

ECHELON CORP  
Form DEF 14A  
April 12, 2012  
Table of Contents

## SCHEDULE 14A

### 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

## ECHELON CORPORATION

(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):

- No fee required.
- Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

1) Title of each class of securities to which transaction applies:

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3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (Set forth the amount on which the filing fee is calculated and state how it was determined):

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1) Amount Previously Paid:

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3) Filing Party:

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**Table of Contents**

**ECHELON CORPORATION**  
**NOTICE OF ANNUAL MEETING OF STOCKHOLDERS**  
**TO BE HELD ON MAY 22, 2012**  
**10:00 A.M. PACIFIC TIME**

We cordially invite you to attend the 2012 Annual Meeting of Stockholders of Echelon Corporation. The meeting will be held on Tuesday, May 22, 2012 at 10:00 a.m., Pacific Time, at 570 Meridian Avenue, San Jose, California 95126. At the meeting we will:

1. Elect three Class B directors for a term of three years and until their successors are duly elected and qualified;
2. Ratify the appointment of KPMG LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2012;
3. Transact any other business as may properly come before the meeting or any postponement or adjournment thereof.

These items are fully discussed in the following pages, which are made part of this Notice. Stockholders who owned our common stock at the close of business on Tuesday, March 27, 2012 are entitled to notice of and to vote at the annual meeting.

Your vote is important. Whether or not you plan to attend the annual meeting, please cast your vote, as instructed in the Notice of Internet Availability of Proxy Materials, via the Internet, as promptly as possible. You may also request a printed set of the proxy materials which will allow you to submit your vote by mail or by telephone, if you prefer. We encourage you to vote via the Internet. It is convenient, is more environmentally friendly, and saves us significant postage and processing costs.

Sincerely,

Ronald A. Sege  
Chairman of the Board and Chief Executive Officer

San Jose, California

April 12, 2012

**Table of Contents**

**2012 ANNUAL MEETING OF STOCKHOLDERS**

**NOTICE OF ANNUAL MEETING AND PROXY STATEMENT**

**TABLE OF CONTENTS**

	<b>Page</b>
<u>NOTICE OF ANNUAL MEETING OF STOCKHOLDERS</u>	
<u>INFORMATION CONCERNING SOLICITATION AND VOTING</u>	1
<u>General</u>	1
<u>Notice of Internet Availability of Proxy Materials</u>	1
<u>Electronic Access to Proxy Materials</u>	1
<u>Costs of Solicitation</u>	2
<u>Record Date and Shares Outstanding</u>	2
<u>QUESTIONS AND ANSWERS REGARDING OUR ANNUAL MEETING</u>	2
<u>Why am I receiving these proxy materials?</u>	2
<u>What is the Notice of Internet Availability?</u>	2
<u>What proposals will be voted on at the annual meeting?</u>	3
<u>What is Echelon's voting recommendation?</u>	3
<u>Who can vote at the annual meeting?</u>	3
<u>What is the difference between holding shares as a stockholder of record and as a beneficial owner?</u>	3
<u>How many votes does Echelon need to hold the annual meeting?</u>	4
<u>What is the voting requirement to approve each of the proposals?</u>	4
<u>Who counts the votes?</u>	4
<u>What happens if I do not cast a vote?</u>	4
<u>How can I vote my shares in person at the annual meeting?</u>	5
<u>How can I vote my shares without attending the annual meeting?</u>	5
<u>How can I change or revoke my vote?</u>	5
<u>Where can I find the voting results of the annual meeting?</u>	6
<u>Who are the proxies and what do they do?</u>	6
<u>What should I do if I receive more than one Notice or set of proxy materials?</u>	6
<u>How may I obtain a separate Notice or a separate set of proxy materials?</u>	6
<u>What happens if additional proposals are presented at the annual meeting?</u>	6
<u>Is my vote confidential?</u>	7
<u>DEADLINE FOR RECEIPT OF STOCKHOLDER PROPOSALS</u>	7
<u>CORPORATE GOVERNANCE AND OTHER MATTERS</u>	8
<u>Corporate Governance</u>	8
<u>Corporate Governance Guidelines</u>	8
<u>Board Leadership Structure and Role in Risk Management</u>	9
<u>Consideration of Stockholder Recommendations and Nominations of Board Members</u>	9
<u>Identifying and Evaluating Nominees for our Board of Directors</u>	10
<u>Standards of Business Conduct</u>	11
<u>Stockholder Communications</u>	11
<u>Meetings and Attendance of our Board of Directors and Committees of our Board of Directors</u>	11
<u>Attendance of Directors at 2011 Annual Meeting of Stockholders</u>	11
<u>Attendance at Board and Committee Meetings</u>	11

