

Vardis



Proposed Management Incentive Plan -- Talisman Acquisition

Illustrative MEIP Value – Dec. 2024 Exit

2019 Revenue = \$180M
2019 EBITDA = \$10.8M (6%)

W. Nelson
Total Units Granted – 3,000,000

Revenue CAGR	EBITDA (% of Sales)	Exit Multiple	MOIC	Time Based Vesting	Performance Vesting	Total Vested
1%	Low - 10%	7.5X	1.5	25%	0%	25%
	Med. - 11.5%	7.5X	2.1	25%	25%	50%
	High - 13%	7.5X	2.8	25%	25%	50%
3%	Low - 10%	8X	2.2	25%	25%	50%
	Med. - 11.5%	8X	3.0	25%	25%	50%
	High - 13%	8X	3.8	25%	25%	50%
5%	Low - 10%	8.5X	3.1	25%	25%	50%
	Med. - 11.5%	8.5X	4.0	25%	25%	50%
	High - 13%	8.5X	5.0	25%	25%	50%
7%	Low - 10%	9X	4.1	25%	25%	50%
	Med. - 11.5%	9X	5.2	25%	25%	50%
	High - 13%	9X	6.3	25%	25%	50%

PRIVATE EQUITY REPORT SERIES:
Portfolio Company Equity Participation Plans
Q4 2020

DISCLAIMER: The numbers are liquid...

/ VARDIS PRIVATE EQUITY REPORT SERIES: Portfolio Company Equity Participation Plans

/ Overview: *We are pleased to share with you the latest in our series of Private Equity Reports – an in-depth review of Portfolio Company Equity Participation Plans. This report is based on 375 survey responses received worldwide from executives of private equity portfolio companies and their private equity sponsors.*

The management incentive programs sponsors employ to link the interests of their portfolio company leadership teams and their investors vary widely in structure, tax treatment, scale and performance hurdles. Variations exist within a single firm's portfolio. Even the terms which are used to define key plan components vary from location to location and plan to plan. Ask someone in the US about "sweet equity" and you are likely to be corrected, "You mean sweat equity, right?"

This report is intended to shed light on both the differences and prevailing norms between Equity Participation Plans. We appreciate the participation of the many executives and private equity professionals who made this report possible. Where questions to these two cohorts were different, we have included both sets of questions and responses. It should be noted that executives were asked to answer questions about their current portfolio company, PE professionals were asked to answer these same questions about "their most recently acquired portfolio company." We thank them for their insights.

/ About Vardis: Vardis is an international executive search firm focused strictly on portfolio company recruitment on behalf of Private Equity investors in North America, Europe and Asia (CEO, CFO, Board Directors, etc.) and in Pre-Deal situations through the introduction of Advisors, potential Board Members and Operating Executives.

Since 2016, Vardis has conducted a series of surveys in the Private Equity marketplace. These include our annual PE CEO and PE CFO Compensation Reports as well as the leadership reports we have published in conjunction with AlixPartners. Copies of past reports are available on the Vardis website at www.Vardis.com.

/ Questions & further information: Should you have questions or want further information on this or Vardis' other surveys, including its annual Leadership surveys (in conjunction with AlixPartners), please feel free to contact any of those listed below.

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/ VARDIS PE REPORT SERIES: **PORTFOLIO COMPANY EQUITY PARTICIPATION PLANS**

/ Report Highlights:

Common Practices

- Not a tool for the rank & file - 39% apply exclusively to CEOs and Direct Reports and only 13% extend broadly through management layers
- Vesting is generally a function of both performance and liquidity. Only 29% of plans vest solely based on time. Two-thirds require a return multiple of 3X or more

Location Drives Plan Structure

- Options, Profits Interests and/or Bonus Plans represent 91% of the N. American market versus 19% of plans outside of N. America.
- In turn, Sweet Equity and Loan Funded Share Plans are 80% of the market outside N. America

Differences Abound

- Incentive Pool allocations vary widely and not representative of a typical bell curve distribution. The median pool is 10.6% of the fully diluted shares but 42% of plans are below 7% or greater than 13%
- Individual grants are similarly inconsistent.
- “Base Case”, the phrase used by investors to outline the expected payout from an Equity Participation Plan varies from firm to firm and partner to partner

Depends Who You’re Asking

- Only 4% of PE Professionals believe that management team payouts are likely to be 75% or less of the “Base Case” compared to 39% of Portfolio Company executives who have been through a liquidity event

Trends Worth Watching

- There is little difference in the size of equity grants between tax advantaged plans and those taxed as ordinary income (e.g. Options or Bonus programs versus Profits Interests). We expect those offering tax advantaged plans to highlight this more effectively to a tax-savvy universe of executives.
- PE investors are taking succession and continuity seriously. More than half of PE portfolio companies now employ a COO, 56% of which have broad P&L responsibilities and 66% of which are likely or possible CEO successors.

