TELLING THE EQUITY STORY

SPEAKERS

Ashish Raina

Founder @ Optimize Talent

ashish@optimizetalent.com

Luke Beseda

VP, Talent @ LSVP

luke@lsvp.com

AGENDA

KEYS TO TELLING THE EQUITY STORY

Fundamentals

- Candidate Motivators
- Common terms
- Offer Structures

Delivering Offers

- Recommendations on positioning offer packages
- Selling against competing offers (the Ubers and Googles)

Offer Process

How to effectively engage and close candidates starting from the very first conversation through startdate

Templates

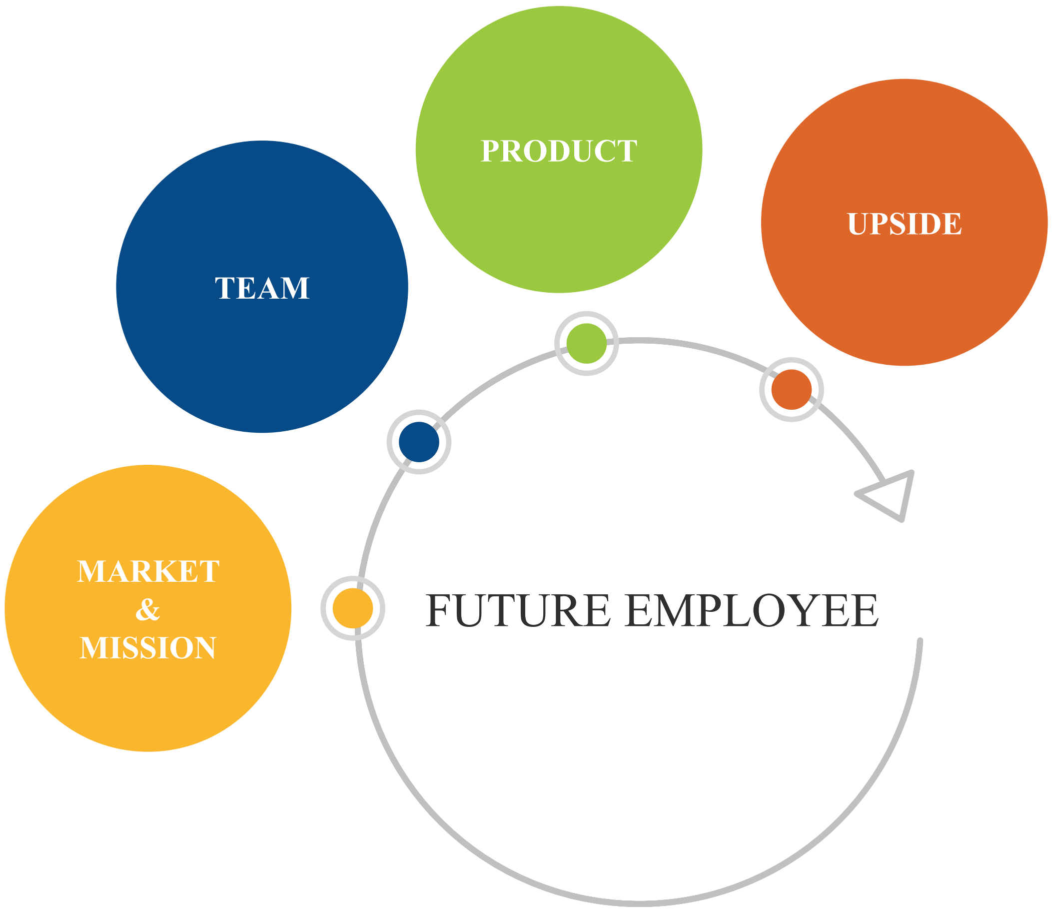
- Excel model to share with candidates.
- This will highlight potential earnings compared to similar companies

DISCUSSION

What are the top 3 challenges you face when negotiating compensation with a candidate?