**Table of Contents**

<u>Committees of our Board of Directors</u>	12
<u>Compensation Committee</u>	12
<u>Audit Committee</u>	12
<u>Nominating and Corporate Governance Committee</u>	13
<u>Director Independence</u>	14
<u>Director Compensation</u>	14
<u>Director Summary Compensation Table for Fiscal 2011</u>	15
<u>PROPOSAL ONE ELECTION OF DIRECTORS</u>	15
<u>General</u>	15
<u>Director Information</u>	16
<u>Current Directors</u>	16
<u>Director Biographies</u>	16
<u>Class B Director Nominees</u>	19
<u>Vote Required</u>	19
<u>Board Recommendation</u>	19
<u>PROPOSAL TWO RATIFICATION OF APPOINTMENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM</u>	19
<u>Audit and Non-Audit Fees</u>	20
<u>Board Recommendation</u>	20
<u>SHARE OWNERSHIP BY PRINCIPAL STOCKHOLDERS AND MANAGEMENT</u>	21
<u>EXECUTIVE COMPENSATION AND RELATED MATTERS</u>	23
<u>Compensation Discussion and Analysis</u>	23
<u>Executive Summary</u>	23
<u>Executive Compensation Questions and Answers</u>	24
<u>Compensation Committee Report</u>	41
<u>Summary Compensation Table</u>	41
<u>Grants of Plan-Based Awards in 2011</u>	43
<u>Outstanding Equity Awards at 2011 Fiscal Year-End</u>	44
<u>Option Exercises and Stock Vested for Fiscal 2011</u>	47
<u>Potential Payments Upon Termination or Change in Control</u>	47
<u>1997 Stock Plan</u>	47
<u>Employment Agreement with Ronald A. Sege</u>	48
<u>Compensation Committee Interlocks and Insider Participation</u>	48
<u>Equity Compensation Plan Information</u>	48
<u>Policies and Procedures with Respect to Related Party Transactions</u>	49
<u>Certain Relationships</u>	50
<u>Agreements with ENEL</u>	50
<u>Legal Services</u>	50
<u>OTHER INFORMATION</u>	50
<u>Section 16(a) Beneficial Ownership Reporting Information</u>	50
<u>No Incorporation by Reference</u>	51
<u>Stockholder Proposals 2013 Annual Meeting</u>	51
<u>Available Information</u>	51
<u>REPORT OF THE AUDIT COMMITTEE OF OUR BOARD OF DIRECTORS</u>	51
<u>OTHER MATTERS</u>	52

**Table of Contents**

**ECHELON CORPORATION**

**PROXY STATEMENT**

**FOR**

**2012 ANNUAL MEETING OF STOCKHOLDERS**

**INFORMATION CONCERNING SOLICITATION AND VOTING**

**General**

Our Board of Directors is soliciting Proxies for the 2012 Annual Meeting of Stockholders to be held at 570 Meridian Avenue, San Jose, California 95126 on Tuesday, May 22, 2012, at 10:00 a.m., Pacific Time. The address of our principal executive office is 550 Meridian Avenue, San Jose, California 95126 and our telephone number at this address is 408-938-5200. This Proxy Statement contains important information for you to consider when deciding how to vote on the matters set forth in the attached Notice of Annual Meeting. Please read it carefully.

Beginning on April 12, 2012, we made copies of this Proxy Statement available to persons who were stockholders at the close of business on March 27, 2012, the record date for the annual meeting.

**Notice of Internet Availability of Proxy Materials**

Pursuant to rules adopted by the Securities and Exchange Commission, or the SEC, we have chosen to provide access to our proxy materials over the Internet. We are sending a Notice of Internet Availability of Proxy Materials (the "Notice") to our stockholders of record and our beneficial owners. All stockholders will have the option to access the proxy materials on a website referred to in the Notice or to request a printed set of the proxy materials. Instructions on how to access the proxy materials over the Internet or to request a printed copy of the proxy materials are included in the Notice. You may also request to receive proxy materials in printed form by mail or electronically by e-mail on an ongoing basis.