The camel has been described as a horse designed by a committee. At the risk of producing something “camel-ly,” the following represents a “typical” Equity Participation Plan.

Plan Overview	Prevailing Practices	Notes
Plan Structure	N. America: Options (Non-Qualified) or Profits Interests (corp. vs. partnership) EU/UK: Sweet Equity using both options and loan plans ROW: Options, loan funded plans	Almost 2/3 of the US market is in vehicles that offer no tax advantage to the employee
Incentive Pool Size	10-11%	Flat distribution with lots of companies on both sides of the average. Surprisingly little, if any, correlation to enterprise value.
Participation	Most commonly CEO and Direct Reports or CEO/Direct Reports & Next Tier.	Some correlation to plan type and enterprise value. Option and bonus plans extended to broader group. The greater the enterprise value the greater the number of participants.
Vesting	Blend of time and performance with acceleration at liquidity. Cash bonus based on equity value popular in N. America.	The Equity-based Bonus programs generally have no vesting other than at liquidity.
Performance Hurdle	Most commonly 2-3X MOIC	Many firms use a threshold IRR in addition to MOIC.
Pool Allocation	CEO: 3 ½ to 4 ½% COO (where present): 1 ½ to 2% CFO: 1 to 1 ½% Chair: 1 to 2% (.5% for other directors)	The COO title was present in about half the companies surveyed, with 2/3 of those have robust COO job responsibilities.

Terms In this Report

Base Case – the financial performance model as well as assumptions of value at acquisition, debt levels, preferred returns and transaction costs used to illustrate the value of an Equity Plan to participants

Options – the right to purchase stock in a corporation at a predetermined price. Gains at distribution are generally taxable at earned income tax rates in the US and as capital gains in the UK & EU. The difference between the strike price of the option and the market value of the shares on the date of exercise is fully deductible at the corporate level.

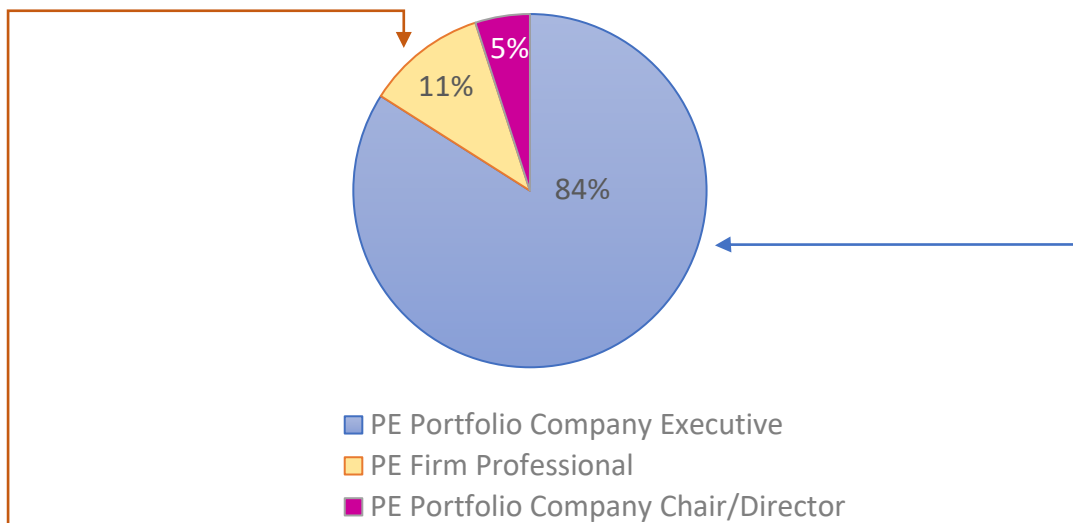
Profits Interests – a financial instrument which provides holders a share in the profits generated by a partnership at liquidity. Gains to employees at distribution are generally taxed at capital gains rates. There is no tax deductibility to the partnership in the US ascribed to the profits.

