

ECHELON CORP  
Form DEF 14A  
April 09, 2013  
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## 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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1) Amount Previously Paid:

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**ECHELON CORPORATION**  
**NOTICE OF ANNUAL MEETING OF STOCKHOLDERS**  
**TO BE HELD ON MAY 21, 2013**  
**10:00 A.M. PACIFIC TIME**

We cordially invite you to attend the 2013 Annual Meeting of Stockholders of Echelon Corporation. The meeting will be held on Tuesday, May 21, 2013, at 10:00 a.m., Pacific Time, at 570 Meridian Avenue, San Jose, California 95126. At the meeting we will:

1. Elect three Class C directors for a term of three years and until their successors are duly elected and qualified;
2. Approve our Amended and Restated 1997 Stock Plan;
3. Ratify the appointment of KPMG LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2013; and
4. 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 Wednesday, March 27, 2013, 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 9, 2013

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**2013 ANNUAL MEETING OF STOCKHOLDERS**

**NOTICE OF ANNUAL MEETING AND PROXY STATEMENT**

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**ECHELON CORPORATION**

**PROXY STATEMENT**

**FOR**

**2013 ANNUAL MEETING OF STOCKHOLDERS**

**INFORMATION CONCERNING SOLICITATION AND VOTING**

**General**

Our Board of Directors is soliciting Proxies for the 2013 Annual Meeting of Stockholders to be held at 570 Meridian Avenue, San Jose, California 95126 on Tuesday, May 21, 2013, 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 9, 2013, copies of this Proxy Statement were first sent or made available to persons who were stockholders at the close of business on March 27, 2013, 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.

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### **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, 2013, are entitled to attend and vote at the annual meeting. On the record date, 43,057,160 shares of our common stock were outstanding and held of record.

## **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 21, 2013. 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 mailed the Notice on or about April 9, 2013, 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.



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

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

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

Approval of the amendment and restatement of our 1997 Stock Plan; and

Ratification of the appointment of KPMG LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2013.

***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 C nominees to our Board of Directors, FOR approval of our amended and restated 1997 Stock Plan, and FOR ratification of the appointment of KPMG LLP as our independent registered public accounting firm.

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

**A:** Other than the three 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 C 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.

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

**A:** Our Board of Directors has set March 27, 2013 as the record date for the annual meeting. All stockholders who owned Echelon common stock at the close of business on March 27, 2013 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, 2013, 43,057,160 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.

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### *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.

### ***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 also 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 C nominees for election as director.

**Proposals Two and Three** The affirmative vote of a majority of the shares present in person or represented by proxy and entitled to vote is required to (i) approve the amendment and restatement of our 1997 Stock Plan and (ii) ratify the appointment of KPMG LLP as our company's independent registered public accounting firm. You may vote FOR, AGAINST or ABSTAIN on Proposals Two and Three. Abstentions are deemed to be votes cast and have the same effect as a vote against the 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 the 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.

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**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) and in favor of our Amended and Restated 1997 Stock Plan (Proposal Two), because if you do not indicate how you want your shares voted on such proposals, your bank, broker or other nominee is not allowed to vote those shares on your behalf 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 and with respect to our Amended and Restated 1997 Stock Plan, no votes will be cast on your behalf. 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 Three).

### ***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 20, 2013, or by following the instructions at [www.proxyvote.com](http://www.proxyvote.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.

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### ***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.

**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 20, 2013.

### ***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

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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: 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 2014 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 10, 2013, 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 2014 proxy statement.

Alternatively, under our Bylaws, a proposal or a nomination that the stockholder does not seek to include in our 2014 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 2014 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 2014 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 2014 annual meeting was mailed or public disclosure was made. For example, if we provide notice of our 2014 annual meeting on April 22, 2014 for a 2014 annual meeting on May 20, 2014, any such proposal or nomination will be considered untimely if submitted to us after May 2, 2014. 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 2014 annual meeting.

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The rules of the SEC also establish a different deadline for submission of stockholder proposals that are not intended to be included in our 2014 proxy statement with respect to discretionary voting, or the Discretionary Vote Deadline. The Discretionary Vote Deadline for the 2014 annual meeting is February 23, 2014, 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 2014 annual meeting.

Because the Bylaw Deadline is not capable of being determined until we publicly announce the date of our 2014 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 2014 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 first adopted written 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, the Audit Committee and the 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

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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.

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 October, 2011, our Board of Directors 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 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

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providing, (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 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.

### ***Standards of Business Conduct***

We have adopted a Code of Business Conduct and Ethics that applies to all directors, officers and employees of Echelon. The Code of Business Conduct and Ethics can be viewed at the investor relations section of our website at [www.echelon.com](http://www.echelon.com). We will post any amendments to, or waivers from, our Code of Business Conduct and Ethics at that location on our website.



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### ***Stockholder Communications***

Any stockholder may contact any of our directors by writing to them by mail or express mail c/o Echelon Corporation, 550 Meridian Avenue, San Jose, California 95126.

Any stockholder communications directed to our Board of Directors (other than concerns regarding questionable accounting or auditing matters directed to the Audit Committee or otherwise in accordance with our Financial Information Integrity Policy, which Financial Information Integrity Policy can be viewed at the investor relations section of our website at [www.echelon.com](http://www.echelon.com)) will first go to our General Counsel, who will log the date of receipt of the communication as well as (for non-confidential communications) the identity of the correspondent in our stockholder communications log.

Unless the communication is marked confidential, our General Counsel will review, summarize and, if appropriate, draft a response to the communication in a timely manner. The summary and response will be in the form of a memo, which will become part of our stockholder communications log that our General Counsel maintains with respect to all stockholder communications.

At least quarterly, or more frequently as our General Counsel deems appropriate, our General Counsel will forward all such original stockholder communications along with the related memos to our Board of Directors for review.

Any stockholder communication marked confidential will be logged by our General Counsel as received but will not be reviewed, opened or otherwise held by our General Counsel. Such confidential correspondence will be immediately forwarded to the addressee(s) without a memo or any other comment by our General Counsel.

### **Meetings and Attendance of our Board of Directors and Committees of our Board of Directors**

#### ***Attendance of Directors at 2012 Annual Meeting of Stockholders***

It is the policy of our Board of Directors to strongly encourage board members to attend the annual meeting of stockholders. Six members of our Board of Directors attended in person our annual meeting of stockholders on May 22, 2012.

#### ***Attendance at Board and Committee Meetings***

Our Board of Directors held six meetings in 2012. Each director is expected to attend each meeting of our Board of Directors and those committees on which he or she serves. During 2012, no director attended fewer than 75% of the aggregate of (i) the total number of meetings of our Board of Directors (held during the period for which he or she was a director) and (ii) the total number of meetings held by all committees of our Board of Directors on which such director served (held during the periods that he or she served), except for Livio Gallo, who did not attend the lone applicable meeting. Mr. Gallo resigned from our Board of Directors, for personal reasons, as of March 14, 2012. During 2012, certain matters were approved by our Board of Directors or a committee of our Board of Directors by unanimous written consent.

#### **Committees of our Board of Directors**

Our Board of Directors currently has a standing Audit Committee, Compensation Committee, and Nominating and Corporate Governance Committee. Each of the Audit Committee, Compensation Committee, and Nominating and Corporate Governance Committee has a written charter that has been approved by our

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Board of Directors, copies of which can be viewed at the investor relations section of our website at [www.echelon.com](http://www.echelon.com). Pursuant to our 1997 Stock Plan, our Board of Directors delegated authority to our Chief Executive Officer, Ronald A. Sege, to grant stock options, performance shares, and stock-settled stock appreciation rights (SARs) to employees who are not executive officers of up to a maximum of 25,000 shares per person per year and, generally, up to an aggregate of 250,000 shares per year. The Compensation Committee, Audit Committee, and Nominating and Corporate Governance Committee are described as follows:

***Compensation Committee***

The members of the Compensation Committee are Armas Clifford Markkula, Jr., Richard M. Moley (Chair) and Betsy Rafael. The Compensation Committee held two meetings in 2012. The purposes of the Compensation Committee are to:

discharge the responsibilities of our Board of Directors relating to compensation of our executive officers;

approve and evaluate executive officer compensation plans, policies and programs; and

produce an annual report on executive compensation for inclusion in our proxy statement.

The responsibilities of the Compensation Committee include annually reviewing and approving, for our Chief Executive Officer and our other executive officers, (1) annual base salary, (2) annual incentive bonus, including the specific goals and amount, (3) equity compensation, (4) employment agreements, severance arrangements and change in control agreements and provisions, and (5) any other benefits, compensation or arrangements. In addition, the Compensation Committee will conduct an annual review of the performance of our Chief Executive Officer, and will oversee the management of risks associated with executive and employee compensation and plans to ensure that our company's compensation programs remain consistent with our stockholders' interests and that such programs do not encourage excessive risk-taking. The Compensation Committee also approves our company-wide pay-for-performance evaluation plan, as well as general metrics for employee base salaries when compared to peer companies and the scope of our annual equity compensation grant to employees.

***Audit Committee***

The members of the Audit Committee are Robyn M. Denholm, Robert J. Finocchio, Jr. (Chair) and Betsy Rafael. Our Board of Directors has determined that directors Denholm, Finocchio and Rafael are audit committee financial experts, as that term is defined in Item 401(h) of Regulation S-K of the Securities Act of 1933, as amended, and that all members of our Audit Committee are independent within the meaning of Rule 5605(a)(2) of the listing standards of the Marketplace Rules of NASDAQ. The Audit Committee held four meetings in 2012. The purposes of the Audit Committee are to:

oversee our accounting and financial reporting processes and the internal and external audits of our financial statements;

assist our Board of Directors in the oversight and monitoring of (1) the integrity of our financial statements, (2) our compliance with legal and regulatory requirements, (3) the independent auditor's qualifications, independence and performance, and (4) our internal accounting and financial controls;

outline to our Board of Directors the results of its monitoring and recommendations derived therefrom and improvements made, or to be made, in internal accounting controls;

prepare the report that the rules of the SEC require to be included in our annual proxy statement;

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appoint our independent registered public accounting firm; and

provide to our Board of Directors such additional information and materials as it may deem necessary to make our Board of Directors aware of significant financial matters that require the attention of our Board of Directors.