**Electronic Access to Proxy Materials**

The Notice will provide you with instructions on how to:

View on the Internet our proxy materials for our annual meeting; and

Instruct us to send our future proxy materials to you electronically by e-mail.

Choosing to receive future proxy materials by e-mail will save us the cost of printing and mailing the proxy materials to you and will reduce the environmental impact of our annual meeting. If you choose to receive future proxy materials by e-mail, you will receive an e-mail next year with instructions including a link to the proxy materials and a link to the proxy voting site. Your election to receive proxy materials by e-mail will remain in effect until you terminate it.

## **Table of Contents**

### **Costs of Solicitation**

Echelon will pay the costs of soliciting proxies from stockholders. In addition, we may reimburse brokerage firms and other persons representing beneficial owners of shares for their expenses in forwarding solicitation material to such beneficial owners, including fees associated with:

Forwarding the Notice to beneficial owners;

Forwarding printed proxy materials by mail to beneficial owners who specifically request them; and

Obtaining beneficial owners' voting instructions.

Certain of our directors, officers and employees may solicit proxies on our behalf, without additional compensation, personally or by written communication, telephone, facsimile or other electronic means. We may engage the services of a professional proxy solicitation firm to aid in the solicitation of proxies from certain brokers, bank nominees and other institutional owners. Our costs for such services, if retained, will not be significant.

### **Record Date and Shares Outstanding**

Only stockholders of record at the close of business on March 27, 2012, are entitled to attend and vote at the annual meeting. On the record date, 42,604,213 shares of our common stock were outstanding and held of record. The closing price of our common stock on The Nasdaq Stock Market ( Nasdaq ) on the record date was \$4.59 per share.

## **QUESTIONS AND ANSWERS REGARDING OUR ANNUAL MEETING**

Although we encourage you to read this Proxy Statement in its entirety, we include this question and answer section to provide some background information and brief answers to several questions you may have about the annual meeting or this Proxy Statement.

### ***Q: Why am I receiving these proxy materials?***

**A:** Our Board of Directors is providing these proxy materials for you in connection with our annual meeting of stockholders, which will take place on May 22, 2012. Stockholders are invited to attend the annual meeting and are requested to vote on the proposals described in this Proxy Statement.

### ***Q: What is the Notice of Internet Availability?***

**A:** In accordance with rules and regulations adopted by the SEC, instead of mailing a printed copy of our proxy materials to all stockholders entitled to vote at the annual meeting, we are furnishing the proxy materials to our stockholders over the Internet. If you received a Notice by mail, you will not receive a printed copy of the proxy materials. Instead, the Notice will instruct you as to how you may access and review the proxy materials and submit your vote via the Internet. If you received a Notice by mail and would like to receive a printed copy of the proxy materials, please follow the instructions included in the Notice for requesting such materials.

We expect to mail the Notice on or about April 12, 2012, to all stockholders entitled to vote at the annual meeting. On the date of mailing of the Notice, all stockholders and beneficial owners will have the ability to access all of our proxy materials on a website referred to in the Notice. These proxy materials will be available free of charge.



**Table of Contents**

***Q: What proposals will be voted on at the annual meeting?***

**A:** There are two proposals scheduled to be voted on at the annual meeting:

Election of the three Class B nominees for director set forth in this Proxy Statement; and

Ratification of the appointment of KPMG LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2012.

***Q: What is Echelon's voting recommendation?***

**A:** Our Board of Directors unanimously recommends that you vote your shares FOR each of the three Class B nominees to our Board of Directors and FOR ratification of the appointment of KPMG LLP as our independent registered public accounting firm.

***Q: Who can vote at the annual meeting?***

**A:** Our Board of Directors has set March 27, 2012 as the record date for the annual meeting. All stockholders who owned Echelon common stock at the close of business on March 27, 2012 may attend and vote at the annual meeting. Each stockholder is entitled to one vote for each share of common stock held as of the record date on all matters to be voted on. Stockholders do not have the right to cumulate votes. On March 27, 2012, 42,604,213 shares of our common stock were outstanding. Shares held as of the record date include shares that are held directly in your name as the stockholder of record and those shares held for you as a beneficial owner through a broker, bank or other nominee.