CANDIDATE MOTIVATORS

There are 4 main categories candidates consider when deciding on an offer

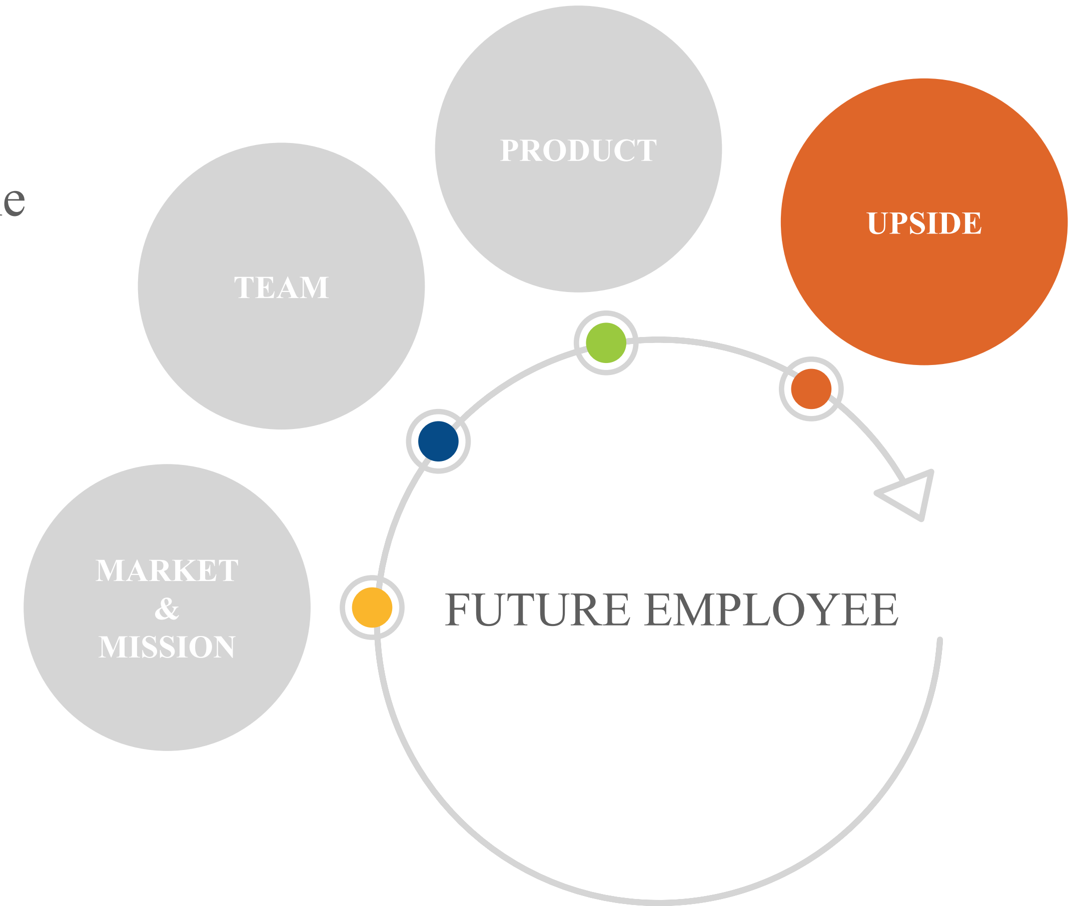


COMPENSATION MATTERS

Based on the 2017-2018 Talent Trends Survey by Lightspeed, the top reasons for offer declines are related to compensation

Top 3 Reasons Candidates Decline

1. Cash Comp
2. Counter Offer
3. Scope of Role



EQUITY:
THE FUNDAMENTALS

COMPONENTS OF COMPENSATION

CASH	EQUITY	OTHER
Base Salary	Stock Options	Sign-On Bonus
Bonus (non-sales)	Common Stock	Relocation
Incentive/ Variable Pay (aka commission)	Restricted Stock Units (RSUs)	Acceleration
	Our focus today	Severance
		Allowances

Employee

- Motivate and retain employees through meaningful, long-term incentives
- Major upside in case of a successful exit or liquidity event
- Express employee importance to business success through ownership in the firm

Equity is meaningful currency to both sides

Startup

- Attract, engage, and retain talent with meaningful incentives common among tech companies
- Align company incentives with individual employee incentives to drive sustained performance
- Drive loyalty and commitment through an “ownership culture”

DISCUSSION

What questions do you commonly get from candidates about equity?

