

Stock Appreciation Rights (SAR) Plan Development

There are several steps in setting up and rolling out this valuable and rewarding plan for key employees. However, once it's in place, updates are only needed annually or if there are employee changes.

PROGRAM SET UP

Determining Share/Unit Value

Responsible Party: Owner and Key Finance Person

Determine the number of company stock shares available to fund and maintain the program.

For example, if a single owner has 100% of company shares, we suggest earmarking no more than 10% of shares for the SAR program and distributing the value of only 7% of the shares, keeping the remaining 3% for future awards. However, if there is more than one owner, contributing shares should be based on percent of ownership to achieve 10%.

Break down the share amount into total units and value per unit at the time of the award.

For example, if 10% or 10 shares of the owner's stock are dedicated to the SAR program, those 10 shares are broken into awardable units. We typically suggest making available 100,000 units. These units will be awarded to key individuals as an incentive to help the company grow.

Be sure to factor program funding into your annual budget. The program doesn't have to be fully funded in year one of a vested program but should be fully funded to support a vested payout in the event of a company sale or employee leaving.

Using your current company valuation and 100,000 units, determine the unit value/price:

Company Valuation: \$12,000,000

\$12,000,000 divided by 100,000 units = \$120.00 / unit (value at time of initial award).

Note this is NOT the amount awarded to the employee but the baseline to determine the increase in the unit value year over year as the company increases in value.

If no current valuation is available, you can create a general valuation based on gross margin (note: it's recommended you get a company valuation if you don't have one.)

Example: Take 1 X of gross margin dollars as the valuation method. We suggest using a simple valuation method so all employees can understand it and can help make improvements. All employees should be able to relate and help control the cost of goods, such as outside purchases, labor efficiencies, or other ways to increase the gross margin and the company value.

Please note that your actual value at the time of sale will vary based on your growth rate, client concentration, contracted or reoccurring revenue, assets/liabilities ratio, and personal desire. If you started your SAR program with a gross margin valuation, keep using the 1X gross margin valuation method each year to avoid large swings in the value. In most cases, the actual sold value should net more than the base value to allow for an early payout at the time of sale.

Stock Appreciation Rights (SAR) Plan Development

Determine Key Employee Awards

Responsible Party: Owner and Key Finance Person

This program is not for every employee but for those key leaders and employees who will help you grow the business, are willing to take on extra duties, and can impact other employees to help drive growth. These could be sales leaders, high-impact/key salespeople, and finance, production, and technology leaders. A SAR program is typically compensation for key leaders; however, in some businesses, like non-manufacturing services, this program could be an incentive for all employees.

Make a list of key employees and rank them by the level of influence/impact on growth. Then, note how many units you would like to award each.

Create a SAR program abstract. The abstract provides a snapshot of the total financial value of the program and is a tool to track and maintain the program on-going. The abstract should be updated annually and acts as a handy reference should a key employee leave, or at the time of sale, or another company event occurs. The abstract we share is one example. Your finance team can develop a tracking abstract as desired.

Refer to file: "SAR Program Abstract Template.xlsx."

Agreements

Responsible Party: Owner and Key Finance Person or Confidential Human Resources Representative

Create a personalized, confidential agreement for each recipient for their SAR award. The contract is legally binding and must be executed by both the company and the employee. The contract documents the unit price at the time of award, the vesting schedule, and other pertinent details. Be sure to keep a copy of the signed agreement for Human Resource files.

Refer to: "Stock Appreciation Right Agreement Template.docx."

Create a company award certificate that is also provided to the employee. The certificate adds value to the SAR program as it provides a visual representation of company "ownership" and the employee's value to the organization. The certificates should be given to employees along with their agreement.

Refer to files: "GeneralCertificate_Editable.pdf" and "GeneralCertificate_Editable SAMPLE.pdf."

PROGRAM ROLL OUT

Presenting to Employees

Responsible Party: Owner

Call a meeting of the employees receiving the awards. Prepare a presentation that thanks this group for their efforts and investments in helping the company grow. As a reward for past and future efforts, explain the program and value of the reward and the company's investment in those employees as leaders.

Refer to file: "SAR Slides Overview Template. pptx".

Each employee should receive their contract and certificate in person within one day after the announcement and be provided an opportunity to review and sign.

Stock Appreciation Rights (SAR) Plan Development

PROGRAM MAINTENANCE

On-going Maintenance

Responsible Party: Owner and Key Finance Person or Confidential Human Resources Representative

Throughout the year, as employee changes may occur (employees leave; additional units awarded for extra efforts, other), update the SAR program abstract and any affected employee agreements.

Annually, after the previous year's books are closed, update the company valuation and update the abstract to ensure you have a clear picture of the value of the program payout amount should there be a company event, vested employees leave, etc. You may also use this time to award additional shares to employees not previously involved in the program but who have helped the business grow or reward employees in the program with additional units based on performance.

This valuable program helps key company leaders and employees feel appreciated, rewarded, and further invested in helping the company grow and achieve great things. As a result, they become "owners" right along with you.