

STEMCELLS INC
Form PRE 14A
October 21, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

SCHEDULE 14A

(RULE 14a-101)

INFORMATION REQUIRED IN PROXY STATEMENT

SCHEDULE 14A INFORMATION

Proxy Statement Pursuant to Section 14(a) of the

Securities Exchange Act of 1934

(Amendment No.)

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

- Preliminary Proxy Statement
- Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**
- Definitive Proxy Statement
- Definitive Additional Materials
- Soliciting Material Pursuant to §240.14a-12

STEMCELLS, INC.

(Name of Registrant as Specified In Its Charter)

(Name of Person(s) Filing Proxy Statement, if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

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(1) Amount Previously Paid:

(2) Form, Schedule or Registration Statement No.:

(3) Filing Party:

(4) Date Filed:

STEMCELLS, INC.

7707 Gateway Blvd.

Newark, California 94560

NOTICE OF ANNUAL MEETING OF STOCKHOLDERS

To be Held on December 20, 2013

To the Stockholders of STEMCELLS, INC.

Notice is hereby given that the Annual Meeting of Stockholders of StemCells, Inc. (StemCells or the company) will be held on Friday, December 20, 2013, at 10 a.m., local time, at 7707 Gateway Boulevard, Newark, California 94560 for the following purposes:

1. to elect the three Class I directors named in the accompanying proxy materials to serve until the 2016 Annual Meeting of Stockholders;
2. to consider and vote upon a proposal to ratify the selection of Grant Thornton LLP as independent public accountants for the company for the fiscal year ending December 31, 2013;
3. to consider and vote upon a proposal to amend the company s restated certificate of incorporation to increase the company s authorized capital by one hundred fifty million shares of common stock;
4. to consider and vote upon a proposal to adopt the 2013 Equity Incentive Plan as proposed; and
5. to transact any and all other business that may properly come before the meeting.

The Board of Directors has fixed the close of business on Friday, October 25, 2013, as the record date for determining those stockholders who are entitled to notice of, and to vote at, the annual meeting of stockholders and any postponements or adjournments thereof. The stock transfer books will not be closed between the record date and the date of the meeting.

Representation of at least a majority of all outstanding shares of common stock of StemCells is required to constitute a quorum. Accordingly, it is important that your shares be represented at the meeting. This year we are again taking advantage of Securities and Exchange Commission rules that allow issuers to furnish proxy materials to their stockholders on the Internet. We believe these rules allow us to provide our stockholders with the information they need, while lowering the costs of delivery and reducing the environmental impact of our Annual Meeting.

Please read the proxy materials carefully. All stockholders are invited to attend the Annual Meeting. Your vote is important, and we appreciate your cooperation in considering and acting on the matters presented.

By Order of the Board of Directors,

Kenneth B. Stratton, J.D.
Secretary

November 4, 2013

Newark, California

PROXY STATEMENT
ANNUAL MEETING OF STOCKHOLDERS
OF
STEMCELLS, INC.

The accompanying proxy is solicited on behalf of the Board of Directors of StemCells, Inc. (the company) for use at its annual meeting of stockholders (the Annual Meeting) to be held on Friday, December 20, 2013, at 10 a.m., local time, at the company's headquarters at 7707 Gateway Boulevard, Newark, California 94560. The company will bear the cost of solicitation of proxies. Directors, officers and employees of the company may solicit proxies by telephone, facsimile or in person for no additional compensation. The company will reimburse banks, brokerage firms, proxy solicitors, and other custodians, nominees and fiduciaries for reasonable expenses incurred by them in sending proxy materials to the beneficial owners of shares.

The Board of Directors has fixed the close of business on Friday, October 25, 2013, as the record date for determining stockholders entitled to notice of, and to vote at, the Annual Meeting or at any postponement or adjournment thereof. There were 54,971,174 shares of our common stock, \$.01 par value, outstanding on October 25, 2013, each of which is entitled to one vote for each share on the matters to be voted upon.

Our 2013 Proxy Materials are Available on the Internet. This year we have again elected to provide access to our proxy materials over the Internet in accordance with rules adopted by the Securities and Exchange Commission. Accordingly, we are sending a Notice of Internet Availability of Proxy Materials (the Notice) to our stockholders of record and beneficial owners, which will instruct them as to how they may access and review all of the proxy materials on the Internet and how they may submit their proxy on the Internet. We expect to begin delivering the Notice to our stockholders on November 4, 2013, our anticipated initial mailing date. Any stockholder wishing to receive a paper copy of our proxy materials can request them from us by following the instructions found in the Notice for requesting such materials, or by calling 1 (800) 579-1639. Requests for a paper copy of our proxy materials should be made on or before December 6, 2013 to facilitate timely delivery.

Stockholders are being asked to vote on four proposals at the company's 2013 Annual Meeting. The proposals to be voted on and related recommendations from the Board of Directors are as follows:

Proposal Number 1 To elect the three director nominees named in this Proxy Statement to serve as Class I directors on the Board until our 2016 annual meeting of stockholders or until that person's successor is duly elected and qualified. The Board of Directors recommends that you vote FOR each of the nominees.

Proposal Number 2 To ratify the appointment of Grant Thornton LLP as the company's independent registered public accounting firm for the fiscal year ending December 31, 2013. The Board of Directors recommends that you vote FOR this proposal.

Proposal Number 3 To adopt the proposed amendment to the company's restated certificate of incorporation to increase the number of authorized shares of common stock by one hundred fifty million (150,000,000) shares as proposed herein. The Board of Directors recommends that you vote FOR this proposal.

Proposal Number 4 To adopt the proposed 2013 Equity Incentive Plan as described herein. The Board of Directors recommends that you vote FOR this proposal.

In the election of directors, which is Proposal Number 1, you may vote FOR all three of the nominees or your vote may be WITHHELD with respect to one or more of the nominees. For Proposal Numbers 2, 3 and 4, you may vote FOR, vote AGAINST or ABSTAIN. If you ABSTAIN as to Proposal Numbers 2 or 4, the abstention will have no effect. If you ABSTAIN as to Proposal Number 3, the abstention will have the same effect as voting AGAINST the proposal.

Shares of our common stock represented by proxies in the form enclosed that are properly executed and returned to us and not revoked will be voted as specified in the proxy by the stockholder. In the absence of contrary instructions, or in instances where no specifications are made, the shares will be voted:

- (i) FOR the election as directors of the nominees as described herein under Proposal Number 1 Election of Directors;
- (ii) FOR ratification of the selection of accountants as described herein under Proposal Number 2 Ratification of Selection of Independent Public Accountants;
- (iii) FOR adoption of the amendment to the company's restated certificate of incorporation to increase the number of authorized shares of common stock by one hundred fifty million (150,000,000) as described herein under Proposal Number 3 Amendment to Restated Certificate of Incorporation to Increase Authorized Shares of Common Stock;
- (iv) FOR adoption of the proposed 2013 Equity Incentive Plan as described herein under Proposal Number 4 Adoption of the 2013 Equity Incentive Plan; and
- (v) in the discretion of the named proxies as to any other matter that may properly come before the Annual Meeting.

Any stockholder signing and delivering a proxy may revoke it at any time before it is voted by delivering to the company's corporate secretary a written revocation or a duly executed proxy bearing a date later than the date of the proxy being revoked. Any stockholder attending the Annual Meeting in person may revoke his, her or its proxy and vote his, her or its shares at the Annual Meeting.

How to vote shares at our 2013 Annual Meeting.

This year company stockholders may cast their vote in any of the following ways:

Vote by Internet. Any stockholder can vote over the Internet at www.proxyvote.com by following the instructions on the Notice or proxy card. Internet voting facilities for stockholders of record will be available 24 hours a day and will close at 11:59 p.m. (EDT) on December 19, 2013.

Vote by Phone. Any stockholder can vote by phone by following the instructions on the proxy card and calling 1 (800) 690-6903 up until 11:59 p.m. (EDT) on December 19, 2013.

Vote by Mail. Any stockholder that receives proxy materials by mail can vote by mail by signing, dating and mailing the enclosed proxy card in the postage-paid envelope provided. If the envelope is missing, such a stockholder can mail the completed proxy card or voting instruction card to Vote Processing, c/o Broadridge, 51 Mercedes Way, Edgewood, New York 11717. The completed card must be received no later than December 19, 2013.

Voting at the Annual Meeting. All company stockholders are invited to attend the Annual Meeting in person. Any stockholder that attends the meeting in person may deliver a completed proxy card in person or vote by completing a ballot, which will be available at the meeting. However, each stockholder intending to vote in person at the Annual Meeting should note that if his, her or its shares are held in the name of a bank, broker or other nominee, such stockholder must obtain a legal proxy, executed in his, her or its favor, from the holder of record to be able to vote at the Annual Meeting. Stockholders should allow enough time prior to the Annual Meeting to obtain this proxy from the holder of record, if needed.

The shares voted electronically or represented by the proxy cards received, properly marked, dated, signed and not revoked, will be voted at the Annual Meeting.

QUORUM, REQUIRED VOTES AND METHOD OF TABULATION

Consistent with Delaware law and the company's amended and restated by-laws, a majority of the votes entitled to be cast on a particular matter, present in person or represented by proxy, constitutes a quorum as to such matter. The company will appoint one or more election inspectors for the meeting to count votes cast by proxy or in person at the Annual Meeting.

If you hold shares beneficially in street name and do not provide your broker or nominee with voting instructions, your shares may constitute broker non-votes. Generally, broker non-votes occur on a matter when a broker is not permitted to vote on that matter without instructions from the beneficial owner and instructions have not been given. This year if you hold shares beneficially in street name and do not vote your shares, your broker or nominee can vote your shares at its discretion only on Proposal Number 2. In tabulating the voting result for any proposal for which the required vote is based on the number of shares present, shares that constitute broker non-votes are not considered entitled to vote on that proposal. Thus, broker non-votes will not affect the outcome of Proposal Numbers 1, 2 and 4, provided a quorum is established. However, for proposals for which the required vote is based on the number of shares of common stock issued and outstanding, broker non-votes have the same effect as a vote AGAINST the proposal.