Common Terms

Equity Terms You Should Know

Restricted Stock Units (RSUs)

Agreement by the company to issue shares of stock or the cash value of shares of stock on a future date

Incentive Stock Options (ISOs)

Option to buy a share of common stock at an "exercise price" – ISOs and NQs operate the same way, but ISOs are far more tax efficient

Outstanding Shares

The number of shares that are held by all shareholders

Strike Price

The fixed price per share at which employees can buy options. This price changes overtime

Dilution

Reduction in the ownership percentage of a share by the issuance of new shares

Vesting Cliff

The "grace period" before options begin vesting. Typically 1 year

TYPES OF EQUITY

Equity is an ownership stake in a company, based on either money or effort invested

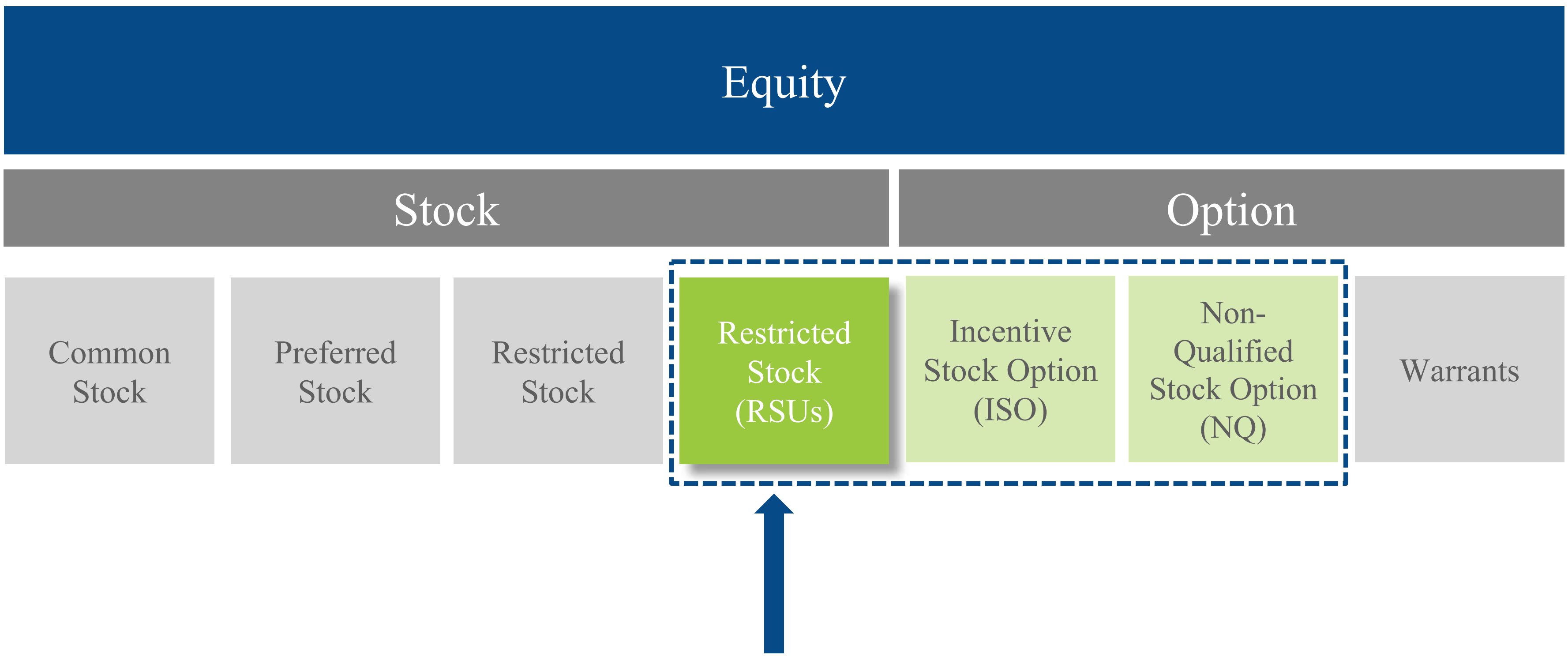
Equity

Stock				Option		
Common Stock	Preferred Stock	Restricted Stock	Restricted Stock (RSUs)	Incentive Stock Option (ISO)	Non-Qualified Stock Option (NQ)	Warrants

Most common to employees: Restricted Stock (RSUs), Incentive Stock Option (ISO), Non-Qualified Stock Option (NQ)

TYPES OF EQUITY

Equity is an ownership stake in a company, based on either money or effort invested