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The responsibilities of the Audit Committee include the continuous review of the adequacy of our system of internal controls; oversight of the work of our independent registered public accounting firm, including a post-audit review of the financial statements and audit findings; oversight of compliance with SEC requirements regarding audit related matters; review, in conjunction with counsel, of any legal matters that could significantly impact our financial statements; and oversight and review of our information technology and management information systems policies and risk management policies, including our investment policies.

### ***Nominating and Corporate Governance Committee***

The members of the Nominating and Corporate Governance Committee are Armas Clifford Markkula, Jr., Richard M. Moley and Larry Sonsini (Chair). The Nominating and Corporate Governance Committee held one meeting in 2012. The purpose of the Nominating and Corporate Governance Committee is to ensure that our Board of Directors is properly constituted to meet its fiduciary obligations to stockholders and our company and that our company has and follows appropriate governance standards. To carry out this purpose, the Nominating and Corporate Governance Committee shall:

assist our Board of Directors by identifying prospective director nominees and to recommend to our Board of Directors the director nominees for the next annual meeting of stockholders;

develop and recommend to our Board of Directors the governance principles applicable to our company;

oversee the evaluation of our Board of Directors and management; and

recommend to our Board of Directors director nominees for each committee.

The responsibilities of the Nominating and Corporate Governance Committee include evaluating the composition, organization and governance of our Board of Directors and its committees, including determining future requirements; overseeing the performance evaluation process of our Board of Directors; making recommendations to our Board of Directors concerning the appointment of directors to committees, selecting Board committee chairs and proposing the slate of directors for election; and making recommendations to our Board of Directors regarding compensation for non-employee directors and Board committee members.

### **Director Independence**

Our Board of Directors has affirmatively determined that each of its members, other than Robert R. Maxfield and Ronald A. Sege, are independent directors under the listing standards of the Marketplace Rules of NASDAQ and applicable SEC rules, and that all of its members, other than Mr. Maxfield and Mr. Sege, were independent directors under the listing standards of the Marketplace Rules of NASDAQ in the three prior years.

Our Board of Directors has also determined that all directors serving as members of our Audit Committee, Compensation Committee, and Nominating and Corporate Governance Committee are independent under the NASDAQ listing standards and the rules of the SEC. Additionally, our Board of Directors has determined that all members of the Compensation Committee meet the non-employee director definition of Rule 16b-3 promulgated under Section 16 of the Securities Exchange Act of 1934, as amended, and the outside director definition of Section 162(m) of the Internal Revenue Code of 1986, as amended.

**Table of Contents****Director Compensation**

In February 2007, our Board of Directors determined that in consideration for service on our Board of Directors, each non-employee director shall receive a cash payment of \$40,000 per fiscal year, to be paid quarterly. In addition, in consideration for service on our Board of Directors or on one or more of our Compensation and/or Nominating and Corporate Governance Committees of our Board of Directors, each non-employee director shall receive a cash payment of \$1,000 per Board of Directors meeting or Committee meeting attended, to be payable on the date of each such meeting so attended. We also determined that in consideration of the significantly greater time commitment and potential risk exposure for serving as a member of our Audit Committee, each director shall receive a cash payment of \$2,000 per Audit Committee meeting attended, to be payable on the date of each such meeting so attended. From time to time, our Board of Directors may establish ad hoc committees constituted for a specific purpose or purposes. Payments, if any, to directors for serving on these committees are determined by our Board of Directors on a real-time basis.

Furthermore, non-employee directors are eligible to participate in our 1997 Stock Plan. Our Board of Directors has adopted a program, effective as of the July 27, 2008 expiration date of our 1998 Director Option Plan, for automatically granting awards of nonqualified stock options to non-employee directors under our 1997 Stock Plan on the same terms as grants previously made under our 1998 Director Option Plan. Such program provides for the automatic grant of an option to purchase 25,000 shares of common stock on the date on which such person first becomes a non-employee director. Additionally, each non-employee director shall automatically be granted a 10,000 share option on the date of each annual meeting of stockholders, provided he or she is re-elected to our Board of Directors or otherwise remains on our Board of Directors on such date and provided that on such date he or she shall have served on our Board of Directors for at least the preceding six months. All options granted under this program are fully vested at grant. On May 22, 2012, the date of our 2012 annual meeting of stockholders, directors Denholm, Finocchio, Maxfield, Markkula, Moley, Rafael and Sonsini were each granted a 10,000 share option at a per share exercise price of \$3.52.

**Director Summary Compensation Table for Fiscal 2012**

The table below summarizes the compensation paid by our company to non-employee directors for the fiscal year ended December 31, 2012.

Name	Fees Earned or	Option Awards	Total (\$)
	Paid in Cash (\$)	(\$)(1)(2)(3)	
Robyn M. Denholm	53,000	13,423	66,423
Robert J. Finocchio, Jr. Livio Gallo (4)	64,000	13,423	77,423
Armas Clifford Markkula, Jr.(5)	49,000	13,423	62,423
Robert R. Maxfield	56,000	13,423	69,423
Richard M. Moley (5)	59,000	13,423	72,423
Betsy Rafael	66,000	13,423	79,423
Larry W. Sonsini (5)	48,000	13,423	61,423

- (1) Amounts shown do not reflect compensation actually received by the directors. Instead, the amounts shown are the grant date fair value of the stock awards (disregarding an estimate of forfeitures) as determined in accordance with FASB ASC Topic 718, which were recognized for financial statement purposes. The assumptions used in the valuation of these awards are set forth in the notes to our consolidated financial statements, which are included in our Annual Report on Form 10-K for the year ended December 31, 2012, filed with the SEC on March 1, 2013. These amounts do not correspond to the actual value that will be recognized by the directors upon exercise or sale of such awards.
- (2) On May 22, 2012, the date of our annual meeting of stockholders, each non-employee director serving in such capacity for at least the prior six months was granted a fully vested option to purchase 10,000 shares at a per share exercise price of \$3.52, the closing price of our common stock on that date.

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- (3) As of December 31, 2012, the aggregate number of shares underlying options outstanding for each of our non-employee directors was:

Name	Aggregate Number of Shares
Robyn M. Denholm	65,000
Robert J. Finocchio, Jr.	50,000
Livio Gallo	
Armas Clifford Markkula, Jr.	50,000
Robert R. Maxfield	30,000
Richard M. Moley	50,000
Betsy Rafael	40,000
Larry W. Sonsini	50,000

- (4) Mr. Gallo was appointed to Echelon's Board of Directors effective June 30, 2011 and resigned effective March 14, 2012. Mr. Gallo elected not to receive any equity or cash compensation during his tenure citing rules imposed by his employer, Enel Distribuzione.
- (5) Cash fees include \$1,000 for a Nominating and Governance Committee meeting held in 2011 but paid in 2012.

**PROPOSAL ONE****ELECTION OF DIRECTORS****General**

We currently have eight members on our Board of Directors. Our Board of Directors is divided into three classes, with each director serving a three-year term and one class being elected at each year's annual meeting of stockholders. Robyn M. Denholm, Richard M. Moley and Betsy Rafael are the Class C directors whose terms will expire at the 2013 Annual Meeting of Stockholders and they have been nominated by our Board of Directors for reelection at the Annual Meeting of Stockholders to be held May 21, 2013. Ronald A. Sege and Larry W. Sonsini are the Class A directors whose terms will expire at the 2014 Annual Meeting of Stockholders, and Robert J. Finocchio, Jr., Armas Clifford Markkula, Jr. and Robert R. Maxfield are the Class B directors whose terms will expire at the 2015 Annual Meeting of Stockholders. All of the directors, including the Class C nominees, are incumbent directors. There are no family relationships among any of our directors or executive officers, including any of the nominees mentioned above. Unless otherwise instructed, the holders of proxies solicited by this Proxy Statement will vote the proxies received by them for the three Class C nominees. In the event that any nominee is unable or declines to serve as a director at the time of the annual meeting, the proxy holders will vote for a nominee designated by the present Board of Directors to fill the vacancy. We are not aware of any reason that any nominee will be unable or will decline to serve as a director. Our Board of Directors recommends a vote **FOR** the election of each of the Class C nominees listed above.

**Director Information****Current Directors**

The names of the members of our Board of Directors, including the Class C nominees, their ages as of March 27, 2013, and certain information about them, are set forth below.

Name	Age	Principal Occupation
Robyn M. Denholm (1) (2)	49	Chief Financial Officer and Executive Vice President of Juniper Networks, Inc.
Robert J. Finocchio, Jr. (2)	61	Corporate director, private investor and part time professor

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<b>Name</b>	<b>Age</b>	<b>Principal Occupation</b>
Armas Clifford Markkula, Jr. (3) (4)	71	Vice Chairman of the Board of Directors of Echelon
Robert R. Maxfield	71	Private investor
Richard M. Moley (1) (3) (4)	74	Private investor
Betsy Rafael (1) (2) (3)	51	Corporate Director
Ronald A. Sege (5)	55	Chairman of the Board, President and Chief Executive Officer of Echelon
Larry W. Sonsini (4)	72	Chairman of Wilson Sonsini Goodrich & Rosati, P.C.

- (1) Denotes nominee for election at the 2013 Annual Meeting of Stockholders.  
(2) Member of the Audit Committee.  
(3) Member of the Compensation Committee.  
(4) Member of the Nominating and Corporate Governance Committee.  
(5) Sole member of the stock option committee.