What vote is required to approve each item?

Election of directors by stockholders, which is Proposal Number 1, will be determined by a plurality of the votes cast by the stockholders entitled to vote at the election that are either present in person or represented by proxy.

For Proposal Numbers 2 and 4, the affirmative FOR vote is required by the holders of a majority of the shares present at the Annual Meeting in person or by proxy and voting. Abstentions will have no effect on the outcome of this proposal.

For Proposal Number 3, amendment of the charter to increase the company's authorized capital, the affirmative FOR vote is required by the holders of a majority of shares issued and outstanding. Abstentions and broker non-votes have the same effect as voting AGAINST charter amendments such as Proposal Number 3.

Management does not know of any matters to be presented at this year's Annual Meeting other than those set forth in this proxy statement and in the notice accompanying this proxy statement. Stockholders will have no appraisal rights under Delaware law with respect to any of the matters expected to be voted on at the Annual Meeting. If other matters should properly come before the meeting, the proxy holders will vote such matters in their discretion. Any stockholder has the right to revoke his, her or its proxy at any time until it is voted.

SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The following table shows the number of shares of our common stock beneficially owned, as of October 15, 2013, by (i) each of our directors, (ii) each of our named executive officers, (iii) all of our directors and executive officers as a group, and (iv) all those known by us to be to a beneficial owner of more than 5% of the company's common stock. In general, beneficial ownership refers to shares that an individual or entity has the power to vote or dispose of, and any rights to acquire common stock that are currently exercisable or will become exercisable within 60 days of October 15, 2013. Unless otherwise indicated, we believe that each person named below, based on information furnished by such owners, holds sole investment and voting power with respect to such shares, subject to community property laws where applicable. We calculated percentage ownership in accordance with the rules of the SEC. The percentage of common stock beneficially owned is based on 54,971,174 shares outstanding as of October 15, 2013. In addition, shares issuable pursuant to options, restricted stock units or other convertible securities that may be acquired within 60 days of October 15, 2013 are deemed to be issued and outstanding and have been treated as outstanding in calculating and determining the beneficial ownership and percentage ownership of those persons possessing those securities, but not for any other persons.

Name and Address of Beneficial Owner*	Amount and Nature of Beneficial Ownership	Percentage of Class Beneficially Owned
Directors and Named Executive Officers		
Eric Bjerkholt(1)	19,000	**
Stewart Craig(2)	59,371	**
R. Scott Greer	31,000	**
Ricardo Levy(3)	9,405	**
Martin McGlynn(4)	242,024	**
Roger Perlmutter(5)	18,405	**
John Schwartz(6)	77,195	**
Ken Stratton(7)	65,307	**
Ann Tsukamoto(8)	101,791	**
Irving Weissman(9)	166,032	**
Rodney Young(10)	86,672	**
All directors and executive officers as a group (twelve persons)	876,202	1.59%
5% Stockholders		
Alpha Capital Anstalt(11)	3,332,660	5.96%

* The address of all directors and executive officers listed in the table is c/o StemCells, Inc., 7707 Gateway Blvd., Newark, California 94560.

** Less than one percent.

(1) Includes 7,000 shares issuable upon exercise of stock options exercisable within 60 days.

(2) Includes 8,750 shares issuable upon exercise of stock options exercisable within 60 days. Includes 15,219 shares in Dr. Craig's 401(k) plan.

(3) Includes 5,405 shares issuable upon exercise of stock options exercisable within 60 days.

(4) Includes 25,625 shares issuable upon exercise of stock options exercisable within 60 days. Includes 17,433 shares in Mr. McGlynn's 401(k) plan.

(5) Includes 15,405 shares issuable upon exercise of 5,405 stock options and 10,000 restricted stock units exercisable within 60 days.

(6) Includes 6,500 shares issuable upon exercise of stock options exercisable within 60 days.

- (7) Includes 15,000 shares issuable upon exercise of stock options exercisable within 60 days. Includes 13,152 shares in Mr. Stratton's 401(k) plan.
- (8) Includes 17,500 shares issuable upon exercise of stock options exercisable within 60 days. Includes 18,668 shares included in Dr. Tsukamoto's 401(k) plan and 3,643 shares held in trust to which Dr. Tsukamoto disclaims beneficial ownership.
- (9) Includes 5,990 shares issuable upon exercise of stock options exercisable within 60 days. Includes 10,508 shares held in trust to which Dr. Weissman disclaims beneficial ownership.
- (10) Includes 33,604 shares issuable upon exercise of stock options exercisable within 60 days. Includes 21,323 shares in Mr. Young's 401(k) plan.
- (11) Beneficial holdings based on a Schedule 13G filed by Alpha Capital Anstalt on February 28, 2012 and the Company's records of its outstanding warrants. According to the Schedule 13G filed February 28, 2012, Alpha Capital may be deemed to beneficially own all shares listed in the table, and has sole dispositive and voting power with respect to all shares listed in the table. The address of the principal place of business of Alpha Capital is Pradafant 7, Furstentums 9490, Vaduz, Liechtenstein.

Board of Directors

We currently have seven directors serving on our Board of Directors. Since June 2010, our Board has been composed of Drs. Ricardo Levy, Roger Perlmutter, John Schwartz, and Irving Weissman and Messrs. Eric Bjerkholt, Scott Greer and Martin McGlynn. The following table shows the names, ages, principal occupations, and public company board memberships for the last five years of our directors, as of October 15, 2013:

Eric Bjerkholt	54	Eric Bjerkholt was elected to the Board of Directors in March 2004. He is Executive Vice President and Chief Financial Officer of Sunesis Pharmaceuticals, Inc., a biopharmaceutical company. Mr. Bjerkholt is a member of the board of directors of Round Table Pizza, Inc.
R. Scott Greer	54	Scott Greer was appointed to the Board of Directors in June 2010. He is currently a principal and managing director of Numenor Ventures LLC, which he founded in 2002 to provide funding and strategic advisory services to early stage enterprises. Mr. Greer currently serves as Chairman of Ablexis, a development stage biotechnology company, and he is also on the board of Nektar Therapeutics.
Ricardo Levy, Ph.D.	68	Ricardo Levy, Ph.D. was elected to the Board of Directors in September 2001. He currently serves as a director on the board of Accelrys, Inc., a public company focused on molecular modeling and simulation software for both life and materials science research.
Martin McGlynn	67	Martin McGlynn was elected to the Board of Directors in February 2001. He is President and Chief Executive Officer of the company, a position he has held since January 2001.

Roger Perlmutter, M.D., Ph.D.	61	Roger Perlmutter, M.D., Ph.D., was elected to the Board of Directors in December 2000. He is President of Merck Research Laboratories, an international pharmaceutical company, where he leads Merck's global research endeavors. Previously, until February 2012, he was Executive Vice President, Research and Development, of Amgen, Inc.
John Schwartz, Ph.D.	79	John Schwartz, Ph.D., was elected to the Board of Directors in December 1998 and was elected Chairman of the Board at the same time. He is currently President of Quantum Strategies Management Company, a registered investment advisor.
Irving Weissman, M.D.	73	Irving Weissman, M.D., was elected to the Board of Directors in September 1997. He is the Virginia and Daniel K. Ludwig Professor of Cancer Research, Professor of Pathology and Professor of Developmental Biology at Stanford University.

Because we have a classified board, with each of our directors serving a staggered three-year term, only three of our directors are standing for reelection at our 2013 Annual Meeting. The following table shows the composition of the three classes of our Board:

Class I Directors (terms scheduled to expire in 2013, but nominated to stand for reelection at our 2013 Annual Meeting):

Eric Bjerkholt
R. Scott Greer
John Schwartz, Ph.D.

Class II Directors (terms scheduled to expire in 2014):

Ricardo Levy, Ph.D.
Irving Weissman, M.D.

Class III Directors (terms scheduled to expire in 2015):

Martin McGlynn
Roger Perlmutter, M.D., Ph.D.

The independent members of our Board, as determined by the Board of Directors in accordance with the existing Nasdaq Listing rules, are Messrs. Bjerkholt and Greer and Drs. Levy, Perlmutter and Schwartz. The Board of Directors held four regular meetings and one special meeting during the fiscal year ended December 31, 2012. Each of our directors attended more than 75% of the meetings of the Board of Directors and of the committees on which he served.

For many years the roles of chairman and chief executive officer at the company have been separated. We believe that this is appropriate under current circumstances, because it allows management to make the operating decisions necessary to manage the business, while helping to maintain Board independence so that it can provide an effective oversight function. We feel that this has provided an appropriate balance of operational focus, flexibility and oversight. Our independent directors meet at regularly scheduled executive sessions without members of management.

Board Committees

Presently, the Board has four standing committees – the Audit Committee, the Compensation and Stock Option Committee (the Compensation Committee), the Corporate Governance and Nominating Committee (the Corporate Governance Committee), and the Strategic Transactions Committee – as well as a single-member committee established under the company’s 2001, 2004 and 2006 equity incentive plans and the Company’s 2012 Commencement Incentive Plan. The Board created the Strategic Transactions Committee in March 2009 as an *ad hoc* committee with direction to consult with management and advise the full Board on various corporate initiatives, such as the acquisition of substantially all of the operating assets of Stem Cell Sciences plc, which the company completed in April 2009. In June 2010, however, the Board reconstituted the Strategic Transactions Committee, which Mr. Greer currently chairs, as a standing committee of the Board. All members of the Audit Committee, the Compensation Committee, and the Corporate Governance Committee are, and are required by the charters of the respective committees to be, independent as determined under Nasdaq Listing rules.