Equity-Based bonus – cash bonus paid at liquidity based on equity value and taxed as ordinary income.

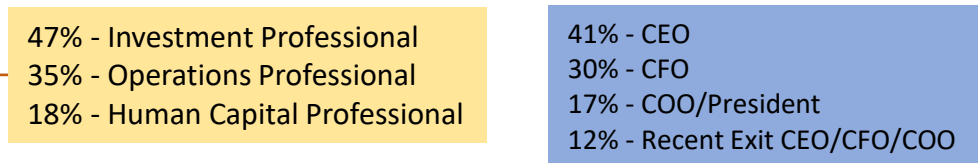
Sweet Equity – Common in the UK & EU, generally options, performance rights, rights to be issued further shares or rights which have the effect of converting preference shares held by investors into ordinary shares at liquidity. Generally taxed at capital gains rates.

Loan Funded Shares – most common in Asia/Pacific, particularly Australia, taxed at capital gains rates.

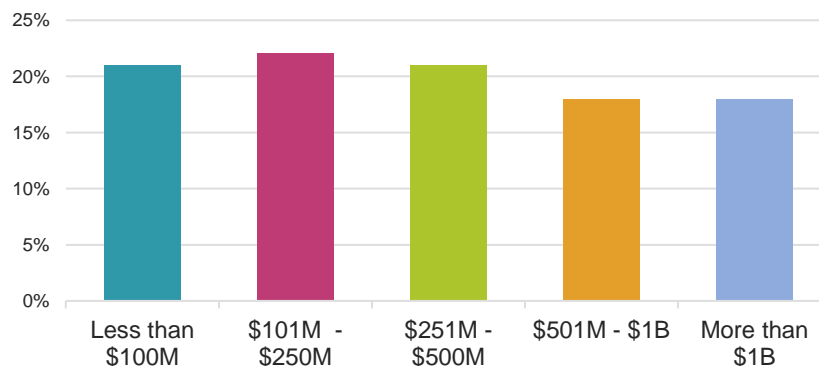
1 Which of the following best describes you?:



2 Your current Role?

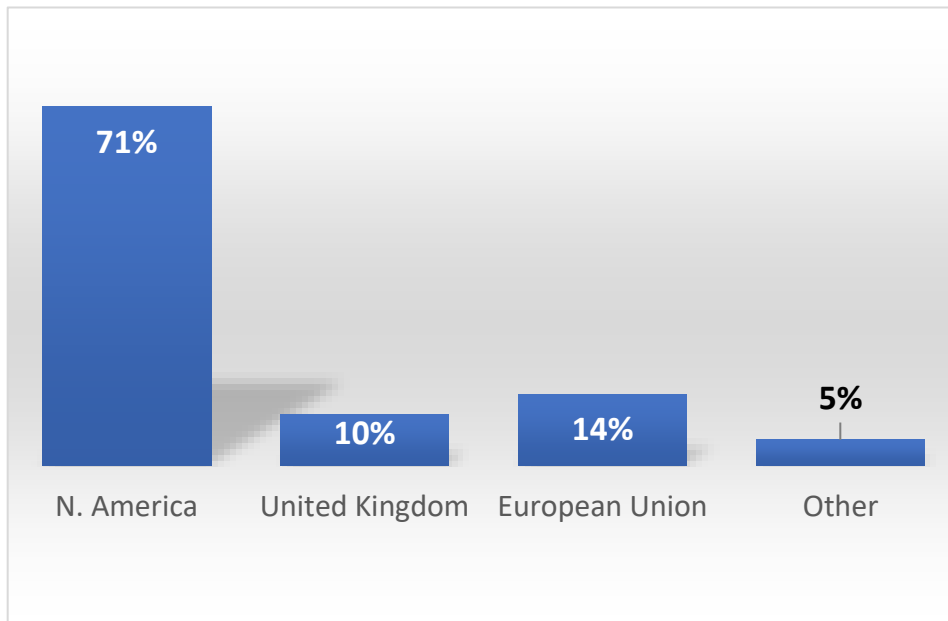


3 What is your Company's approximate enterprise value?



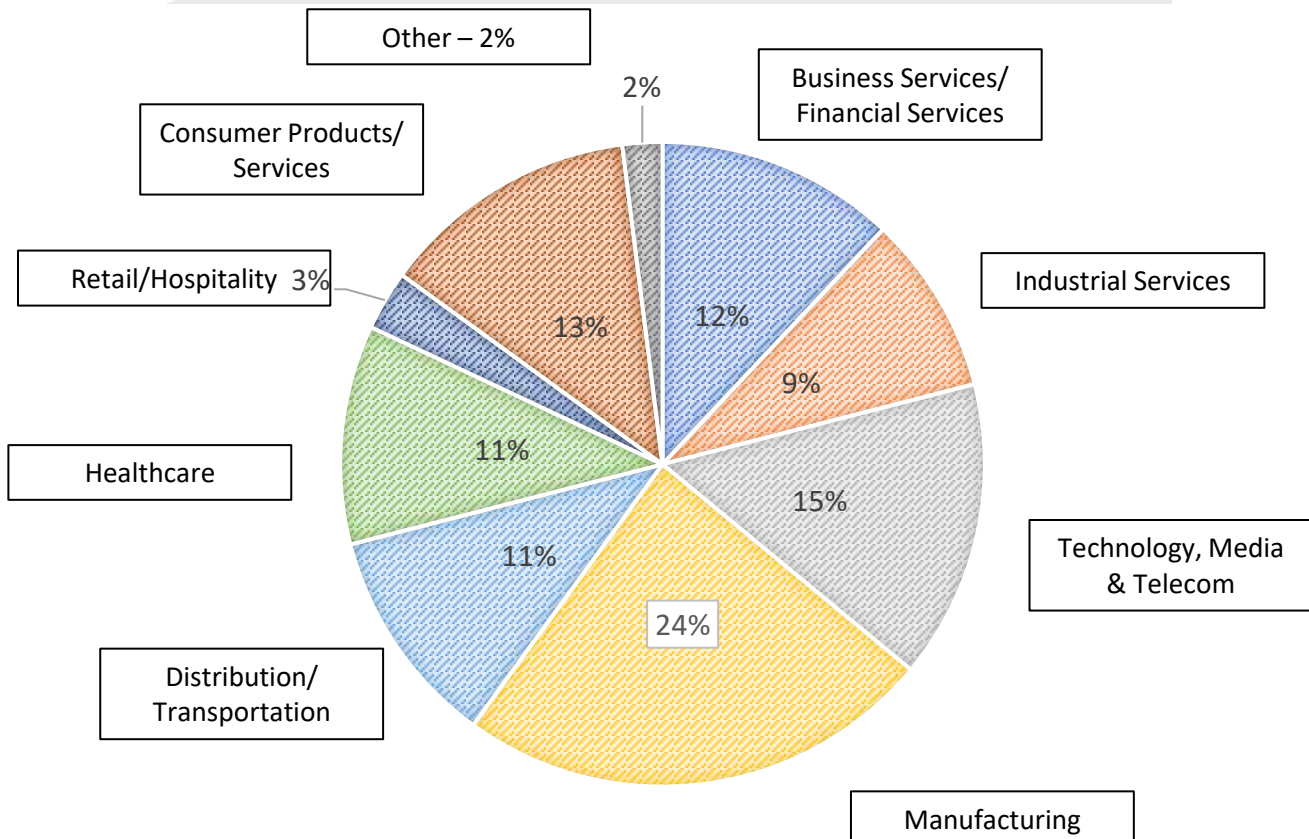
4

Where are Company Headquarters?



5

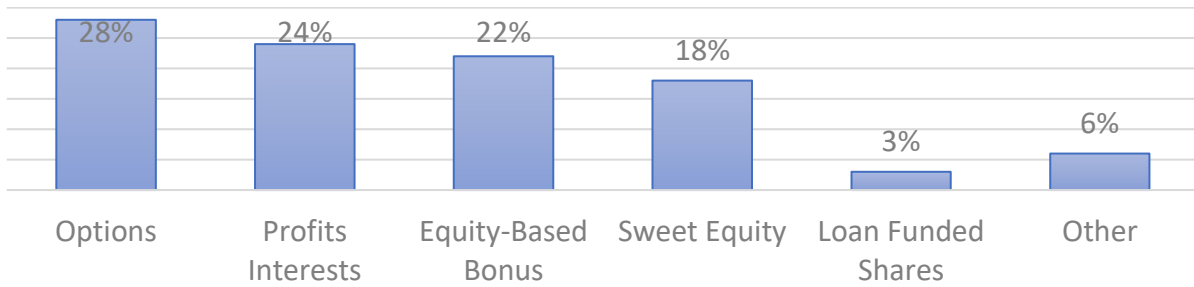
What industry best describes your Company?