- RSUs are most common for late stage and public companies
- When RSUs vest, tax will be owed on the receipt of the shares
- Can be expensive for a startup employee if the company cannot help with the tax burden

TYPES OF EQUITY

Equity is an ownership stake in a company, based on either money or effort invested

Equity

Stock | Option

Common Stock | Preferred Stock | Restricted Stock | Restricted Stock (RSUs) | Incentive Stock Option (ISO) | Non-Qualified Stock Option (NQ) | Warrants

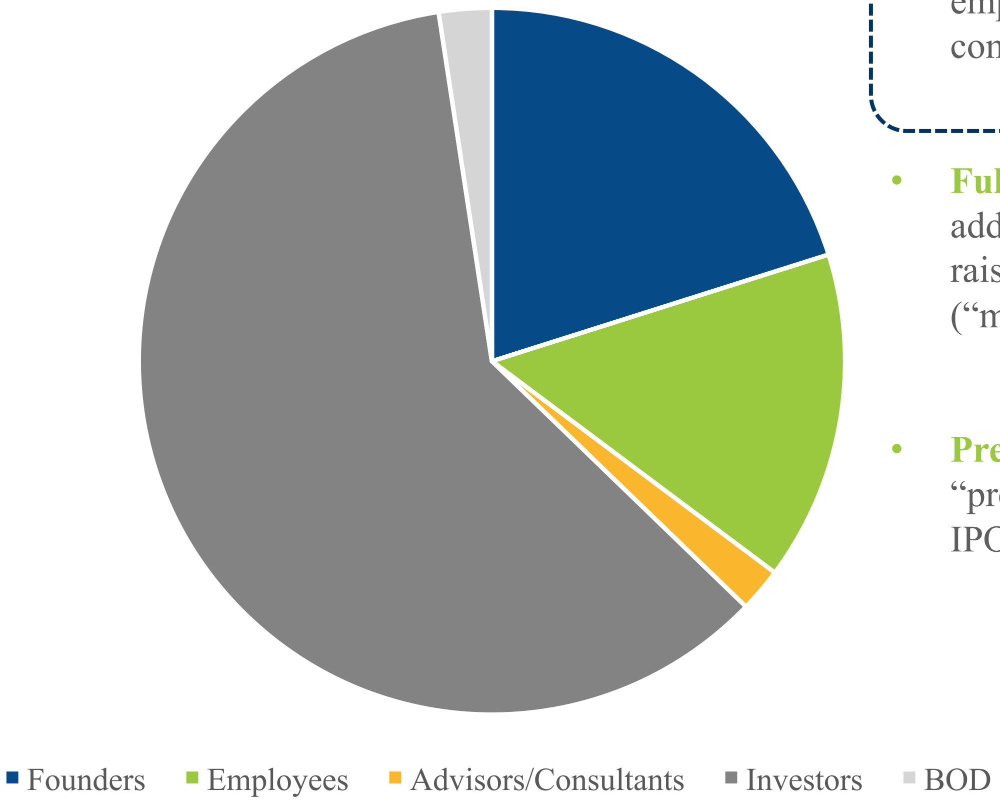
- ISOs are the most common form of equity for early to mid-stage startup employees
- Options allow employees to purchase shares at a fixed price per share (strike price)
- Options expire according to the exercise window

WHO GETS EACH TYPE OF EQUITY?

	Founders	Employees	Advisors, Consultants, Board	Investors
Preferred Stock				✓
Common Stock	✓		✓	
Restricted Stock			✓	
Restricted Stock Unit		✓		
Options- ISO		✓		
Options - NQ		✓	✓	
Warrants			✓	✓

