participants. Using this software removes the human error element which is always present when you rely on manual inputs to spreadsheets. It will also save you on time and labor.

The net effect is that plan administrators know their plan is being managed by safe hands and they can monitor transactions and run reports as required, while participants get to enjoy a personalized portal experience that simplifies the process, enabling them to track and engage with their shareholding with minimum fuss.

Global Shares

Employee Ownership, Simplified.

Contact Global Shares now for more information on how best to move ahead with your employee stock plan.

Get in touch

www.globalshares.com