

STEPAN CO  
Form DEF 14A  
March 31, 2011

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**Washington, D.C. 20549**

**SCHEDULE 14A INFORMATION**

**Proxy Statement Pursuant to Section 14(a) of the**

**Securities Exchange Act of 1934**

**(Amendment No. \_\_)**

Filed by the Registrant ☒ Filed by a Party other than the Registrant ☐

Check the appropriate box:

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

**STEPAN COMPANY**

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(Name of Registrant as Specified In Its Charter)

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

Payment of Filing Fee (Check the appropriate box):

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- x No fee required.
- .. Fee computed on table below per Exchange Act Rules 14a-6(i)(4) and 0-11.
- (1) Title of each class of securities to which transaction applies:
- (2) Aggregate number of securities to which transaction applies:
- (3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):
- (4) Proposed maximum aggregate value of transaction:
- (5) Total fee paid:
- .. Fee paid previously with preliminary materials.
- .. Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.
- (1) Amount Previously Paid:
- (2) Form, Schedule or Registration Statement No.:
- (3) Filing Party:

(4) Date Filed:

**STEPAN COMPANY**

**NOTICE OF ANNUAL MEETING OF STOCKHOLDERS**

**To be held on May 3, 2011**

**at 9:00 a.m. (CDT)**

To the Stockholders:

Notice is hereby given that the Annual Meeting of Stockholders of STEPAN COMPANY (the "Company") will be held at the Company's Administrative and Research Center at Edens Expressway and Winnetka Road, Northfield, Illinois, on Tuesday, May 3, 2011, at 9:00 a.m. (CDT), for the following purposes:

1. To elect two Directors to the Board of Directors for a three-year term.
2. To approve the adoption of the Stepan Company 2011 Incentive Compensation Plan.
3. To approve, on an advisory basis, the compensation paid to the Company's named executive officers.
4. To consider, on an advisory basis, the frequency of future stockholder advisory votes on the compensation of the Company's named executive officers.
5. To ratify the appointment of Deloitte & Touche LLP as the independent registered public accounting firm for the Company for 2011.
6. To transact such other business as may properly come before the meeting.

The Board of Directors has designated the close of business on March 4, 2011, as the record date for determining holders of the Company's 5 1/2% Convertible Preferred Stock and the Company's Common Stock entitled to notice of and to vote at the meeting.

**Important Notice Regarding the Availability of Proxy Materials for the Annual Meeting of Stockholders to Be Held on May 3, 2011.**

**The Proxy Statement and Annual Report to Stockholders are available at <http://www.edocumentview.com/SCL>.**

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The proxy materials available at <http://www.edocumentview.com/SCL> include the Notice of Annual Meeting of Stockholders, Proxy Statement, Form of Proxy, Annual Report to Stockholders, and Form 10-K for the year 2010.

Directions to the Annual Meeting of Stockholders are available at <http://www.stepan.com>, under Investors Annual Meeting for those stockholders who plan to attend the meeting.

By order of the Board of Directors,

KATHLEEN O. SHERLOCK

*Assistant Secretary*

Northfield, Illinois

March 31, 2011

**The Board of Directors extends a cordial invitation to all stockholders to attend the meeting. Whether or not you plan to attend the meeting, please mark, sign and mail the enclosed proxy card in the return envelope provided as promptly as possible.**

**As a reminder, brokers may not vote your shares for non-routine matters such as the election of directors, the approval of an equity compensation plan, the advisory vote on the compensation paid to the Company's named executive officers ( Say-on-Pay vote), or the advisory vote on the frequency of voting on future Say-on-Pay votes in the absence of your specific instructions as to how to vote. Therefore, we urge you to provide your broker with voting instructions by returning your proxy card so your vote for all proposals can be counted.**

March 31, 2011

## **PROXY STATEMENT**

**For the Annual Meeting of Stockholders of**

**STEPAN COMPANY**

**Edens Expressway and Winnetka Road**

**Northfield, Illinois 60093**

**To be held at 9:00 a.m. (CST) on May 3, 2011**

### **INFORMATION CONCERNING SOLICITATION AND VOTING**

The enclosed proxy is solicited by the Board of Directors and the Company will bear the entire expense of solicitation. Such solicitation is being made by mail, and the Company's officers and employees may solicit proxies from stockholders personally or by telephone, mail or other means. The Company will make arrangements with the brokers, custodians, nominees and other fiduciaries who request the forwarding of solicitation material to the beneficial owners of shares of the Company's stock held of record by such brokers, custodians, nominees and other fiduciaries, and the Company will reimburse them for their reasonable out-of-pocket expenses.

At the close of business on March 4, 2011, the record date for the meeting, there were 520,089 shares of the Company's  $\frac{5}{2}\%$  Convertible Preferred Stock ( Preferred Stock ) outstanding, each share of which is convertible into 1.14175 shares of the Company's Common Stock ( Common Stock ) and is entitled to 1.14175 votes on each matter to be voted on at the meeting, and, assuming all outstanding shares of Preferred Stock were converted, there would have been 10,752,948 shares of Common Stock outstanding, each share of which is entitled to one vote on each matter to be voted on at the meeting.

This proxy statement and proxy are first being sent or given to stockholders commencing on or about March 31, 2011.

You may either vote FOR or WITHHOLD authority to vote for each of the nominees for the Board of Directors. You may vote in favor of holding the advisory vote on named executive officer compensation EVERY ONE YEAR, EVERY TWO YEARS OR EVERY THREE YEARS, or you may choose to ABSTAIN from voting on this proposal. You may vote FOR, AGAINST or ABSTAIN on the other proposals.

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In connection with any other business that may properly come before the meeting, of which the Board of Directors is not currently aware, votes will be cast pursuant to the authority granted by the enclosed proxy in accordance with the best judgment of a majority of the persons present and acting under the proxy.

If you submit your proxy but abstain from voting or withhold authority to vote on one or more matters, your shares will be counted as present at the meeting for the purposes of determining a quorum. Your shares also will be counted as present at the meeting for the purpose of calculating the vote on the particular matter with respect to which you abstained from voting or withheld authority to vote. Any proxy given pursuant to this solicitation may be revoked by the stockholder at any time prior to the voting of the proxy.

If you abstain from voting on a proposal, your abstention has the same effect as a vote against that proposal. If you withhold your authority to vote for any director nominee, your withholding has the same effect as a vote against that director.

If you hold your shares in street name and do not provide voting instructions to your broker, custodian, nominee or other fiduciary, your shares will be considered "broker non-votes" and will not be voted on any non-routine matters, which include the election of directors, the approval of the equity compensation plan, the advisory vote on executive compensation, and the advisory vote on the frequency of future stockholder advisory votes on executive compensation. Shares that constitute broker non-votes may be voted on the ratification of auditors and will be counted as present at the meeting for the purpose of determining a quorum, but will not be entitled to vote on non-routine proposals. Please instruct your broker or bank so your vote can be counted on all proposals.

The required quorum at the Annual Meeting of Stockholders is a majority of the outstanding shares of the Company's voting stock as of the record date. In order to ensure the presence of holders of shares representing the necessary quorum at the Annual Meeting of Stockholders, please mark, sign and return the enclosed proxy promptly in the envelope provided. No postage is required if mailed in the United States. Even if you sign and return your proxy, you are invited to attend the meeting.

### **ELECTION OF DIRECTORS**

Stockholders and the persons named in the enclosed proxy will vote, pursuant to the authority granted by the stockholder in the enclosed proxy, on the election of Messrs. Joaquin Delgado and F. Quinn Stepan, Jr. as Directors of the Company to hold office until the Annual Meeting of Stockholders to be held in the year 2014.

In the event any one or more of such nominees is unable to serve as Director, votes will be cast, pursuant to the authority granted in the enclosed proxy, for such person or persons as may be designated by the Board of Directors. The Board of Directors at this time is not aware of any nominee who is or will be unable to serve as Director, if elected.

Under the Company's Certificate of Incorporation and By-laws, Directors are elected by a plurality of the voting power of the shares of Preferred Stock and Common Stock present in person or represented by proxy at the meeting and entitled to vote, voting together as a single class. The outcome of the election will not be affected by holders of shares of Preferred Stock or Common Stock that withhold authority to vote in the election of Directors.

The Board of Directors is divided into three classes serving staggered three-year terms. Directors for each class are elected at the Annual Meeting of Stockholders in the year in which the term for their class expires.

**Nominees For Director**

The following table sets forth certain information about the nominees for Director:

Name of Nominee	Principal Occupation, Business Experience and Other Directorships During the Past Five Years, and Age	Year of First Election as Director	Number and Percent of Shares of Common Stock Beneficially Owned(1)	
Joaquin Delgado	Executive Vice President, Electro and Communications Business of 3M Company, a global diversified technology company, since 2009. Vice President and General Manager, Electronic Markets Materials Division of 3M Company, from 2007 to 2009. Vice President, Research and Development and New Business Ventures, Consumer and Office Business of 3M Company, from 2005 to 2007. President of 3M Korea Ltd. from 2003 to 2005.  Age 51	N/A	0	*
F. Quinn Stepan, Jr.	President and Chief Executive Officer of the Company since January 2006. President and Chief Operating Officer of the Company from February 1999 to December 2005. Director of Follett Corporation.  Age 50	1999	791,837(2)  (3)	7.3%

\* Less than one percent of outstanding shares of Common Stock.

- Represents number of Common Stock shares beneficially owned as of March 4, 2011. Number of shares for each Director includes (a) shares of Common Stock owned by the spouse of the Director and shares held by the Director or his spouse as trustee or custodian for the benefit of children and family members for which the Director or his spouse as trustee or custodian has voting or investment power, (b) shares of Common Stock which may be acquired through conversion of shares of Preferred Stock, and (c) shares pledged as security by the Director or the Director's family members. In addition, the Company calculates the total number of shares of Common Stock outstanding by assuming all shares of Preferred Stock are converted into Common Stock, and adding such amount to the number of shares of Common Stock outstanding.
- Includes 337,248 shares held by the Company's qualified plans and deemed beneficially owned by the Plan Committee, of which James Hurlbutt, Gregory Servatius and F. Quinn Stepan, Jr. are members and employees of the Company. The Plan Committee selects the investment manager of the Stepan Company Trust for Qualified Plans and Profit Sharing Plan Trust under the terms of a Trust Agreement effective August 1, 2003, with Russell Investment Group ( Russell ). Russell expressly disclaims any beneficial ownership in the securities of these plans.
- Includes (a) 184,716 shares that F. Quinn Stepan, Jr. has the right to acquire within 60 days through the exercise of stock options granted pursuant to the Company's stock option plans, (b) 1,386 shares allocated to F. Quinn Stepan, Jr. under the Employee Stock Ownership Plan ( ESOP ), (c) 2,638 shares of Common Stock and 553 shares of Preferred Stock allocated to F. Quinn Stepan, Jr. under the Employee Stock Ownership Plan II ( ESOP II ), and (d) 43,675 shares credited to F. Quinn Stepan, Jr.'s stock account under the Management Incentive Plan (As Amended and Restated Effective January 1, 2010), (the Management Incentive Plan ). Amounts credited to an employee's stock account will be paid to the employee at the time of separation of service from the Company as the employee has elected under the provisions of the Management Incentive Plan. Also includes 31,950 shares pledged as security for two bank loan agreements and 54,212 shares held in a margin account.

**PROPOSAL:** The Board of Directors recommends that the stockholders vote FOR the election of Messrs. Joaquin Delgado and F. Quinn Stepan, Jr. to the Board of Directors for a three-year term.



**Directors Whose Terms Continue**

The following table sets forth certain information about those Directors who are not up for re-election as their respective term of office does not expire this year:

Name of Director	Principal Occupation, Business Experience and Other Directorships During the Past Five Years, and Age	Year of First Election as Director	Term Expires	Number and Percent of Shares of Common Stock Beneficially Owned(1)	
Michael R. Boyce	Chairman and Chief Executive Officer of PQ Corporation, an industrial chemicals company, since 2005. Chairman and Chief Executive Officer of Peak Investments, an operating and acquisition company, since 1998. From 1990 to 1998, President and Chief Operating Officer of Harris Chemical Group, Inc. Director of PQ Corporation and AAR Corp.  Age 63	2010	2013	333(2)	*
Gary E. Hendrickson	President and Chief Operating Officer of The Valspar Corporation, a global paints and coatings manufacturer, since February 2008. Senior Vice President, Wood Coatings, Architectural, and Federal Business Units; and President, Asia Pacific of The Valspar Corporation, from 2005 to February 2008. Group Vice President, Global Wood Coatings; and President, Asia Pacific of The Valspar Corporation from 2004 to 2005. Director of The Valspar Corporation.  Age 54	2009	2012	3,458(3)	*
Gregory E. Lawton	Consultant. President and Chief Executive Officer of JohnsonDiversey, Inc., a manufacturer of cleaning products, from October 2000 to February 2006. From January 1999 to September 2000, President and Chief Operating Officer of Johnson Wax Professional. President of NuTone, Inc., a subsidiary of Williams plc based in Cincinnati, Ohio from 1994 to 1998. From 1989 to 1994, served with Procter & Gamble as Vice President and General Manager of several consumer product groups. Director of General Cable and American Trim.  Age 60	2006	2012	7,465(4)	*

Name of Director	Principal Occupation, Business	Year of First Election as Director	Term Expires	Number and Percent of Shares of Common Stock Beneficially Owned(1)	
	Experience and Other Directorships				
	During the Past Five Years, and Age				
F. Quinn Stepan	Chairman of the Company since November 1984. Chief Executive Officer of the Company from November 1984 to December 2005.  Age 73	1967	2013	1,609,458(5)	14.9%
Edward J. Wehmer	President, Chief Executive Officer and founder of Wintrust Financial Corporation, a financial services company, since May 1998. Prior to May 1998, President and Chief Operating Officer of Wintrust Financial Corporation since its formation in 1996. Director of Wintrust Financial Corporation. Involved in several charitable and professional organizations.  Age 56	2003	2013	12,530(6)	*

\*Less than one percent of outstanding shares of Common Stock.

- (1) See Note (1) to table under Nominees for Director.
- (2) Includes 333 shares credited to the Director's account pursuant to the Stepan Company 2006 Incentive Compensation Plan.
- (3) Includes (a) 692 shares that the Director has the right to acquire within 60 days through the exercise of stock options granted pursuant to the Company's stock option plans, (b) 1,940 shares credited to the Director's account pursuant to the Directors Deferred Compensation Plan Amended and Restated as of January 1, 2005, and (c) 826 shares credited to the Director's account pursuant to the Stepan Company 2006 Incentive Compensation Plan.
- (4) Includes (a) 3,280 shares that the Director has the right to acquire within 60 days through the exercise of stock options granted pursuant to the Company's stock option plans, and (b) 2,535 shares credited to the Director's account pursuant to the Stepan Company 2006 Incentive Compensation Plan.
- (5) See Notes (3), (5) and (6) to tables under Security Ownership of Certain Beneficial Owners.
- (6) Includes (a) 5,159 shares that the Director has the right to acquire within 60 days through the exercise of stock options granted pursuant to the Company's stock option plans, and (b) 3,171 shares credited to the Director's account pursuant to the Stepan Company 2006 Incentive Compensation Plan.

#### Family Relationships

F. Quinn Stepan, Jr. is the son of F. Quinn Stepan.

## SECURITY OWNERSHIP

## Security Ownership of Certain Beneficial Owners

As of March 4, 2011, the following persons were the only persons known to the Company to beneficially own more than five percent of the Company's Common Stock:

Name and Address(1)	Number of Shares of Common Stock Beneficially Owned(2)(6)		Total Shares	Percentage of Outstanding Shares of Common Stock
	Voting and/or Investment Power			
	Sole	Shared		
F. Quinn Stepan(4)	1,304,689(5)	304,769(3)	1,609,458	14.9%
Royce & Associates, LLC(7)	672,479		672,479	6.2%
BlackRock, Inc.(8)	614,195		614,195	5.7%

As of March 4, 2011, the following persons were the only persons known to the Company to beneficially own more than five percent of the Company's Preferred Stock:

Name and Address(1)	Number of Shares of Preferred Stock Beneficially Owned(2)		Total Shares	Percentage of Outstanding Shares of Preferred Stock
	Voting and/or Investment Power			
	Sole	Shared		
F. Quinn Stepan(4)	22,162	166,480(3)	188,642	36.2%
Stepan Venture II	0	166,480(3)	166,480	32.0%
Mary Louise Wehman(4)	89,684		89,684	17.2%
John A. Stepan(4)	76,872		76,872	14.7%
Charlotte Stepan Shea(4)	35,244		35,244	6.7%

- (1) Except as otherwise set forth in the footnotes below, the address of all persons named is Stepan Company, Edens Expressway and Winnetka Road, Northfield, Illinois 60093.
- (2) Represents number of shares beneficially owned as of March 4, 2011. The Company calculates the total number of shares of Common Stock outstanding by assuming all shares of Preferred Stock are converted into Common Stock, and adding such amount to the number of shares of Common Stock outstanding. In addition, number of shares owned includes shares held by the persons listed in the table, as trustee or custodian for the benefit of children and family members if such trustee or custodian has voting or investment power and, with respect to F. Quinn Stepan, shares held by the spouse of F. Quinn Stepan.
- (3)

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F. Quinn Stepan and Paul H. Stepan are managing partners of a family-owned limited partnership that is the sole general partner of another family-owned limited partnership, Stepan Venture II, which owns 114,691 shares of Common Stock and 166,480 shares of Preferred Stock. The partnership has pledged a total of 95,152 shares of Common Stock and 166,480 shares of Preferred Stock as security for a bank loan agreement. The shares owned by the partnership are included in the tables for both F. Quinn Stepan and Stepan Venture II.

- (4) F. Quinn Stepan, Paul H. Stepan, John A. Stepan, Mary Louise Wehman and Charlotte Stepan Shea are the children of the late Mary Louise Stepan and the late Alfred C. Stepan, Jr.
- (5) Includes (a) 5,135 shares of Common Stock allocated to F. Quinn Stepan under ESOP, (b) 36,722 shares of Common Stock and 9,350 shares of Preferred Stock allocated to F. Quinn Stepan under ESOP II, (c) 196,300 shares of Common Stock credited to F. Quinn Stepan's stock account under the Management Incentive Plan, (d) 123,064 shares which F. Quinn Stepan has the right to acquire within 60 days through the exercise of stock options granted pursuant to the Company's stock option plans, and (e) 127,630 shares of Common Stock pledged as security for a bank loan agreement.

- (6) Includes the number of shares of Common Stock that the specified person has the right to acquire by conversion of shares of Preferred Stock beneficially owned by such person.
- (7) As reported in a Schedule 13G filed with the Securities and Exchange Commission ( SEC ) on February 3, 2011, by Royce & Associates, LLC, an investment adviser, 745 Fifth Avenue, New York, New York, 10151 ( Royce ). In the Schedule 13G, Royce reported that, as of December 31, 2010, it had sole voting and dispositive power as to 672,479 shares.
- (8) As reported in a Schedule 13G/A filed with the SEC on February 8, 2011, by BlackRock, Inc., a parent holding company, 40 East 52<sup>nd</sup> Street, New York, New York, 10022 ( BlackRock ). In the Schedule 13G/A, BlackRock reported that, as of December 31, 2010, it had sole voting and dispositive power as to 614,195 shares.

## Security Ownership of Management

The following table sets forth, as of the close of business on March 4, 2011, the security ownership of each Executive Officer listed in the Summary Compensation Table in this proxy statement, each Director and nominee for Director, and all Directors and Executive Officers as a group:

Name	Number and Percent of Shares of Common Stock Beneficially Owned(1)	
James E. Hurlbutt	369,069(2)	3.4%
John V. Venegoni	49,355(3)	*
Robert J. Wood	48,420(4)	*
F. Quinn Stepan	1,609,458(5)	14.9%
F. Quinn Stepan, Jr	791,837(6)	7.3%
Michael R. Boyce	333(7)	*
Joaquin Delgado	0(8)	*
Thomas F. Grojean	20,004(9)	*
Gary E. Hendrickson	3,458(10)	*
Gregory E. Lawton	7,465(11)	*
Edward J. Wehmer	12,530(12)	*
All Directors and Executive Officers(13)	2,686,565	24.9%

\* Less than one percent of outstanding shares of Common Stock.

- (1) Number of shares for each Director, nominee for Director, and Executive Officer (and all Directors and Executive Officers as a group) includes (a) shares of Common Stock owned by the spouse of each Director, nominee for Director, or Executive Officer, and shares held by each Director, nominee for Director, or Executive Officer, or such person's spouse as trustee or custodian for the benefit of children and family members if such trustee or custodian has voting or investment power, (b) shares of Common Stock that may be acquired within 60 days through the exercise of stock options granted pursuant to the Company's stock option plans or conversion of shares of Preferred Stock, and (c) shares pledged as security by such Director, nominee for Director, or Executive Officer, or such person's family members. In addition, the Company calculates the total number of shares of Common Stock outstanding by assuming all shares of Preferred Stock are converted into Common Stock, and adding such amount to the number of shares of Common Stock outstanding.
- (2) Includes (a) 752 shares allocated to James E. Hurlbutt under ESOP, (b) 1,397 shares of Common Stock and 293 shares of Preferred Stock allocated to James E. Hurlbutt under ESOP II, (c) 14,500 shares that James E. Hurlbutt has the right to acquire within 60 days through the exercise of stock options granted pursuant to the Company's stock option plans, and (d) 8,707 shares credited to James E. Hurlbutt's stock account under the Management Incentive Plan. Also includes 337,248 shares in the Company's qualified plans and deemed beneficially owned by the Plan Committee, of which James Hurlbutt, Gregory Servatius and F. Quinn Stepan, Jr. are members and employees of the Company. The Plan Committee selects the investment manager of the Stepan Company Trust for Qualified Plans and Profit Sharing Plan Trust under the terms of

- a Trust Agreement effective August 1, 2003, with Russell. Russell expressly disclaims any beneficial ownership in the securities of these plans.
- (3) Includes (a) 1,325 shares allocated to John V. Venegoni under ESOP, (b) 2,672 shares of Common Stock and 522 shares of Preferred Stock allocated to John V. Venegoni under ESOP II, (c) 10,000 shares that John V. Venegoni has the right to acquire within 60 days through the exercise of stock options granted pursuant to the Company's stock option plans, and (d) 12,923 shares credited to John V. Venegoni's stock account under the Management Incentive Plan.
- (4) Includes (a) 1,361 shares allocated to Robert J. Wood under ESOP, (b) 3,202 shares of Common Stock and 617 shares of Preferred Stock allocated to Robert J. Wood under ESOP II, (c) 26,532 shares that Robert J. Wood has the right to acquire within 60 days through the exercise of stock options granted pursuant to the Company's stock option plans, and (d) 14,121 shares credited to Robert J. Wood's stock account under the Management Incentive Plan.
- (5) See Note (5) to table under Directors Whose Terms Continue.
- (6) See Notes (2) and (3) to table under Nominees for Director.
- (7) See Note (2) to table under Directors Whose Terms Continue.
- (8) Dr. Delgado is a Nominee for Director.
- (9) Includes (a) 6,702 shares that Thomas F. Grojean has the right to acquire within 60 days through the exercise of stock options granted pursuant to the Company's stock option plans, and (b) 3,169 shares credited to Thomas F. Grojean's account pursuant to the Stepan Company 2006 Incentive Compensation Plan. Mr. Grojean's term as a Director expires on May 3, 2011, the date of the 2011 Annual Meeting of Stockholders. Mr. Grojean is not eligible for re-election as a Director.
- (10) See Note (3) to table under Directors Whose Terms Continue.
- (11) See Note (4) to table under Directors Whose Terms Continue.
- (12) See Note (6) to table under Directors Whose Terms Continue.
- (13) As of March 4, 2011, all Directors and Executive Officers as a group beneficially owned 191,216 shares of Preferred Stock, including 11,924 shares of Preferred Stock allocated to Company-employed Directors and Executive Officers under ESOP II, and which collectively represented 36.7% of the outstanding shares of Preferred Stock and were convertible into 218,320 shares (2.0%) of Common Stock. As of March 4, 2011, Company-employed Directors and Executive Officers as a group had the right to acquire 408,170 shares of Common Stock under stock options exercisable within 60 days, 11,276 shares of Common Stock allocated to them under ESOP, 50,505 shares of Common Stock allocated to them under ESOP II, and 282,879 shares of Common Stock credited to their stock accounts under the Management Incentive Plan.

### Equity Compensation Plan Information

The following table provides information as of December 31, 2010, about the Company's securities that may be issued under the Company's existing equity compensation plans, all of which have been approved by the stockholders:

Plan Category	Number of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted-average exercise price of outstanding options, warrants and rights	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
	(a)	(b)	(c)
Equity compensation plans approved by security holders	679,128	\$ 32.44	278,143(1)
Equity compensation plans not approved by security holders			
<b>Total</b>	<b>679,128</b>	<b>\$ 32.44</b>	<b>278,143</b>

- (1) Under the Company's existing equity compensation plans, shares may be issued in the form of performance stock awards as awarded by the Compensation and Development Committee of the Board of Directors.



## Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act of 1934 and the rules thereunder require the Company's Executive Officers and Directors, and persons who own more than 10 percent of the Common Stock or Preferred Stock, to file reports of beneficial ownership and changes in beneficial ownership of Common Stock or Preferred Stock with the SEC, the New York Stock Exchange, the Chicago Stock Exchange and the Company. Based solely upon a review of the copies of such forms received by it during or with respect to its most recent fiscal year, or written representations from certain reporting persons, the Company believes that all such required reports have been timely filed except for four late reports for four transactions by each of the following Company Executive Officers: Messrs. F. Quinn Stepan, F. Quinn Stepan, Jr., James E. Hurlbutt, Gregory Servatius, John V. Venegoni, Robert J. Wood, and H. Edward Wynn. These late reports were caused by a minor administrative error which has been corrected for reporting deferred quarterly dividend equivalents pursuant to a new 2010 incentive compensation plan. All such transactions have since been properly reported. In addition, one late report of two transactions each in both 2009 and 2010 were also filed by Mr. F. Quinn Stepan due to minor administrative errors which have been corrected to comply with the minimum required distribution rules for the Company's two Employee Stock Ownership Plans. All such transactions have since been properly reported.

## Policies and Procedures for Approving Related Person Transactions

The Company adopted a written policy entitled "Stepan Company Related Party Transactions Policy and Procedures" which was initially approved by the Audit Committee of the Board of Directors in February 2007, and has been annually reviewed by the Audit Committee at each subsequent February meeting ("Related Party Transactions Policy"). This policy applies to transactions ("Related Party Transactions") involving the Company and a Related Party, which is defined as a person or entity who is a Company executive officer, Director, or nominee for election as a Director, or a beneficial owner of 5% or more of the Company's stock, or an immediate family member of these persons. The Related Party Transactions Policy states that the Company will enter into or ratify Related Party Transactions only when the Board of Directors, acting through the Audit Committee or as otherwise set forth in the Related Party Transactions Policy, approves the Related Party Transaction after determining that it is in, or is not inconsistent with, the best interests of the Company and its stockholders. The Audit Committee will review the material facts of all Related Party Transactions under the Related Party Transactions Policy, as discussed below, in order to make such determination and to decide whether to approve or disapprove such Related Party Transaction. No Director may participate in any discussion or approval of a Related Party Transaction for which he or she is a Related Party, except that the Director must provide any material information concerning the Related Party Transaction requested by the Audit Committee.

As set forth in the Related Party Transactions Policy, the Audit Committee has reviewed and approved certain types of Related Party Transactions and determined that the following types of Related Party Transactions will be generally deemed to be pre-approved under the terms of the Related will be able to sell shares of common stock purchased in this offering at a price equal to or greater than the subscription price.

*We do not have a history of paying cash dividends on our common stock.*

We have never declared a cash dividend on our common stock and do not anticipate doing so in the foreseeable future.

*You must act promptly and follow instructions carefully if you want to exercise your rights.*

Eligible participants and, if applicable, brokers acting on their behalf, who desire to purchase common stock in the rights offering must act promptly to ensure that all required certificates and payments are actually received by the subscription agent, Mellon Investor Services LLC, with respect to the rights before the expiration of the \$7 subscription period at 5:00 p.m. New York City time, on \_\_\_\_\_, \_\_\_\_\_, 2005 or,

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with respect to the \$8 subscription period at 5:00 p.m. New York City time, on \_\_\_\_\_, \_\_\_\_\_, 2005. **The time period to exercise rights is limited.** If you or your broker fail to complete and sign the required rights certificate, send an incorrect payment amount, or otherwise fail to follow the procedures that apply to the exercise of your rights, we may, depending on the circumstances, reject your exercise of rights or accept it to the extent of the payment received, in which event, your current investment in our company would be diluted. Neither we nor the subscription agent undertake to contact you concerning, or attempt to correct, an incomplete or incorrect rights certificate or payment or contact you concerning whether a broker holds rights on your behalf. We have the sole discretion to determine whether an exercise properly follows the applicable procedures.

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**USE OF PROCEEDS**

If all of the rights are exercised at a subscription price of \$7, we will receive approximately \$112.4 million, before deducting any offering expenses. If none of the rights are exercised at a subscription price of \$7 and all of the rights are exercised at a subscription price of \$8, we will receive approximately \$128.4 million, before deducting any offering expenses. As described more fully in The Rights Offering Reasons for the Rights Offering, if we do not receive at least \$25.0 million in proceeds during the first month of the rights offering, The Price Group will purchase, in a private placement, enough shares of our common stock to ensure that we receive \$25.0 million of new equity financing through the rights offering and such purchase. The expenses associated with the rights offering are estimated to be \$0.6 million. We plan to use \$7.0 million of proceeds from the rights offering for site work and construction of a fourth warehouse club in Costa Rica and \$7.2 million to retire short-term debt associated with six separate facilities with various maturity dates extending through March 2005 and interest rates ranging from 6.25% to 10.0%. Further, we plan to use \$3.0 million of proceeds received from the rights offering to repay a \$3.0 million loan extended to us by The Price Group, the proceeds of which were used for the acquisition of land for the new Costa Rica location. The \$3.0 million loan from The Price Group was entered into on November 3, 2004 and bears interest at 5% per annum with a term of 90 days. The remaining proceeds received from the rights offering will be used for working capital and general corporate purpose. If the rights offering generates significantly more than \$25.0 million in proceeds, we may elect to use a portion of the proceeds to retire portions of our long-term debt.

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### **THE RIGHTS OFFERING**

#### **General**

As soon as practicable, we will distribute to each holder of our common stock, at no charge, one transferable subscription right for each share of our common stock owned by such holder as of the close of business on the record date. The rights will be evidenced by rights certificates.

Each right entitles its holder to purchase: (i) for a period of one month, 1.5 shares of our common stock for each share of common stock they own as of the November 24, 2004, at a price of \$7 per share; and (ii) for a period of eleven months beginning after the one month period referred to in part (i) above expires, 1.5 shares of common stock for each share of common stock they own as of November 24, 2004, at a price of \$8 per share. If a rights holder exercises a right at a subscription price of \$7, such rights holder may not also exercise that right at a subscription price of \$8. Therefore, in total, stockholders will only receive sufficient rights to enable them to purchase 1.5 shares of common stock for each share they own as of November 24, 2004, regardless of when they exercise their rights. If a right is subscribed at \$7, the subscription price would reflect an approximately 20% discount to the \$8.80 per share last sales price of our common stock on the Nasdaq National Market on September 3, 2004, the last trading day before the announcement of the subscription prices. Rights holders will not have the right to subscribe for shares not purchased by rights holders who hold rights at the expiration of the \$8 subscription period and elect not to exercise their rights.

The following describes the rights offering in general and assumes (unless specifically provided otherwise) that you are a record holder of our common stock. If you hold your shares of our common stock in a brokerage account or through a dealer or other nominee, please see the information included below under the heading **Beneficial Owners**. As used in this prospectus and in the related instructions for completing rights certificates, the term **business day** means any day on which securities may be traded on the Nasdaq National Market.

#### **Reasons for the Rights Offering**

As previously disclosed in our Current Report on Form 8-K filed with the Securities and Exchange Commission on November 4, 2004, we have begun implementing a transaction designed to improve our profitability by reducing our interest payments and eliminating our preferred stock dividend obligations. As of the date of this prospectus, substantially all of the common stock issuable to our affiliates pursuant to such transaction has been issued. The purposes of this rights offering are to provide holders of our common stock not affiliated with us or the Prices, an opportunity to further invest in us and maintain a portion, if not all, of their proportionate interest in our common stock at a lower price per share than was offered to the Prices in connection with our exchange of common stock for obligations owed by us to the Prices and for shares of preferred stock held by the Prices, as described below, and to allow us to obtain long-term financing through an equity offering to our common stockholders. On October 29, 2004, we held a special meeting of stockholders to approve elements of the transaction as required by Nasdaq Marketplace Rules and the Delaware General Corporation Law. The transaction includes the following elements, each of which was approved by our common stockholders at the special meeting:

a private placement of 3,164,726 shares of our common stock, at a price of \$8 per share, to The Price Group to be funded through the conversion of a \$25.0 million bridge loan, together with accrued and unpaid interest, extended to us by The Price Group on August 31, 2004;

an issuance of an aggregate of 2,200,000 shares of our common stock to the Sol and Helen Price Trust, the Price Family Charitable Fund, the Robert and Allison Price Charitable Remainder Trust, the Robert and Allison Price Trust 1/10/75 and The Price Group in

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exchange for all of the outstanding shares of our 8% Series B Cumulative Convertible Redeemable Preferred Stock, par value \$.0001 per share;

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an issuance of 2,597,200 shares of our common stock, valued for such purpose at a price of \$8 per share, to The Price Group in exchange for up to \$20.0 million of current obligations, plus accrued and unpaid interest, we owed to The Price Group;

an issuance of up to 16,052,668 shares of our common stock in connection with the rights offering described herein;

an issuance of up to 3,125,000 shares of our common stock, at a price of \$8 per share, to The Price Group to ensure that this rights offering generates at least \$25.0 million in proceeds;

an issuance of up to 2,223,104 shares of our common stock associated with an offer to exchange common stock, valued for such purpose at a price of \$10 per share, to the holders of all of the shares of our 8% Series A Cumulative Convertible Redeemable Preferred Stock, par value \$.0001 per share, in exchange for all of the outstanding shares of our Series A Preferred Stock at its initial stated value of \$20.0 million plus all accrued and unpaid dividends; and

an amendment to our Amended and Restated Certificate of Incorporation to increase our number of authorized shares of common stock from 20,000,000 to 45,000,000 shares.

As previously disclosed in our Current Report on Form 8-K filed with the SEC on October 8, 2004, on October 4, 2004 we entered into a Common Stock Purchase Agreement with The Price Group, the Sol and Helen Price Trust, the Price Family Charitable Fund, the Robert and Allison Price Charitable Remainder Trust and the Robert and Allison Price Trust 1/10/75 to effectuate the private placement and the exchange of shares of our common stock for all of our outstanding Series B Preferred Stock and the current obligations, as described above. On October 25, 2004, the Price Family Charitable Fund donated its shares of Series B Preferred Stock to a public charity on the condition that such charity agree to be subject to the terms and conditions of the Common Stock Purchase Agreement. On October 29, 2004, following approval by our common stockholders of the above described transaction at a special meeting of stockholders called for such purpose, we issued an aggregate of 7,161,926 shares of common stock to The Price Group, the Sol and Helen Price Trust and the Robert and Allison Price Trust 1/10/75 to consummate the private placement and the exchange of common stock for all of our outstanding Series B Preferred Stock and the current obligations on the condition that such entities agree not to exercise or convey any rights they may receive pursuant to this rights offering on such shares. In connection therewith, we also issued 300,000 shares of common stock to the Robert and Allison Price Charitable Remainder Trust. We have agreed to register with the SEC for resale all 7,461,926 of these shares together with 500,000 shares of common stock issued to the public charity pursuant to the exchange of our common stock for all of our Series B Preferred Stock. On November 23, 2004, we issued 61,135 shares of our common stock to the Sol and Helen Price Trust pursuant to the offer to the holders of our Series A Preferred Stock to exchange shares of our common stock for all of our outstanding shares of Series A Preferred Stock. The Sol and Helen Price Trust has agreed not to exercise or convey any rights it may receive on the 61,135 shares of common stock it received pursuant to such exchange.

As mentioned above, if upon expiration of the \$7 subscription period we have not received at least \$25.0 million in proceeds from the rights offering, The Price Group has agreed to purchase from us the number of shares of our common stock equal to the shortfall, if any, divided by \$8, at a price of \$8 per share. Concurrent with this purchase of common stock by The Price Group, we will grant The Price Group a non-transferable put option giving The Price Group the right, at its election, to require us to purchase at any time during the thirty (30) days following the end of the rights offering subscription period a number of shares equal to the lesser of (i) the dollar amount raised by us from the exercise of rights upon the conclusion of the \$8 subscription period divided by \$8, and (ii) the number of shares purchased by The Price Group upon the conclusion of the \$7 subscription period, in each case at a price of \$8 per share. We have agreed to register with the SEC for resale the shares of our common stock issuable in connection with the purchase by The Price Group upon the conclusion of the \$7 subscription period, if any. If the rights offering is 0% subscribed upon expiration of the \$7 subscription period, this purchase by The Price Group will require the issuance of 3,125,000 shares of common stock.

As previously stated, the Prices comprise a group that may be deemed to beneficially own greater than 50% of our common stock. The following table reflects the dilution of the Prices' ownership in our common stock



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through the rights offering assuming different levels of stockholder participation in the rights offering. The table assumes each stockholder will subscribe in the rights offering proportionately to the overall level of subscription, meaning that if the rights offering is 50% subscribed, each individual stockholder will exercise 50% of his, her or its rights. This table also assumes that the Prices do not exercise any rights granted to them pursuant to the rights offering. However, the Prices may exercise rights granted to them pursuant to the rights offering on an aggregate of 3,566,512 shares of common stock.

		Stockholder Subscription of the Rights Offering		
		50% Subscribed	25% Subscribed	0% Subscribed
The Prices	Beneficial Ownership of Common Stock	40%	47%	61%

As described above, the Prices are the beneficial owners of greater than 50% of our common stock, and depending on the extent to which the rights offering is subscribed by our common stockholders, may continue to be the beneficial owners of greater than 50% of our common stock following the rights offering.

**Determination of Subscription Price**

After discussions with management about our financial condition and long-term operating goals and after a consideration of what would be fair to us and our unaffiliated stockholders, representatives of The Price Group proposed the value to be ascribed to our common stock for purposes of the \$25.0 million private placement, the exchange of common stock for all of our outstanding Series B Preferred Stock and the exchange of our common stock for the up to \$20.0 million in current obligations owed to The Price Group. Concurrently therewith, such representatives also proposed the prices per share for this rights offering, the potential purchase by The Price Group of up to 3,125,000 shares of our common stock at \$8 per share upon the conclusion of the \$7 subscription period and the exercise price of the put option that would be granted in connection with such purchase by The Price Group, if any. Except for the \$7 per share price applicable during the first month of the rights offering, the deemed values for the common stock were greater than the market price of the common stock at the time the initial proposals were made to us. The deemed exchange value for the common stock used in the offer to exchange our common stock for all of our outstanding Series A Preferred Stock was separately negotiated by our outside counsel and counsel to plaintiffs in the federal class action lawsuit entitled *Performance Capital, L.P. v. PriceSmart, Inc. et al.* These exchange values were estimates only, and there can be no assurance that our common stock will attain, or maintain for any period of time, a market price approaching such estimate in the future.

**Expiration Time**

You may exercise your subscription privilege at any time before the expiration time, which is 5:00 p.m., New York City time, on \_\_\_\_\_, 2005, in order to exercise a right at a subscription price of \$7, or from the expiration of the \$7 subscription period until 5:00 p.m., New York City Time on \_\_\_\_\_, 2005 to exercise a right at a subscription price of \$8, unless the rights offering is terminated or extended. If you do not exercise your rights before the expiration of the \$8 subscription period, your rights will expire and become null and void. If you desire to exercise your rights during the \$7 subscription period, we will not be obligated to honor your exercise of rights if the subscription agent receives any of the required documents relating to your exercise of such subscription privilege after the expiration time for the \$7 subscription period, regardless of when you transmitted the documents, unless you have timely transmitted the documents pursuant to the guaranteed delivery procedures described below. If the subscription agent receives documents related to an exercise of rights at a subscription price of \$7 after the expiration of the \$7 subscription period, your subscription price will be returned to you. We will not be obligated to honor your exercise of rights if the subscription agent receives any of the required documents relating to your exercise of subscription privileges after the expiration of the \$8 subscription period, regardless of when you transmitted the documents, unless you have timely transmitted the documents pursuant to the guaranteed delivery procedures described below.



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We may extend the expiration time for the \$7 subscription period or the \$8 subscription period for any reason, and you will not be able to revoke your exercise of subscriptions.

If we elect to extend the expiration time for the \$7 subscription period or the \$8 subscription period, we will issue a press release announcing the extension before 9:00 a.m. Pacific time on the first business day after the most recently announced expiration time.

## **Subscription Privilege**

Each right entitles the holder to purchase 1.5 shares of our common stock, upon delivery of the required documents and payment of the proper subscription price per share, prior to the expiration time. You are not required to exercise your subscription privilege.

## **Exercising Your Rights**

You may exercise your rights by delivering the following to the subscription agent before the expiration time for the \$7 subscription period or the \$8 subscription period:

your properly completed and executed rights certificate evidencing the exercised rights with any required signature medallion guarantees or other supplemental documentation; and

your payment in full of the subscription price for each share of common stock subscribed for pursuant to the subscription privilege.

Alternatively, if you deliver a notice of guaranteed delivery together with your subscription price payment prior to the expiration time for the \$7 subscription period or the \$8 subscription period, as the case may be, you must deliver the rights certificate within three business days following the expiration time for the \$7 subscription period or the \$8 subscription period, as the case may be, using the guaranteed delivery procedures described below under the heading **Guaranteed Delivery Procedures**.

## **Payment of Subscription Price**

Your cash payment of the subscription price for the rights must be made by either certified check, bank draft or money order payable to Mellon Investor Services LLC. Your cash payment of the subscription price for the rights will be deemed to have been received by the subscription agent only when the subscription agent receives your certified check, bank draft or money order.

We will retain any interest earned on any cash funds held by the subscription agent in connection with the rights offering prior to the consummation of the rights offering or the return of such funds, if required, pursuant to this prospectus.

The subscription agent will hold your payment of the subscription price for the rights in a segregated account with other payments received from holders of rights until we issue to you your shares of common stock or return your overpayment, if any.

### **Exercising a Portion of Your Rights**

If you subscribe for fewer than all of the shares of common stock that you are eligible to purchase pursuant to the subscription privilege represented by your rights certificate, you may, under certain circumstances, request from the subscription agent, a new rights certificate representing the unused rights and then attempt to sell your unused rights. See [Method of Transferring and Selling Rights](#) below.

Alternatively, you may transfer a portion of your rights and request from the subscription agent, a new rights certificate representing the rights you did not transfer.

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### **Calculation of Rights Exercised**

If you do not indicate the number of shares being purchased for the rights you receive, or do not forward full payment of the aggregate subscription price for the number of shares that you indicate are being purchased, then you will be deemed to have exercised the subscription privilege with respect to the maximum number of shares that may be purchased for the aggregate subscription price payment received by the subscription agent. If your full subscription price payment is not applied to your purchase of shares of common stock, the subscription agent will return to you by mail or similarly prompt means, or as otherwise instructed by us, the excess amount without interest or deduction as soon as practicable.

### **Instructions for Completing the Rights Certificates**

You should read and follow the instructions accompanying the rights certificates carefully. If you want to exercise your rights, you must send your completed rights certificates, any necessary accompanying documents and payment of the subscription price to the subscription agent. **You should not send the rights certificates, any related documentation or payment of the subscription price to us.** Any rights certificates and other items received by us relating to the subscriptions will be returned to the sender.

You bear all risk for the method of delivery of rights certificates, any necessary accompanying documents and payment of the subscription price to the subscription agent. If you send the rights certificates and other items by mail, we recommend that you send them by registered mail, properly insured, with return receipt requested. You should allow a sufficient number of days to ensure delivery and clearance of cash payment prior to the expiration time.

### **Signature Medallion Guarantee May Be Required**

Your signature on each rights certificate must be medallion guaranteed by an eligible institution such as a member firm of a registered national securities exchange, a member of the National Association of Securities Dealers, Inc. or a commercial bank or trust company having an office or correspondent in the United States, subject to standards and procedures adopted by the subscription agent, unless:

your rights certificate is registered in your name; or

you are an eligible institution.

### **Delivery of Subscription Materials and Payment**

You should deliver your rights certificate and payment for the common stock subscribed for, as well as any nominee holder certifications, notices of guaranteed delivery and any other required documentation to the subscription agent, Mellon Investor Services LLC as follows:

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*By Mail:*

PriceSmart, Inc.

c/o Mellon Investor Services LLC

Attention: Reorganization Dept.

P.O. Box 3301

South Hackensack, NJ 07606

*By Hand:*

PriceSmart, Inc.

c/o Mellon Investor Services LLC

Attention: Reorganization Dept.

120 Broadway, 13th Floor

New York, NY 10271

*By Overnight Courier:*

PriceSmart, Inc.

c/o Mellon Investor Services LLC

Attention: Reorganization Dept.

85 Challenger Road, 2<sup>nd</sup> Floor

Overpeck Centre

Ridgefield Park, NJ 07660

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### **Guaranteed Delivery Procedures**

If you wish to exercise your rights, but you do not have sufficient time to deliver the rights certificate evidencing your rights to the subscription agent before the expiration of the \$7 or \$8 subscription period, as the case may be, you may exercise your rights by the following guaranteed delivery procedures:

provide your payment in full of the subscription price for each share of common stock being subscribed for pursuant to the subscription privilege to the subscription agent before the applicable expiration time;

deliver a notice of guaranteed delivery to the subscription agent at or before the expiration time; and

deliver the properly completed rights certificate evidencing the rights being exercised (and, if applicable for a nominee holder, the related nominee holder certification), with any required signatures medallion guaranteed, to the subscription agent, within three business days following the expiration time for the \$7 subscription period or the \$8 subscription period, as the case may be.

Your notice of guaranteed delivery must be substantially in the form provided with the Instructions for Use of PriceSmart, Inc. Common Stock Rights Certificates distributed to you with your rights certificate. Your notice of guaranteed delivery must come from an eligible institution which is a member of, or a participant in, a signature guarantee medallion program acceptable to the subscription agent. In your notice of guaranteed delivery you must state:

your name;

the number of rights represented by your rights certificate, the number of shares of common stock you are subscribing for pursuant to the subscription privilege; and

your guarantee that you will deliver to the subscription agent any rights certificates evidencing the rights you are exercising within three business days following the expiration time for the \$7 subscription period or the \$8 subscription period, as the case may be.

You may deliver the notice of guaranteed delivery to the subscription agent in the same manner as the rights certificate at the addresses set forth under Delivery of Subscription Materials and Payment above.

Eligible institutions may also transmit the notice of guaranteed delivery to the subscription agent by facsimile transmission to (201) 296-4293. To confirm facsimile deliveries, you may call (201) 296-4860.

The information agent will send you additional copies of the form of notice of guaranteed delivery if you need them. Please call the information agent at (888) 684-7182.

### **Notice to Nominees**

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If you are a broker, a dealer, a trustee or a depositary for securities who holds shares of our common stock for the account of others as a nominee holder, you should notify the respective beneficial owners of those shares of the issuance of the rights as soon as possible to find out the beneficial owners' intentions. You should obtain instructions from the beneficial owner with respect to the rights, as set forth in the instructions we have provided to you for your distribution to beneficial owners. If the beneficial owner so instructs, you should complete the appropriate rights certificates and submit them to the subscription agent with the proper payment. A nominee holder that holds shares of common stock for the account(s) of more than one beneficial owner may exercise the number of rights to which all such beneficial owners in the aggregate otherwise would have been entitled if they had been direct record holders of common stock on the record date, so long as the nominee submits the appropriate rights certificates and certifications and proper payment to the subscription agent.

If you hold shares of common stock as a nominee holder for beneficial owners whose address is outside the United States, see Foreign Stockholders.

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### **Beneficial Owners**

If you are a beneficial owner of shares of our common stock or rights that you hold through a nominee holder, we will ask your broker, dealer or other nominee to notify you of this rights offering. If you wish to exercise your rights, you will need to have your broker, dealer or other nominee act for you. To indicate your decision with respect to your rights, you should complete and return to your broker, dealer or other nominee the form entitled Beneficial Owners Election Form. You should receive this form from your broker, dealer or other nominee with the other subscription materials. If you are outside the United States, see Foreign Stockholders.

### **Procedures for DTC Participants**

We expect that the rights will be eligible for transfer, and that your exercise of your subscription privilege with respect to rights may be made, through the facilities of DTC.

### **Determinations Regarding the Exercise of Rights**

We will decide all questions concerning the timeliness, validity, form and eligibility of your exercise of rights. Our decisions will be final and binding. We, in our sole discretion, may waive any defect or irregularity, or permit a defect or irregularity to be corrected within whatever time we determine. We may reject the exercise of any of your rights because of any defect or irregularity. Your subscription will not be deemed to have been received or accepted until all irregularities have been waived by us or cured by you within the time we decide, in our sole discretion.

We reserve the right to reject your exercise of rights if your exercise is not in accordance with the terms of the rights offering or in proper form. Neither we nor the subscription agent will have any duty to notify you of a defect or irregularity in your exercise of the rights. We will not be liable for failing to give you that notice. We will also not accept your exercise of rights if our issuance of shares of common stock pursuant to your exercise could be deemed unlawful or materially burdensome. See Regulatory Limitation and Compliance with Regulations Pertaining to the Rights Offering below.

### **No Revocation of Exercised Rights**

Once you have exercised your subscription privilege and you may not revoke your exercise. Even if we extend the expiration time for the \$7 subscription period or the \$8 subscription period, you may not revoke your exercise.

### **Subscription Agent**

We have appointed Mellon Investor Services LLC as subscription agent for the rights offering. We will pay its fees and expenses related to the rights offering and have agreed to indemnify it from liabilities it may incur in connection with the rights offering.

**Information Agent**

We have appointed Mellon Investor Services LLC as information agent for the rights offering. We will pay its fees and expenses related to the rights offering and have agreed to indemnify it from liabilities it may incur in connection with the rights offering. You may direct any questions or requests for assistance concerning the method of exercising your rights, additional copies of this prospectus, the instructions for the rights, the nominee

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holder certification, the notice of guaranteed delivery or other subscription materials referred to herein, to the information agent for the rights offering, at the following telephone number and address:

Mellon Investor Services LLC

85 Challenger Road, 2<sup>nd</sup> Floor

Overpeck Centre

Ridgefield Park, NJ 07660

TOLL FREE: (888) 684-7182

## **Method of Transferring and Selling Rights**

We have applied for the rights to be listed for trading on the Nasdaq National Market under the symbol **PSMTR**. We expect that the rights may be purchased or sold through usual investment channels until 5:00 p.m., New York City time, on \_\_\_\_\_, \_\_\_\_\_, 2005, the expiration time for the \$8 subscription period. You may not sell, transfer or send your rights or rights certificate to anyone outside the United States unless the foreign person provides evidence satisfactory to us that such sale or transfer is lawful. There has been no prior public market for the rights, and we cannot assure you that a trading market for the rights, will exist or develop or, if a market develops, that the market will remain available throughout the subscription period. We also cannot assure you of the price at which the rights will trade, if at all. If you do not exercise or sell your rights you will lose any value inherent in the rights. See **General Considerations Regarding the Partial Exercise, Transfer or Sale of Rights** below.

## **Transfer of Rights**

You may transfer rights in whole by endorsing the rights certificate for transfer and by following the instructions for transfer included in the information sent to you with your rights certificate. If you wish to transfer only a part of the rights, you should deliver your properly endorsed rights certificate to the subscription agent. With your rights certificate, you should include instructions to register in the name of the transferee such portion of the rights evidenced thereby that you wish to transfer and to issue a new rights certificate to the transferee evidencing that portion of the rights that you wish to transfer. You may only transfer whole rights and not fractions of a right. If there is sufficient time before the expiration of the \$8 subscription period, the subscription agent will send you a new rights certificate evidencing the balance of the rights issued to you but not transferred to the transferee. You may also instruct the subscription agent to send the rights certificate to one or more additional transferees. If you wish to sell your remaining rights, you may request that the subscription agent transfer your certificates representing your remaining rights to your broker or dealer so that you may sell them through your broker or dealer. You may also request that the subscription agent, sell your rights for you, as described below.

We and the subscription agent reserve the right without liability to treat as invalid any exercise or purported exercise of rights evidenced by a completed rights certificate or any transfer or purported transfer of a rights certificate that appears to us or the subscription agent to have been executed, effected or dispatched into, in or from a jurisdiction other than the United States or if the transferee of any purported transfer of a rights certificate appears to be resident outside the United States unless it is otherwise lawful for them to do so. At the time of transfer or exercise, these foreign persons must provide evidence satisfactory to us, such as a legal opinion from local counsel, that it is lawful for them to do so.

If you wish to transfer all or a portion of your rights, you should allow a sufficient amount of time prior to the expiration of the \$8 subscription period for the subscription agent to:

receive and process your transfer instructions; and

issue and transmit a new rights certificate to your transferee or transferees with respect to transferred rights, and to you with respect to any rights you retained.

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Neither we nor the subscription agent will have any liability to you if you or your transferee does not receive any new rights in time to exercise or transfer such rights.

If you wish to transfer your rights, your rights certificate must be medallion guaranteed by an eligible institution.

## **Sales of Rights through the Subscription Agent**

If you choose not to sell your rights through your broker or dealer, you may seek to sell your rights only through the subscription agent. If you wish to have the subscription agent seek to sell your rights, you must deliver your properly executed rights certificate, with appropriate instructions, to the subscription agent. If you want the subscription agent to seek to sell only part of your rights, you must send the subscription agent instructions setting forth what you would like done with the rights, along with your rights certificate. You may only seek to sell whole rights and not fractions of a right through the subscription agent.

If the subscription agent sells rights for you, the subscription agent will send you by mail a check for the net proceeds from the sale of any of your rights as soon as practicable after such sale. If your rights can be sold, the sale will be placed, to the extent possible, with a broker on the next trading day on the Nasdaq National Market following receipt of the sale request. You will be deemed to have sold your rights at the actual sale price received for such sale. The fees charged by the subscription agent for selling rights will be deducted from the sale price for such rights sold. We cannot assure you, however, that a market will develop for the rights or that the subscription agent will be able to sell your rights.

You must have your order to sell your rights to the subscription agent before 11:00 a.m., New York City time, on \_\_\_\_\_, \_\_\_\_\_, 2005, the fifth business day before the expiration of the \$8 subscription period. If less than all sales orders received by the subscription agent are filled, the sales proceeds will be prorated among you and the other rights holders based upon the number of rights that each holder has instructed be sold during that period, irrespective of when during the period the instructions are received. The subscription agent is required to sell your rights only if the subscription agent is able to find buyers. If the subscription agent cannot sell your rights by 5:00 p.m., New York City time, on \_\_\_\_\_, \_\_\_\_\_, 2005, the third business day before the expiration of the \$8 subscription period, the subscription agent will return your rights certificate to you by overnight delivery.

IF YOU SELL YOUR RIGHTS THROUGH YOUR BROKER OR DEALER, YOU MAY RECEIVE A DIFFERENT AMOUNT OF PROCEEDS THAN IF YOU SELL THE SAME AMOUNT OF RIGHTS THROUGH THE SUBSCRIPTION AGENT. IF YOU SELL YOUR RIGHTS THROUGH YOUR BROKER OR DEALER INSTEAD OF THE SUBSCRIPTION AGENT, YOUR SALES PROCEEDS WILL BE THE ACTUAL SALES PRICE OF YOUR RIGHTS LESS ANY FEES, COMMISSIONS AND EXPENSES.

## **General Considerations Regarding the Partial Exercise, Transfer or Sale of Rights**

The amount of time needed by your transferee to exercise or sell its rights depends upon the method by which the transferor delivers the rights certificates, the method of payment made by the transferee and the number of transactions which the holder instructs the subscription agent to effect. You should allow a sufficient amount of time for your transferee to exercise or sell the rights transferred to it. Neither we nor the subscription agent will be liable to a transferee or transferor of rights if rights certificates or any other required documents are not received in time for exercise or sale prior to the expiration of the \$7 subscription or the \$8 subscription period.

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You will receive a new rights certificate upon a partial exercise, transfer or sale of rights only if the subscription agent receives your properly endorsed rights certificate no later than 5:00 p.m., New York City time, on Friday, \_\_\_\_\_, 2005, five business days before the expiration of the \$8 subscription period. Neither the subscription agent nor we will issue a new rights certificate if your rights certificate is

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received after that time and date. If your instructions and rights certificate are received by the subscription agent after that time and date, you will not receive a new rights certificate and therefore will not be able to sell or exercise your remaining rights.

You are responsible for all commissions, fees and other expenses (including brokerage commissions and transfer taxes) incurred in connection with the purchase, sale or exercise of your rights, except that we will pay any fees of the subscription agent associated with the exercise of rights. Any amounts you owe will be deducted from your account.

A request to exercise rights will constitute a warranty by you that you and the beneficial owner of the rights are within the United States, except if you have otherwise provided evidence to our satisfaction, such as a legal opinion from local counsel, that it is lawful for you to receive rights and exercise rights and acquire shares. A transfer of rights will constitute a warranty that the transferor is within the United States or is otherwise entitled to transfer the rights and a warranty from the transferee that the transferee and any beneficial owner of the rights for whom the transferee acts are within the United States or that it is otherwise lawful for them to receive rights and exercise rights and acquire shares of common stock.

If you do not exercise your rights before the expiration of the \$8 subscription period, your rights will expire and will no longer be exercisable.

## **Effect on Stock Options**

All of our outstanding stock options were issued pursuant to plans previously adopted by our board of directors. Holders of options to purchase shares of our common stock will not receive rights. We plan to make an equitable adjustment to all of our outstanding stock options to preserve the benefits or potential benefits intended to be made available pursuant to the options. Such future adjustment shall be made by the Compensation Committee of our Board of Directors.

## **No Recommendations to Rights Holders**

Neither we nor our board of directors has made any recommendation as to whether you should exercise your rights or transfer your rights. You should decide whether to transfer your rights, subscribe for shares of our common stock or simply take no action with respect to your rights, based upon your own assessment of your best interests.

## **Termination**

There are no conditions to the consummation of the rights offering. However, we may terminate the rights offering for any reason at any time before the expiration of the \$7 subscription period or the \$8 subscription period. If we terminate the rights offering, we will promptly issue a press release announcing the termination, and we will promptly thereafter return all subscription payments, provided that shares of common stock have not been issued pursuant to such subscription payment. We will not be obligated to issue shares to rights holders that have exercised their rights prior to the termination of the rights offering. We will not pay interest on, or deduct any amounts from, subscription payments if we terminate the rights offering.

## Foreign Stockholders

We will not mail rights certificates to stockholders on the record date or to subsequent transferees whose addresses are outside the United States because their exercise of rights may be prohibited by the laws of the country in which they live. Instead, we will have the subscription agent hold the rights certificates for those holders' accounts. Foreign holders may exercise their subscription privilege at any time before 11:00 a.m., New York City time, on \_\_\_\_\_, \_\_\_\_\_, 2005, in order to exercise a right at a subscription price of \$7,

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or from the expiration of the \$7 subscription period until 11:00 a.m., New York City Time on \_\_\_\_\_, 2005 to exercise a right at a subscription price of \$8, unless the rights offering is terminated or extended. To transfer their rights, foreign holders must notify the subscription agent before 11:00 a.m., New York City time, on \_\_\_\_\_, 2005, five business days prior to the expiration of the \$8 subscription period and must establish to our satisfaction that such exercise or transfer is permitted under applicable law. If a foreign holder does not establish to our satisfaction that such exercise or transfer is permitted under applicable law, and notify, and provide acceptable instructions to, the subscription agent by such time (and if no contrary instructions have been received by such time), the subscription agent will seek to sell the foreign holder's rights, subject to the subscription agent's ability to find a purchaser. Any such sales will be deemed to have been made at the actual sale price received in such sale by the subscription agent. If the subscription agent sells a foreign holder's rights, the subscription agent will send the foreign holder by mail a check for the net proceeds from the sale of any rights of the foreign holder. See Method of Transferring and Selling Rights, Transfer of Rights and Sales of Rights Through the Subscription Agent above. The proceeds, if any, resulting from sales of rights of holders whose addresses are not known by the subscription agent or to whom delivery cannot be made will be held in an interest bearing account. Any amount remaining unclaimed on the second anniversary of the expiration time will be turned over to us. If you live outside of the United States, you should consult with your legal advisor about the particular laws of the country in which you live.

If you hold shares of our common stock through a broker, a dealer, a trustee or a depository within the United States as a nominee holder and you are outside the United States, neither you nor your nominee may attempt to exercise any rights unless you have provided evidence satisfactory to us, such as a legal opinion from local counsel, that it is not unlawful for you to receive and exercise rights without any requirement being imposed on us to be registered or licensed.

## **Regulatory Limitation**

We will not be required to issue to you shares of our common stock pursuant to the rights offering if, in our opinion, you would be required to obtain prior clearance or approval from any state or federal regulatory authorities to own or control such shares and if, at the time of the expiration of the \$8 subscription period, you have not obtained such clearance or approval.

## **Issuance of Common Stock**

Unless we earlier terminate the rights offering, the subscription agent will issue the shares of our common stock purchased in the rights offering as soon as practicable following receipt of a properly completed and signed rights certificate together with payment of the subscription price for each share of common stock subscribed for. Each subscribing holder's new shares will be issued in the same form, certificated or book-entry, as the rights exercised by that holder.

Your payment of the aggregate subscription price for our common stock will be retained by the subscription agent and will not be delivered to us, unless and until your subscription is accepted and you are issued your shares of common stock. We will not pay you any interest on funds paid to the subscription agent, regardless of whether the funds are applied to the subscription price or returned to you. You will have no rights as a stockholder of our company with respect to the subscribed for shares of our common stock until the certificates representing such shares are issued to you or the shares are deposited in the book-entry account held on your behalf. Upon our issuance of the certificates or the deposit of the shares in the applicable book-entry account, you will be deemed the owner of the shares you purchased by exercise of your rights. Unless otherwise instructed in the rights certificates, the shares issued to you pursuant to your subscription will be registered in your name or the name of your nominee, if applicable. We will not issue any fractional shares of common stock.

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### **Shares of Common Stock Outstanding**

As of November 24, 2004, we had outstanding 17,524,840 shares of our common stock, not including treasury shares. The number of outstanding shares of our common stock will increase by 16,052,668 shares, following the issuance of all shares purchased in the rights offering (assuming that the rights offering is fully subscribed and given that the Prices have agreed not to exercise any rights they may receive on 7,223,061 shares of our common stock beneficially owned by them as of the record date). This represents an approximate 92% increase in the number of outstanding shares of our common stock as of November 24, 2004.

### **Compliance with Regulations pertaining to the Rights Offering**

We are not making the rights offering in any state or other jurisdiction in which it is unlawful to do so. We will not sell or accept an offer to purchase shares of our common stock from you if you are a resident of any state or other jurisdiction in which the sale or offer of the rights would be unlawful. We may delay the commencement of the rights offering in certain states or other jurisdictions in order to comply with the laws of those states or other jurisdictions. However, we may decide, in our sole discretion, not to modify the terms of the rights offering as may be requested by certain states or other jurisdictions. If that happens and you are a resident of the state or jurisdiction that requests the modification, you will not be eligible to participate in the rights offering. We do not expect that there will be any changes in the terms of the rights offering.

## **MATERIAL UNITED STATES FEDERAL INCOME TAX CONSEQUENCES**

### **Scope of Discussion**

The following discussion is a summary of the U.S. federal income tax consequences that are expected to be material to a typical U.S. holder (defined below) that receives rights distributed pursuant to the rights offering and that either (i) exercises such rights, (ii) allows such rights to expire, or (iii) sells, exchanges, or otherwise disposes of such rights. With the exception of the tax consequences described below under the heading Termination of Rights Offering, the following discussion assumes that we will not terminate the rights offering.

This discussion is based on current provisions of the Internal Revenue Code, which we refer to as the Code, applicable current, temporary and proposed Treasury regulations promulgated thereunder, which we refer to as the Treasury Regulations, the legislative history of the Code and publicly available administrative and judicial interpretations thereof, all as in effect as of the date of this prospectus and all of which are subject to change, possibly with retroactive effect, or to different interpretations. In addition, the administrative interpretations and practices of the Internal Revenue Service include its practices and policies as expressed in private letter rulings which are not binding on the Internal Revenue Service, except with respect to the particular taxpayers who requested and received these rulings. This discussion is included for general information purposes only and does not purport to be a complete technical analysis or listing of all potential tax considerations that may be relevant to U.S. holders in light of their particular circumstances. This discussion does not address any state, local or foreign tax consequences or any non-income tax consequences (such as estate or gift tax consequences). This discussion applies only to U.S. holders that hold shares of our common stock as capital assets and that will hold the rights distributed pursuant to the rights offering as capital assets (and, in the event such rights are exercised, will hold newly acquired shares of our common stock as capital assets), in each case, within the meaning of Section 1221 of the Code. This discussion also does not address the United States federal income tax consequences to a U.S. holder that is one of our affiliates or that is subject to special rules under the Code, including but not limited to:

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a financial institution, insurance company, or regulated investment company;

persons who are subject to alternative minimum tax;

a tax-exempt organization, retirement plan, or mutual fund;

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a dealer, broker, or trader in securities;

non-U.S. holders (as defined below);

an entity treated as a partnership for U.S. federal income tax purposes;

a stockholder that owns its shares of our common stock indirectly through an entity treated as a partnership for United States federal income tax purposes, or a trust or estate;

persons deemed to sell their shares of common stock under the constructive sale provisions of the Code;

a stockholder that holds its shares of our common stock as part of a hedge, appreciated financial position, straddle or conversion transaction; or

a stockholder that acquired our common stock pursuant to the exercise of compensatory stock options or otherwise as compensation.

We will not seek a ruling from the Internal Revenue Service, or the IRS, with respect to the rights offering. The IRS could take positions concerning the tax consequences of the rights offering that are different from those described in this discussion, and, if litigated, a court could sustain any such positions taken by the IRS.

For purposes of this discussion, the term U.S. holder means a holder of shares of our common stock that, for U.S. federal income tax purposes, is:

a citizen or resident of the U.S.;

a corporation, a partnership or other entity treated as a corporation or a partnership for U.S. federal income tax purposes created or organized in the U.S. or under U.S. laws or the laws of any state or political subdivision thereof;

an estate the income of which is subject to U.S. federal income taxation regardless of its source; or

a trust (i) if, in general, a court within the U.S. is able to exercise primary jurisdiction over its administration and one or more U.S. persons have authority to control all of its substantial decisions or (ii) that has a valid election in effect under applicable Treasury Regulations to be treated as a U.S. person.

A non-U.S. holder is a holder other than a U.S. holder.

If a holder of our common stock is treated as a partnership for U.S. federal income tax purposes, the tax consequences of the rights offering to such partnership and its partners will depend on a variety of factors, including the activities of such partnership and its partners. A holder of our common stock that is treated as a partnership for U.S. federal income tax purposes, or that is a partner in an entity that is treated as a partnership

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for U.S. federal income tax purposes, is urged to consult its own tax advisor regarding the tax consequences associated with the rights offering.

**Holders of our common stock are urged to consult their own tax advisors regarding the specific tax consequences associated with the rights offering, including the applicability and effect of any state, local, foreign, or other tax laws as well as changes in applicable tax laws.**

### **Distribution of Rights**

Pursuant to Section 305 of the Code and the Treasury Regulations issued thereunder, a U.S. holder that receives rights pursuant to the rights offering will not be required to recognize taxable income for U.S. federal income tax purposes upon the receipt of such rights unless, among other things, the distribution of rights results in both the receipt of property by some stockholders and an increase in the proportionate interests of other stockholders in our assets or earnings and profits. In this discussion, we refer to a distribution that has both of

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these consequences as a disqualified distribution. For the purpose of determining whether a disqualified distribution has occurred, the term stockholder includes a holder of rights to acquire our stock.

As described under the heading The Rights Offering Effect on Stock Options, we plan to adjust the terms of our outstanding stock options. The Treasury Regulations under Section 305 of the Code provide that the failure to properly adjust stock options following the distribution of stock rights may cause the stock rights to be a disqualified distribution. However, the Treasury Regulations do not adequately address whether the terms of compensatory stock options must be adjusted and, if an adjustment is required, how the adjustment should be made. We believe that the adjustments we plan to make to our stock options should satisfy the requirements in the Treasury Regulations if those regulations apply to our compensatory stock options. However, there is a risk that the IRS might not agree with our approach.

Based on our belief that the adjustment of our stock options does not cause the rights offering to be a disqualified distribution, we believe that a U.S. holder that receives rights pursuant to the rights offering should not be required to recognize taxable income for U.S. federal income tax purposes and we intend to report the rights offering accordingly. However, if our intended treatment of the rights offering were challenged by the IRS and if such challenge were ultimately upheld, the U.S. federal income tax consequences to a U.S. holder that receives rights pursuant to the rights offering may differ from the consequences described herein, and it is possible that a U.S. holder's receipt of rights pursuant to the rights offering may be taxable as a dividend.

**Basis and Holding Period of Rights**

If, in accordance with Section 307 of the Code, the fair market value of the rights which we distribute to a U.S. holder is less than 15% of the fair market value of such U.S. holder's shares of our common stock with respect to which such rights were distributed, such U.S. holder's basis in the rights distributed generally will be zero. A U.S. holder may elect, however, to allocate its basis in our common stock between such common stock and the rights received in proportion to the fair market value of such common stock and such rights. This election may be made pursuant to Section 307 of the Code and the Treasury Regulations thereunder and will be irrevocable once made.

If the fair market value of the rights which we distribute to a U.S. holder is 15% or more of the fair market value of such U.S. holder's shares of our common stock with respect to which such rights were distributed, such U.S. holder will be required to allocate its basis between such common stock and such rights in proportion to their relative fair market values.

In either case, a U.S. holder's holding period for the rights that we distribute to such U.S. holder will include the holding period of such U.S. holder's shares of our common stock with respect to which such rights were distributed.

**Exercise of Rights; Basis and Holding Period of Acquired Shares; Sale, Exchange or Other Disposition of Acquired Shares**

A U.S. holder will not recognize gain or loss upon the exercise of the rights. A U.S. holder's basis in our common stock acquired through exercise of the rights generally will equal the sum of (i) the subscription price paid by such U.S. holder to acquire such common stock and (ii) such U.S. holder's basis in the rights exercised. A U.S. holder's holding period in shares of our common stock acquired through the exercise of rights will begin on the day such U.S. holder exercises the rights.

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Upon the sale, exchange or other disposition of our common stock acquired upon the exercise of rights, a U.S. holder generally will recognize gain or loss equal to the difference between the amount realized and such U.S. holder's basis in such common stock. Such gain or loss will be capital gain or loss and will be long-term

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capital gain or loss if a U.S. holder's holding period exceeds one year at the time of the sale, exchange or other disposition. Long-term capital gains of certain non-corporate taxpayers generally are taxed at lower rates than items of ordinary income. The deductibility of capital losses is subject to limitations.

## **Expiration of Rights**

If a U.S. holder receives rights pursuant to the rights offering and allows the rights to expire unexercised, then such U.S. holder will not be permitted to recognize a taxable loss. In addition, such U.S. holder's basis in its shares of our common stock will not be affected by this rights offering and such U.S. holder's decision to allow its rights to expire and will remain the same as before the rights offering.

## **Sale, Exchange or Other Disposition of Rights**

Upon the sale, exchange or other disposition of rights, a U.S. holder generally will recognize capital gain or loss equal to the difference between the amount realized and such U.S. holder's basis in the rights. Such gain or loss will be long-term capital gain or loss if a U.S. holder's holding period in the rights is more than one year on the date of the sale, exchange or other disposition. Long-term capital gains generally are taxed at lower rates than items of ordinary income. The deductibility of capital losses is subject to limitations.

## **Termination of Rights Offering**

If a U.S. holder receives rights pursuant to the rights offering and retains such rights, then, if we subsequently terminate the rights offering: (i) such U.S. holder will not recognize income, gain or loss as a result of the distribution, ownership or termination of the rights; and (ii) such U.S. holder's basis in its shares of our common stock with respect to which the rights were distributed will not be affected by the rights offering.

If a U.S. holder receives rights pursuant to the rights offering and such U.S. holder sells, exchanges or otherwise disposes of such rights, then, while the matter is not entirely free from doubt, if we subsequently terminate the rights offering: (i) such U.S. holder should not recognize income or gain as a result of the prior distribution of the rights; (ii) such U.S. holder's basis in the shares of our common stock with respect to which the rights were distributed and such U.S. holder's basis in the rights should be determined as described above under the heading "Basis and Holding Period of Rights"; and (iii) such U.S. holder should recognize gain or loss equal to the difference between the amount realized upon the sale of the rights and such U.S. holder's basis, if any, in the rights. Such gain or loss will be long-term gain or loss if such U.S. holder's holding period for the rights exceeds one year at the time of sale, exchange or other disposition.

## **Backup Withholding**

A U.S. holder that sells, exchanges or otherwise disposes of shares of our common stock acquired upon the exercise of rights or that sells, exchanges or otherwise disposes of rights may be subject to backup withholding on the proceeds received, unless such U.S. holder:

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is a corporation or other exempt recipient and, when required, establishes this exemption; or

provides a correct taxpayer identification number, certifies that it is not currently subject to backup withholding, and otherwise complies with the applicable requirements of the backup withholding rules.

Backup withholding is not an additional tax. Any amount withheld under the backup withholding rules will generally be creditable against the United States federal income tax liability of a U.S. holder if appropriate information is provided to the IRS. If a U.S. holder does not provide the appropriate party with the correct taxpayer identification number or any other proper document or certification required by the IRS (generally a Form W-9 in the case of a U.S. holder), such U.S. holder may be subject to penalties imposed by the IRS.

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**THE FOREGOING DOES NOT PURPORT TO BE A COMPLETE ANALYSIS OF THE POTENTIAL TAX CONSIDERATIONS RELATING TO THE RIGHTS OFFERING AND IS NOT TAX ADVICE. THEREFORE, HOLDERS OF OUR COMMON STOCK ARE URGED TO CONSULT THEIR TAX ADVISORS AS TO THE SPECIFIC TAX CONSEQUENCES TO THEM OF THE RIGHTS OFFERING, INCLUDING THE APPLICABILITY OF FEDERAL, STATE, LOCAL, FOREIGN AND OTHER TAX LAWS.**

**PLAN OF DISTRIBUTION**

We are making this rights offering directly to you, the holders of our common stock, on a pro rata basis for each share of our common stock held at the close of business on Wednesday, November 24, 2004, the record date for this rights offering.

We will pay Mellon Investor Services LLC, the subscription and information agent, a fee of approximately \$21,250 for their services in connection with this rights offering (which includes the subscription agent's fees associated with the exercise of rights). We have also agreed to reimburse Mellon Investor Services LLC, the subscription and information agent, their reasonable expenses and indemnify them from liabilities they may incur in connection with the rights offering.

We estimate that our total expenses in connection with the rights offering, including registration, legal and accounting fees, will be approximately \$0.6 million.

We have not employed any brokers, dealers or underwriters in connection with the solicitation or exercise of rights. Except as described in this section, we are not paying any other commissions, fees or discounts in connection with the rights offering. Some of our employees may solicit responses from you as a holder of rights, but we will not pay our employees any commissions or compensation for such services other than their normal employment compensation.

**LEGAL MATTERS**

The discussion set forth under the heading "Material United States Federal Income Tax Consequences" and the validity of the shares of our common stock and rights offered by this prospectus will be passed upon for us by Latham & Watkins LLP, San Diego, California.

**EXPERTS**

Ernst & Young LLP, independent registered public accounting firm, has audited our consolidated financial statements and schedule included in our Annual Report on Form 10-K for the year ended August 31 2004, as set forth in their report, which is incorporated by reference in this prospectus and elsewhere in the registration statement. Our financial statements and schedule are incorporated by reference in reliance on Ernst & Young LLP's report, given on their authority as experts in accounting and auditing.

**WHERE YOU CAN FIND MORE INFORMATION**

We are subject to the informational requirements of the Securities Exchange Act of 1934, as amended, and file annual, quarterly and special reports, proxy statements and other information with the SEC. You may read and copy any reports, proxy statements and other information we file at the SEC's public reference room at 450 Fifth Street, N.W., Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. You may also access filed documents at the SEC's web site at [www.sec.gov](http://www.sec.gov).

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We are incorporating by reference some information about us that we file with the SEC. We are disclosing important information to you by referencing those filed documents. Any information that we reference in this way is considered part of this prospectus. The information in this prospectus supersedes information incorporated by reference that we have filed with the SEC prior to the date of this prospectus, while information that we file with the SEC after the date of this prospectus that is incorporated by reference will automatically update and supersede this information.

We incorporate by reference the following documents we have filed, or may file, with the SEC:

our Annual Report on Form 10-K for the fiscal year ended August 31, 2004;

our Current Reports on Form 8-K filed on September 3, 2004, September 20, 2004, October 8, 2004, October 25, 2004, October 28, 2004, November 4, 2004 and November 30, 2004;

the description of our common stock contained in our Amended Registration Statement on Form 10 filed with the SEC on August 13, 1997, including any amendments or reports filed for the purpose of updating the description; and

all documents filed by us with the SEC under Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934, as amended, after the date of this prospectus and before termination of this offering.

You may request a free copy of any of the documents incorporated by reference in this prospectus by writing or telephoning us at the following address:

PriceSmart, Inc.

9740 Scranton Road

San Diego, California 92121-1745

(858) 404-8800

**Table of Contents****PART II****INFORMATION NOT REQUIRED IN PROSPECTUS****Item 14. Other Expenses of Issuance and Distribution.**

Our estimated expenses in connection with the distribution of the securities being registered are as set forth in the following table:

SEC Registration Fee	\$ 16,271
Nasdaq listing fee	\$ 46,000*
Printing Expenses	\$ 200,000*
Legal Fees and Expenses	\$ 200,000*
Accounting Fees and Expenses	\$ 25,000*
Subscription Agent Fee	\$ 18,000*
Information Agent Fee	\$ 3,250*
Miscellaneous	\$ 41,479*
	<hr/>
<b>Total</b>	<b>\$ 550,000*</b>

\* Estimated

**Item 15. Indemnification of Directors and Officers.**

Our officers and directors are covered by the provisions of the Delaware General Corporation Law, our amended and restated certificate of incorporation and amended and restated bylaws, as amended, individual indemnification agreements with us and insurance policies which serve to limit, and, in some instances, to indemnify them against, certain liabilities which they may incur in such capacities. These various provisions are described below.

*Elimination of Liability in Certain Circumstances.* In June 1986, Delaware enacted legislation which authorizes corporations to limit or eliminate the personal liability of directors to corporations and their stockholders for monetary damages for breach of directors' fiduciary duty of care. This duty of care requires that, when acting on behalf of the corporation, directors must exercise an informed business judgment based on all significant information reasonably available to them. Absent the limitations now authorized by such legislation, directors are accountable to corporations and their stockholders for monetary damages for conduct constituting negligence or gross negligence in the exercise of their duty of care. Although the statute does not change directors' duty of care, it enables corporations to limit available relief to equitable remedies such as injunction or rescission. Our amended and restated certificate of incorporation limits the liability of directors to us or our stockholders (in their capacity as directors but not in their capacity as officers) to the fullest extent permitted by such legislation. Specifically, our directors will not be personally liable for monetary damages for breach of a director's fiduciary duty as director, except for liability:

for any breach of the director's duty of loyalty to us or our stockholders;

for acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law;

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for unlawful payments of dividends or unlawful share repurchases or redemptions as provided in Section 174 of the Delaware General Corporation Law; or

for any transaction from which the director derived an improper personal benefit.

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*Indemnification and Insurance.* As a Delaware corporation, we have the power, under specified circumstances generally requiring the directors or officers to have acted in good faith and in a manner they reasonably believe to be in or not opposed to our best interests, to indemnify our directors and officers in connection with actions, suits or proceedings brought against them by a third party or in our name, by reason of the fact that they were or are such directors or officers, against expenses, judgments, fines and amounts paid in settlement in connection with any such action, suit or proceeding. Our amended and restated certificate of incorporation generally provides for mandatory indemnification of our directors and officers to the fullest extent provided by Delaware corporate law. In addition, we have entered into indemnification agreements with our directors and officers which generally provide for indemnification of the officers and directors to the fullest extent permitted under Delaware law, including under circumstances for which indemnification would otherwise be discretionary under Delaware law.

We have purchased and intend to maintain insurance on behalf of any person who is or was a director or officer, or is or was a director or officer serving at our request as a director, officer, employee or agent of another corporation, partnership, joint venture, trust, employee benefit plan or other enterprise against any liability asserted against him or her and incurred by him or her in any such capacity, or arising out of his or her status as such, whether or not we would have the power or obligation to indemnify him or her against such liability under the provisions of its certificate of incorporation or bylaws.

**Item 16. Exhibits.**

<b><u>Exhibit No.</u></b>	<b><u>Description</u></b>
4.1	Specimen of Common Stock certificate*
4.2	Specimen transferable subscription rights certificate for holders of Common Stock*
4.3	Instructions for Use of PriceSmart, Inc. Common Stock Right Certificates*
5.1	Opinion of Latham & Watkins LLP**
8.1	Opinion of Latham & Watkins LLP**
23.1	Consent of Ernst & Young, LLP, Independent Registered Public Accounting Firm*
23.2	Consent of Latham & Watkins LLP**
23.3	Consent of Latham & Watkins LLP**
24.1	Power of Attorney (included on signature page hereto)
99.1	Form of Notice of Guaranteed Delivery*
99.2	Form of letter from PriceSmart to brokers, dealers and nominees*
99.3	Form of letter from brokers, dealers and nominees to clients*
99.4	Form of Beneficial Owner Election Form*
99.5	Form of Nominee Holder Certification*
99.6	Form of Subscription Form **
99.7	Instructions for Certification of Taxpayer Identification Number on Form W-9*
99.8	Form of Subscription Agent and Information Agent Agreement by and between PriceSmart, Mellon Bank, N.A. and Mellon Investor Services LLC.**

\* Filed herewith.

\*\* To be filed by amendment.



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### **Item 17. Undertakings**

(a) The undersigned registrant hereby undertakes:

(1) To file, during any period in which offers or sales are being made, a post-effective amendment to this registration statement:

(i) To include any prospectus required by Section 10(a)(3) of the Securities Act of 1933;

(ii) To reflect in the prospectus any facts or events arising after the effective date of the registration statement (or the most recent post-effective amendment thereof) which, individually or in the aggregate, represent a fundamental change in the information set forth in the registration statement. Notwithstanding the foregoing, any increase or decrease in volume of securities offered (if the total dollar value of securities offered would not exceed that which was registered) and any deviation from the low or high end of the estimated maximum offering range may be reflected in the form of prospectus filed with the SEC pursuant to Rule 424(b) if, in the aggregate, the changes in volume and price represent no more than a 20 percent change in the maximum aggregate offering price set forth in the Calculation of Registration Fee table in the effective registration statement; and

(iii) To include any material information with respect to the plan of distribution not previously disclosed in the registration statement or any material change to such information in this registration statement;

*provided, however*, that subparagraphs (a)(1)(i) and (a)(1)(ii) above do not apply if the information required to be included in a post-effective amendment by those paragraphs is contained in periodic reports filed with or furnished to the SEC by the registrant pursuant to Section 13 or Section 15(d) of the Securities Exchange Act of 1934 that are incorporated by reference in this registration statement.

(2) That, for the purpose of determining any liability under the Securities Act of 1933, each such post-effective amendment shall be deemed to be a new registration statement relating to the securities offered herein, and the offering of such securities at that time shall be deemed to be the initial bona fide offering thereof.

(3) To remove from registration by means of a post-effective amendment any of the securities being registered which remain unsold at the termination of the offering.

(b) The undersigned registrant hereby further undertakes that, for the purposes of determining any liability under the Securities Act of 1933, each filing of the registrant's annual report pursuant to Section 13(a) or Section 15(d) of the Securities Exchange Act of 1934 (and, where applicable, each filing of an employee benefit plan's annual report pursuant to Section 15(d) of the Securities Exchange Act of 1934) that is incorporated by reference in this registration statement shall be deemed to be a new registration statement relating to the securities offered herein, and the offering of such securities at that time shall be deemed to be the initial bona fide offering thereof.

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(c) Insofar as indemnification for liabilities arising under the Securities Act of 1933 may be permitted to directors, officers and controlling persons of the registrant pursuant to existing provisions or otherwise, the registrant has been advised that in the opinion of the SEC such indemnification is against public policy as expressed in the Securities Act of 1933 and is, therefore, unenforceable. In the event that a claim for indemnification against such liabilities (other than the payment by the registrant of expenses incurred or paid by a director, officer or controlling person of the registrant in the successful defense of any action, suit or proceeding) is asserted by such director, officer or controlling person in connection with the securities being registered, the registrant will, unless in the opinion of its counsel the matter has been settled by controlling precedent, submit to a court of appropriate jurisdiction the question whether such indemnification by it is against public policy as expressed in the Securities Act of 1933 and will be governed by the final adjudication of such issue.

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Pursuant to the requirements of the Securities Act of 1933, as amended, PriceSmart, Inc. certifies that it has reasonable grounds to believe that it meets all of the requirements for filing on Form S-3 and has duly caused this registration statement to be signed on its behalf by the undersigned, thereunto duly authorized, in the City of San Diego, State of California, on December 2, 2004.

**PriceSmart, Inc.**

By: /s/ ROBERT E. PRICE  
**Robert E. Price**  
**Interim Chief Executive Officer**

**POWER OF ATTORNEY**

Pursuant to the requirements of the Securities Act of 1933, this Registration Statement has been signed below by the following persons in the capacities and on the dates indicated.

KNOW ALL PERSONS BY THESE PRESENTS, that each person whose signature appears below constitutes and appoints Robert E. Price and John M. Heffner, and each of them, as his true and lawful attorneys-in-fact and agents, with full power of substitution and resubstitution, for him and in his name, place, and stead, in any and all capacities, to sign any and all amendments (including post-effective amendments, exhibits thereto and other documents in connection therewith) to this Registration Statement and any subsequent registration statement filed by the Registrant pursuant to Rule 462(b) of the Securities Act of 1933, as amended, which relates to this Registration Statement, and to file the same, with all exhibits thereto, and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite and necessary to be done in connection therewith, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorney-in-fact and agents, or any of them, or their or his substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

<b><u>Signature</u></b>	<b><u>Title</u></b>	<b><u>Date</u></b>
<u>/s/ ROBERT E. PRICE</u> <b>Robert E. Price</b>	Interim Chief Executive Officer and Chairman of the Board of Directors (Principal Executive Officer)	December 2, 2004
<u>/s/ JOHN M. HEFFNER</u> <b>John M. Heffner</b>	Chief Financial Officer (Principal Financial and Accounting Officer)	December 2, 2004
<u>/s/ JAMES F. CAHILL</u> <b>James F. Cahill</b>	Director	December 2, 2004
<u>/s/ MURRAY L. GALINSON</u>	Director	December 2, 2004

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**Murray L. Galinson**

/s/ KATHERINE L. HENSLEY

Director

December 2, 2004

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**Katherine L. Hensley**

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<b><u>Signature</u></b>	<b><u>Title</u></b>	<b><u>Date</u></b>
<u>/s/ LEON C. JANKS</u>	Director	November 30, 2004
<b>Leon C. Janks</b>		
<u>/s/ LAWRENCE B. KRAUSE</u>	Director	December 2, 2004
<b>Lawrence B. Krause</b>		
<u>/s/ ANGEL LOSADA M.</u>	Director	December 2, 2004
<b>Angel Losada M.</b>		
<u>/s/ JACK McGRORY</u>	Director	December 2, 2004
<b>Jack McGrory</b>		
<u>Edgar A. Zurcher</u>	Director	December , 2004

**Table of Contents****EXHIBIT INDEX**

The following exhibits are filed as part of this Registration Statement on Form S-3 or are incorporated herein by reference.

<b><u>Exhibit No.</u></b>	<b><u>Description</u></b>
4.1	Specimen of Common Stock certificate*
4.2	Specimen transferable subscription rights certificate for holders of Common Stock*
4.3	Instructions for Use of PriceSmart, Inc. Common Stock Right Certificates*
5.1	Opinion of Latham & Watkins LLP**
8.1	Opinion of Latham & Watkins LLP**
23.1	Consent of Ernst & Young, LLP, Independent Registered Public Accounting Firm *
23.2	Consent of Latham & Watkins LLP**
23.3	Consent of Latham & Watkins LLP**
24.1	Power of Attorney (included on signature page hereto)
99.1	Form of Notice of Guaranteed Delivery*
99.2	Form of letter from PriceSmart to brokers, dealers and nominees*
99.3	Form of letter from brokers, dealers and nominees to clients*
99.4	Form of Beneficial Owner Election Form*
99.5	Form of Nominee Holder Certification*
99.6	Form of Subscription Form**
99.7	Instructions for Certification of Taxpayer Identification Number on Form W-9*
99.8	Form of Subscription Agent and Information Agent Agreement by and between PriceSmart, Mellon Bank, N.A. and Mellon Investor Services LLC.**

\* Filed herewith.

\*\* To be filed by amendment.