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ARTICLE | DEC 2024 |

Rethinking Equity Plan Proposals in Biotech



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It has long been common practice for newly public companies to hit the market with an equity plan containing an “evergreen” provision that provides for an annual increase in the number of shares that are available for issuance. These provisions are as well regarded as gold. If companies can slowly draw down on the initial pool and prudently manage the annual share burn rate to approximate the evergreen increase then they can run these evergreen plans to full term, which is typically 10 years. This puts off the administrative lift, expense, and risk—albeit small—of needing to seek approval from public company shareholders for a pool increase or a new plan.

Yet, an increasing number of public biotech companies are putting equity plan proposals on their proxy ballots. Some of this is driven by the number of “aging” public companies, but there are also an increasing number of public companies that, given external market forces, are choosing to seek new plans before their evergreen plans expire. Many of these companies have 4% evergreen provisions, which used to be the norm. As the public markets reopened in mid-2020 following the pandemic’s initial onset, we observed a shift in practice with companies going public with 5% evergreen provisions. This larger benefit helped push market burn rates higher as many companies in the sector pursued more aggressive equity strategies. Competition for talent was fierce with candidates routinely weighing multiple offers as stock prices fell and companies sought to address underwater option balances with outsized awards and/or retention programs.

The widely held view has been that public company shareholders will not approve equity plans with evergreen provisions. The proxy advisory firms’ policies have worked to reinforce this belief, for example ISS views an evergreen provision as an overriding factor triggering an “Against” vote recommendation. However, having an evergreen provision itself doesn’t cement an unfavorable vote outcome. Shareholders typically dig deeper to evaluate the proposal’s potential dilution. A 10-year evergreen provision will certainly trip any quantitative assessment of dilution and overhang. But what about an evergreen with a shorter life?

Considering a New Approach

Companies that have forgone evergreen provisions in equity plan proposals try to maximize the pool of shares that shareholders will approve. In development biotech, high levels of overhang typically limit share pool proposals to three years in a best-case scenario. In these instances, the pool may be 12-15% of common shares outstanding depending on burn rate projections. The issue with a plan proposal with a fixed number of shares in the pool is that it doesn't accommodate future dilution. Most companies will need to raise additional capital during the expected three-year life of a share pool. Equity financings increase the number of common shares outstanding of a company. The fixed share pool, or what remains of it, then constitutes a smaller percentage of the overall company immediately after each financing. A company must then either deplete the pool faster if it wants to maintain its burn rate on a percent of company basis or reduce its burn rate to a level that may no longer provide competitive equity awards to its employee population. The extent of the dilution will impact whether a company will be able to remain competitive with its equity program within the approved pool. If it cannot, then it will need to put forth another equity plan proposal sooner.

An evergreen provision eliminates the risk that future equity financings shorten the expected life of the plan and its pool. Since the evergreen increase is calculated on a percent of common shares basis, the pool replenishes itself with a greater number of shares as the common shares outstanding base grows. A company can continue to deploy an equity program matching its target annual share burn rate.

If the evergreen provision's life (within the plan itself) is short—say three years—overhang models may hold in the same way they hold for plans with a fixed pool of shares projecting a three-year life.

It's also important to understand that ISS does not have a lot of influence on these proposals within biotech. In fact, ISS recommended "Against" 132 of 204 shareholder proposals in 2024, or 65%. All but four of those proposals passed. Sector investors understand the unique nature of incentive programs in biotech. They support equity's use as a high risk/high reward vehicle and tolerate ongoing dilution ahead of commercialization in ways that aren't typical in other sectors. Proposing a short-term evergreen provision can be a better path for companies and this investor base may be understanding of that.

Key Considerations

As with any proxy proposal, it is important that a company consider its shareholder base. This unique approach to share plan proposals will most likely succeed in instances where shareholders are meaningfully represented on the board of directors, a company's stock is tightly held, and/or the company has very strong relationships with its shareholders. Strong recent performance doesn't hurt either, as taking a less orthodox approach will always be easier in the context of success and positive returns.

If embarking on this strategy, we suggest further reducing the risk by doing so at least one full annual cycle before an increase of any kind is needed, in other words before the plan terminates or the pool is otherwise depleted. This provides a safety net as the company

can simply propose an alternative plan or pool at the following annual meeting avoiding the complexity and expense of a special meeting.

For companies preparing equity plan proposals on 2025 proxy ballots, this strategy may be an effective alternative to the more traditional approach of sizing the pool as a fixed number of shares without an evergreen provision. Initially, it is substantially similar to the fixed share approach and mirrors the initial pool life projection, but has built-in flexibility to account for future changes in the company's cap table. Consider whether a short evergreen provision is a viable path that could ease plan administration challenges down the road.

About the Author

Matt advises life sciences and technology companies on executive compensation, specializing in benchmarking, incentive design, pay-for-performance alignment, security arrangements, and CD&A disclosure.

About Pearl Meyer

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