**Director Biographies**

The business experience and other specific skills, attributes and qualifications of each of the nominees is as follows:

*Robyn M. Denholm* has been a director of our company since 2008. Ms. Denholm is currently Chief Financial Officer and Executive Vice President of Juniper Networks. Prior to joining Juniper Networks in August 2007, Ms. Denholm was employed at Sun Microsystems where she served as Senior Vice President, Corporate Strategic Planning. In that role, she was responsible for Sun's corporate operating system, and the global sales and service administration function and she served as the leader of Sun's business transformation initiative. Ms. Denholm joined Sun in 1996 and served in executive assignments that included Senior Vice President, Finance; Vice President and Corporate Controller (Chief Accounting Officer); Vice President, Finance; Service Division, Director, Shared Financial Services APAC and Controller, Australia/New Zealand. Prior to joining Sun, Ms. Denholm served at Toyota Motor Corporation Australia for seven years and at Arthur Andersen and Company for five years, in various finance assignments. Ms. Denholm is a Fellow of the Institute of Chartered Accountants of Australia and holds a Bachelors degree in Economics from the University of Sydney and a Masters of Commerce degree from the University of New South Wales.

Our Nominating and Corporate Governance Committee has reviewed Ms. Denholm's qualifications and background and has determined that based on her extensive executive and financial experience, Ms. Denholm is well qualified to serve as a director of our company in light of our company's business activities.

*Robert J. Finocchio, Jr.* has been a director of our company since 1999. Mr. Finocchio served as Chairman of the Board of Informix Corporation, an information management software company, from August 1997 to September 2000. Since September 2000, Mr. Finocchio has been a dean's executive professor at Santa Clara University's Leavey School of Business. From July 1997 until July 1999, Mr. Finocchio served as President and Chief Executive Officer of Informix. From December 1988 until May 1997, Mr. Finocchio was employed with 3Com Corporation, a global data networking company, where he held various positions, most recently serving as President, 3Com Systems. Mr. Finocchio also serves as a director of Broadcom Corporation and served as a director of Altera Corp. from 2002 to December 2011 and as a director of Sun Microsystems from 2006 to January 2010. Mr. Finocchio is Chair of the Board of Trustees of Santa Clara University. Mr. Finocchio holds a B.S. degree in Economics from Santa Clara University and an M.B.A. degree from the Harvard Business School.

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Our Nominating and Corporate Governance Committee has reviewed Mr. Finocchio's qualifications and background and has determined that based on his extensive executive and financial experience, Mr. Finocchio is well qualified to serve as a director of our company in light of our company's business activities.

*Armas Clifford Markkula, Jr.* is the founder of our company and has served as a director since 1988. He has been Vice Chairman of our Board of Directors since 1989. Mr. Markkula was Chairman of the Board of Apple Computer from January 1977 to May 1983 and from October 1993 to February 1996 and was a director from 1977 to 1997. A founder of Apple, he held a variety of positions there, including President/Chief Executive Officer and Vice President of Marketing. Prior to founding Apple, Mr. Markkula was with Intel Corporation as Marketing Manager, Fairchild Camera and Instrument Corporation as Marketing Manager in the Semiconductor Division, and Hughes Aircraft as a member of the technical staff in the company's research and development laboratory. Mr. Markkula is a former trustee of Santa Clara University and served as Chair of the Board of Trustees from 2003 through 2009. Mr. Markkula received B.S. and M.S. degrees in Electrical Engineering from the University of Southern California.

Our Nominating and Corporate Governance Committee has reviewed Mr. Markkula's qualifications and background and has determined that based on his extensive executive experience, Mr. Markkula is well qualified to serve as a director of our company in light of our company's business activities.

*Robert R. Maxfield* has been a director of our company since 1989 and served as President and Chief Executive Officer of our company from November 2009 until August 18, 2010 and as assistant to the CEO/President from August 19, 2010 to November 4, 2010. He also served as our company's Senior Vice President of Products from April 2008 through September 2008 and a consultant to our company from October 2008 through April 2009. He was a co-founder of ROLM in 1969, and served as Executive Vice President and a director until ROLM's merger with IBM in 1984. Following the merger, he continued to serve as Vice President of ROLM until 1988. Since 1988, he has been a private investor. Mr. Maxfield was a venture partner with Kleiner, Perkins, Caufield & Byers, a venture capital firm, from 1989 to 1992. Mr. Maxfield received B.A. and B.S.E.E. degrees from Rice University, and M.S. and Ph.D. degrees in Electrical Engineering from Stanford University.

Our Nominating and Corporate Governance Committee has reviewed Mr. Maxfield's qualifications and background and has determined that based on his extensive executive experience, Mr. Maxfield is well qualified to serve as a director of our company in light of our company's business activities.

*Richard M. Moley* has been a director of our company since 1997. Since August 1997, Mr. Moley has been a private investor. From July 1996 to August 1997, he served as Senior Vice President, Wide Area Business Unit and as a director of Cisco Systems, following Cisco Systems purchase of StrataCom, where he was Chairman of the Board, Chief Executive Officer and President. Mr. Moley also serves as a director of Linear Technology. Mr. Moley received a B.S. degree in Electrical Engineering from Manchester University, an M.S. degree in Electrical Engineering from Stanford University and an M.B.A. degree from Santa Clara University.

Our Nominating and Corporate Governance Committee has reviewed Mr. Moley's qualifications and background and has determined that based on his extensive executive experience, Mr. Moley is well qualified to serve as a director of our company in light of our company's business activities.

*Betsy Rafael* has been a director of our company since 2005. Ms. Rafael served as Principal Accounting Executive of Apple Inc. from January 2008 to October 19, 2012 and as its Vice President and Corporate Controller until October 19, 2012. From September 2006 to August 2007, Ms. Rafael held the



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position of Vice President, Corporate Finance for Cisco Systems. From April 2002 to September 2006, she served as Vice President, Corporate Controller and Principal Accounting Officer of Cisco Systems. From December 2000 to April 2002, Ms. Rafael was the Executive Vice President, Chief Financial Officer, and Chief Administrative Officer of Aspect Communications, Inc., a provider of customer relationship portals. From April 2000 to November 2000, Ms. Rafael was Senior Vice-President and CFO of Escalate Inc., an enterprise e-commerce application service provider. From 1994 to 2000, Ms. Rafael held a number of senior positions at Silicon Graphics, culminating her career at Silicon Graphics as Senior Vice President and Chief Financial Officer. Prior to SGI, Ms. Rafael held senior management positions in finance with Sun Microsystems and Apple Computer. Ms. Rafael began her career with Arthur Young & Company. Ms. Rafael received a B.S.C. degree in Accounting from Santa Clara University.

Our Nominating and Corporate Governance Committee has reviewed Ms. Rafael's qualifications and background and has determined that based on her extensive executive and financial experience, Ms. Rafael is well qualified to serve as a director of our company in light of our company's business activities.

*Ronald A. Sege* has been President, Chief Executive Officer and a member of our Board of Directors since August 19, 2010. Our Board of Directors appointed Mr. Sege as Chairman of the Board on October 12, 2011. Mr. Sege served as President and Chief Operating Officer and a member of the board of directors of 3Com Corporation ( 3Com ) from April 2008 until the acquisition of 3Com by Hewlett-Packard Company effective April 12, 2010. Prior to re-joining 3Com, Mr. Sege served as President and Chief Executive Officer of Tropos Networks, Inc., a provider of wireless broadband networks, from 2004 to 2008. Prior to Tropos, Mr. Sege was President and Chief Executive Officer of Ellacoya Networks, Inc., a provider of broadband service optimization solutions based on deep packet inspection technology, from 2001 to 2004. Prior to Ellacoya, Mr. Sege was Executive Vice President of Lycos, Inc., an internet search engine, from 1998 to 2001. Prior to Lycos, Mr. Sege spent nine years at 3Com, from 1989 to 1998, serving in a variety of senior management roles including Executive Vice President, Global Systems Business Unit. Mr. Sege joined the Board of Directors of Ubiquiti Networks, Inc. in October 2012. Mr. Sege holds an M.B.A. from Harvard University and a B.A. degree from Pomona College.

Our Nominating and Corporate Governance Committee has reviewed Mr. Sege's qualifications and background and has determined that based on his extensive executive experience, Mr. Sege is well qualified to serve as a director of our company in light of our company's business activities.

*Larry W. Sonsini* has been a director of our company since 1993. Mr. Sonsini serves as Chairman of the law firm of Wilson Sonsini Goodrich & Rosati, P.C., where he has practiced since 1966. Mr. Sonsini received an A.B. degree in Political Science and Economics and an L.L.B. degree from the University of California at Berkeley. Mr. Sonsini served as a director of LSI Logic Corporation (currently LSI Corporation), from 2000 to 2006, as a director of Pixar from 1995 to 2006 and as a director of Silicon Valley Bancshares from 2003 to 2006.

Our Nominating and Corporate Governance Committee has reviewed Mr. Sonsini's qualifications and background and has determined that based on his extensive executive and legal experience, Mr. Sonsini is well qualified to serve as a director of our company in light of our company's business activities.

***Class C Director Nominees***

Robyn M. Denholm

Richard M. Moley

Betsy Rafael

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***Vote Required***

Directors shall be elected by a plurality vote. The three Class C nominees for director receiving the highest number of affirmative votes of the shares entitled to be voted for them shall be elected as directors. Votes against, abstentions and broker non-votes have no legal effect on the election of directors due to the fact that such elections are by a plurality.

**Board Recommendation**

**OUR BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS A VOTE FOR THE PROPOSED SLATE OF CLASS C DIRECTORS.**

**PROPOSAL TWO**

**APPROVAL OF THE AMENDED AND RESTATED 1997 STOCK PLAN**

We are asking stockholders to approve the amendment and restatement of the Echelon Corporation 1997 Stock Plan (the Plan). The Board has determined it is in the best interest of the Company and our stockholders to amend and restate the Plan to (i) extend the term of the Plan through April 3, 2023; (ii) establish an aggregate reserve of 10,905,404 shares of our Common Stock issuable under the Plan, which represents a substantial reduction to the Plan's current share reserve; (iii) eliminate the annual evergreen share increase provision and establish limits on the number of shares issuable under the Plan in the form of restricted shares or restricted stock units; (iv) establish annual limits on equity awards under the Plan to non-employee members of our Board; and (v) approve a revised menu of performance-based compensation measures under Section 162(m) of the Internal Revenue Code (Section 162(m)).