6

What is the primary structure of your Equity Participation Plan?

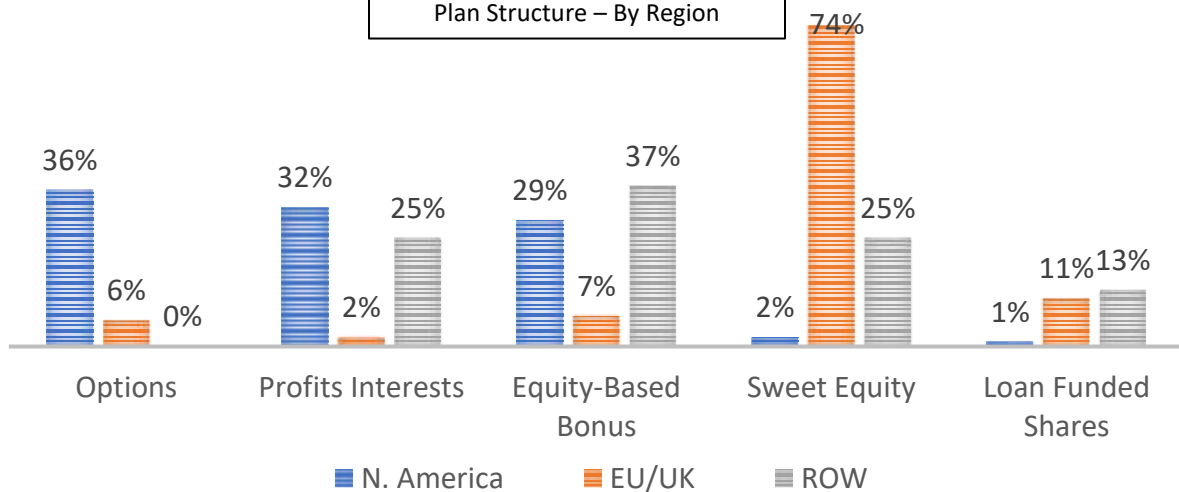
Plan Structure – All Responses



6

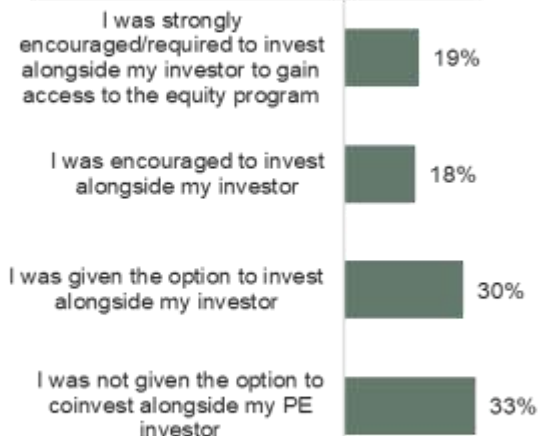
What is the primary structure of your Equity Participation Plan?

Plan Structure – By Region



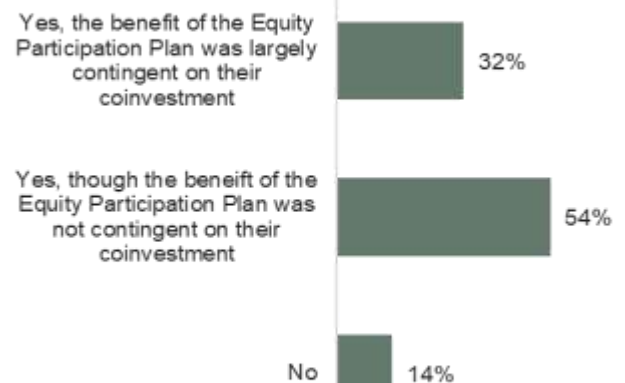
Portfolio Company Executives

7 What best describes your situation?



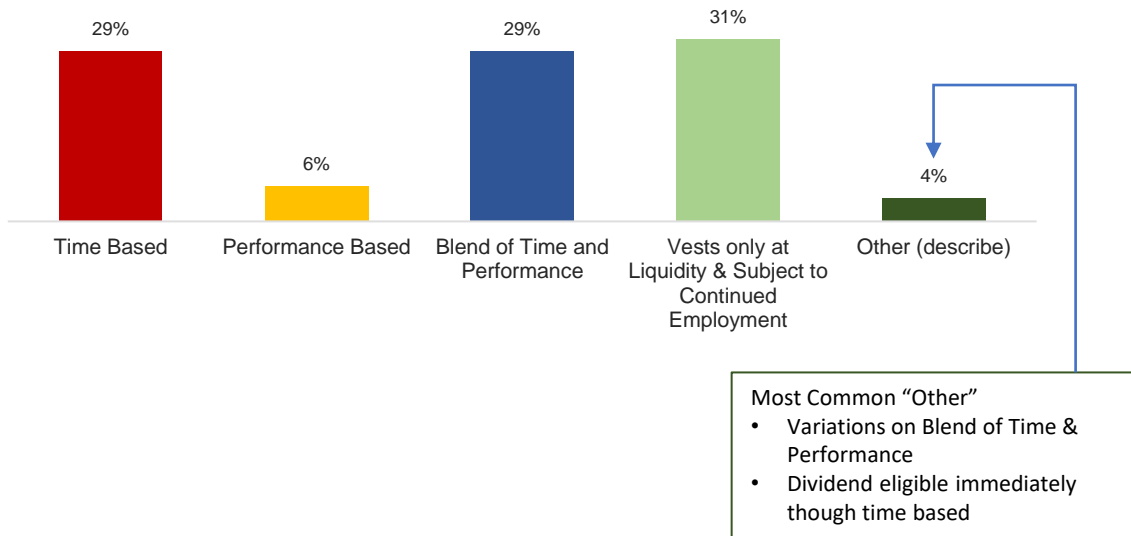
Private Equity Professionals

7 In your most recently acquired Company, did you encourage coinvestment from the executives?



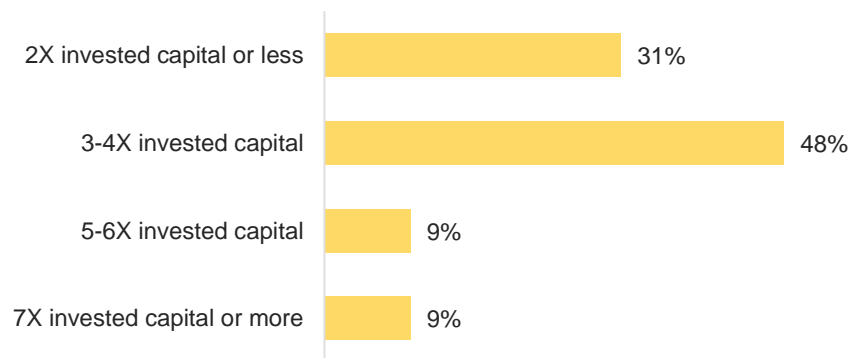
8

How does your Equity Participation Plan vest?



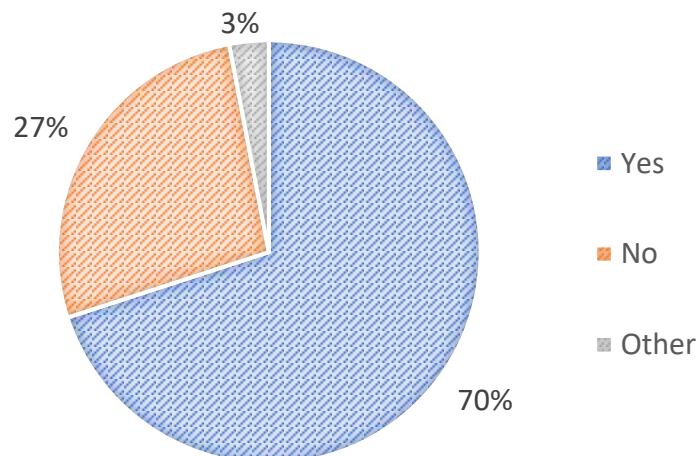
9

What is the target MOIC (multiple of invested capital) on which your equity "base case" was based?