Audit Committee. The Audit Committee is composed of Mr. Bjerkholt and Drs. Schwartz and Levy. The Audit Committee held four meetings during the fiscal year ended December 31, 2012. The primary function of the Audit Committee is to assist our Board in fulfilling its oversight responsibilities. The committee does this primarily by reviewing our financial reports and other financial information as well as the company’s systems of internal controls regarding finance, accounting, legal compliance, and ethics that management and the Board have established. The committee also assesses our auditing, accounting and financial processes more generally. The Audit Committee meets quarterly, and at such other times as it finds necessary. It recommends to our Board the appointment of a firm of independent auditors to audit the financial statements of the company and meets with such personnel of the company to review the scope and the results of the annual audit, the amount of audit fees, the company’s internal accounting controls, the company’s financial statements contained in this proxy statement and other related matters. Each of the members of the Audit Committee is independent, and the Board has determined that Mr. Bjerkholt is an audit committee financial expert, as defined in SEC rules. The Audit Committee acts pursuant to a written charter which is available through our website at www.stemcellsinc.com.

Compensation Committee. The Compensation Committee is composed of Drs. Schwartz and Levy and Mr. Bjerkholt. The Compensation Committee held five meetings during the fiscal year ended December 31, 2012. The Compensation Committee makes recommendations to our Board and management concerning salaries in general, determines executive compensation and, except to the extent that such decisions have been delegated to, and made by, the single-member committee, approves incentive compensation for our employees and consultants. The Compensation Committee acts pursuant to a written charter which is available through our website at www.stemcellsinc.com.

Corporate Governance Committee. The Corporate Governance Committee is composed of Drs. Levy, Perlmutter and Schwartz. The Corporate Governance Committee held one meeting in 2012 to discuss a slate of actual and potential nominees to the Board of Directors. The committee oversees nominations to the Board and considers the experience, ability and character of potential nominees to serve as directors, as well as particular skills or knowledge that may be desirable in light of the company’s position at any time. From time to time, the committee has engaged the services of a paid search firm to help the committee identify potential nominees to the Board. The Company’s Governance Committee and Board seek to nominate and appoint candidates to the Board who have significant business experience, technical expertise or personal attributes, or a combination of these,

sufficient to suggest, in the Board's judgment, that the candidate would have the ability to help direct the affairs of the company and enhance the Board as a whole. The Committee may identify potential candidates through any reliable means available, including recommendations of past or current members of the Board from their knowledge of the industry and of the company. The Committee also considers past service on the Board or on the board of directors of other publicly traded or technology focused companies. The committee has not adopted a formulaic approach to evaluating potential nominees to the Board; it does not have a formal policy concerning diversity, for example. Rather, the committee weighs and considers the experience, expertise, intellect, and judgment of potential nominees irrespective of their race, gender, age, religion, or other personal characteristics. The committee often looks for nominees that can bring new skill sets or diverse business perspectives. Potential candidates recommended by security holders will be considered as provided in the company's Policy Regarding Shareholder Candidates for Nomination as a Director, which sets forth the procedures and conditions for such recommendations. This policy is available through our website at www.stemcellsinc.com. The Corporate Governance Committee operates pursuant to a written charter, a copy of which is also available through our website at www.stemcellsinc.com. The members of the Corporate Governance Committee approved the nomination of the Class I directors standing for reelection at the Annual Meeting.

Strategic Transactions Committee. The Strategic Transactions Committee is composed of Messrs. Bjerkholt, Greer and McGlynn and Dr. Levy. The Strategic Transactions Committee held five meetings during the fiscal year ended December 31, 2012. The Committee was created at the suggestion of our Chief Executive Officer in March 2009 to provide advice and direction, on an *ad hoc* basis, on a range of strategic initiatives being considered at the time, such as the acquisition of substantially all of the operating assets of Stem Cell Sciences plc. The Committee does not have a formal charter. However, the Board of Directors has authorized the Committee to be available to advise, consult and participate with management, as requested by the company's Chief Executive Officer, with respect to the identification, implementation, evaluation, and negotiation of potential strategic corporate transactions, with the exception of financings. Since June 2010, the Strategic Transactions Committee has been the Board's fourth standing committee, and as such it routinely provides recommendations both to management and to the full Board with regard to such matters as the Committee may deem advisable.

The following table shows the members of our four standing Board committees:

Director	Independent	Audit Committee	Compensation Committee	Corporate Governance Committee	Strategic Transactions Committee
Eric Bjerkholt	Yes	Chair	ü		ü
R. Scott Greer	Yes				Chair
Ricardo Levy, Ph.D.	Yes	ü	ü	Chair	ü
Martin McGlynn	No				ü
Roger Perlmutter, M.D., Ph.D.	Yes			ü	
John Schwartz, Ph.D.	Yes	ü	Chair	ü	
Irving Weissman, M.D.	No				

Director Oversight and Qualifications

While management is responsible for the day-to-day management of the risks the company faces, the Board, as a whole and through its committees, has responsibility for the oversight of risk management. An important part of risk management is not only understanding the risks facing the company and what steps management is taking to manage those risks, but also understanding what level of risk is appropriate for the company. In support of this oversight function, the Board receives regular reports from our Chief Executive Officer and members of senior management on operational, financial, legal, and regulatory issues and risks. The Audit Committee additionally is charged under its charter with oversight of financial risk, including the company's internal controls, and it receives regular reports from management, the company's internal auditors and the company's

independent auditors. The Chairman of the Board and independent members of the Board work together to provide strong, independent oversight of the company's management and affairs through its standing committees and, when necessary, special meetings of directors.

We believe each of our directors brings valuable skills, experience, judgment, and perspectives to our company. The Board took the following qualifications into consideration, among other things, when nominating or appointing our current directors:

- | | |
|---------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Eric Bjerkholt | Mr. Bjerkholt is a financial expert and currently serves as the Executive Vice President and Chief Financial Officer of Sunesis Pharmaceuticals, Inc., a biopharmaceutical company. His business experience spans more than 20 years, during which time he founded a nutraceutical company and worked as an investment banker. Mr. Bjerkholt currently serves on the board of directors of Round Table Pizza. We believe Mr. Bjerkholt's qualifications to serve on our Board of Directors include his considerable financial and business experience, especially in the life sciences industry. Mr. Bjerkholt has served on our Board for over eight years. |
| R. Scott Greer | Mr. Greer was appointed to our Board in June 2010. He is a financial expert with over 25 years of experience in the life sciences industry. He was founder, CEO and Chairman of Abgenix, Inc., a biotechnology company he took public in 1998 and then sold to Amgen in 2006. Mr. Greer currently serves as Chairman of Ablexis, a development stage biotechnology company, and is also on the board of Nektar Therapeutics. We believe Mr. Greer's qualifications to serve on our Board include his more than 25 years of experience in the life sciences industry. |
| Ricardo Levy, Ph.D. | Dr. Levy has over 30 years of experience leading technology companies in both North and South America. In 1974, he cofounded Catalytica, Inc., a manufacturing technology and energy systems company, and served as CEO from 1991 until the company was sold in 2000. Dr. Levy currently serves as director of Accerlys Inc. (formerly Pharmacopeia, Inc.) and NovoDynamics, Inc. We believe his qualifications to serve on our Board of Directors include his more than 30 years of business experience. Dr. Levy has served on our Board for over twelve years. |
| Martin McGlynn | Mr. McGlynn has been our President and Chief Executive Officer since January 2001. He has held management positions of increasing responsibility in several countries for more than 30 years. Prior to joining our company, Mr. McGlynn was President and Chief Executive Officer of Pharmadigm, Inc., a privately held company in the fields of inflammation and genetic immunization. Prior to this, he was President and General Manager of Abbott Canada Ltd. and President of Anaquest, Inc., a company focused on anesthesia and acute care pharmaceuticals. We believe Mr. McGlynn's qualifications to serve on our Board of Directors include his significant managerial experience in our industry and his intimate knowledge of our operations as a result of his day to day leadership as our President and Chief Executive Officer. Mr. McGlynn has served on our Board for over twelve years. |

Roger Perlmutter, M.D., Ph.D.

Dr. Perlmutter is Executive Vice President of Merck & Co, an international pharmaceutical company, and President of Merck Research Laboratories, where he leads Merck's global research endeavors. Previously, until February 2012, Dr. Perlmutter was the Executive Vice President of Research and Development of Amgen, Inc., a world leading biotechnology company, a position he held for approximately eleven years. Prior to joining Amgen, he held scientific leadership positions of increasing responsibility at Merck. He also worked as a researcher and administrator at the University of Washington. We believe Dr. Perlmutter's pharmaceutical industry experience brings an important industry perspective to the Board. Dr. Perlmutter has served on our Board for over twelve years.

John Schwartz, Ph.D.

Dr. Schwartz has over 40 years of business and legal experience, including several years spent in the 1990s as President and Chief Executive Officer of Systemix, Inc., a cell-based therapeutics company which was acquired by Novartis in 1997. Before joining Systemix as its Senior Vice President and General Counsel in 1993, Dr. Schwartz served as the Vice President and General Counsel of Stanford University. He currently runs a registered investment advisor firm called Quantum Strategies Management Company. We believe Dr. Schwartz's qualifications to serve on our Board of Directors include his over 40 years of business and legal experience in our industry as well as his significant experience working at Stanford University. Dr. Schwartz has served on our Board for over fourteen years.

Irving Weissman, M.D.

Dr. Weissman has been a leader in the stem cell field for over 20 years. He is a professor at Stanford University and serves as the director of the Stanford Institute for Stem Cell Biology and Regenerative Medicine. He co-founded Systemix in 1988 and Cellerant Therapeutics, Inc., a hematopoietic stem cell development company, in 2001. He is a member of several scientific advisory boards and national science institutes, including the National Academy of Science, the American Academy of Arts and Science, and the Institute of Medicine of the National Academy of Sciences. We believe Dr. Weissman's qualifications to serve on our Board of Directors include the fact that he has been a leader in stem cell research for over 20 years as well as his substantial business experience in our industry. Dr. Weissman has served on our Board for over sixteen years and serves as the chairman of our Scientific Advisory Board.