We believe strongly that approving the Plan is essential to our continued success and therefore is in the best interest of the Company and our stockholders. Our employees are our most valuable assets. The Board believes that grants of equity awards available under the Plan will help create long-term equity participation in the Company and thereby assist us in attracting, retaining, motivating and rewarding employees, directors, and consultants.

In setting the share reserve under the Plan, we considered the number of outstanding awards and our forecasted grants under the Plan. As of March 29, 2013, a total of 20,972,838 shares of our Common Stock were reserved for issuance under the Plan, of which 5,505,404 shares were subject to outstanding awards and 15,467,434 shares remained available for new awards under the Plan. If shareholders approve the Plan, the total number of shares issuable under the Plan after April 3, 2013, will be reduced from 20,972,838 to 10,905,404, including the 5,505,404 shares subject to current outstanding awards plus an additional 5,400,000 shares for future new awards. The shares added for future awards are anticipated to be sufficient to meet our expected grants under the Plan for the next two to three years, however future business needs may affect this projection. In determining size of the share reserve, we took into account our historical grant practices and our rate of granting equity awards (burn rate). Over the past three year period ending in 2012, our average annual burn rate has been 7.49%, which is above industry guidelines recommended by proxy advisory firms. If our stockholders approve the amendment and restatement of the Plan, we have committed not to exceed a three year average burn rate of 5.77% over the next three year period ending in 2015.

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Under the amended and restated Plan, the annual evergreen share replenishment will be eliminated prospectively and a limitation on the number of shares issuable as restricted stock units and restricted shares (referred to as full value awards ) will be added to the Plan. The latter change would be effected by adding a fungible share ratio to the Plan whereby grants of full value awards after May 21, 2013, reduce the number of shares issuable under the Plan by 1.7 shares for each share subject to such awards. If shares subject to such awards are subsequently forfeited or otherwise would return to the Plan reserve, the unvested or cancelled shares will be returned to the share reserve as 1.7 shares for each share forfeited or otherwise returned to the Plan share reserve.

We are also seeking to approve the menu of performance-based compensation measures to be used under the Plan as required by Section 162(m). Our stockholders have previously approved similar performance-based compensation measures, and we are asking for approval of a new expanded menu, as required under Section 162(m) in order to potentially qualify for the availability of federal tax deductions for certain performance-based compensation. If this proposal is not approved by our stockholders, we will make no future equity awards under the Plan on or after the date of our 2013 annual stockholder meeting.

We are also seeking approval of an annual limit on awards to non-employee members of our Board of 50,000 shares.

Our Board approved as of April 3, 2013, subject to stockholder approval, the amendment and restatement of the Plan, which is attached as Appendix A to this Proxy Statement and described in this proposal. If the stockholders approve the amended and restated Plan, it will replace the current version of the Plan. Otherwise, the current version of the Plan will remain in effect.

Our executive officers and directors have an interest in the amendment and restatement of the Plan because they are eligible for awards under the Plan.

### **Description of the Amended and Restated 1997 Stock Plan**

The following description of the principal features of the amended and restated Plan is qualified in its entirety by reference to the text of the amended and restated Plan, which is attached as Appendix A to this Proxy Statement.

#### ***Purpose***

The purpose of the Plan is to attract and retain the best available personnel for positions of substantial responsibility, to provide additional incentive to employees, directors and consultants, and to promote the success of the Company's business.

#### ***Eligibility***

Awards may be granted to employees, directors and consultants of the Company and employees and consultants of any parent or subsidiary corporation of the Company. Incentive stock options may be granted only to employees who, as of the time of grant, are employees of the Company or any parent or subsidiary corporation of the Company. As of March 27, 2013, the Company had approximately 221 employees (full-time and part-time employees), including five named executive officers seven non-employee directors, who would be eligible to participate in the Plan.

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### ***Administration of Plan***

The Plan is administered by our Board or a committee of individuals satisfying applicable laws appointed by the Board (the Committee). To make grants to certain officers and key employees of the Company, the members of the Committee must qualify as non-employee directors under Rule 16b-3 of the Securities Exchange Act of 1934. In the case of awards intended to qualify for the performance-based compensation exemption under Section 162(m) of the Code, administration must be by a compensation committee comprised solely of two or more outside directors within the meaning of Section 162(m) of the Code. Note that the Committee is not required to structure awards in a manner that qualifies for the performance-based compensation exemption under Section 162(m) of the Code and may structure them in a different manner if it feels that it is appropriate.

### ***Share Reserve***

If stockholders approve this proposal, a total of 10,905,404 shares of our Common Stock will be authorized for issuance under the Plan. This number includes 5,505,404 shares subject to outstanding awards as of March 29, 2013, consisting of stock options and stock-settled SARs to purchase 3,658,154 shares of our Common Stock and performance shares and restricted stock units to acquire 1,847,250 shares of our Common Stock. The outstanding stock options and stock-settled SARs had a weighted average exercise price of \$5.785 and a weighted average contractual term of 5.41 years. In addition, the Plan reserve will include 5,400,000 shares of our Common Stock available for future awards.

Any shares subject to an award granted prior to May 21, 2013, the date of our 2013 annual meeting of stockholders, with a per share price less than the fair market value of our Common Stock on the date of grant were counted against the authorized share reserve as 1 share for every 1 share subject to the award, and if returned to the Plan such shares are counted as 1 shares for every 1 share returned. For any awards granted on or after May 21, 2013, any shares subject to an award with a per share price less than the fair market value of our Common Stock on the date of grant will be counted against the authorized share reserve as 1.7 shares for every 1 share subject to such award, and if returned to the Plan such shares will be counted as 1.7 shares for every 1 share returned.

If an award expires or becomes unexercisable without having been exercised in full, or, with respect to restricted stock, RSUs, performance shares or performance units, is forfeited to or repurchased by the Company, the unpurchased shares (or for awards other than stock options and SARs, the forfeited or repurchased shares) will become available for future grant or sale under the Plan. If a SAR is settled in shares, the gross number of shares exercised will cease to be available under the Plan. Shares that actually have been issued under the Plan under any award will not be returned to the Plan and will not become available for future distribution under the Plan.

If unvested shares of restricted stock, RSUs, performance shares or performance units are repurchased by the Company or are forfeited to the Company, such shares will become available for future grant under the Plan. Shares used to pay the exercise or purchase price of an award (including pursuant to a net exercise of a stock option) and/or to satisfy the tax withholding obligations related to a stock option or SAR will not become available for future grant or sale under the Plan. Notwithstanding the foregoing however, and for the avoidance of doubt, shares used to satisfy tax withholding obligations related to restricted stock, RSUs, deferred stock units, performance shares or performance units shall become available for future grant or sale under the Plan. Awards paid out in cash rather than shares will not reduce the number of shares available for issuance under the Plan.

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### ***Limitations***

The Plan contains annual grant limits intended to satisfy Section 162(m). Specifically, the maximum number of shares which could be issued to any one individual in any fiscal year pursuant to stock options or SARs is limited to 1,000,000. The maximum which could be issued to any one individual in any fiscal year pursuant to the grant of restricted shares or RSUs is 500,000 shares. The maximum which could be issued to any one individual in any fiscal year pursuant to performance units or performance shares is \$1,000,000 and 1,000,000 shares, respectively. In addition, an individual may be granted stock options or SARs to purchase up to an additional 1,000,000 shares of Common Stock, or restricted shares or RSUs with respect to 1,000,000 shares, in connection with his or her initial hiring by the Company.

The Committee will adjust the maximum number and type of securities that may be granted pursuant to the Plan, the limitations on annual grants to individuals or in connection with an individual's initial hiring, as well as the number and type of securities subject to outstanding awards, the grant price or the other price of shares subject to outstanding awards, in the event of a stock split, reverse stock split, stock dividend, combination or reclassification of our Common Stock, or other increase or decrease in the number of shares of Common Stock effected without the receipt of consideration.

Separately, the Plan limits the shares subject to awards that can be made each year to our non-employee Board members to 50,000 per fiscal year.

### ***Awards***

The Plan provides for the grant of incentive stock options, non-statutory stock options, restricted stock, restricted stock units ( RSUs ), stock appreciation rights ( SARs ), performance units and performance shares. Set forth below is a general description of the types of awards that may be granted under the Plan. On April 3, 2013 the closing price of our Common Stock on the NASDAQ was \$2.28 per share.

### ***Stock Options***

The per share exercise price for the shares to be issued pursuant to exercise of a stock option shall be no less than 100% of the fair market value of our Common Stock on the date of grant. The term of any stock option, including specifically an incentive stock option, may not exceed ten years, except that with respect to any participant who owns 10% of the voting power of all classes of our outstanding stock, the term of an incentive stock option must not exceed five years and the exercise price must equal at least 110% of the fair market value on the grant date. The Committee determines the term of all other stock options.

Upon termination of a participant's service with us or any parent or subsidiary of ours, he or she may exercise his or her stock option for the period of time stated in the stock option agreement. Generally, if termination is due to death or disability, the stock option will remain exercisable for 12 months. In all other cases, the stock option will generally remain exercisable for thirty days. However, a stock option may never be exercised later than the expiration of its term.

### ***Stock Appreciation Rights***

SARs allow the recipient to receive the appreciation in the fair market value of our Common Stock between the exercise date and the date of grant. The Committee determines the terms of SARs, including when such rights become exercisable and whether to pay the increased appreciation in cash or with shares of our Common Stock, or a combination thereof. Notwithstanding the foregoing, the terms of a SAR will require that the per share exercise price for the shares to be issued pursuant to the exercise of a SAR shall be no less than 100% of the fair market value of our Common Stock on the date of grant and the term of any SAR may not exceed ten years.