Option Pool

Employee equity typically makes up 10-20% of the total option pool



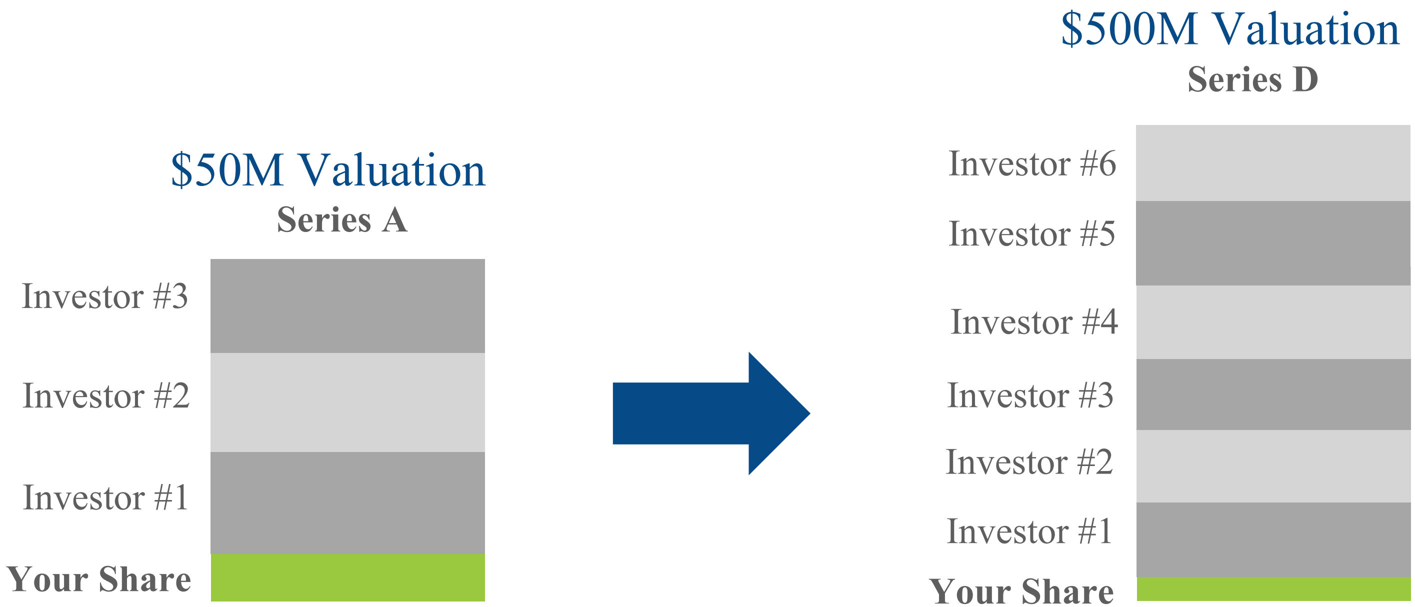
- **Option pool:** Equity that can be offered to employees as part of a defined "option pool" comprising part of the company's capitalization

- **Fully Diluted Shares:** Size of the "pie" if shares are added. "Pie" will grow over time as the company raises $ and issues more shares to new investors ("more dilution").

- **Preferred vs. Common:** Investors receive "preferred" shares while others receive common. At IPO, all shares become common shares.

Dilution

Dilution is a necessary means for growth. It's beneficial when the capital raised drives a larger valuation over time



Grant: 100,000 options
Capital Raised: $25M
Fully Diluted: 10M shares
Your ownership: 1.0% = ~$500K

Grant: 100,000 options (no refresh)
Capital Raised: $125M
Fully Diluted: 50M shares
Your ownership: 0.2% = ~$1M

VALUING EQUITY

DISCUSSION

How have you effectively positioned an offer when you didn’t have the highest compensation package?

VALUING EQUITY: THE MATH

Dilution is a necessary means for growth. It's beneficial when the capital raised drives a larger valuation over time

Options: ISOs & NQs

Total Value = (Value of Share x Quantity) – (Strike Price x Quantity)

Today: ($3/share x 10,000) – ($1/share x 10,000)= $20,000

Future: ($15/share x 10,000) – ($1/share x 10,000)=$140,000

Stock: RSUs

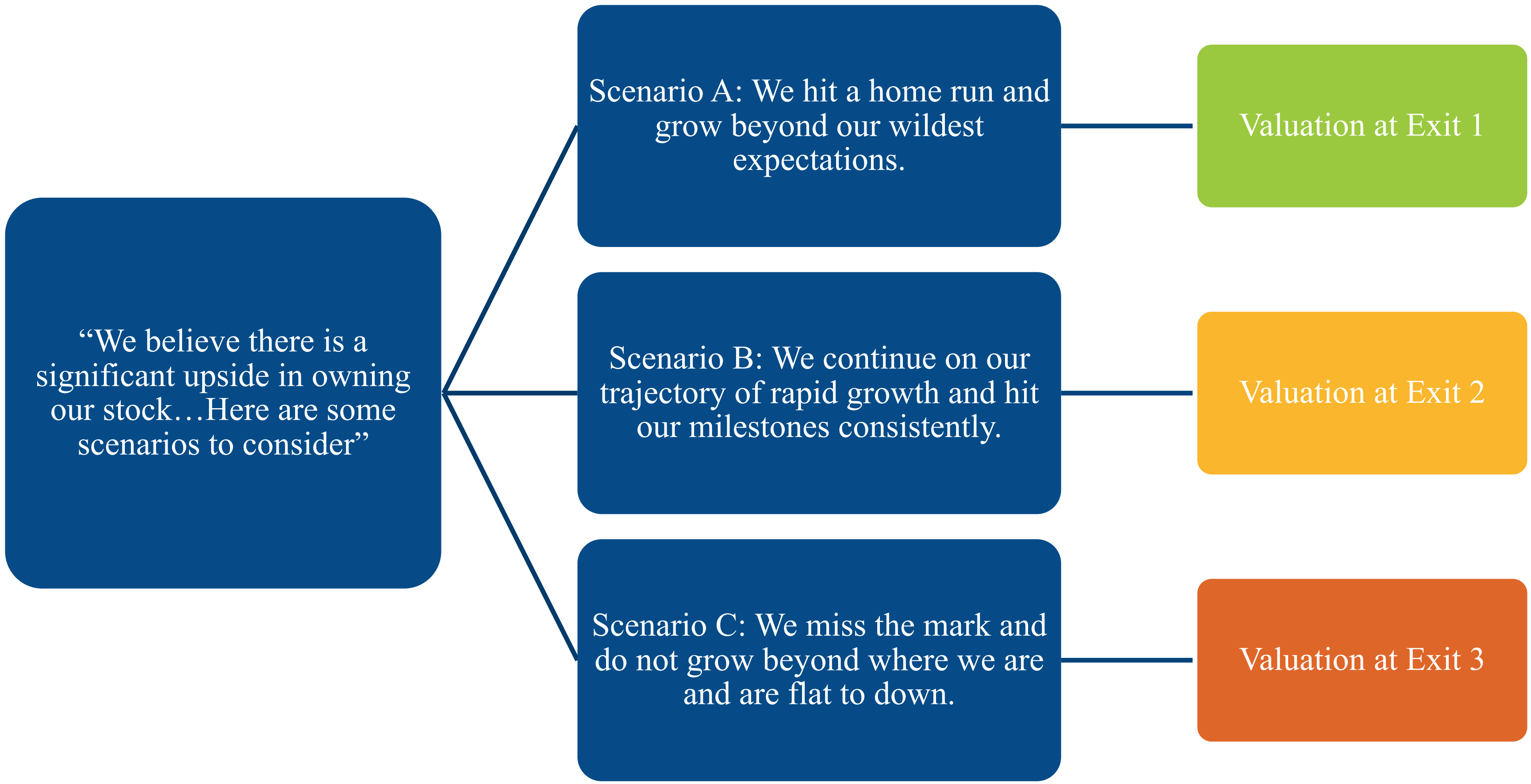
Total Value = (Value of Share x Quantity)

Today: $10/share x 5,000 shares = $50,000

Future: $15/share x 5,000 shares = $75,000

LONG-TERM UPSIDE

We suggest telling a story with different outcomes to help candidates understand potential value



TIPS FOR DEVELOPING SCENARIOS

Work with your executive team to develop relevant scenarios you can share with candidates

- ✓ Make sure you have leadership approval to use equity scenarios
- ✓ Work with founders and/or finance to identify comparable public or acquired companies – high, medium, low
- ✓ Model out scenarios using existing compensation ranges
- ✓ Practice explaining the scenarios. Make it simple and reinforce company story
- ✓ Tip: If the story is not compelling compared to competing offers, **do not use this method**

Equity Scenario Sheet

Modeling out long-term compensation is a valuable tool in the closing process. Allow candidate to play with future valuations. Sell the dream!

Offer Details			
Salary	$100,000	Equity Type	Options
Target Bonus	$10,000	Equity Grant	50,000
Yearly Commission	$0	Your Strike Price	$1
Benefits	$30,000	Vesting Schedule	4 years, 1 year cliff then monthly
Other Compensation	$0		

Potential Outcomes	Scenario A	Scenario B	Scenario C	Other Outcome
Valuation at Exit	$4B	$4B	$3.7B	
Value per Share at Exit	$20	$16	$14	$30
Value of Your Equity (Fully Vested)	$937,500	$737,500	$637,500	$1,437,500

<Your Company> Offer	
Yearly Compensation	$140,000
Equity Grant	50,000
Strike Price	$1
Potential Outcome	Scenario A
Equity Value (Fully Vested)	$937,500
Total Over 4 Years	**$1,497,500**

https://docs.google.com/spreadsheets/d/1Se0PT8ZEt_idN5dFruoAnJtj3LA1pJmKsDUSmzvjgIg/edit?usp=sharing

SELLING POINTS BY STAGE

Every stage has it's pros, learn how to sell yours effectively

Early Stage

- ✓ High impact and high ownership – scope of role
- ✓ No red tape – innovate quickly
- ✓ Highest percentage of equity – eg. 10x on original value

Expansion Stage

- ✓ Meaningful influence on decisions and growing stability
- ✓ Increasing scale – expanding responsibilities and internal mobility
- ✓ Still meaningful equity with diminishing risk

Late Stage

- ✓ Recognizable brand – "halo effect"
- ✓ Large scale – rapid growth of customers, data, revenue, etc.
- ✓ Short time to value of equity - minimal risk

Public

- ✓ Global scale and recognizable brand
- ✓ Stability – defined process, support structures, company viability, etc
- ✓ Higher cash, lower equity % but with immediate value

DISCUSSION

What organizational changes will you make to improve the way you talk about equity?

ADDITIONAL TIPS

TIPS FOR NEGOTIATING

Make it a conversation!

- Have a story around equity that you believe in. It should not rely on crazy assumptions (ideally the medium scenario).
- Be clear on the assumptions and caveats – it's not about being exact, but making a compelling and viable case
- Understand where the candidate's starting point is in valuing your equity – are they in the right ballpark?
- Give yourself room to move on equity – remember it's a negotiation and there will be tradeoffs

TIPS FOR NEGOTIATING

Make it a conversation!

- ✗ Take candidate demands at face value and allow them to drive the conversation
- ✗ Sell value only based on last round
- ✗ Be defensive when questions arise or withhold basic information
- ✗ Overuse equity to compensate for other weaknesses in your “deal”
- ✗ Make a firm promise on future or current value

DISCUSSION

Any additional questions?

APPENDIX

OTHER RESOURCES

There are tons of online resources available

Equity Definitions:

INVESTOPEDIA

http://www.investopedia.com/university/employee-stock-options-eso/eso1.asp

Another Equity Calculator:

FRONT

https://comp.data.frontapp.com/

How Do Stock Options and RSUs Differ:

wealthfront

https://blog.wealthfront.com/stock-options-versus-rsu/

Startup Equity – A Guide for Employees:

in SlideShare

https://www.slideshare.net/StockOptionCnsl/startup-standards-stock-option-counsel

eshares – A Better Offer Letter

https://blog.esharesinc.com/a-better-offer-lette

eShares

Holloway Guide to Equity

https://www.holloway.com/g/equity-compensation

Common Terms

Equity Terms You Should Know

Restricted Stock Units (RSUs)

Agreement by the company to issue shares of stock or the cash value of shares of stock on a future date

Incentive Stock Options (ISOs)

Option to buy a share of common stock at an "exercise price" – ISOs and NQs operate the same way, but ISOs are far more tax efficient

Outstanding Shares

The number of shares that are held by all shareholders

Strike Price

The fixed price per share at which employees can buy options. This price changes overtime

Dilution

Reduction in the ownership percentage of a share by the issuance of new shares

Vesting Cliff

The "grace period" before options begin vesting. Typically 1 year

Common Terms

Equity Terms You Should Know

Early Exercise

Ability to exercise unvested options. This unvested stock is subject to right of repurchase by the company upon termination

Secondary Market

(Rare) Ability to sell private company shares to an accredited investor

Right of First Refusal

An employee cannot sell their shares to 3rd party without offering to sell them to the company first

Liquidity Preference

Clause in a term sheet that specifies how investors are compensated upon a liquidity event

409a Valuation

Formal report on the value of a company

Acceleration

Vesting is triggered when a company is sold (single trigger) and/or if it is sold and the employee is let go (double trigger)

THANK YOU

This deck and discussion do not constitute legal or tax advice in any way.