***Q: What is the difference between holding shares as a stockholder of record and as a beneficial owner?***

**A:** Most stockholders of Echelon hold their shares through a broker, bank or other nominee rather than directly in their own name. As summarized below, there are some distinctions between shares held of record and those owned beneficially.

*Stockholders of Record*

If your shares are registered directly in your name with Echelon's transfer agent, Computershare, you are considered the stockholder of record with respect to those shares and the Notice has been sent directly to you. As the stockholder of record, you have the right to grant your voting proxy directly to Echelon or to vote in person at the annual meeting.

*Beneficial Owners*

If your shares are held in a stock brokerage account or by a bank or other nominee, you are considered the beneficial owner of shares held in street name, and the Notice has been forwarded to you by your broker, bank or other nominee who is considered, with respect to those shares, the stockholder of record. As the beneficial owner, you have the right to direct your broker, bank or other nominee on how to vote and are also invited to attend the annual meeting. However, since you are not the stockholder of record, you may not vote these shares in person at the annual meeting unless you request a legal proxy from the broker, bank or other nominee who holds your shares, giving you the right to vote the shares at the annual meeting.

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**Table of Contents**

***Q: How many votes does Echelon need to hold the annual meeting?***

**A:** A majority of Echelon's outstanding shares as of the record date must be present at the annual meeting in order to hold the meeting and conduct business. This is called a quorum. Both abstentions and broker non-votes are counted as present for the purpose of determining the presence of a quorum. A broker non-vote occurs when a nominee holding shares for a beneficial owner does not vote on a particular proposal because the nominee does not have discretionary voting power with respect to that item and has not received instructions from the beneficial owner.

Shares are counted as present at the meeting if you:

are present and vote in person at the meeting; or

have properly submitted a proxy card or voting instruction card or voted via the Internet or by telephone.

***Q: What is the voting requirement to approve each of the proposals?***

**A: Proposal One** Directors are elected by a plurality vote, and therefore the three individuals receiving the highest number of FOR votes will be elected. Votes of WITHHOLD and broker non-votes have no legal effect on the election of directors due to the fact that such elections are by a plurality. You may vote either FOR or WITHHOLD on each of the three Class B nominees for election as director.

**Proposal Two** The affirmative vote of a majority of the votes duly cast is required to ratify the appointment of KPMG LLP as our company's independent registered public accounting firm. You may vote FOR, AGAINST or ABSTAIN on Proposal Two. Abstentions are deemed to be votes cast and have the same effect as a vote against this proposal. However, broker non-votes are not deemed to be votes cast and, therefore, are not included in the tabulation of the voting results on this proposal.

***Q: Who counts the votes?***

**A:** Voting results are tabulated and certified by Broadridge Financial Solutions, Inc.

***Q: What happens if I do not cast a vote?***

**A: Stockholders of record** If you are a stockholder of record and you do not cast your vote, no votes will be cast on your behalf on any of the items of business at the annual meeting. However, if you submit a signed proxy card with no further instructions, the shares represented by that proxy card will be voted as recommended by our Board of Directors.

**Beneficial owners** If you hold your shares in street name it is critical that you cast your vote if you want it to count in the election of directors (Proposal One). In the past, if you held your shares in street name and you did not indicate how you wanted your shares voted in the election of directors, your bank, broker or other nominee was allowed to vote those shares on your behalf in the election of directors as they felt appropriate. Recent rule changes eliminate the ability of your bank, broker or other nominee to vote your uninstructed shares in the election of directors on a discretionary basis. Thus, if you hold your shares in street name and you do not instruct your bank, broker or other nominee how to vote in the election of directors, no votes will be cast on your behalf. For more information on this topic, see the SEC Investor Alert issued in February 2010 entitled "New Shareholder Voting Rules for the 2010 Proxy Season" at <http://www.sec.gov/investor/alerts/votingrules2010.htm>. Your bank, broker or other nominee will, however, continue to have discretion to vote any uninstructed shares on the ratification of the appointment of our company's independent registered public accounting firm (Proposal Two).

## **Table of Contents**

### ***Q: How can I vote my shares in person at the annual meeting?***

**A:** Shares held directly in your name as the stockholder of record may be voted in person at the annual meeting. If you choose to vote in person, please bring your proxy card or proof of identification to the annual meeting. Even if you plan to attend the annual meeting, Echelon recommends that you vote your shares in advance as described below so that your vote will be counted if you later decide not to attend the annual meeting. If you hold your shares in street name, you must request a legal proxy from your broker, bank or other nominee in order to vote in person at the annual meeting.

### ***Q: How can I vote my shares without attending the annual meeting?***

**A:** Whether you hold shares directly as the stockholder of record or beneficially in street name, you may direct how your shares are voted without attending the annual meeting. If you are a stockholder of record, you may vote by submitting a proxy; please refer to the voting instructions in the Notice or below. If you hold shares beneficially in street name, you may vote by submitting voting instructions to your broker, bank or other nominee; please refer to the voting instructions provided to you by your broker, bank or other nominee.

**Internet** Stockholders of record with Internet access may submit proxies by following the **Vote by Internet** instructions on the Notice until 11:59 p.m., Eastern Time, on May 21, 2012 or by following the instructions at [www.proxymvote.com](http://www.proxymvote.com). Most of our stockholders who hold shares beneficially in street name may vote by accessing the website specified in the voting instructions provided by their brokers, banks or other nominees. A large number of banks and brokerage firms are participating in Broadridge Financial Solutions, Inc.'s (formerly ADP Investor Communication Services) online program. This program provides eligible stockholders the opportunity to vote over the Internet or by telephone. Voting forms will provide instructions for stockholders whose bank or brokerage firm is participating in Broadridge's program.

**Telephone** If you request a printed set of the proxy materials, you will be eligible to submit your vote by telephone.

**Mail** If you request a printed set of the proxy materials, you may indicate your vote by completing, signing and dating the proxy card or voting instruction form where indicated and by returning it in the prepaid envelope that will be provided.

### ***Q: How can I change or revoke my vote?***

**A:** Subject to any rules your broker, bank or other nominee may have, you may change your proxy instructions at any time before your proxy is voted at the annual meeting.

**Stockholders of record** If you are a stockholder of record, you may change your vote by (1) filing with our General Counsel, prior to your shares being voted at the annual meeting, a written notice of revocation or a duly executed proxy card, in either case dated later than the prior proxy relating to the same shares, or (2) attending the annual meeting and voting in person (although attendance at the annual meeting will not, by itself, revoke a proxy). Any written notice of revocation or subsequent proxy card must be received by our General Counsel prior to the taking of the vote at the annual meeting. Such written notice of revocation or subsequent proxy card should be hand delivered to our General Counsel or should be sent so as to be delivered to our principal executive offices, Attention: General Counsel.

## **Table of Contents**

**Beneficial owners** If you are a beneficial owner of shares held in street name, you may change your vote (1) by submitting new voting instructions to your broker, bank or other nominee, or (2) if you have obtained, from the broker, bank or other nominee who holds your shares, a legal proxy giving you the right to vote the shares, by attending the annual meeting and voting in person.

In addition, a stockholder of record or a beneficial owner who has voted via the Internet or by telephone may also change his, her or its vote by making a timely and valid later Internet or telephone vote no later than 11:59 p.m., Eastern Time, on May 21, 2012.

***Q: Where can I find the voting results of the annual meeting?***

**A:** The preliminary voting results will be announced at the annual meeting. The final results will be reported in a current report on Form 8-K filed within four business days after the date of the annual meeting.

***Q: Who are the proxies and what do they do?***

**A:** The two persons named as proxies on the proxy card, Kathleen B. Bloch, our Senior Vice President and General Counsel, and William R. Slakey, our Executive Vice President and Chief Financial Officer, were designated by our Board of Directors. All properly executed proxies will be voted (except to the extent that authority to vote has been withheld) and where a choice has been specified by the stockholder of record as provided in the proxy card, it will be voted in accordance with the instructions indicated on the proxy card. If you are a stockholder of record and submit a signed proxy card, but do not indicate your voting instructions, your shares will be voted as recommended by our Board of Directors.

***Q: What should I do if I receive more than one Notice or set of proxy materials?***

**A:** If you received more than one Notice or set of proxy materials, your shares are registered in more than one name or brokerage account. Please follow the voting instructions on each Notice or voting instruction card that you receive to ensure that all of your shares are voted.

***Q: How may I obtain a separate Notice or a separate set of proxy materials?***

**A:** If you share an address with another stockholder, each stockholder may not receive a separate Notice or a separate copy of the proxy materials. Stockholders who do not receive a separate Notice or a separate copy of the proxy materials may request to receive a separate Notice or a separate copy of the proxy materials by contacting our Investor Relations department (i) by mail at 550 Meridian Avenue, San Jose, California 95126, (ii) by calling us at 408-938-5252 or (iii) by sending an email to mlarsen@echelon.com. Alternatively, stockholders who share an address and receive multiple Notices or multiple copies of our proxy materials may request to receive a single copy by following the instructions above.

***Q: What happens if additional proposals are presented at the annual meeting?***

**A:** Other than the two proposals described in this Proxy Statement, Echelon does not expect any additional matters to be presented for a vote at the annual meeting. If you are a stockholder of record and grant a proxy, the persons named as proxy holders, Kathleen B. Bloch, our Senior Vice President and General Counsel, and William R. Slakey, our Executive Vice President and Chief Financial Officer, will have the discretion to vote your shares on any additional matters properly presented for a vote at the annual meeting. If for any unforeseen reason any of Echelon's Class B nominees is not available as a candidate for director, the persons named as proxy holders will vote your proxy for such other candidate or candidates as may be nominated by our Board of Directors.

**Table of Contents**

***Q: Is my vote confidential?***

**A:** Proxy instructions, ballots and voting tabulations that identify individual stockholders are handled in a manner that protects your voting privacy. Your vote will not be disclosed either within Echelon or to third parties except (1) as necessary to meet applicable legal requirements, (2) to allow for the tabulation of votes and certification of the vote or (3) to facilitate a successful proxy solicitation by our Board of Directors. Occasionally, stockholders provide written comments on their proxy cards, which are then forwarded to Echelon's management.

**DEADLINE FOR RECEIPT OF STOCKHOLDER PROPOSALS**

Our stockholders may submit proposals that they believe should be voted upon at our next year's annual meeting or nominate persons for election to our Board of Directors. Stockholders may also recommend candidates for election to our Board of Directors (See *Corporate Governance and Other Matters - Consideration of Stockholder Recommendations and Nominations of Board Members* ). Pursuant to Rule 14a-8 under the Securities Exchange Act of 1934, as amended, some stockholder proposals may be eligible for inclusion in our 2013 proxy statement and proxy. Any such stockholder proposals must be submitted in writing to the attention of Kathleen B. Bloch, Senior Vice President, General Counsel and Secretary, Echelon Corporation, 550 Meridian Avenue, San Jose, California 95126, no later than December 13, 2012, which is the date 120 calendar days prior to the one-year anniversary of the mailing date of this Proxy Statement. Stockholders interested in submitting such a proposal are advised to contact knowledgeable legal counsel with regard to the detailed requirements of applicable securities laws. The submission of a stockholder proposal does not guarantee that it will be included in our 2013 proxy statement.

Alternatively, under our Bylaws, a proposal or a nomination that the stockholder does not seek to include in our 2013 proxy statement pursuant to Rule 14a-8 may be submitted in writing to Kathleen B. Bloch, Senior Vice President, General Counsel and Secretary, Echelon Corporation, 550 Meridian Avenue, San Jose, California 95126, for the 2013 annual meeting of stockholders not less than 20 days nor more than 60 days prior to the date of such meeting. Note, however, that in the event we provide less than 30 days notice or prior public disclosure to stockholders of the date of the 2013 annual meeting, any stockholder proposal or nomination not submitted pursuant to Rule 14a-8 must be submitted to us not later than the close of business on the tenth day following the day on which notice of the date of the 2013 annual meeting was mailed or public disclosure was made. For example, if we provide notice of our 2013 annual meeting on April 23, 2013 for a 2013 annual meeting on May 21, 2013, any such proposal or nomination will be considered untimely if submitted to us after May 3, 2013. For purposes of the above, public disclosure means disclosure in a press release reported by the Dow Jones News Service, Associated Press or a comparable national news service, or in a document publicly filed by us with the SEC. As described in our Bylaws, the stockholder submission must include certain specified information concerning the proposal or nominee, as the case may be, and information as to the stockholder's ownership of our common stock. If a stockholder gives notice of such a proposal after the deadline computed in accordance with our Bylaws, or the Bylaw Deadline, the stockholder will not be permitted to present the proposal to our stockholders for a vote at the 2013 annual meeting.

The rules of the SEC also establish a different deadline for submission of stockholder proposals that are not intended to be included in our 2013 proxy statement with respect to discretionary voting, or the Discretionary Vote Deadline. The Discretionary Vote Deadline for the 2013 annual meeting is February 26, 2013, the date which is 45 calendar days prior to the one-year anniversary of the mailing date of this Proxy Statement. If a stockholder gives notice of such a proposal after the Discretionary Vote Deadline, our proxy holders will be allowed to use their discretionary voting authority to vote against the stockholder proposal when and if the proposal is raised at the 2013 annual meeting.

## **Table of Contents**

Because the Bylaw Deadline is not capable of being determined until we publicly announce the date of our 2013 annual meeting, it is possible that the Bylaw Deadline may occur after the Discretionary Vote Deadline. In such a case, a proposal received after the Discretionary Vote Deadline but before the Bylaw Deadline would be eligible to be presented at the 2013 annual meeting and we believe that our proxy holders at such meeting would be allowed to use the discretionary authority granted by the proxy to vote against the proposal at such meeting without including any disclosure of the proposal in the proxy statement relating to such meeting.

### **CORPORATE GOVERNANCE AND OTHER MATTERS**

#### **Corporate Governance**

##### *Corporate Governance Guidelines*

Our Board of Directors adopted Corporate Governance Guidelines in November 2002 that outline, among other matters, the role and functions of our Board of Directors and the composition and responsibilities of various committees of our Board of Directors. The Corporate Governance Guidelines are available, along with other important corporate governance materials, at the investor relations section of our website at [www.echelon.com](http://www.echelon.com).

The Corporate Governance Guidelines provide, among other things, that:

A majority of the directors must meet the independence criteria established by Nasdaq.

If the Chairman of the Board is not an independent director, then a Presiding Director must be appointed by the outside directors to assume the responsibility of chairing the regularly scheduled meetings of outside directors.

Our Board of Directors shall have a policy of holding separate meeting times for outside directors.

All of the members of the Nominating and Governance Committee, Audit Committee and Compensation Committee must meet the criteria for independence established by Nasdaq, except that our Board of Directors may make exceptions to this policy with respect to the Nominating and Governance Committee that are consistent with regulatory requirements.

Our Board of Directors shall have responsibility over such matters as overseeing our Chief Executive Officer and other senior management in the competent and ethical operation of our company, gathering and analyzing information obtained from management, retaining counsel and expert advisors, and overseeing and monitoring the effectiveness of governance practices. In April, 2008, our Board of Directors appointed Robert J. Finocchio, Jr. as Presiding Director. Pursuant to the Corporate Governance Guidelines, the Presiding Director was selected by our non-employee directors and assumed the responsibilities of chairing meetings of non-employee directors, serving as the liaison between our Chief Executive Officer, Chairman of the Board and our independent directors, approving Board of Directors meeting agendas and schedules and information flow to our Board of Directors and such further responsibilities that the non-employee directors as a whole designate from time to time.

## **Table of Contents**

As the operation of our Board of Directors is a dynamic process, our Board of Directors regularly reviews changing legal and regulatory requirements, evolving best practices and other developments. Accordingly, our Board of Directors may modify the Corporate Governance Guidelines from time to time, as it deems appropriate.

In addition, in November 2009, we announced that M. Kenneth Oshman, Echelon's Chairman of the Board and Chief Executive Officer had stepped down as our Chief Executive Officer, but would continue to serve as Executive Chairman of the Board. Mr. Oshman served as Executive Chairman of the Board until his death on August 6, 2011. In October, 2011, our Board appointed Ronald A. Sege, our Chief Executive Officer and President, to also serve as Chairman of the Board. At the same time, our Board reaffirmed Mr. Finocchio's appointment as our Presiding Director.