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### ***Restricted Stock***

Restricted stock awards are shares of our Common Stock that vest in accordance with terms and conditions established by the Committee. The Committee will determine the number of shares of restricted stock granted to any employee. The Committee may impose whatever conditions to vesting it determines to be appropriate. For example, the Committee may set restrictions based on the achievement of specific performance goals. Shares of restricted stock that do not vest are subject to our right of repurchase or forfeiture.

### ***Restricted Stock Units***

Restricted stock units (RSUs) represent the right to receive shares of our Common Stock after satisfying applicable vesting conditions established by the Committee. RSUs also may be settled in cash. The Committee will set vesting criteria in its discretion, which, depending on the extent to which the criteria are met, will determine the number of RSUs that will be paid out to the employee. The Committee may set vesting criteria based upon service with the Company, the achievement of Company-wide, business unit, or individual goals, performance goals or any other basis determined by the Committee in its discretion. Unless and until the RSUs vest, the employee will have no right to receive shares or a cash payment under such RSUs.

### ***Performance-Based Compensation***

Performance units and performance shares are awards that will result in a payment to a participant only if performance goals established by the Committee are achieved or the awards otherwise vest. As described below, the Committee will establish organizational or individual performance goals in its discretion within the parameters of the Plan, which, depending on the extent to which they are met, will determine the degree of granting, vesting and/or payout value of performance units and performance shares to be paid out to participants. Performance units will have an initial dollar value established by the Committee on or before the grant date. Performance shares will have an initial value equal to the fair market value of our Common Stock on the grant date.

The Plan, as proposed to be amended and restated and subject to stockholder approval, provides specific measures from which the Committee may base performance goals. Specifically, performance goals to be used for awards shall be chosen from one or more of the following measures: revenue, gross margin, operating margin, operating income, pre-tax profit, earnings before interest, taxes and depreciation (EBITDA), net income, operating cash flow, cash position, expenses, the market price of a Common Stock, earnings per share, return on stockholder equity, return on capital, total shareholder return, economic value added, number of customers, market share, return on investments, profit after taxes, objective customer indicators, productivity improvements, supplier awards from significant customers, new product development, working capital, objectively determinable individual objectives, return on equity, return on assets, return on sales, and sales. The performance goals may differ from participant to participant and from award to award, may be used to measure the performance of the Company as a whole or a business unit or other segment of the Company, or one or more product lines or specific markets and may be measured relative to a peer group or index. Any criteria used may be measured in absolute terms or in terms of growth, compared to other companies, measured against the market as a whole or and/or according to applicable market indices, measured against the Company as a whole or a segment of the Company, and/or measured on a pre-tax or post-tax basis, if applicable.

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Prior to the beginning of any applicable performance period or such later date as permitted under Section 162(m), the Compensation Committee will establish one or more performance goals applicable to the awards of the executive officers covered by Section 162(m). The target levels with respect to these performance measures may be expressed on an absolute basis or relative to a standard specified by the Committee. The degree of attainment of these performance measures will, according to criteria established by the Committee, be computed before the effect of changes in accounting standards, restructuring charges and similar extraordinary items occurring after the establishment of the performance goals applicable to a performance award.

Following completion of the applicable performance period, the Compensation Committee will certify, as to the executive officers covered by Section 162(m), the extent to which the applicable performance goals have been attained and the resulting value to be paid to each such executive officer. The Committee retains the discretion to eliminate or reduce, but not increase, the amount that would otherwise be payable to such executive officer on the basis of the performance goals attained. However, no such reduction may increase the amount paid to any other executive officer. Performance award payments may be made in lump sum or in installments. If any payment is to be made on a deferred basis, the Committee may provide for the payment of dividend equivalents or interest during the deferral period. In no event will any dividend equivalents be paid in connection with an stock options or stock appreciation rights granted under the Plan.

The Company reserves the right to grant awards that do not qualify for the Section 162(m) performance-based exception and does not guarantee that any award intended to qualify as performance-based compensation under Section 162(m) so qualifies.

### ***Effect of a Merger or Asset Sale***

The Plan provides that in the event of a merger or sale of substantially all assets of the Company, each outstanding award may be assumed or substituted by the successor corporation or a parent or subsidiary of the successor corporation. If there is no assumption or substitution of outstanding awards, such awards will become fully vested and exercisable prior to such transaction, and the Committee will provide notice to the recipient that he or she has the right to exercise outstanding awards for a period of 15 days from the date of the notice. Awards will terminate upon the expiration of the 15-day period. Awards made to a non-employee director that are assumed or substituted for will become fully vested if such participant's status as a director of the successor corporation terminates after a merger or sale of assets qualifying as a change of control other than due to an involuntary resignation. Awards made to our employees and consultants will be subject to a double-trigger full accelerated vesting if such employee or consultant is terminated by us or a successor to us without cause or if such employee or consultant resigns for involuntary termination, provided that the termination or resignation occurs within the 12 months following a change in control.

### ***Transferability***

Unless otherwise permitted by the Committee, the Plan generally does not allow for the transfer of awards, and, consequently, only the recipient of an award generally may exercise an award during his or her lifetime.

### ***Prohibition on Repricing Awards***

Unless approved by our stockholders, no stock option or SAR may be amended to reduce its exercise price or measurement price, and no outstanding stock option or SAR may be cancelled in exchange for the grant in substitution thereof any new awards with a lower exercise price or measurement price, and no outstanding stock option or SAR may be cancelled in exchange for cash, except in connection with a reorganization event or change of control.

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### ***Termination and Amendment***

The Plan will automatically terminate on April 3, 2023, unless we terminate it sooner. In addition, the Committee has the authority to amend, suspend or terminate the Plan provided such action does not impair the rights of any participant. However, the Company intends to obtain stockholder approval with respect to any further amendments to the Plan to the extent required by applicable law.

### **Summary of U.S. Federal Income Tax Consequences**

The following summary is intended only as a general guide to the U.S. federal income tax consequences of participation in the Plan and does not attempt to describe all possible federal or other tax consequences of such participation or tax consequences based on particular circumstances.

***Incentive Stock Options.*** An optionee recognizes no taxable income for regular income tax purposes as a result of the grant or exercise of an incentive stock option qualifying under Section 422 of the Internal Revenue Code. Optionees who neither dispose of their shares within two years following the date the stock option was granted nor within one year following the exercise of the stock option will normally recognize a capital gain or loss equal to the difference, if any, between the sale price and the purchase price of the shares. If an optionee satisfies such holding periods upon a sale of the shares, the Company will not be entitled to any deduction for federal income tax purposes. If an optionee disposes of shares within two years after the date of grant or within one year after the date of exercise (a disqualifying disposition), the difference between the fair market value of the shares on the determination date (see discussion under *Nonstatutory Stock Options* below) and the stock option exercise price (not to exceed the gain realized on the sale if the disposition is a transaction with respect to which a loss, if sustained, would be recognized) will be taxed as ordinary income at the time of disposition. Any gain in excess of that amount will be a capital gain. If a loss is recognized, there will be no ordinary income, and such loss will be a capital loss. Any ordinary income recognized by the optionee upon the disqualifying disposition of the shares generally should be deductible by the Company for federal income tax purposes, except to the extent such deduction is limited by applicable provisions of the Code.

The difference between the stock option exercise price and the fair market value of the shares on the determination date of an incentive stock option (see discussion under *Nonstatutory Stock Options* below) is treated as an adjustment in computing the optionee's alternative minimum taxable income and may be subject to an alternative minimum tax which is paid if such tax exceeds the regular tax for the year. Special rules may apply with respect to certain subsequent sales of the shares in a disqualifying disposition, certain basis adjustments for purposes of computing the alternative minimum taxable income on a subsequent sale of the shares and certain tax credits which may arise with respect to optionees subject to the alternative minimum tax.

***Nonstatutory Stock Options.*** Stock options not designated or qualifying as incentive stock options will be nonstatutory stock options having no special tax status. An optionee generally recognizes no taxable income as the result of the grant of such a stock option. Upon exercise of a nonstatutory stock option, the optionee normally recognizes ordinary income in the amount of the difference between the stock option exercise price and the fair market value of the shares on the determination date (as defined below). If the optionee is an employee, such ordinary income generally is subject to withholding of income and employment taxes. The determination date is the date on which the stock option is exercised unless the shares are subject to a substantial risk of forfeiture (as in the case where an optionee is permitted to exercise



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an unvested stock option and receive unvested shares which, until they vest, are subject to the Company's right to repurchase them at the original exercise price upon the optionee's termination of service) and are not transferable, in which case the determination date is the earlier of (i) the date on which the shares become transferable or (ii) the date on which the shares are no longer subject to a substantial risk of forfeiture. If the determination date is after the exercise date, the optionee may elect, pursuant to Section 83(b) of the Code, to have the exercise date be the determination date by filing an election with the Internal Revenue Service no later than 30 days after the date the stock option is exercised. Upon the sale of stock acquired by the exercise of a nonstatutory stock option, any gain or loss, based on the difference between the sale price and the fair market value on the determination date, will be taxed as capital gain or loss. No tax deduction is available to the Company with respect to the grant of a nonstatutory stock option or the sale of the stock acquired pursuant to such grant. The Company generally should be entitled to a deduction equal to the amount of ordinary income recognized by the optionee as a result of the exercise of a nonstatutory stock option, except to the extent such deduction is limited by applicable provisions of the Code.

***Stock Appreciation Rights.*** No taxable income is reportable when a SAR is granted to a participant. Upon exercise, the participant will recognize ordinary income in an amount equal to the amount of cash received and the fair market value of any shares of our Class A Common Stock received. Any additional gain or loss recognized upon any later disposition of the shares would be capital gain or loss.