Stockholders who wish to communicate with our Board of Directors or with a particular director may send a letter to our corporate secretary at the following address: StemCells, Inc., 7707 Gateway Blvd., Newark, California 94560 (c/o Legal Department). Any communication should clearly specify that it is intended to be made to the entire Board or to one or more particular director(s). Our corporate secretary will review all such correspondence and forward to our Board a summary of all such correspondence and copies of all correspondence that, in the opinion of the secretary, deals with the functions of the Board or committees thereof or that he otherwise determines requires their attention. The secretary maintains a log of all correspondence received by us that is addressed to members of the Board, and any director may at any time review and request copies of any such correspondence.

Concerns relating to accounting, internal controls or auditing matters will immediately be brought to the attention of the chairman of the Audit Committee and handled in accordance with established procedures, which are set out in the Audit Committee's Policy on Receipt, Retention and Treatment of Complaints Regarding Accounting, Internal Controls and Auditing Matters. A copy of this policy is available through our website at www.stemcellsinc.com.

Executive Officers, Positions Held

Following are the name, age and other information for our named executive officers, as of October 15, 2013. All company officers have been elected to serve until their successors are elected and qualified or until their earlier resignation or removal.

<p>Martin McGlynn</p> <p>President and Chief Executive Officer</p>	<p>67</p>	<p>Martin McGlynn joined the company in January 2001, when he was appointed President and Chief Executive Officer of the company and of its wholly-owned subsidiaries. Mr. McGlynn was elected to the Board of Directors in February 2001.</p>
<p>Rodney Young</p> <p>Chief Financial Officer and Vice President, Finance and Administration</p>	<p>51</p>	<p>Rodney Young joined the company in September 2005 as Chief Financial Officer and Vice President, Finance. In November 2006 he became CFO and Vice President, Finance and Administration. He is responsible for functions that include Finance, Information Technology and Investor Relations. From 2003 to 2005, Mr. Young was Chief Financial Officer and a director of Extropy Pharmaceuticals, Inc., a private biopharmaceutical company focused on developing drugs for pediatric indications.</p>
<p>Eliseo Salinas, M.D.</p> <p>Executive Vice President, Head of Research and Development</p>	<p>57</p>	<p>Eliseo Salinas, M.D., joined the company in June 2013 as Executive Vice President and Head of Research and Development, with responsibility for the company's scientific and clinical development programs. Prior to joining StemCells, Dr. Salinas served as Executive Vice President, Head of Development, and Chief Medical Officer of Elan Pharmaceuticals. Before joining Elan, Dr. Salinas was Senior Vice President, Research and Development and Chief Medical Officer of Adolor Corporation; Executive Vice President, Specialty Pharma, Research and Development and Chief Scientific Officer of Shire plc.</p>

<p>Stewart Craig, Ph.D. Executive Vice President, Development and Operations</p>	<p>52</p>	<p>Stewart Craig, Ph.D., joined the company in September 2008 with responsibilities for Development, Manufacturing, Regulatory, Quality Systems, and Facilities. From 2005 to 2008, Dr. Craig was Chief Technology Officer and Vice President of Progenitor Cell Therapy, a contract services provider for research, development, manufacture, and commercialization of cell-based therapies, prior to which he has held executive positions at Xcyte Therapies, Osiris Therapeutics and SyStemix.</p>
<p>Ann Tsukamoto, Ph.D. Executive Vice President, Scientific and Strategic Alliances</p>	<p>61</p>	<p>Ann Tsukamoto, Ph.D., joined the company in November 1997 as Senior Director of Scientific Operations; was appointed Vice President, Scientific Operations in June 1998; Vice President, Research and Development in February 2002; Chief Operating Officer in November 2006; and Executive Vice President, Research and Development, in October 2008. In June 2013, Dr. Tsukamoto was appointed Executive Vice President, Scientific and Strategic Alliances, with responsibility for developing the Company's alliances with research institutions, corporations, government agencies, and disease foundations. Dr. Tsukamoto is married to one of our outside directors.</p>
<p>Ken Stratton, J.D. General Counsel</p>	<p>45</p>	<p>Ken Stratton, J.D., joined the company in February 2007 as General Counsel, with responsibility for corporate compliance and legal affairs. In March 2008, he assumed responsibility for the Human Resources function. Prior to joining StemCells, Mr. Stratton served as Deputy General Counsel for Threshold Pharmaceuticals and as Senior Legal Counsel for Medtronic, Inc.'s Vascular business unit.</p>

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act of 1934, as amended (the Exchange Act), requires our executive officers, directors, and persons who own more than 10% of a registered class of our equity securities, to file with the SEC reports of ownership of our securities and changes in reported ownership. Executive officers, directors and greater than 10% beneficial owners are required by SEC rules to furnish us with copies of all Section 16(a) reports they file. Based solely on a review of the copies of such forms furnished to us, or written representations from the reporting persons that no Form 5 was required, we believe that, during the fiscal year ended December 31, 2012, all Section 16(a) filing requirements applicable to our officers, directors and greater

than 10% beneficial owners have been met, with the following exception: the Form 4 filed by Dr. Levy on October 2, 2012, reporting his annual equity grant for Board service, was filed two days late.

Code of Business Conduct and Ethics

We have adopted a Code of Ethics and Conduct that applies to all of our directors, officers, employees, and consultants. A copy of our code of ethics is posted on our website at www.stemcellsinc.com. We intend to disclose any substantive amendment or waivers to this code on our website. There were no substantive amendments or waivers to this code in 2012.

EXECUTIVE COMPENSATION

Compensation Discussion and Analysis

We structure our compensation programs to attract and retain talented employees and reward them for helping us achieve our short-term and long-term goals. We intend for our compensation programs to be equitable and competitive when measured against those offered by companies against whom we compete for high-level scientific and executive personnel. We also intend for them to link pay to both company and individual performance.

In seeking to accomplish these objectives, we follow a compensation strategy designed, ultimately, to reward increasing stockholder value. However, because achievement of our principle mission—the research, development and commercialization of stem cell therapeutics and related tools and technologies for academia and industry—is a long, expensive and challenging process, we often set individual compensation by using surrogate endpoints to gauge employee contributions towards building sustained stockholder value, such as:

the achievement of stated corporate goals adopted from time to time by the Board;

the leadership an executive officer has shown in inspiring and marshaling excellent performances in his or her direct reports;

the anticipation, identification and successful disposition of issues and problems that, if not addressed timely and effectively, might have a deleterious effect on the company; and

the speed and effectiveness with which an executive officer discovers, assesses and, where appropriate, pursues promising opportunities for the company.

Compensation elements. We, like most biotechnology companies, use a combination of base salary, bonuses and equity awards to compensate our employees, including our executive officers. As a small company—we have approximately 50 employees in total and only six executive officers—we feel that having so few people in each job classification and level makes it inefficient to establish a formulaic allocation of total compensation among its various elements; we rely, instead, on our experience and judgment.

In exercising this judgment, we periodically collect and review information (i) from third party market reports such as the *Radford Biotechnology Survey Executive Report*; and (ii) from the proxy statements of other similar biotechnology companies, especially those operating in the San Francisco Bay Area, as well as

those pursuing cell-based therapeutics.¹ In the case of the executive officers who report directly to the chief executive officer, we also carefully consider the recommendations of the chief executive officer when setting compensation. We integrate all of this information with our evaluation of the individual performance of each of our executive officers.

While we believe our officers and other employees are outstanding, we realize that the company is not yet profitable and that it is still in a relatively early stage of development. We therefore generally prefer to target our compensation practices so that our employees' base salaries, bonuses, equity compensation, and benefits all fall close to the 50th percentile paid by comparable companies for similar positions. Actual compensation may fall slightly above or below these targets, however, because of any number of factors such as general economic conditions, market competition for specific jobs, personal performance, and the need for internal equities within the company. For example, we have recently paid many of our employees, including some of our executive officers, at below the 50th percentile because of the recent global recession and crisis in the financial markets. At the same time, however, we have paid many of our employees, including some of our executive officers, at above the 50th percentile because of highly competitive demand for workers with their unique skill sets.

Interaction of compensation elements. The basic compensation elements—base salary, bonuses and equity awards—are, as noted, standard in our industry. Though not set independently of one other, we use each element as a portion of total compensation because we believe we would not otherwise be competitive and because we feel that together they are the proper components of a balanced compensation package:

base salary is compensation for current efforts;

bonuses, whether in cash or equity, are paid at the Board's discretion typically for achievements in meeting or exceeding corporate goals; and

equity awards are inducements to remain with the company and to build future value.

On occasion, we have considered our employee compensation programs, including our executive compensation programs, and the effect they may have on company risk. We have concluded that our employee compensation programs are simple and straight-forward and consistent with those of similarly situated research and development companies. In determining that our compensation policies and practices do not present risks that are likely to have a material adverse effect on our business, our directors have, from time to time, discussed with management the various pay practices used to compensate our employees at both the executive and non-executive levels. These inquiries have included discussions about our three primary components of compensation, namely base compensation, cash bonuses and equity incentive compensation.

Our Board of Directors has also periodically considered how bonus awards are determined and calculated by the company, noting that all bonuses are awarded entirely at the discretion of our Board after taking into consideration the progress of our company's programs. Based on its review, our Board has concluded that our bonus program properly aligns compensation with our overall goals, all of which are designed to have a positive impact on our business.

In addition, our Board has periodically examined our equity compensation practices, noting that we typically grant customary equity awards that vest over many years after the date of grant. We believe

¹ In 2012, for example, we collected executive compensation information from the recent SEC filings of Aastrom Biosciences, Inc.; Affymax, Inc.; Alexza Pharmaceuticals, Inc.; Anacor Pharmaceuticals, Inc.; Athersys, Inc.; Cerus Corporation; Cytokinetics, Incorporated; Cytori Therapeutics, Inc.; Dynavax Technologies Corporation; Geron Corporation; InterMune, Inc.; MAP Pharmaceuticals, Inc.; Maxygen, Inc.; Medivation, Inc.; Neuralstem, Inc.; Osiris Therapeutics, Inc.; Rigel Pharmaceuticals, Inc.; Sangamo Biosciences, Inc.; and Sunesis Pharmaceuticals, Inc.

discretionary equity compensation that vests over multiple years does not encourage short-term or high-risk opportunistic behavior and instead aligns our employees' interests with the long-term interests of our stockholders by encouraging activities intended to build long-term value for the Company.

