



### Section 409A and Stock Options

There are five basic requirements applicable to stock options and stock appreciation rights ("SARs") under Internal Revenue Code Section 409A, as follows:

1. **ISOs and ESPPs Excluded Options:** Incentive Stock Options and stock options issued under "employee stock purchase plans" under Code Section 423 are exempt provided that they continue to meet applicable qualification requirements.
2. **Exercise Price Must be FMV:** Non-qualified stock options and SARs may not provide for a discounted exercise price (i.e., the exercise price must be at least equal to the fair market value of the underlying shares as of the grant date). (For this purpose, dividend equivalents are treated as a reduction to the exercise price.) The following specific valuation requirements apply to the determination of "fair market value":
  - a. Public Companies must base fair market value on a reasonable method using actual sales such as the last sale, closing price or average price on the day before or the day of grant (may use an average over a specified period in certain circumstances – the period must be specified in advance).
  - b. Private Companies must base fair market value on a reasonable application of reasonable valuation methods based on factors such as assets value, anticipated cash flows, stock value of comparable entities, recent arm's length sales, and valuation methods used for other non-compensatory purposes. A safe harbor presumption of a reasonable valuation is available for (i) independent appraisals within the prior 12 months, (ii) a repurchase formula generally applicable for compensatory and noncompensatory purposes that qualifies for the determination of fair market value under Code Section 83, or (iii) in the case of a start-up company, requires valuation efforts of a "qualified individual" (5 years experience in business valuation, appraisal, finance, investment banking, secured lending, etc.) and only when no change of control (within 90 days) or public offering (within 180 days) is anticipated.
3. **Solely Stock of Employer or Parent:** Solely stock of the entity receiving the services of the service provider or its 50% or greater parent company (or the parent's 50% or greater parent, etc.) may be subject to the non-qualified stock option or SAR (i.e., up the 50% or greater ownership chain is permissible but down the ownership chain is not). However, the 50% ownership requirement is relaxed to 20% where there are legitimate business criteria for the granting of the option due to the nexus between the service provider and the optioned entity. Thus, compensatory stock options and/or SARs may no longer be issued to

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employees of or other service providers to subsidiaries or other non-parent affiliates.

4. **Solely Common Stock:** Solely stock that qualifies as “common stock” may underlie a stock option or SAR granted to the service provider. The stock may be subject to restrictions but may not have preferences of any kind other than on liquidation, and may not be subject to a non-lapse mandatory repurchase obligation or put or call right at a price other than fair market value.
5. **No Deferrals or Modifications:** A stock option or SAR may not provide for a deferral feature (i.e., cannot provide for the deferral of the delivery of the shares upon exercise) or be exchanged for other deferred compensation. Material modifications are treated as a new grant and may require re-pricing. Extensions of the right to exercise upon termination are permitted to the lesser of the original exercise period or 10 years.

Each stock option or equity compensation plan which provides for the issuance of stock options and/or SARs, and each individual stock option and/or SAR arrangement, should be reviewed for compliance with these rules.

## The Deadline for Written Compliance Is December 31, 2007.

Any required shareholder approval can take place after December 31, 2007, provided that it is affected within the required period under the regular rules.

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