10

Are the business plan targets used to secure financing the same as those used for the Equity Participation Plan, i.e. is there a single, consistent set of targets?



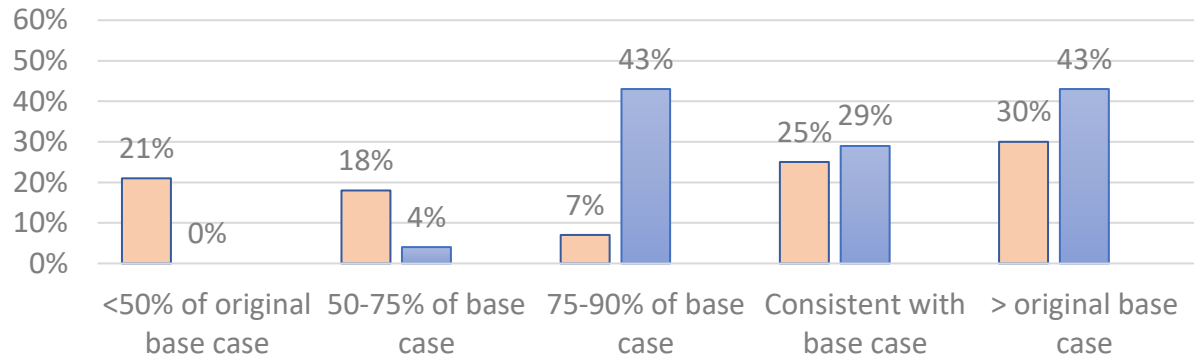
/ SURVEY RESPONSES: SECTION III, PLAN STRUCTURE

Portfolio Company Executives

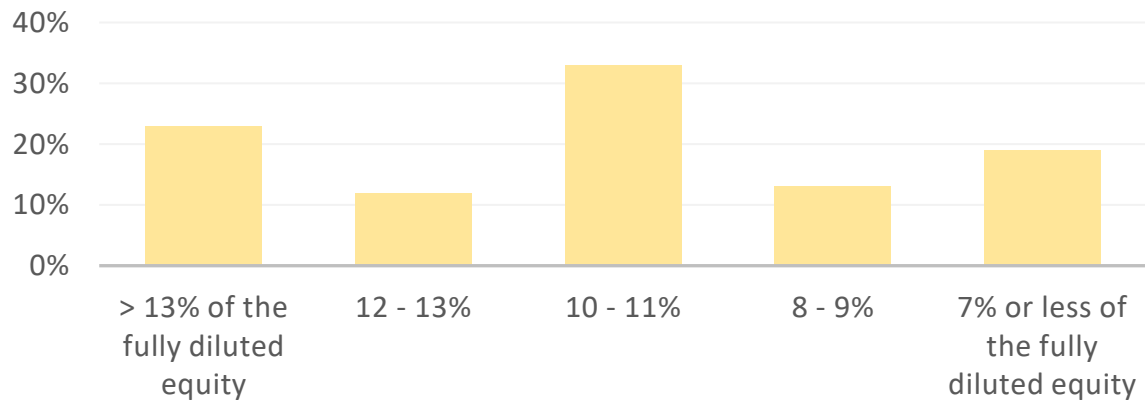
Private Equity Professionals

11 If How have previously achieved a liquidity event with a PE-backed company, how did your equity payout compare to your original "base case" target?

11 How would you describe the historical performance of the executive teams in your firm's Portfolio Companies in achieving the "base case" equity payouts at exit?



