

The Director's Guide to Management Equity Grant Committees

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There is now more flexibility for Delaware corporations to delegate equity award grants to management - should they use it?

Recent changes to the Delaware General Corporation Law provide more flexibility for boards of Delaware corporations to delegate to management the authority to grant equity awards (referred to as a management equity grant committee). These changes, which were effective Aug. 1, 2022, allow a management equity grant committee to make more decisions regarding the structure of equity awards it grants. Before deciding how much authority to delegate to a management equity grant committee, boards should carefully consider the corporate governance implications of such a delegation. As a reminder, many issues related to the backdating of stock options 10 or more years ago involved a delegate who made the stock option grants, not the board or a board committee.

A fundamental duty of the board of a Delaware corporation is to approve the issuance of the corporation's capital stock, including the creation and issuance of rights or options to acquire stock. Such issuances are subject to fiduciary considerations and the technical requirements of the Delaware statutes, which include who can authorize the issuance and what consideration is required to be paid for those issuances. More requirements also may be imposed by the corporation's certificate of incorporation, bylaws and agreements with third parties (e.g., shareholder agreements).

Boards may authorize the issuance of stock and equity awards like restricted stock units, stock options and stock appreciation rights. Duly authorized board committees (committees made up solely of members of the board, like the compensation committee) may take any action with respect to the issuance of stock that the full board can take. The limitations on boards and board committees regarding such issuances and grants generally are:

- Statutory provisions requiring that the consideration received by the corporation must be at least equal to the stock's par value (if any).
- Any limitations that are included in the corporation's certificate of incorporation.

Additionally, the corporation must have sufficient "headroom" to issue the shares (i.e., enough shares of stock not already issued, subscribed for or otherwise committed to be issued), and the corporation must receive fair value for the shares.



Boards and board committees have been able

to delegate the authority to grant rights and options respecting stock to officers and employees of the corporation. However, this ability to delegate used to allow delegations only to officers of the corporation and limited the delegation to selecting the officers or employees of the corporation or any of its subsidiaries who receive rights or options and the number of rights or options to be granted. These limits meant that management equity grant committees could not grant to contractors or consultants, could not determine the terms of the grants (e.g., customized vesting schedules) and could not alter the forms of award used to document the grant. The net result was that, to ensure validity, board or committee resolutions delegating authority to a management equity grant committee had to be incredibly detailed regarding possible grant parameters and any nonstandard grants had to be made by the board or a board committee.

The New Rules

The Aug. 1 changes to the Delaware statute allow the board to delegate to a person or body (e.g., the management equity grant committee) the authority to grant stock, rights or options on terms approved by the committee as long as the board's delegation sets:

- The maximum number of rights, options or stock (including the maximum number of shares issuable on the exercise of rights or options) that the management equity grant committee can grant
- The time period during which the delegation is effective and when the rights, options or stock (including any stock issued pursuant to the exercise of rights or options) can be issued
- The minimum consideration payable

This new flexibility allows:

- Non-officers to serve on a management equity grant committee
- The management equity grant committee to grant to non-employees
- The management equity grant committee to determine varied vesting and other terms

Practical Considerations for Boards Considering Delegation

When a board decides what authority, if any, to delegate to a management equity grant committee, there is tension between permitting maximum flexibility and ensuring the board has appropriate oversight over the issuance of dilutive equity awards. Here are some considerations for directors thinking about delegation:

- **Your level of comfort with giving up control over dilutive issuances.** Some boards are comfortable giving complete flexibility, but others prefer more granular oversight and do not want to delegate authority.
- **Your level of comfort with internal controls and the ability of management to properly operate within its delegated authority.**
- **The hiring pace of the corporation.** A fast hiring pace might result in the board and management wanting to allow a management equity grant committee to make ordinary-course new hire grants faster so employees get their equity awards soon after their start date.

Not every board will choose to delegate authority to management to grant equity awards, but those that do should ask the following questions:

- **Who will serve on the management equity grant committee?** Is every management equity grant committee member required to approve a grant, or could a lesser number of members act?
- **What total number of shares and awards will the management equity grant committee be permitted to grant?** The statute requires a total cap and an expiration date for the management equity grant committee's authority, but the board may want to curtail this authority to allow only a lower limit in a shorter period (e.g., 5 million shares in 10 years, but no more than 1 million shares in any one year).
- **Which groups may receive grants under this delegated authority?** Does the authority affect new hires only or other groups as well?
- **Should the quantity of shares that can be granted to a single individual be limited and/or restricted to ranges by level or position previously approved by the board?** If the ranges are in dollar values, a methodology for converting dollar values to share numbers should be specified.
- **How should the exercise price for options be determined?**
- **How frequently will the management equity grant committee make grants?** Will it always be scheduled, or will the management equity grant committee be permitted to make ad hoc grants? Can the management equity grant committee act during blackout periods?
- **How often will the board and/or compensation committee review grants and renew the authority delegated to a management equity grant committee?**
- **If the management equity grant committee is not limited in the vesting schedules or types of awards it is permitted to grant, what process will ensure that any changes from the corporation's standard practices do not result in negative legal, accounting or tax consequences?**

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