***Restricted Stock Awards.*** A participant acquiring restricted stock generally will recognize ordinary income equal to the fair market value of the shares on the determination date (as defined above under *Nonstatutory Stock Options*). If the participant is an employee, such ordinary income generally is subject to withholding of income and employment taxes. If the determination date is after the date on which the participant acquires the shares, the participant may elect, pursuant to Section 83(b) of the Code, to have the date of acquisition be the determination date by filing an election with the Internal Revenue Service no later than 30 days after the date the shares are acquired. Upon the sale of shares acquired pursuant to a restricted stock award, any gain or loss, based on the difference between the sale price and the fair market value on the determination date, will be taxed as capital gain or loss. The Company generally should be entitled to a deduction equal to the amount of ordinary income recognized by the participant on the determination date, except to the extent such deduction is limited by applicable provisions of the Code.

***Restricted Stock Units.*** There are no immediate tax consequences of receiving an award of RSUs. A participant who is awarded RSUs will be required to recognize ordinary income in an amount equal to the fair market value of shares issued to such participant at the end of the applicable vesting period or, if later, the settlement date elected by the Committee or a participant. Any additional gain or loss recognized upon any later disposition of any shares received would be capital gain or loss. The Company generally should be entitled to a deduction equal to the amount of ordinary income recognized by the participant on the determination date, except to the extent such deduction is limited by applicable provisions of the Code.

***Performance Shares and Performance Unit Awards.*** A participant generally will recognize no income upon the grant of a performance share or performance unit award. Upon the settlement and/or payment of such awards, participants normally will recognize ordinary income in the year of receipt in an amount equal to the cash received and the fair market value of any nonrestricted shares received. If the participant is an employee, such ordinary income generally is subject to withholding of income and employment taxes. If the participant receives shares of restricted stock, the participant generally will be taxed in the same manner as described above (see discussion under *Restricted Stock*). Upon the sale of any shares received, any gain or loss, based on the difference between the sale price and the fair market value on the determination date (as defined above under *Nonstatutory Stock Options*), will be taxed as capital gain or loss. The Company generally should be entitled to a deduction equal to the amount of ordinary income recognized by the participant on the determination date, except to the extent such deduction is limited by applicable provisions of the Code.

**Table of Contents****Number of Awards Granted to Employees, Consultants, and Directors**

Benefits and amounts that may be received by each of the Named Executive Officers, the executive officers as a group and all other employees under the Plan cannot be determined at this time because the Committee has full discretion to determine the number, type and value of awards under the Plan. The one exception is that under our director grant policy, each of our non-employee directors will be granted an option under the Plan covering 10,000 shares of our Common Stock on the date of our annual meeting of stockholders. The following table sets forth the following persons or groups who received stock options or Performance Shares with respect to our Common Stock under the Plan in fiscal 2012:

Name and Position	Number of Shares Subject to Stock Options	Weighted Average Exercise Price	Number of Performance Shares	Dollar Value of Performance Shares
Ronald A. Sege Chairman of the Board, President and Chief Executive Officer	150,000	\$ 3.17	37,500	\$ 118,875
William R. Slakey Executive Vice President and Chief Financial Officer	82,200	\$ 3.17	20,550	\$ 65,144
Michael T. Anderson Senior Vice President of Worldwide Markets	97,200	\$ 3.17	24,300	\$ 77,031
Kathleen B. Bloch Senior Vice President & General Counsel	72,400	\$ 3.17	18,100	\$ 57,377
Russell R. Harris Senior Vice President of Operations	72,400	\$ 3.17	18,100	\$ 57,377
All current executive officers of the Company as a group	650,200	\$ 3.17	162,550	\$ 515,284
All current directors who are not executive officers as a group	70,000	\$ 3.52		
All employees and consultants of the Company (excluding executive officers) as a group	1,163,188	\$ 3.21	538,437	\$ 1,762,042

**Vote Required**

Proposal Two requires the affirmative vote of a majority of the voting power of the shares present and entitled to vote on Proposal Two at the 2013 annual meeting of stockholders in person or by proxy. Under the rules of NASDAQ, brokers are prohibited from giving proxies to vote on equity compensation plan matters unless the beneficial owner of such shares has given voting instructions on the matter. This means that if your broker is the record holder of your shares, you must give voting instructions to your broker with respect to Proposal Two if you want your broker to vote your shares on the matter.

**Table of Contents****Board Recommendation**

**OUR BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT YOU VOTE FOR THE AMENDMENT AND RESTATEMENT OF THE COMPANY S 1997 STOCK PLAN.**

**PROPOSAL THREE****RATIFICATION OF APPOINTMENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

With authority granted by our Board of Directors, the Audit Committee of our Board of Directors has appointed KPMG LLP as our independent registered public accounting firm to audit our consolidated financial statements for the fiscal year ending December 31, 2013, and our Board of Directors recommends that our stockholders vote FOR ratification of such appointment.

KPMG LLP was originally appointed as our independent registered public accounting firm on March 21, 2002, when we retained the firm to perform the annual audit of our financial statements for the fiscal year ended December 31, 2002. A representative of KPMG LLP is expected to be present at the annual meeting, will have an opportunity to make a statement if he or she so desires and is expected to be available to respond to appropriate questions from our stockholders.

**Audit and Non-Audit Fees**

The following table sets forth fees for services KPMG LLP provided during fiscal years 2012 and 2011:

	2012	2011
Audit fees (1)	\$ 926,069	\$ 982,564
Audit-related fees	\$	\$
Tax fees	\$ 3,568	\$
All other fees (2)	\$ 37,700	\$ 12,725
<b>Total</b>	<b>\$ 967,337</b>	<b>\$ 995,289</b>

- (1) Represents fees for professional services provided in connection with the audit of our annual financial statements and our internal control over financial reporting, the review of our quarterly financial statements, and other advice on accounting matters. The audit fees for 2012 represent the amount billed to our company as of the date of this Proxy Statement.
- (2) All other fees in 2012 and 2011 represent fees for due diligence services provided in connection with contemplated business transactions.
- (3) Represents fees for professional services provided to assist expatriate non-executive employees to comply with U.S. and/or local tax requirements.

Our Audit Committee has considered whether the non-audit services provided by KPMG LLP are compatible with maintaining the independence of KPMG LLP and has concluded that the independence of KPMG LLP is maintained and is not compromised by the services provided. In accordance with its charter, the Audit Committee approves in advance all audit and non-audit services to be provided by KPMG LLP. During fiscal year 2012, 100% of the services were pre-approved by the Audit Committee in accordance with this policy.

Stockholder ratification of the selection of KPMG LLP as our independent registered public accounting firm is not required by our Bylaws or other applicable legal requirement. However, our Board of Directors is submitting the selection of KPMG LLP to our stockholders for ratification as a matter of good

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corporate practice. If our stockholders fail to ratify the selection, the Audit Committee will reconsider whether or not to retain that firm. Even if the selection is ratified, the Audit Committee at its discretion may direct the appointment of a different independent accounting firm at any time during the year if it determines that such a change would be in our best interests and the best interests of our stockholders.

**Board Recommendation**

**OUR BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT YOU VOTE FOR RATIFICATION OF THE APPOINTMENT OF KPMG LLP AS OUR INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM.**

**SHARE OWNERSHIP BY PRINCIPAL STOCKHOLDERS AND MANAGEMENT**

To our knowledge, the following table sets forth certain information with respect to beneficial ownership of our common stock, as of March 27, 2013, for:

each person who we know beneficially owns more than 5% of our common stock;

each of our directors and director nominees;

each of our Named Executive Officers; and

all of our directors and executive officers as a group.

Beneficial ownership is determined in accordance with the rules of the SEC and includes voting or investment power with respect to the securities. Except as indicated by footnote, and subject to applicable community property laws, each person identified in the table possesses sole voting and investment power with respect to all shares of common stock shown held by them. The number of shares of common stock outstanding used in calculating the percentage for each listed person includes shares of common stock underlying options or other rights held by such person that are exercisable within 60 calendar days of March 27, 2013, but excludes shares of common stock underlying options or other rights held by any other person. Percentage of beneficial ownership is based on 43,057,160 shares of common stock outstanding as of March 27, 2013.

Name	Shares Beneficially Owned	Percentage Beneficially Owned
<b>5% Stockholders:</b>		
Barbara S. Oshman (1)	4,588,064	10.7%
ENEL Investment Holding BV (2)	3,000,000	7.0%
BlackRock, Inc. (3)	2,363,730	5.5%
<b>Directors and Executive Officers:</b>		
Armas Clifford Markkula, Jr. (4) (5)	1,827,038	4.2%
Robert R. Maxfield (4) (6)	403,983	*
Ronald A. Sege (4) (7)	344,434	*
Richard M. Moley (4) (8)	225,589	*
Kathleen B. Bloch (4)	157,104	*
Russell R. Harris (4) (9)	137,143	*
Robert J. Finocchio, Jr. (4) (10)	115,000	*
Michael T. Anderson (4)	102,711	*
Larry W. Sonsini (4)	64,261	*
Betsy Rafael (4)	50,000	*

Robyn M. Denholm (4)

40,000

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Name	Shares Beneficially Owned	Percentage Beneficially Owned
William R. Slakey (4)	32,915	*
All directors and executive officers as a group (16 persons) (4)	3,843,487	8.8%

\* Less than 1%.