For these reasons, we have concluded that our employee compensation programs are designed with the appropriate balance of risk and reward in relation to our company's overall business strategy and do not incentivize executives or other employees to take unnecessary or excessive risks. As a result, we believe that risks arising from our employee compensation policies and practices are not reasonably likely to have a material adverse effect on the company.

Other compensation elements and benefits. We offer all employees various health and welfare benefit plans. Our executive officers may participate in these on the same terms as other employees. We do not have a pension plan nor do we use non-qualified deferred compensation.² We offer our U.S. employees (again, including executive officers on the same terms as others) a 401(k) defined contribution plan, and match employee contributions on a 1:2 basis (*i.e.*, \$1 contribution by the company for every \$2 contribution made by the employee) up to a maximum of 3% of the employee's salary, subject to legal limitations. At this time, our 401(k) match is made in the form of shares of common stock in the company. We offer our U.K. employees a tax preferred pension scheme, and match employee contributions on a 1:1 basis up to a maximum of 12% of the employee's salary.

Compensation of Named Executive Officers

Base salary compensation; target bonuses. We consider base salary to be a critical component of our executive officers' overall compensation packages. We intend the salaries of our executive officers to reflect their actual responsibilities and job scope. We also endeavor to set base compensation levels so that their salaries are competitive with salaries paid by comparable companies to employees with similar experience, taking into account the cost of living in the San Francisco Bay Area. Accordingly, we have made occasional adjustments to the salaries of certain employees to address perceived below market anomalies, address specific retention concerns or reward special contributions made to the company. As described below, we changed the base compensation paid to certain of our executive officers in 2009, 2010, 2012, and 2013.

In addition to base salary, each full-time employee of the company, including each of our named executive officers, is given a personal target bonus (calculated as a percentage of base salary), based upon factors such as seniority, job title and the existing targets of co-workers with comparable job responsibilities within the company. Bonuses at the company are discretionary and awarded by the Board in its sole discretion. But when bonuses are awarded, we use the personal target of each employee to calculate his or her bonus amount.

With these various principles in mind, we recently took the following actions with respect to the base compensation and bonus targets of our executive officers.

From March 2007 through 2008, we maintained the annual base salary of Mr. McGlynn at \$385,000, plus a housing and transportation allowance. Effective January 2009, however, we eliminated Mr. McGlynn's housing and transportation allowance of approximately \$200,000 per year and increased Mr. McGlynn's annual base salary by \$140,000, from \$385,000 to \$525,000, and began providing him a car allowance in the amount of \$10,000 per year. The net effect of these changes was a decrease in Mr. McGlynn's base compensation of approximately 11% for 2009. Concurrent with these changes, we increased Mr. McGlynn's target bonus from 40 percent to 55 percent of his base salary, beginning with the 2009 fiscal year, to reflect the Board's view that Mr. McGlynn's leadership is a major factor in the achievement of the company's corporate goals and to further

² Accordingly, we omit tables showing pension benefits and non-qualified deferred compensation.

align his compensation to corporate success. Effective February 1, 2012, we increased Mr. McGlynn's base salary to \$550,000. More recently, effective June 17, 2013, we increased Mr. McGlynn's base salary to \$570,000 in recognition of contributions made on behalf of the company and market factors.

From March 2007 through 2009, we maintained the annual base salary of Mr. Young at \$275,000. In January 2010, however, we increased Mr. Young's annual base salary to \$325,000 in recognition of contributions made on behalf of the company and job scope. In January 2010, we also increased Mr. Young's target bonus rate from 25% to 30% of his base salary, beginning with the 2010 fiscal year, to further align his compensation to corporate success. In February 2011, we increased Mr. Young's target bonus rate from 30% to 40% of his base salary for the same reason.

From March 2007 through 2011, we maintained the annual base salary of Dr. Tsukamoto at \$300,000. In January 2010, however, we increased Dr. Tsukamoto's target bonus from 25% to 30% of her base salary, beginning with the 2010 fiscal year, to further align her compensation to corporate success. In February 2011, we increased Dr. Tsukamoto's target bonus rate from 30% to 40% of her base salary for the same reason. Effective February 1, 2012, we increased Dr. Tsukamoto's base salary to \$335,000 in recognition of contributions made on behalf of the company and market factors. More recently, effective June 6, 2013, we increased Dr. Tsukamoto's base salary to \$350,000 in recognition of contributions made on behalf of the company, market factors and her new role and responsibilities as executive vice president of scientific and strategic alliances.

Dr. Craig joined the company in September 2008, with an annual base salary of \$275,000 and a target bonus rate of 25% of his base salary. In January 2010, however, we increased Dr. Craig's target bonus from 25% to 30% of his base salary, beginning with the 2010 fiscal year, to further align his compensation to corporate success. In February 2011, we increased Dr. Craig's target bonus rate from 30% to 40% of his base salary for the same reason. Effective February 1, 2012, we increased Dr. Craig's base salary to \$300,000. More recently, effective June 17, 2013, we increased Dr. Craig's base salary to \$320,000 in recognition of contributions made on behalf of the company and market factors.

Mr. Stratton joined the company in February 2007, with an annual base salary of \$220,000 and a target bonus rate of 20% of his base salary. In February 2008, however, we increased Mr. Stratton's annual base salary to \$250,000 in recognition of contributions made on behalf of the company and because he had assumed additional responsibilities in early 2008. In January 2010, we increased Mr. Stratton's annual base salary to \$275,000 in recognition of contributions made on behalf of the company and job scope. In January 2010, we also increased Mr. Stratton's target bonus rate from 20% to 30% of his base salary, beginning with the 2010 fiscal year, to further align his compensation to corporate success. In February 2011, we increased Mr. Stratton's target bonus rate from 30% to 40% of his base salary for the same reason. Effective February 1, 2012, we increased Mr. Stratton's base salary to \$300,000. Most recently, effective June 17, 2013, we increased Mr. Stratton's base salary to \$320,000 in recognition of contributions made on behalf of the company and market factors.

Dr. Salinas joined the company in June 2013, with an annual base salary of \$475,000 and a target bonus rate of 50% of his base salary.

The base compensation and target bonus information presented above can be summarized as follows:

	Year Ended 12/31/09 Base Compensation/ Target Bonus	Year Ended 12/31/10 Base Compensation/ Target Bonus	Year Ended 12/31/11 Base Compensation/ Target Bonus	Year Ended 12/31/12 Base Compensation/ Target Bonus	Current Base Compensation/ Target Bonus
CEO	\$ 525,000/55%	\$ 525,000/55%	\$ 525,000/55%	\$ 550,000/55%	\$ 570,000/55%
CFO	\$ 275,000/25%	\$ 325,000/30%	\$ 325,000/40%	\$ 325,000/40%	\$ 325,000/40%
EVP, R&D(1)					\$ 475,000/50%
EVP, D&O	\$ 275,000/25%	\$ 275,000/30%	\$ 275,000/40%	\$ 300,000/40%	\$ 320,000/40%
EVP, Alliances(2)	\$ 300,000/25%	\$ 300,000/30%	\$ 300,000/40%	\$ 335,000/40%	\$ 350,000/40%
GC	\$ 250,000/20%	\$ 275,000/30%	\$ 275,000/40%	\$ 300,000/40%	\$ 320,000/40%

- (1) The company's executive vice president and head of research and development joined the company in June 2013.
- (2) The company's executive vice president of scientific and strategic alliances served as the company's executive vice president of research and development from October 2008 until June 2013.

Bonus compensation. We view periodic bonuses, whether paid in cash or equity, as an important element of compensation for several reasons. Bonuses help align individual employee efforts with overall corporate strategies and objectives. Bonuses also help us manage salary expense, while still allowing us to reward successes. By using discretionary bonuses as part of the compensation mix, we have greater flexibility in managing the timing and amounts of compensation. Accordingly, each year we estimate for planning purposes an aggregate bonus pool, which is calculated by using the base salaries of all our full-time employees and their respective target bonuses, and which assumes the Board will elect to award each full-time employee 100% of his or her personal target bonus amount for the year. However, as explained below, the actual bonus award for any particular year is entirely within the Board's discretion.

In practice, over the past few years, we have awarded bonuses on an annual basis after considering, among other things, the company's accomplishments against stated corporate goals adopted by the Board, the company's financial position, the status of its development programs, clinical progress and corporate development activities, and general economic factors. This has necessarily involved a subjective assessment by the Compensation Committee of corporate performance and market conditions each year.

The process of establishing our corporate goals over the past few years has been a lengthy one. For each fiscal year, our executive officers have presented the Compensation Committee of the Board with approximately five to ten proposed corporate goals, each often consisting of multiple sub-parts. Management has usually presented its recommended corporate goals to the Compensation Committee concurrent with our proposed corporate budgets for the following fiscal year. Goals have been designed to be challenging, so that one would not expect consistent achievement of all of them. Typically these goals have included some preclinical and clinical goals for our HuCNS-SC cell product candidate, financing and corporate development goals, goals related to advancement in cell manufacturing practices, and goals related to advancement of our Liver Program. While all these goals have been considered important, and we have used a cross-functional and balanced approach to setting them, we have typically prioritized our goals by assigning relative weightings to each of them, with all of them together adding up to 100%. However, by design, no one goal has ever accounted for a majority of the relative weightings.

After receiving management's recommended goals, members of the Compensation Committee typically review them with our executive officers and oftentimes provide suggestions for additional goals or changes to the recommended goals. After our executive officers and directors have completed this iterative process, which has often taken several weeks, the Compensation Committee adopts revised corporate goals consistent with the foregoing principles and recommends the updated corporate goals to the full Board for consideration and approval.

Thereafter, during each fiscal year, our executive officers have used the Board-approved corporate goals as a management tool, for example to coordinate activities, motivate personnel and help prioritize the use of company resources. The executive officers have sometimes referred back to the corporate goals when providing business updates to the Board, similar to management's reference back to an approved annual budget.

Recently, at the end of each fiscal year or shortly afterwards, our Chief Executive Officer has presented the Compensation Committee with his assessments of corporate performance against the Board-approved corporate goals, together with a summary of any important factors that weighed in his assessments, which he has provided as context.

Because our corporate goals have not been formulaic or quantitative in nature (we have not had a corporate goal tied to specific stock price, revenues or expenses, for example), our CEO's assessments have been largely qualitative in nature. Along with these assessments, our CEO has provided a percentage score for each goal reflecting the degree to which each goal was or was not, in his judgment, achieved during the year.

The Compensation Committee has usually considered these percentage scores as well as our CEO's commentary about corporate performance and more general assessments of the state of our business when determining whether to award employees a company-wide corporate bonus in any given year, and if so how much of the available bonus pool to award. However, the Compensation Committee members have used their own judgment to determine the size of any bonus award, if any. In any given year, the Board may decide in its judgment to award more than 100% of the bonus pool for the year. The Board may also decide to award less than 100% of the bonus pool, even if all of the corporate goals have been achieved, if it decides doing so would be in the best interests of the company. While the Compensation Committee and the Board as a whole use the corporate goals as a measure of success, the amount of any bonus grant, as well as how and when it will be paid, is completely within the Board's sole discretion.

With these various principles in mind, we recently took the following actions with respect to corporate bonuses for 2012.

In December 2012, as part of its annual year-end review of performance, the Compensation Committee (with input from the Chief Executive Officer and other Board members) considered, among other things, significant company performance accomplishments in 2012, the company's successes measured against its 2012 corporate goals, the degree of difficulty in achieving these goals, as well as other events and circumstances that affected performance. The 2012 goals, as approved by our Board, consisted generally of the following: (i) progress in our CNS Program, including activities aimed at testing our proprietary HuCNS-SC cells in multiple disease indications within the CNS, including the initiation of a study of HuCNS-SC cells in age related macular degeneration, the dosing of additional patients in our spinal cord injury trial, and preparation for initiating a Phase II controlled study in Pelizaeus-Merzbacher disease; (ii) partnering and corporate development activities; and (iii) successful fundraising efforts.

Highlights of the 2012 accomplishments taken into account by the Compensation Committee in determining the overall company performance included:

Therapeutic Product Development

In January 2012, we published preclinical data demonstrating that our proprietary HuCNS-SC cells protect host photoreceptors and preserve vision in a well-established animal model of retinal disease. Moreover, the number of cone photoreceptors, which are responsible for central vision, remained constant over an extended period. In humans, degeneration of the core photoreceptors accounts for the unique pattern of vision loss in dry AMD. The data was featured as the cover article in the peer-reviewed *European Journal of Neuroscience*.

Also in January 2012, the FDA authorized the initiation of a Phase I/II clinical trial of our proprietary HuCNS-SC cells in dry AMD, the most common form of AMD. AMD is the leading cause of vision loss and blindness in people over 55 years of age, and approximately 30 million people worldwide are afflicted with the disease. There are no approved treatments for dry AMD.

In February 2012, the fourth and final patient in our Phase I PMD trial completed the twelve-month follow up and evaluations required by the trial protocol, and the trial was completed.

In April 2012, we presented preliminary evidence of progressive and durable donor-cell derived myelination in all four patients who were transplanted with our proprietary HuCNS-SC cells in our Phase I clinical trial for PMD, a rare hypomyelination disorder in children. In addition, clinical assessment revealed small but measureable gains in motor and/or cognitive function in three of the four patients; the fourth patient remained clinically stable. The study was conducted by researchers at the University of California, San Francisco (UCSF). A summary of the trial results were presented at the 2012 European Leukodystrophy Association (ELA) *Families/Scientists Meeting* in Paris, France.

In May 2012, we presented data from the first interim safety review of our Phase I/II spinal cord injury clinical trial, which indicated that the surgery, immunosuppression and the HuCNS-SC cell transplants have been well tolerated. The trial, which was designed to evaluate the safety and preliminary efficacy of our proprietary HuCNS-SC cells, represents the first time that neural stem cells have been transplanted as a potential therapeutic agent for spinal cord injury. A summary of the data was presented at the Interdependence 2012 Global SCI Conference in Vancouver, Canada.

In June 2012, we initiated our Phase I/II clinical trial of our proprietary HuCNS-SC cells in dry AMD. The trial is being conducted at the Retina Foundation of the Southwest (RFSW) in Dallas, Texas, and at the Byers Institute at Stanford.

In July 2012, we presented preclinical data demonstrating that our proprietary human neural stem cells restored memory and enhanced synaptic function in two animal models relevant to Alzheimer's disease. Importantly, these results did not require reduction in beta amyloid or tau, substances that accumulate in the brains of patients with Alzheimer's disease and account for the pathological hallmarks of the disease. The data was presented at the *Alzheimer's Association International Conference 2012* in Vancouver, Canada.

In July 2012, the governing board of the California Institute for Regenerative Medicine (CIRM) approved an award to us for up to a \$20 million under the Disease Team Therapy Development Award program (RFA 10-05) to fund preclinical development of our HuCNS-SC cells in cervical spinal cord. Under RFA 10-05, funding would have been in the form of a forgivable loan. However, in March 2013, we elected not to borrow these funds from CIRM.

Also in July 2012, the Japan Patent Office granted us Patent Number 5007003 which broadly covers the prospective isolation and enrichment of neural stem and progenitor cells using antibody selection, as well as the use of these cells to treat disorders of the central nervous system. Some of the more noteworthy claims in this patent include methods for isolating human neural stem cells, as well as compositions of matter comprising enriched neural stem cells, such as our proprietary HuCNS-SC cells, and the use of enriched neural stem cells as a medicament for the treatment of neurodegenerative diseases, acute brain injury and dysfunction of the central nervous system. The term of this patent extends into 2020.

In September 2012, we presented interim six-month data from the first patient cohort in our Phase I/II clinical trial of our HuCNS-SC cells for chronic spinal cord injury. The first patient cohort all have no sensory or motor function below the level of injury and are considered to have complete spinal cord

injuries. The interim data continues to demonstrate a favorable safety profile, and showed considerable gains in sensory function in two of the three patients compared to pre-transplant baselines; the third patient remained stable. The data was presented at the *51st Annual Scientific Meeting* of the International Spinal Cord Society in London, England.

Also in September 2012, the first patient with an incomplete spinal cord injury was enrolled and dosed in our Phase I/II clinical trial in chronic spinal cord injury. Patients who retain some sensory function below the level of trauma are considered to have an incomplete injury.

Also in September 2012, the governing board of CIRM approved a second disease team award to us for up to \$20 million under RFA 10-05. This second award is to fund preclinical development of our HuCNS-SC cells in Alzheimer's disease.

In October 2012, the first patient in our Phase I/II clinical trial in dry age-related macular degeneration (AMD) was enrolled and dosed.

In October 2012, two papers reporting clinical and preclinical data demonstrating the therapeutic potential of our proprietary HuCNS-SC cells for a range of myelination disorders were published in *Science Translational Medicine*, the peer-reviewed journal of the American Association for the Advancement of Science. The first paper summarized the data from our Phase I trial in Pelizaeus-Merzbacher disease (PMD), which showed preliminary evidence of progressive and durable donor cell-derived myelination in all four patients transplanted with HuCNS-SC cells. Three of the four patients showed modest gains in neurological function; the fourth patient remained stable. The second paper demonstrated that transplantation of our neural stem cells in an animal model of severe myelin deficiency results in new, functional myelin. Sophisticated analytical techniques were used to confirm that changes measured by magnetic resonance images were in fact derived from new human myelin generated by the transplanted HuCNS-SC cells and these results supported the use of similar techniques to detect and evaluate the degree of myelination in our Phase I PMD trial.

Also in October 2012, we were issued U.S. Patent Number 8,283,164 which broadly covers purified populations of human liver cells, including our human liver engrafting cells (hLEC). The hLEC cells were first isolated by our researchers in the late 1990s, and our scientists have repeatedly demonstrated the cells' engraftment and robust bioactivity *in vivo* and that they are expandable. While our hLEC cells are purified from donated adult livers not suitable for transplant, the newly issued 164 patent claims cells independent of tissue source, and therefore, has potential relevance to those deriving liver cells from induced pluripotent or embryonic stem cell platforms. The term of the 164 patent extends into 2022.

Tools and Technologies Programs

In March 2012, we entered into a license agreement under which we granted genOway a worldwide, exclusive license to our Internal Ribosome Entry Site (IRES) technology for use in the development and commercialization of genetically engineered mice. We received an upfront license fee and could receive royalties on product sales.

In October 2012, we launched four new SC Proven human neural stem cell kits for use in neuroscience research. Each kit will contain high purity, multipotent neural stem cells derived from a different area of the human central nervous system, and will provide researchers with a reproducible and scalable serum-free platform with which to perform a broad range of assays. With these kits, researchers will now have the ability to compare and contrast the biological, functional and neural differentiation properties of human neural stem cells isolated from specific regions of the central nervous system, as well as to screen for the effects of different compounds on such cells.

Also in October 2012 we partnered with a UK-based biomedical company to develop and commercialize a range of cell lines and reagents to facilitate iPS cell-based research for regenerative medicine applications. The first product under the partnership, an ultra-primary human fibroblast cell line from which researchers can generate iPS cell lines, was launched under the SC Proven brand.

Financing and Other Business-related Activities

In 2012, we sold an aggregate of 9,647,471 shares of our common stock for gross proceeds of approximately \$20,452,000. These sales were made under a sales agreement entered into in June 2009 and the sales agent was paid compensation equal to 3% of gross proceeds. The shares were offered under our shelf registration statement previously filed with, and declared effective by, the SEC.

In 2012, an aggregate of 2,700,000 Series B Warrants were exercised and we received gross proceeds of \$3,375,000. The remaining 5,300,000 Series B Warrants expired unexercised by their terms on May 2, 2012. For the exercise of these warrants, we issued 2,700,000 shares of our common stock and 2,700,000 Series A Warrants.

In 2012, an aggregate of 2,198,571 Series A Warrants were exercised. For the exercise of these warrants, we issued 2,198,571 shares of our common stock and received gross proceeds of approximately \$3,078,000.

Following this review, the Compensation Committee awarded a discretionary bonus equal to 70% of the available bonus pool, based upon the committee members' assessments of market conditions, corporate risks, our market comparables, and the company's performance in 2012 measured against its 2012 corporate goals, including the successes highlighted above, among other things. The bonuses were calculated using each employee's annual base salary as of January 1, 2012, and paid in January 2013.

Accordingly, in January 2013, the company paid Mr. McGlynn a 2012 bonus in the amount of \$202,125, because on January 1, 2012 his base salary and target bonus were, respectively, \$525,000 and 55%. The company paid Mr. Young a 2012 bonus in the amount of \$91,000, because on January 1, 2012 his base salary and target bonus were, respectively, \$325,000 and 40%, and the company paid Dr. Tsukamoto a 2012 bonus in the amount of \$84,000, because on January 1, 2012 her base salary and target bonus were, respectively, \$300,000 and 40%. The company also paid Dr. Craig and Mr. Stratton each a 2012 bonus in the amount of \$77,000, because on January 1, 2012 their base salary and target bonus were, respectively, \$275,000 and 40%.

Equity Compensation general practices. We believe that equity compensation awards are an important component of our overall compensation policy because equity compensation can provide strong inducement to remain with the company and to build future stockholder value. In order to achieve these objectives, we believe that equity compensation awards need to be structured to provide both meaningful value and a meaningful opportunity to realize that value. Accordingly, from time to time, we have considered several forms of equity compensation awards, including stock options, stock appreciation rights, restricted stock, and restricted stock units, because each of these have certain advantages and disadvantages relative to the others with respect to how they might reward effort and success and how they might help us retain high contributors. Generally speaking, over the years, we have used stock options and restricted stock units as the most common equity compensation instruments. We feel each of these forms of equity has unique and important features for employee retention and for incentivizing the executive officers to build a profitable and sustainable business. Unless otherwise specifically noted in the tables herein, all option awards:

to our employees, including our executive officers, are intended to be qualified incentive stock options (ISOs) to the fullest extent permitted by law;

have an exercise price set at the closing market price of our common stock on the grant date, or on an adjacent market trading date if the market on which we are listed (currently the Nasdaq Capital Market) is not open on the grant date; and

vest over four years, with one-fourth of the shares included in any grant vesting on the first anniversary of the grant and the remainder vesting 1/48th per month thereafter, always provided that the grantee remains in the company's employ on the vesting dates. These awards are time-vesting and do not depend on performance factors.

We have typically granted stock option awards to newly hired employees, effective as of their date of hire, and occasionally to existing employees upon their promotion. Both on-hire awards to non-executive officers and awards upon the promotion of current employees are usually made by either Mr. McGlynn, acting as the Board's single-member committee, or by the Compensation Committee. Awards to executive officers are made by either the Compensation Committee or by the full Board. We have not granted company-wide equity awards to full-time employees since June 2010. Instead, we have granted targeted equity awards to individual employees within the company following a careful review of equity held by each of our employees and the retention value that such awards may provide. In awarding equity grants to existing employees, we consider their contributions to the company, their roles and responsibilities, their past performance, and market conditions generally for similarly situated employees.

With these various principles in mind, we recently took the following actions with respect to equity compensation.

In June 2010, after a review of the market and company-specific information described above, the Compensation Committee approved a company-wide award to employees of 190,000 restricted stock units and options to purchase up to 184,500 shares of common stock, in the aggregate. Of particular importance, the Compensation Committee noted that a majority of the stock options previously issued to employees had strike prices significantly above the current market price of the company's stock and were therefore of limited retention value. All of the restricted stock units awarded in June 2010 have four-year vesting, with one-fourth vesting on each of the first four anniversaries following the grant date, except for the restricted stock units granted to Mr. McGlynn and Dr. Tsukamoto, each of which has three-year vesting, with one-third vesting on each of the first three anniversaries following the grant date. All of the options awarded at this time will vest one-fourth on the first anniversary following the grant and then 1/48th each month thereafter, in keeping with the company's standard practices. In this June 2010 grant, our named executive officers received, in the aggregate, 250,000 restricted stock units and options to purchase up to 265,000 shares of common stock. In September 2010, Mr. McGlynn voluntarily surrendered his rights and interests in 20,000 restricted stock units from this June 2010 grant in order to bring his grant into accordance with the provisions of the company's equity incentive plan under which the grant was made.

In January 2011, we awarded Mr. McGlynn 20,000 additional restricted stock units in recognition of his service and importance to the company's long-term goals.

In January 2012, after a review of the market and company-specific information described above, the Compensation Committee approved a targeted award of 1,231,000 restricted stock units, in aggregate, to certain employees considered to be key contributors with leadership roles within the company and therefore most likely to have a direct role in building stockholder value. Of particular importance, the Compensation Committee noted that a majority of the stock options issued to employees had strike prices significantly below the current market price of the company's stock and were therefore of limited retention value. All of the restricted stock units awarded at this time have four-year vesting, with one-fourth vesting on each of the first four anniversaries

following the grant date, except for the restricted stock units granted to Mr. McGlynn and Dr. Tsukamoto, each of which has three-year vesting, with one-third vesting on each of the first three anniversaries following the grant date. In this January 2012 grant, our named executive officers received, in the aggregate, 796,000 restricted stock units.

In August 2012, all of our executive officers decided to voluntarily surrender certain of their stock option awards under our 2004 and 2006 equity incentive plans, so that the option shares would be available for future grants under these plans. Collectively, the executive officers surrendered both vested and unvested options to acquire a total of 297,336 shares.

The following table summarizes the restricted stock units awarded to our named executive officers in June 2010, January 2011, and January 2012:

Name & Principal Position	Number of Restricted Stock Units Granted(1)		
	June 2010	January 2011	January 2012
Martin McGlynn President and CEO	100,000(2)	20,000	406,000
Ann Tsukamoto, Ph.D. EVP, Alliances	70,000		130,000
Rodney Young CFO and VP, Finance & Administration	20,000		
Stewart Craig, Ph.D. EVP, Development & Operations	20,000		130,000
Ken Stratton, J.D. General Counsel	20,000		130,000

(1) All share numbers reported on a post-split adjusted basis.

(2) Mr. McGlynn was granted 120,000 restricted stock units in June 2010, however, he voluntarily surrendered 20,000 of these in September 2010 in order to bring his grant into accordance with the provisions of the company's equity incentive plan under which the grant was made.

In December 2012, our Compensation Committee engaged The Croner Company, an executive compensation consultancy firm referred to us by our outside corporate counsel, to advise the Committee on setting a compensation peer group for the purpose of evaluating the different components of compensation paid to our chief executive officer. During the first half of 2013, our Compensation Committee held six meetings, many of which were attended by representatives from The Croner Company, to discuss a variety of recommendations made by The Croner Company, including a recommendation that the company establish a new equity incentive plan. The Compensation Committee also discussed with representatives from both management and The Croner Company a possible peer group for evaluating executive compensation market practices. After considerable discussion and a review of peer information requested by the Committee, we agreed upon a peer group consisting of fifteen (15) publicly traded companies as being closely comparable to the company because of such business factors as location, nature of operations, industry, and size.³

Since these deliberations, and after consideration of our peer group's compensation practices, we have granted a number of equity awards to our executive officers and to other key employees. In May and June 2013, for example, we awarded a total of 1,120,000 million restricted stock units, each with four-year vesting, to key employees, including grants of 280,000 restricted stock units to each of Drs. Tsukamoto, Craig and Mr. Stratton.

³ By June 2013, the company considered the following companies as being close comparables for purposes of evaluating executive compensation: Aastrom Biosciences, Inc.; Advanced Cell Technology, Inc.; Athersys, Inc.; BioCryst Pharmaceuticals, Inc.; BioTime, Inc.; Cel-Sci Corporation; Cytokinetics, Incorporated; Cytori Therapeutics, Inc.; Geron Corporation; Medicinova, Inc.; Neostem, Inc.; Neuralstem, Inc.; Nova Bay Pharmaceuticals, Inc.; Osiris Therapeutics, Inc.; and Sangamo Biosciences, Inc.

In June 2013, we granted our chief executive officer 700,000 restricted stock units with four-year vesting in recognition of his anticipated central role in achieving the company's short- and long-term growth and future programmatic success. Also, in June 2013, we awarded Dr. Salinas, in connection with the start of his employment at the company, a total of 390,000 restricted stock units from the Company's 2012 Commencement Incentive Plan, with one-fourth vesting on each of the first four anniversaries of his hire date. Also in 2013, we granted an aggregate of 156,965 restricted stock units to other newly hired employees under our 2012 Commencement Incentive Plan.

Employment, Severance and Change-in-Control Agreements

Employment agreements. Mr. McGlynn joined the company as our president and chief executive officer on January 15, 2001. Under the terms of an employment agreement between Mr. McGlynn and the company, dated January 2, 2001, as amended, Mr. McGlynn received an initial annual base salary of \$275,000 per year, reviewable annually by the Board of Directors, and a bonus, in the Board's sole discretion, of up to 25% of his base salary. Over time, however, we have increased Mr. McGlynn's base salary and target bonus so that they are, respectively, \$570,000 and 55% of his base salary. Pursuant to his January 2001 employment agreement, we granted Mr. McGlynn an option to purchase 40,000 shares of our common stock with an exercise price equal to the fair market value of the common stock on the initial date of his employment, one-fourth to vest on the first anniversary of his employment and the remaining three-fourths to vest in equal monthly installments during his second through fourth years of employment. These options remained unexercised and expired in 2011. Mr. McGlynn's employment agreement also provided that the Board could, in its sole discretion, grant him a bonus option to purchase up to an additional 2,500 shares, which it did. These options also remained unexercised and expired in 2011. We also agreed to pay Mr. McGlynn a \$50,000 relocation bonus and to reimburse him for relocation expenses, which we did. Since January 2009, we have been paying Mr. McGlynn an annual car allowance of \$10,000.