12 What is the approximate size of the Equity Participation pool at your Company/Most Recent Portfolio Company acquired?



13 What best describes those who are eligible to participate in the Equity Participation plan?

CEO & direct reports only

39%

CEO, direct reports & next tier executives

24%

CEO, direct reports, next tier & select others

25%

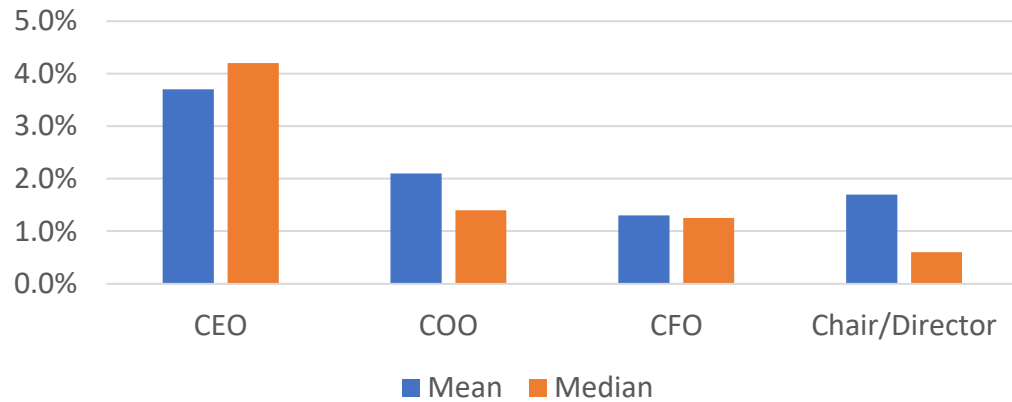
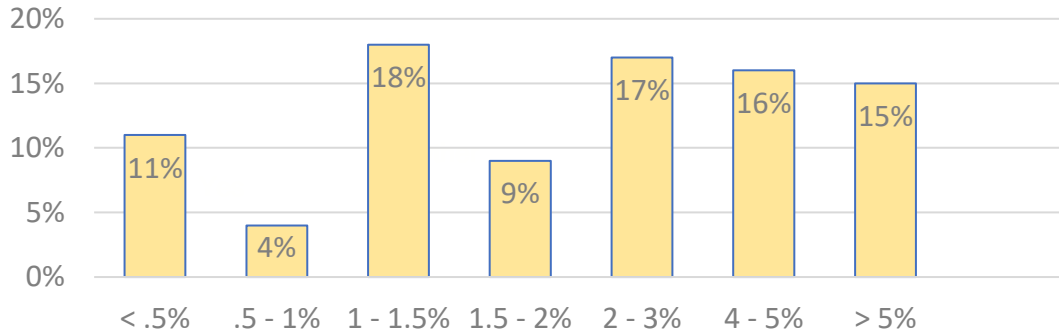
Broad participation across management ranks

13%

Portfolio Company Executives

14

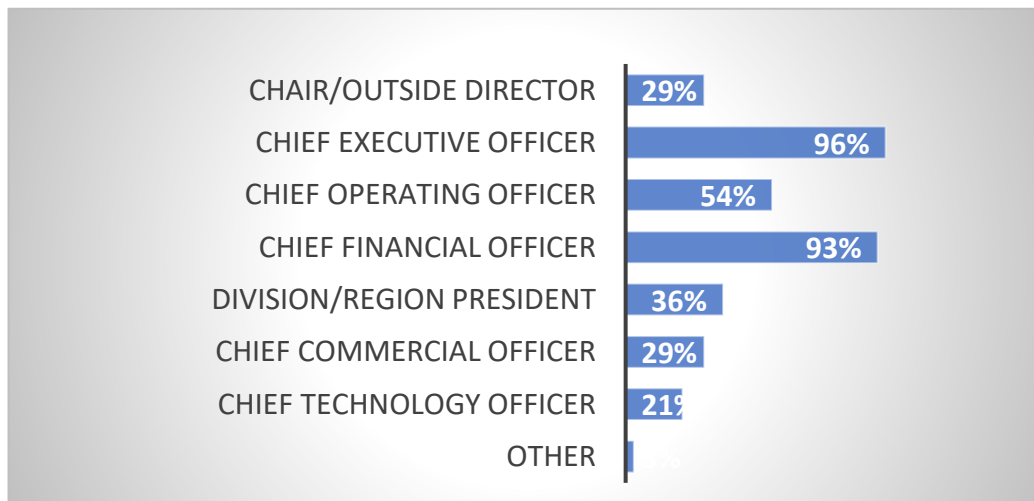
On what percentage of the fully diluted equity is your Equity Participation based?



Private Equity Professionals

14

In your most recently acquired Portfolio Company, which four executives had the largest share of the Equity Participation pool? (check four)



Portfolio Company Executives

Private Equity Professionals

15 If the global pandemic has materially diminished the long term value of your Equity Participation plan, do you anticipate your investor/Board of Directors will adjust your Equity Participation plan to provide a continued incentive to those in the plan?

15 If the global pandemic has materially diminished the long term value of the Equity Participation plan, do you anticipate adjusting or resetting the value of the plan to provide a continued incentive to plan participants?