- (1) The number of shares beneficially owned is as reported in a Schedule 13G/A filed by Barbara S. Oshman, with the SEC on January 22, 2013. Barbara S. Oshman's address is c/o 545 Middlefield Road, Suite 165, Menlo Park, CA 94025. As of December 31, 2012 and following the death of M. Kenneth Oshman on August 6, 2011, shares were held by the following trusts, of which Barbara S. Oshman serves as sole trustee: (i) 3,487,968 by the M. Kenneth and Barbara S. Oshman Trusts dated July 10, 1979, (ii) 50,048 by the M. Kenneth Oshman 2011 Annuity Trust #1 dated February 25, 2011; (iii) 50,048 by the Barbara S. Oshman 2011 Annuity Trust #1 dated February 25, 2011; (iv) 500,000 by the Peter Lawrence Oshman 2010 Trust; and (v) 500,000 by the David Ross Oshman 2010 Trust.
- (2) Affiliate of Enel S.p.A. The principal address is Viale Regina Margherita 137, Rome, Italy 00198.
- (3) The number of shares beneficially owned is as reported in a Schedule 13G filed by BlackRock, Inc. with the SEC on January 30, 2013. The address of BlackRock, Inc. is 40 East 52<sup>nd</sup> Street, New York, NY 10022.
- (4) Includes, for the applicable director or executive officer, the following shares exercisable within 60 days of March 27, 2013 upon the exercise of options, performance shares and/or SARs. The number of shares issued upon the exercise of SARs will be reduced at the time of exercise by (i) a number of shares sufficient to cover the grant price times the number of shares with respect to which the SAR is being exercised plus (ii) a number of shares sufficient to cover the amount of certain minimum withholding taxes due at the time of exercise. The number of shares withheld to cover the grant price and withholding taxes will be calculated based on the fair market value of our common stock on the date of exercise.

	Options	Performance Shares	SARs
Armas Clifford Markkula, Jr.	50,000	0	0
Robert R. Maxfield	30,000	0	0
Ronald A. Sege	0	0	125,000
Richard M. Moley	50,000	0	0
Kathleen B. Bloch	0	10,250	56,250
Russell R. Harris	0	10,250	63,750
Robert J. Finocchio, Jr.	50,000	0	0
Michael T. Anderson	0	8,750	56,260
Larry W. Sonsini	50,000	0	0
Betsy Rafael	40,000	0	0
Robyn M. Denholm	40,000	0	0
William R. Slakey	0	0	25,000
All directors and executive officers as a group	310,000	59,396	475,111

- (5) Includes 1,655,110 shares held by Armas Clifford Markkula, Jr. and Linda Kathryn Markkula, Trustees of the Restated Arlin Trust Dated December 12, 1990, and 121,928 shares held by the Markkula Family Limited Partnership. Mr. Markkula and his spouse disclaim beneficial ownership of all but 27,500 of the shares held by the Markkula Family Limited Partnership.
- (6) Includes 373,983 shares held by Robert R. Maxfield, Trustee UA DTD 12/14/87.
- (7) Includes 94,434 shares held by R. A. Sege & E. Sege Co-TTEE Ronald A. and Eugenia Sege TR U/T/A DTD 10/19/2010. See *Executive Compensation and Related Matters Compensation Discussion and Analysis*, *Outstanding Equity Awards at 2012 Fiscal Year-End*, footnotes (3) and (6), and *Potential Payments Upon Termination or Change in Control Employment Agreement with Ronald A. Sege* for information regarding vesting criteria applicable to the outstanding shares held by Mr. Sege.
- (8) Includes 175,589 shares held by the Richard Michael Moley and Elizabeth Moley 1989 Revocable Trust dtd 9/29/89, as amended 8/23/02.

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- (9) Includes 43,143 shares held by The Harris living Trust dated March 22, 2004, and 20,000 shares held by The Russell R. Harris 2004 Children's Trust dated April 22, 2004.
- (10) Includes 65,000 shares held by the Robert J. and Susan H. Finocchio Family Trust dated January 9, 1990.

**EXECUTIVE COMPENSATION AND RELATED MATTERS**

**Compensation Discussion and Analysis**

This section discusses the principles underlying our policies and our Compensation Committee's decisions concerning the compensation of our executive officers and the reasons those decisions were made.

***Executive Summary***

***Pay for Performance***

The cornerstone of our executive compensation program is pay for performance. Accordingly, while we pay competitive base salaries and other benefits, a significant portion of our Named Executive Officers' compensation opportunity is based on variable pay.

***Corporate Governance Best Practices***

Our Compensation Committee, assisted by Compensia, its independent compensation consultant, stays informed of developing executive compensation best practices and strives to implement them. In this regard, our stockholders should note:

If a change of control occurs, all of our Named Executive Officers have double-trigger, not single-trigger, equity vesting acceleration protection;

None of our Named Executive Officers or other employees has any golden parachute excise tax gross-up benefits;

We have adopted share ownership guidelines for our executive officers and for our Board of Directors;

Under our management bonus plan for 2012, 100% of the targeted bonus for our Chief Executive Officer, Chief Financial Officer and other key executive officers was tied to our company's ability to generate revenue, control spending and improve our non-GAAP operating income;

Under our 2013 management bonus plan, 100% of the targeted bonus for our Chief Executive Officer, Chief Financial Officer and other key executive officers and director level managers is tied to our company's ability to generate revenue, improve our non-GAAP operating income, control product costs, control spending and/or maintain cash levels;

We do not provide single-trigger vesting acceleration in any of our equity awards; and

We do not provide any club memberships, private travel on executive aircraft, or similar perquisites to any of our Named Executive Officers.

***Executive Compensation Questions and Answers***

***Q. What is our company's overall executive compensation philosophy?***

A. Our executive compensation programs are designed to meet the following objectives:

Attract and retain motivated and talented employees with a view to the competitive nature of the marketplace in Silicon Valley and other areas in which we seek talent;



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Motivate our employees to perform to their best abilities through a compensation strategy that includes meaningful pay for performance;

Position base salary, targeted variable compensation and equity compensation to the 50th to 75th percentile of competitive ranges when compared to similarly situated companies;

Link executive compensation to our company's performance and the individual's performance;

Align the interests of our executives with those of our stockholders by (i) providing our executive officers with incentives to attain our company's long-term goals, (ii) specifically linking our financial and operating results to compensation paid to executive officers, and (iii) with respect to long-term equity compensation, generally keeping within industry guidelines for dilution; and

Provide a compensation structure that is not only competitive in our geographic and industry areas, but is internally equitable and consistent based on level of responsibilities and performance.

These objectives fit within our overall compensation philosophy by giving incentive to our executives to continuously improve our company's performance, while recognizing the need to secure the future potential of our business. Our compensation philosophy is also intended to enhance stockholder value, provide proper compliance with regulatory and related requirements, and create a cohesive executive team.

To meet these objectives, we have implemented an executive compensation program based on the following general policies:

Pay cash compensation in the form of executive base pay that is competitive with the practices of other comparable high technology companies in our area.

Pay for performance:

through an annual management bonus plan that is based upon our company's performance when compared to strategic business objectives; and

by providing significant long-term incentives in the form of equity compensation awards, which may include stock options, performance shares (also referred to as restricted stock units), stock appreciation rights (also referred to as SARs), and/or restricted stock, in order to retain those individuals with the leadership abilities necessary to increase long-term stockholder value.

***Q. Who are the officers on our company's executive team?***

**A.** Our executive team is comprised of the following individuals as of the date of this Proxy Statement:

Title	Name
Chairman of the Board, Chief Executive Officer and President	Ronald A. Sege
Executive Vice President and Chief Financial Officer	William R. Slakey
Senior Vice President and General Manager - Grid Modernization	Michael T. Anderson

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Senior Vice President and General Counsel

Kathleen B. Bloch

Senior Vice President of Operations

Russell R. Harris

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Title	Name
Senior Vice President and General Manager Internet of Things Markets	Varun Nagaraj
Senior Vice President of Engineering	Robert Hon
Vice President, Principal Accounting Officer and Controller	C. Michael Marszewski

Robert Hon will serve as our Senior Vice President of Engineering until April 12, 2013, when he will cease to be an employee of our company. In addition, Anders Axelsson, our Senior Vice President of Strategic Accounts and Business Development, served as an executive officer until February 13, 2013.

Throughout this proxy statement, our executive team is referred to as the executive officers and includes our Named Executive Officers, who are listed in the Summary Compensation Table on page 45 of this proxy statement.

***Q. What is the role of our company's Compensation Committee?***

A. The Compensation Committee is responsible for ensuring compliance with our company's executive compensation objectives and policies. Accordingly, the Compensation Committee reviews and approves our company's annual executive compensation arrangements, including approving specific performance objectives. These arrangements include annual base salary, annual incentive bonus, equity compensation, and other benefits or compensation. In performing these duties, the Compensation Committee is assisted by our Human Resources Department and receives input from our executive management, particularly our Chief Executive Officer. Management provides the Compensation Committee with information about our company and individual executive performance, market data, and management's perspective and recommendations on compensation matters. The Compensation Committee is authorized to obtain the assistance of compensation consultants at any time, and may also rely on consultants retained by our company. In 2012 our company retained the services of Compensia, a management compensation consulting firm that provides executive compensation advisory services, to provide input regarding executive compensation, including base salary, bonuses and long-term equity incentives.

Our Compensation Committee approves and interprets our executive compensation and benefits plans and policies, including our stockholder-approved 1997 Stock Plan. Our Compensation Committee is appointed by our Board of Directors, and consists entirely of directors who are independent for purposes of the listing standards of the NASDAQ Stock Market, outside directors for purposes of Section 162(m) of the Internal Revenue Code of 1986, as amended, and non-employee directors for purposes of Rule 16b-3 under the Securities Exchange Act of 1934, as amended. The members of our Compensation Committee currently are Armas Clifford Markkula, Jr., Richard M. Moley and Betsy Rafael, and the Compensation Committee is chaired by Mr. Moley. Our Compensation Committee operates under a written charter adopted by our Board of Directors which is available at the Investor Relations section of our website at [www.echelon.com](http://www.echelon.com). The Compensation Committee held two meetings during 2012. Our Compensation Committee regularly meets in executive session without management present.

***Q. What is the role of our Chief Executive Officer in compensation decisions?***

A. Our Chief Executive Officer sets individual performance objectives, in line with the corporate objectives, for each executive officer (other than himself) near the beginning of the calendar year and reviews the performance of our executive officers during the year as well as during an annual review process following the end of the calendar year. Our CEO then presents his findings to our Compensation

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Committee, together with recommendations for their compensation structures. In 2012, our Chief Executive Officer also obtained input about compensation practices within comparator high technology companies from Compensia.