Dr. Tsukamoto joined the company in November 1997 and has served as our executive vice president of research and development since September 2008. Under the terms of an employment agreement between Dr. Tsukamoto and the company, dated February 2, 1998, Dr. Tsukamoto received an annual base salary of \$130,000 per year and a discretionary target bonus of up to 10% of her base salary. Over time, however, we have increased her base salary and target bonus so that they are, respectively, \$350,000 and 40% of her base salary. Also pursuant to her employment agreement, we provide Dr. Tsukamoto with \$750,000 of term life insurance on an annual basis during her employment.

Mr. Young joined the company in September 2005 as our chief financial officer and vice president of finance. Under the terms of his agreement with the company, dated August 16, 2005, Mr. Young received an initial annual base salary of \$250,000 per year, with a target bonus of up to 25% of his base salary. Over time, however, we have increased Mr. Young's base salary and target bonus so that they are, respectively, \$325,000 and 40% of his base salary. Pursuant to his August 2005 employment agreement, we granted Mr. Young an option to purchase 45,000 shares of our common stock. This option vested over 48 months; with one-fourth of the shares having vested on the first anniversary of the date on which Mr. Young's employment began and with the remaining shares having vested at the rate of 1/48th per month on the last day of each month during the ensuing 36 months. In addition, the employment agreement provided for an option grant on the first anniversary of his employment to acquire an additional 2,500 shares of our common stock. The grant of 2,500 shares was duly made, and vested in the same manner as his earlier option grant over 48 months.

Dr. Craig joined the company in September 2008 as our senior vice president of development and operations. Under the terms of his agreement with the company, dated July 24, 2008, Dr. Craig has received an annual base salary of \$275,000 per year, with a target bonus of up to 25% of his base salary. Over time, however,

we have increased Dr. Craig's base salary and target bonus so that they are, respectively, \$320,000 and 40% of his base salary. Pursuant to Dr. Craig's July 2008 employment agreement, we granted him an option to purchase 20,000 shares of our common stock. This option will vest over 48 months, with one-fourth of the shares having vested on the first anniversary of the date on which Dr. Craig's employment began and with the remaining shares vesting, subject to his continued employment by the company, at the rate of 1/48th per month on the last day of each month during the ensuing 36 months.

Mr. Stratton joined the company in February 2007 as our general counsel. Under the terms of his agreement with the company, dated February 2, 2007, Mr. Stratton received an initial annual base salary of \$220,000 per year, with a target bonus of up to 20% of his base salary. Over time, however, we have increased Mr. Stratton's base salary and target bonus so that they are, respectively, \$320,000 and 40% of his base salary. Pursuant to Mr. Stratton's February 2007 employment agreement, we granted him an option to purchase 15,000 shares of our common stock. This option vested over 48 months, with one-fourth of the shares having vested on the first anniversary of the date on which Mr. Stratton's employment began and with the remaining shares having vested at the rate of 1/48th per month on the last day of each month during the ensuing 36 months.

Dr. Salinas joined the company as our executive vice president and head of research and development on June 6, 2013. Under the terms of an employment agreement between Dr. Salinas and the company, dated June 5, 2013, Dr. Salinas receives an annual base salary of \$475,000 per year, with a target bonus of up to 50% of his base salary. In addition, we agreed to pay Dr. Salinas a sign-on bonus of \$100,000, payable on a quarterly basis over his first year of employment, as well as a relocation allowance of \$50,000, which is repayable in the event Dr. Salinas voluntarily terminates his employment within 12 months of his receipt of the allowance. Furthermore, pursuant to his June 2013 employment agreement, we granted Dr. Salinas 390,000 restricted stock units, with one-fourth vesting on each of the first four anniversaries of his employment.

Severance arrangements. Each of our executive officers has entered into a severance agreement with the company under which he or she would receive payments upon termination of his or her employment by us without cause⁴ or consequent to a change of control or, in the case of Mr. McGlynn, by virtue of disability.

In the case of Mr. McGlynn, upon termination without cause, we would continue to pay his salary and provide benefits for one year, at the base wage rate then in effect. If the termination of Mr. McGlynn's employment were associated with a change of control, the company would pay (in a lump sum) (i) two years of his salary and the reasonably projected cost of healthcare benefits, (ii) a bonus with respect to the termination year at 25% of the base salary, pro-rated for the portion of the year served, and (iii) a tax gross up for his continued healthcare benefits. In addition, all unvested stock options would vest and all stock options would be exercisable for two years after termination. If Mr. McGlynn's employment were terminated on account of disability, we would continue to pay his salary for up to six months (or until he obtained other employment or became eligible for disability income under a company plan, if sooner).

In the case of Dr. Tsukamoto, upon involuntary termination without cause whether or not associated with a change of control, we would continue to pay Dr. Tsukamoto's salary and provide benefits for twelve months, at the rate then in effect.

In the case of Mr. Young, upon involuntary termination without cause, we would continue to pay his salary and provide benefits for six months, at the rate then in effect. If the termination were associated with a change of control, we would continue to pay Mr. Young's salary and provide benefits (including his share of COBRA, grossing up for the tax effects, if any) for twelve months; in this event, any unvested options and any other stock awards held by him would vest upon termination.

⁴ Or termination by the executive officer for good reason, as defined in their respective agreements.

In the case of Dr. Craig, upon involuntary termination without cause, whether or not associated with a change of control, we would continue to pay his salary and provide benefits for six months, at the rate then in effect.

In the case of Mr. Stratton, upon involuntary termination without cause, we would continue to pay his salary and provide benefits for six months, at the rate then in effect. If the termination were associated with a change of control, we would continue to pay Mr. Stratton's salary and provide benefits for twelve months; in this event, any unvested options and any other stock awards held by him would vest upon termination.

In the case of Dr. Salinas, upon involuntary termination without cause, we would continue to pay his salary and provide benefits for twelve months, at the rate then in effect. Likewise, in the event of involuntary termination or voluntary termination because his job responsibilities have been materially and adversely impacted as a result of a company change of control, we would continue Dr. Salinas' salary and benefits for twelve months.

If we terminate the employment of any executive officer for cause, or if the officer resigns without good cause, he or she would not be entitled to any severance or other benefits.

Potential Payments Upon Termination or Change-in-Control

The following table displays the value of what the executive officers would have received from us had their employment been terminated on December 31, 2012:

Officer	Salary	Bonus	Health	Accelerated Vesting of Options and Restricted Stock Units*	Total
Martin McGlynn					
Terminated without cause	\$ 550,000		\$ 31,663		\$ 581,663
Terminated, change of control Disability(2)	\$ 1,100,000	\$ 137,500	\$ 116,731(1)	\$ 736,544	\$ 2,090,775
	\$ 275,000				\$ 275,000
Ann Tsukamoto, Ph.D.					
Terminated without cause	\$ 335,000		\$ 15,688		\$ 350,688
Terminated, change of control	\$ 335,000		\$ 15,688	\$ 253,737(3)	\$ 604,425
Rodney Young					
Terminated without cause	\$ 162,500		\$ 8,630		\$ 171,130
Terminated, change of control	\$ 325,000		\$ 17,260	\$ 25,537(3)	\$ 367,797
Stewart Craig, Ph.D.					
Terminated without cause	\$ 150,000		\$ 10,286		\$ 160,286
Terminated, change of control	\$ 150,000		\$ 10,286	\$ 232,004(3)	\$ 392,290
Ken Stratton, J.D.					
Terminated without cause	\$ 150,000		\$ 10,192		\$ 160,192
Terminated, change of control	\$ 300,000		\$ 20,384	\$ 232,004(3)	\$ 552,388

* Value shown represents the difference between the closing market price of our stock on December 31, 2012 of \$1.63 per share and the applicable exercise price of each grant.

(1) Includes tax gross-up on two years of healthcare costs.

(2) Payments stop before six months if individual obtains other full-time employment or qualifies for payments under any disability income plan provided by the company.

- (3) All unvested options and restricted stock units issued under the applicable equity incentive plans vest upon a change of control under the terms of those plans.

Compensation and Stock Option Committee Report

The Compensation Committee has reviewed and discussed the Compensation Discussion and Analysis required by Item 402(b) of SEC Regulation S-K with management. Based on this review and these discussions, the Compensation Committee has recommended to the Board of Directors that the Compensation Discussion and Analysis be included in the company's proxy statement for 2013.

COMPENSATION AND STOCK OPTION COMMITTEE

John Schwartz, Ph.D., Chairman
Eric Bjerkholt
Ricardo Levy, Ph.D.

Notwithstanding anything to the contrary set forth in any of our filings under the Securities Act of 1933, as amended, or the Exchange Act that incorporate future filings, in whole or in part, the foregoing Compensation and Stock Option Committee Report shall not be incorporated by reference into any such filings.

Executive Officer Compensation Tables

The following tables set forth information with respect to the compensation of our executive officers for the fiscal years ended December 31, 2012, 2011 and 2010.

Because the Stock awards and Option awards column reflects the dollar amounts recognized as compensation expense for financial statement reporting purposes in accordance with U.S. GAAP, these imputed values include amounts from awards granted from 2005 through 2012.

Summary Compensation Table

Name and Principal Position	Year	Salary	Bonus	Stock	Option	All Other	Total
		(\$)(1)	(\$)(2)	Awards (\$)(3)	Awards (\$)(3)	Compensation (\$)(4)	(\$)
Martin McGlynn	2012	550,000	202,125				