### ***Board Leadership Structure and Role in Risk Management***

Our company's management is responsible for the day to day assessment and management of the risks we face, while our Board of Directors administers its risk oversight function directly and through the Audit Committee and the Compensation Committee. Management regularly reports to our Board of Directors and/or the relevant Committee regarding identified or potential risks. The areas of material risk to our company include strategic, operational, financial, regulatory and legal risks. Our Board of Directors regularly reviews our company's strategies and attendant risks, and provides advice and guidance with respect to strategies to manage these risks while attaining long- and short-term goals. Operational risks, including supply risks that might cause, and reputational risks that might result from, operational issues, and financial risks, including internal controls and credit risk associated with our customers, as well as overall economic risks, are the purview of our Audit Committee. The Audit Committee's review is accompanied by regular reports from management and assessments from our company's internal and external auditors. In assessing legal or regulatory risks, our Board of Directors and the Audit Committee are advised by management, counsel and experts, as appropriate. The Compensation Committee is responsible for overseeing the management of risks associated with executive and employee compensation plans and retention, to ensure that our company's compensation programs remain consistent with our stockholders' interests, that such programs do not encourage excessive risk-taking, and that such programs are designed to retain valued executives and employees.

### ***Consideration of Stockholder Recommendations and Nominations of Board Members***

The Nominating and Corporate Governance Committee of our Board of Directors will consider both recommendations and nominations from stockholders for candidates to our Board of Directors. A stockholder who desires to recommend a candidate for election to our Board of Directors shall direct the recommendation in writing to the Company Corporate Secretary, Echelon Corporation, 550 Meridian Avenue, San Jose, California 95126, and must include the candidate's name, home and business contact information, detailed biographical data and qualifications, information regarding any relationships between the candidate and our company within the last three years and evidence of the nominating person's ownership of our stock and amount of stock holdings. For a stockholder recommendation to be considered by the Nominating and Corporate Governance Committee as a potential candidate at an annual meeting, nominations must be received on or before the deadline for receipt of stockholder proposals.

If, instead, a stockholder desires to nominate a person directly for election to our Board of Directors, the stockholder must follow the rules set forth by the SEC (see *Deadline for Receipt of Stockholder Proposals* above) and meet the deadlines and other requirements set forth in our Bylaws, including, (1) as to each person, if any, whom the stockholder proposes to nominate for election or re-election as a director: (a) the name, age, business address and residence address of such person, (b) the principal occupation or

## **Table of Contents**

employment of such person, (c) the class and number of shares of our company which are beneficially owned by such person, (d) any other information relating to such person that is required by law to be disclosed in solicitations of proxies for election of directors and (e) such person's written consent to being named as a nominee and to serving as a director if elected; and (2) as to the stockholder giving the notice: (a) the name and address, as they appear on our company's books, of such stockholder, (b) the class and number of shares of our company which are beneficially owned by such stockholder and (c) a description of all arrangements or understandings between such stockholder and each nominee and any other person or persons (naming such person or persons) relating to the nomination.

### ***Identifying and Evaluating Nominees for our Board of Directors***

The Nominating and Corporate Governance Committee shall use the following procedures to identify and evaluate the individuals that it selects, or recommends that our Board of Directors select, as director nominees:

The Committee shall review the qualifications of any candidates who have been properly recommended or nominated by stockholders, as well as those candidates who have been identified by management, individual members of our Board of Directors or, if the Committee determines, a search firm. Such review may, in the Committee's discretion, include a review solely of information provided to the Committee or may also include discussions with persons familiar with the candidate, an interview with the candidate or other actions that the Committee deems proper.

The Committee shall evaluate the performance and qualifications of individual members of our Board of Directors eligible for re-election at the annual meeting of stockholders.

The Committee shall consider the suitability of each candidate, including the current members of our Board of Directors, in light of the current size and composition of our Board of Directors. In evaluating the suitability of the candidates, the Committee considers many factors, including, among other things, issues of character, judgment, independence, age, expertise, diversity of experience, length of service, other commitments and the like. Diversity is also an important factor for the Committee to consider, as evidenced by the fact that two of the more recent additions to our company's Board of Directors have added to its diversity. The Committee evaluates such factors, among others, and considers each individual candidate in the context of the current perceived needs of our Board of Directors as a whole. Except as may be required by rules promulgated by Nasdaq or the SEC, it is the current sense of the Committee that there are no specific minimum qualifications that must be met by each candidate for our Board of Directors, nor are there specific qualities or skills that are necessary for one or more of the members of our Board of Directors to possess.

After such review and consideration, the Committee selects, or recommends that our Board of Directors select, the slate of director nominees, either at a meeting of the Committee at which a quorum is present or by unanimous written consent of the Committee.

The Committee will endeavor to notify, or cause to be notified, all director candidates of its decision as to whether to nominate such individual for election to our Board of Directors.