Beginning in 2012, we implemented an employee performance management appraisal program under which each employee, including each of our executive officers, is charged with annually establishing specific, measurable performance objectives that are consistent with our company's overall goals, as well as professional development goals. Each employee's objectives are approved by his or her manager and the employee is evaluated periodically against those objectives. In evaluating each executive officer, it is the view of our Chief Executive Officer and the Compensation Committee that each executive officer is expected to perform at a very high level and to also function as an integral part of a cohesive team. The goals of the performance management appraisal program are to provide objective criteria against which to evaluate the performance of our executive officers and support a pay for performance culture.

The Compensation Committee considers these findings and recommendations, but makes its own final determinations. This review process is generally conducted in advance of annual salary adjustments, if any, the adoption of the annual management bonus program described below, and the grant of annual equity compensation award.

The Compensation Committee alone or in consultation with the full Board of Directors (other than our Chief Executive Officer) reviews the performance of our Chief Executive Officer. As with the other executive officers, our Chief Executive Officer is expected to perform at a very high level.

***Q: What is the role of compensation consultants and benchmarking in determining executive compensation?***

**A.** In 2012, our company engaged Compensia, a management compensation consulting firm, to provide input regarding key trends in executive compensation practices, including base salary, bonuses and long-term equity, by our peer companies. In 2012, as part of the process of evaluating competitiveness of our company's executive pay programs, this independent compensation consultant was also requested to develop a peer group closely aligned with Echelon's business profile and reflecting a reasonable comparator group for executive jobs of similar scope and complexity. For compensation purposes, the comparability was based in part on the following principles:

When other variables are held constant, revenue is generally the best indicator of cash compensation levels;

A best practice is to keep the peers within a range of roughly 0.5x to 2.0x our company's revenue. This is consistent with the approach of certain institutional investor advisors in developing peer groups;

Market capitalization generally has the greatest influence on equity compensation levels;

Industry is an important factor, particularly where it reflects the general profitability of the business model or the complexity of successfully running the organization; and

Other considered factors were revenue growth, profitability, valuation and number of employees.

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In 2012 the Compensation Committee employed the following set of peer companies for executive compensation decisions:

Bigband Networks, Inc.	Falconstor Software, Inc.	Radisys Corporation
Blue Coat Systems, Inc.	Globecom Systems Inc.	Silver Spring Networks, Inc.
DDi Corp	Infinera Corporation	Sonus Networks, Inc.
Demandtec, Inc.	Internap Network Services Corporation	Tessera Technologies, Inc.
Digi International Inc.	Maxwell Technologies Inc.	TiVo Inc.
Emulex Corporation	OPNET Technologies, Inc.	Zygo Corporation
Extreme Networks, Inc.	Powersecure International, Inc.	

The overall competitive market framework represented a 50/50 blend of survey data from the July 2011 Radford Executive Compensation Report's broad industry data set of companies with revenues between \$50 million-\$200 million and the proxy data from the 20 above-listed peer companies recommended by Compensia and approved by the Compensation Committee.

***Q. What are the elements of our company's executive compensation program?***

**A.** Our executive officers' compensation has three primary components:

Base salary;

Participation in the management bonus plan; and

Participation in the annual equity compensation award.

In addition, we provide our executive officers with employee benefits that are generally available to all salaried employees in the geographical location in which they are based. We generally do not provide pension arrangements, deferred compensation or other similar benefits to our current executive officers.

We believe that this combination of elements provides an appropriate mix of fixed and variable pay, balances short-term operational performance with long-term stockholder value, and is conducive to executive recruitment and retention.

***Q. When are decisions concerning executive compensation made?***

**A.** The Compensation Committee typically makes its decisions concerning executive officer base salaries early in the year, as was the case in 2012. Decisions regarding executive compensation may also be made at other times of the year.

The management bonus plan is also typically established early in the year. The management bonus plan was implemented in March of 2012. This plan is described below.

Our Company's equity compensation grant guidelines, which are described below, call for annual equity compensation grants to be made effective on the date of our company's annual meeting of stockholders. Although our company's annual meeting of stockholders was held on May 22, 2012, because we had then only recently implemented a restructuring of our company, the 2012 equity compensation grant to our Named Executive Officers was delayed until June 11, 2012.

***Q: How are individual performance and other factors taken into consideration when making executive compensation decisions?***

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**A:** As noted above, the Compensation Committee relies on input from our Chief Executive Officer to evaluate the performance of the executive officers. For example, our Chief Executive Officer

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meets frequently with each of the executive officers, enabling him to develop in-depth knowledge of each executive officer's performance. Beginning in 2011, we implemented an employee performance management appraisal program under which each employee, including each of our executive officers, is charged with annually establishing specific, measurable performance objectives that are consistent with our company's overall goals, as well as professional development goals. This program continued in 2012, and under this program, each executive officer's objectives reflected the applicable department's overall objectives and were approved by our Chief Executive Officer. Our Chief Executive Officer and each executive officer are expected to periodically evaluate the executive officer's performance against those objectives. The Chief Executive Officer then reviews the strengths, accomplishments and areas for growth of each executive with the Compensation Committee.

In establishing executive compensation, the Compensation Committee may consider previous award amounts or expected pay-outs under prior awards or the management bonus plan.

***Q: How are base salaries determined?***

**A:** Base salary fits into our overall compensation program as a means to attract and retain qualified Named Executive Officers, and to be competitive in our geographic and industry areas. Base salaries are designed to compensate our Named Executive Officers for services rendered during the year, and to meet competitive norms and reward performance on an annual basis. As outlined above, we rely on data from compensation consultants and the Radford survey, as well as general market sources, to keep our base salaries competitive when compared to our peer companies. Adjustments to salaries, if any, may be made based on an individual's current and expected future performance, pay relative to competitors and internal equity.

For 2012, following a review of salary levels at the peer companies referenced above and among our company's executive officers, given the continued challenging business environment faced our company, the Compensation Committee made no adjustment to the base salaries of our Named Executive Officers. Our company made Mr. Anderson, who is a resident of the state of Washington, whole for 2012 California state income taxes paid on his salary.

**Summary.** The following table summarizes the actual annual base salaries paid for 2012 for our Named Executive Officers:

<b>Named Executive Officer</b>	<b>Title</b>	<b>2012 Salary</b>
Ronald A. Sege	Chairman and Chief Executive Officer	\$ 400,000
William R. Slakey	Executive Vice President and Chief Financial Officer	\$ 312,000
Michael T. Anderson	Senior Vice President and General Manager - Grid Modernization (formerly Senior Vice President of Worldwide Markets)	\$ 325,000
Kathleen B. Bloch	Senior Vice President and General Counsel	\$ 357,000
Russell R. Harris	Senior Vice President of Operations	\$ 345,000

**2012 Management Bonus Plan.** For 2012, our management determined that the key imperatives for our company continue to be to increase revenues, move towards profitability and control spending. As a result, our Chief Executive Officer and other management members reviewed the structure of the management bonus plans for the prior year and proposed a management bonus plan that would be tied to, and would reward, comparable success in achieving our company's targets for revenue generation and

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non-GAAP operating income or loss, or NGOI. In March 2012, the Compensation Committee implemented a 2012 bonus plan under which our Named Executive Officers, including our Chief Executive Officer, were eligible to earn cash payouts upon the achievement of specified performance targets.

None of the requisite performance targets for the 2012 bonus plan, which are described below, were met, so no bonuses were paid out in respect of the 2012 bonus plan.

Key elements of the 2012 Bonus Plan were as follows:

***Non-Sales Named Executive Officers.*** For our Named Executive Officers, including our Chief Executive Officer but excluding our Senior Vice President of Worldwide Markets the 2012 bonus plan was tied to our company's revenue and expense control measures.

50% of the bonus amount was tied to performance targets based on our company's actual revenue and 50% of the bonus amount was tied to performance targets based on our company's NGOI. NGOI was to be calculated as our company's actual net operating income or loss for full year 2012, adjusted to remove stock-based compensation charges and payments under the 2012 bonus plan itself.

For the revenue portion of the 2012 bonus plan (i.e., 50% of the total targeted bonus for each participant), the 2012 bonus plan had specified tiers, as follows:

The first tier had a cliff below 85% of targeted revenue, in which case no revenue-based bonus would be paid. If 85% of targeted revenue were achieved, then 70% of the revenue-based bonus would be paid;

The second tier had a primary bonus rate on revenue from 85% up to and including 100% of targeted revenue, which primary rate was calculated such that the remaining 30% of the revenue-based bonus would be paid over the remaining 15% of targeted revenue; and

The third tier had an accelerated bonus rate on revenue over 100% of targeted revenue, which accelerated rate would be equal to 3% of the bonus amount for each 1% increase in revenue over the 100% target amount.

For the NGOI portion of the 2012 bonus plan (i.e., 50% of the total targeted bonus for each participant), the 2012 bonus plan had four tiers, as follows:

At the first tier, 20% of the NGOI-based bonus would be paid if the primary NGOI target were achieved. No NGOI-based bonus would be paid if this target were not achieved;

At the second tier, an additional 20% of the 2012 bonus plan would be paid for each of three specified, more stringent NGOI milestones, each of which was a cliff. For example, no second tier NGOI-based bonus would be paid if the first milestone was not met, and the full second tier NGOI-based bonus would be paid if all milestones were met;

At the third tier, the remaining targeted NGOI-based bonus would be paid if a third, even more stringent, NGOI target were met. The aggregate amount of the first through third tiers of NGOI-based bonuses would be equal to 100% of the total targeted NGOI-based bonus; and



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At the fourth tier, an additional 10% of the total targeted NGOI-based bonus would be paid for each additional specified milestone above the overall NGOI target.

The total 2012 Management Bonus for non-sales executives was limited to a total of 150% of target.

**Sales Executive Officer.** For our Senior Vice President of Worldwide Sales, the 2012 bonus plan was tied 50% to performance targets based on our company's revenue and 50% to new orders (bookings) during 2012.

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The 2012 bonus for the Senior Vice President of Global Sales also had three tiers: