

INSMED INC  
Form PRE 14A  
April 18, 2013

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

**SCHEDULE 14A**

Proxy Statement Pursuant to Section 14(a) of  
the Securities Exchange Act of 1934 (Amendment No.        )

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

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

**INSMED INCORPORATED**

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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):

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

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**NOTICE**  
**and**  
**PROXY STATEMENT**  
**for**  
**ANNUAL MEETING OF SHAREHOLDERS**  
**MAY 23, 2013**

**9 Deer Park Drive, Suite C**  
**Monmouth Junction, New Jersey 08852-1923**

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## Insmmed Incorporated

9 Deer Park Drive, Suite C  
Monmouth Junction, NJ 08852-1923  
(732) 997-4600

### ANNUAL MEETING OF SHAREHOLDERS

April 29, 2013

To the Shareholders:

We cordially invite you to attend the 2013 Annual Meeting of Shareholders to be held at the Hilton East Brunswick Hotel and Executive Meeting Center, 3 Tower Center Boulevard, East Brunswick, New Jersey 08816, on May 23, 2013, at 9:00 a.m. local time. A formal notice of the meeting, together with a proxy statement and proxy form, is enclosed with this letter. The notice points out that you will be asked to:

- (i) elect three Class I directors to serve until the 2016 Annual Meeting of Shareholders;
- (ii) ratify the appointment of Ernst & Young LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2013;
- (iii) ratify and approve certain equity compensation awards previously granted to certain current and former employees and directors under our 2000 Stock Incentive Plan;
- (iv) approve the Insmmed Incorporated 2013 Incentive Plan; and
- (v) transact such other business as may properly come before the meeting.

Please read the notice and proxy statement carefully, and vote by telephone, electronically through the Internet, by completing, signing and mailing the enclosed proxy card promptly, or in person at the Annual Meeting.

Whether or not you plan to attend the Annual Meeting in person and regardless of the number of shares of Insmmed common stock you own, please vote promptly.

Sincerely yours,  
/s/ DONALD HAYDEN, JR.

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DONALD HAYDEN, JR.  
*Chairman of the Board*

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## **INSMED INCORPORATED**

**9 Deer Park Drive, Suite C  
Monmouth Junction, NJ 08852-1923  
(732) 997-4600**

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### **NOTICE OF ANNUAL MEETING OF SHAREHOLDERS TO BE HELD ON MAY 23, 2013**

NOTICE IS HEREBY GIVEN that the 2013 Annual Meeting of Shareholders of Insmmed Incorporated will be held at the Hilton East Brunswick Hotel and Executive Meeting Center, 3 Tower Center Boulevard, East Brunswick, New Jersey 08816, on May 23, 2013, at 9:00 a.m. local time and at any adjournment or postponement thereof, for the following purposes:

1. To elect three Class I directors to serve until the 2016 Annual Meeting of Shareholders;
2. To ratify the appointment of Ernst & Young LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2013;
3. To ratify and approve certain equity compensation awards previously granted to certain current and former employees and directors under our 2000 Stock Incentive Plan;
4. To approve the Insmmed Incorporated 2013 Incentive Plan; and
5. To transact such other business as may properly come before the meeting.

Holders of record of shares of Insmmed common stock at the close of business on March 28, 2013, will be entitled to vote at the Annual Meeting.

You are requested to vote promptly by telephone, electronically through the Internet, or by completing, signing and mailing the enclosed proxy card, regardless of whether you expect to attend the Annual Meeting. If you are present at the Annual Meeting, you may vote in person even if you already have sent in your proxy.

By Order of the Board of Directors  
*/s/ ANDREA HOLTZMAN DRUCKER*

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Andrea Holtzman Drucker  
*Corporate Secretary*

April 29, 2013

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**PROXY STATEMENT**  
**for**  
**ANNUAL MEETING OF SHAREHOLDERS**  
**of**  
**INSMED INCORPORATED**  
**To be held May 23, 2013**

**THE PROXY STATEMENT AND FORM OF PROXY FOR OUR 2013 ANNUAL MEETING AND OUR ANNUAL REPORT ON FORM 10-K FOR THE YEAR ENDED DECEMBER 31, 2012, ARE AVAILABLE AT: [www.insmed.com](http://www.insmed.com) under the heading "Investor Relations SEC Filings."**

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In this Proxy Statement, we use the words "Insmmed Incorporated" to refer to Insmmed Incorporated, a Virginia corporation, and we use the words the "Company," "Insmmed," "we," "us" and "our" to refer to Insmmed Incorporated and its consolidated subsidiaries. ARIKACE® is a registered trademark and Insmmed™ is a trademark of Insmmed Incorporated. This Proxy Statement also contains trademarks of third parties. Each trademark of another company appearing in this Proxy Statement is the property of its owner.

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**PROXY STATEMENT**  
**for**  
**ANNUAL MEETING OF SHAREHOLDERS**  
**of**  
**INSMED INCORPORATED**  
**To be held May 23, 2013**

**GENERAL INFORMATION ABOUT THE ANNUAL MEETING AND VOTING**

**Solicitation of Proxies**

The Board of Directors (the "Board") of Insmmed Incorporated ("Insmmed," which may be referred to as the "Company", "we", "us" or "our") is soliciting your proxy for the Annual Meeting of Shareholders to be held at the Hilton East Brunswick Hotel and Executive Meeting Center, 3 Tower Center Boulevard, East Brunswick, New Jersey 08816, on May 23, 2013, at 9:00 a.m., local time and any adjournment or postponement thereof (the "Annual Meeting"). This Proxy Statement is first being distributed to our shareholders on or about April 29, 2013.

**Information about the Annual Meeting**

**Who May Vote.** Shareholders of record at the close of business on March 28, 2013 (the "Record Date"), will be entitled to notice of and to vote at the Annual Meeting. As of the Record Date, we had 31,571,806 outstanding shares of our common stock, \$0.01 par value per share (the "Common Stock"). Each share of our Common Stock entitles the holder to one vote with respect to all matters submitted to shareholders at the Annual Meeting. Beneficial owners of shares of our Common Stock may direct the record holder of the shares on how to vote the shares held on their behalf.

Of the Common Stock outstanding as of the Record Date, 1,765,271 shares represent shares retained by us as security for potential indemnification payments (the "Holdback Shares"), as described in the Agreement and Plan of Merger with Transave, Inc. (the "Merger Agreement"), filed as Exhibit 2.1 to our Annual Report on Form 10-K for the year ended December 31, 2012. Such Holdback Shares will not be represented at the Annual Meeting for quorum purposes and will not be voted on any of the matters presented at the Annual Meeting.

**Shareholders of Record.** If on the Record Date, shares of our Common Stock were registered directly in your name with our transfer agent, then you are a shareholder of record. As a shareholder of record, you may vote in person or by proxy at the Annual Meeting. Whether or not you plan to attend the Annual Meeting, we hope you will take the time to vote your shares.

**How can you vote?** If you are a record holder, meaning your shares are registered in your name, you may vote or submit a proxy:

1. **By Telephone** Dial 1-800-PROXIES (1-800-776-9437) using any touch-tone phone to transmit your voting instructions up until 5:00 p.m. Eastern Time the day before the meeting date. Have your proxy card in hand when you call and follow the voting instructions given to you over the phone.
2. **By Mail** Complete and sign the enclosed proxy card and mail it in the enclosed postage prepaid envelope. Your shares will be voted according to your instructions. If you sign your proxy card but do not specify how you want your shares voted, they will be voted as recommended by our board of directors. Unsigned proxy cards will not be voted.
3. **By Internet** If you have Internet access, you may authorize the voting of your shares by following the "Submit a proxy by Internet" instructions set forth on the enclosed proxy card. You must specify how you want your shares voted or your vote will not be completed and you will receive an error message. Your shares will be voted according to your instructions.

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4.

*In Person at the Meeting* If you attend the Annual Meeting, you may deliver a completed and signed proxy card in person or you may vote by completing a ballot, which we will provide to you at the Annual Meeting.

**Beneficial Owners of Shares.** If on the Record Date, your shares of our Common Stock were not held in your name, but rather were held in an account at a brokerage firm, bank, dealer, or other similar organization, then you are the beneficial owner of shares held in "street name," and these proxy materials have been forwarded to you by that organization. The organization holding your account is considered to be the shareholder of record for purposes of voting at the Annual Meeting and is required to vote those shares in accordance with your instructions. If you do not give instructions to the organization holding your account, then the organization will have discretion to vote the shares with respect to "routine" matters but will not be permitted to vote the shares with respect to "non-routine" matters. Accordingly, if you do not instruct your broker or other agent on how to vote your shares with respect to the "non-routine" matters, your shares will be "broker nonvotes" with respect to that proposal, which means your shares will not be voted. Proposal 1, the election of directors, is a non-routine matter. Proposal 2, the ratification of independent registered public accounting firm, is a routine matter. Proposal 3, the ratification and approval of certain equity compensation awards, is a non-routine matter. Proposal 4, the approval of the 2013 Incentive Plan, is a non-routine matter. As a beneficial owner, you have the right to direct your broker or other agent on how to vote the shares in your account. You are also invited to attend the Annual Meeting. If you are a beneficial owner and not the shareholder of record, you may not vote your shares in person at the Annual Meeting unless you request and obtain a valid proxy from your broker or other agent.

**Quorum and Vote Required to Approve Each Item on the Proxy.** Shares of our Common Stock representing a majority of the votes entitled to be cast on a matter at the Annual Meeting will constitute a quorum for the transaction of business with respect to such matter, unless otherwise provided by law or in our Articles of Incorporation, as amended ("Articles of Incorporation").

Proposal 1, the election of directors, requires the affirmative vote of the holders of a plurality of the votes cast in the election of directors. This means that the nominee(s) who receive the highest number of affirmative votes cast are elected irrespective of how small the number of affirmative votes is in comparison to the total number of shares voted. Signing and returning your proxy will constitute a vote "for" the nominees unless your proxy specifies that you are withholding authority to vote for the nominees or for a specific nominee. Any votes that are withheld and any broker non-votes will not be included in determining the number of votes cast. In the event that any of the nominees are unavailable for election, the Board may either reduce the number of directors or choose a substitute nominee. If the Board selects a substitute nominee, the shares represented by proxy will be voted "for" the substitute nominee unless other instructions are given in the proxy. The Board has no reason to believe that any nominee will be unavailable.

Proposal 2, ratification of a registered public accounting firm, does not require shareholder ratification under Virginia law, our Articles of Incorporation or our Amended and Restated Bylaws ("Bylaws"). However, the Board is submitting the appointment of Ernst & Young LLP to the shareholders for ratification as a matter of good corporate practice. Approval of Proposal 2 requires the affirmative vote of a majority of the votes cast, in person or by proxy, at the Annual Meeting. In the event that Proposal 2 is not approved, the Audit Committee of the Board will consider the vote and the reasons therefore in future independent auditor selection decisions.

Proposal 3, the ratification and approval of certain equity compensation awards, requires the affirmative vote of a majority of the votes cast, in person or by proxy, at the Annual Meeting. Signing and returning your proxy will constitute a vote "for" the ratification and approval of the equity compensation awards unless your proxy specifies that you are abstaining from voting on Proposal 3. Any abstentions and any broker non-votes will not be included in determining the number of votes cast.



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Proposal 4, approval of the 2013 Incentive Plan, requires the affirmative vote of a majority of the votes cast, in person or by proxy, at the Annual Meeting. Signing and returning your proxy will constitute a vote "for" the approval of the 2013 Incentive Plan unless your proxy specifies that you are abstaining from voting on Proposal 4. Any abstentions and any broker non-votes will not be included in determining the number of votes cast.

**Revoking a Proxy.** Anyone giving a proxy may revoke it at any time before it is voted by voting in person at the Annual Meeting or by delivering a later dated proxy or written notice of revocation to our Corporate Secretary. Attendance at the Annual Meeting will not itself revoke a proxy. A proxy, if executed and not revoked, will be voted at the Annual Meeting.

**Cost of Soliciting Proxies.** We will pay the cost of soliciting proxies. In addition to the use of mail, proxies may be solicited in person or by telephone by our employees. We have engaged Georgeson Inc. to assist us in the solicitation of proxies from brokers, nominees, fiduciaries and other custodians. We will pay Georgeson approximately \$15,000 for their services and reimburse them for their out-of-pocket expenses for such items as mailing, copying, phone calls, faxes and other related items. We will indemnify Georgeson from any losses arising from that firm's proxy soliciting services on our behalf.

### **Principal Executive Offices of Insmmed**

The address of our principal executive offices is 9 Deer Park Drive, Suite C, Monmouth Junction, New Jersey, 08852-1923.

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**PROPOSAL NO. 1**

**ELECTION OF DIRECTORS**

The Board has nominated three current Class I directors, Al Altomari, Steinar Engelsen, M.D., and Will Lewis (the "nominees" and each a "nominee") for re-election at the Annual Meeting for the three-year term expiring at the 2016 Annual Meeting of Shareholders. Each of the nominees was recommended for election by the Nominations and Governance Committee and the other members of the Board. Below is some information on the nominees. Mr. Altomari, who joined the Board in August 2012, was recommended by a current non-management director.

*Al Altomari* age 54. Mr. Altomari was elected to our Board in August 2012. Since October 2010, Mr. Altomari has served as President and Chief Executive Officer of Agile Therapeutics. Mr. Altomari is also a member of Agile's board of directors and prior to being named President and CEO, he served as Agile's Executive Chairman. From 2008 to September 2010, Mr. Altomari was also a consultant. From 2003 to 2008, Mr. Altomari held multiple senior management positions at Barrier Therapeutics, Inc., including Chief Commercial Officer, Chief Operating Officer, and Chief Executive Officer. In 2008, in his role as Chief Executive Officer and as a member of Barrier's board of directors, Mr. Altomari completed the successful sale of Barrier to Stiefel Laboratories, which was subsequently acquired by GlaxoSmithKline plc. From 1982 to 2003, Mr. Altomari held numerous executive roles in general management, commercial operations, business development, product launch preparation, and finance with Johnson & Johnson. Mr. Altomari also serves on the Board of NB Therapeutics, Inc. Mr. Altomari received an M.B.A. from Rider University and his B.S. from Drexel University.

**Key Attributes, Experience and Skills:** Mr. Altomari is a pharmaceutical industry veteran with more than 30 years of experience. The Board believes that Mr. Altomari's experience in pharmaceutical companies with commercialized products, the launch of certain products and more than 20 years of focus on the development and marketing of specialty pharmaceutical products makes him uniquely suited to guide the Board in strategic planning, operational and commercial matters.

*Steinar J. Engelsen, M.D.* age 62. Dr. Engelsen has been a member of our Board since our inception in November 1999 and was a director of Insmmed Pharmaceuticals, our predecessor entity, from 1998 to 2000. Since November 1996, Dr. Engelsen has been a partner of Teknoinvest AS, a venture capital firm based in Norway. In addition, from January to November 2000, Dr. Engelsen was acting CEO of Centaur Pharmaceuticals, Inc., a biopharmaceutical company. From 1989 until October 1996, Dr. Engelsen held various management positions within Hafslund Nycomed AS, a pharmaceutical company based in Europe, and its affiliated companies. He was responsible for therapeutic research and development, serving as Senior Vice President, Research and Development of Nycomed Pharma AS from January 1994 until October 1996. Dr. Engelsen received his M.Sc. in nuclear chemistry and his M.D. from the University of Oslo and is a Certified European Financial Analyst (C.E.F.A.).

**Key Attributes, Experience and Skills:** Dr. Engelsen has more than 20 years of experience in the pharmaceutical industry, including his experience as a financial analyst and as an investor in biopharmaceutical companies. The Board believes that Dr. Engelsen's finance and management experience in biopharmaceutical companies enables him to provide operating insights to the Board. In addition, his experience and background in research and development is an asset to the Board.

*Will Lewis* age 44. Mr. Lewis joined us in September 2012 as our President and Chief Executive Officer and as a member of our Board. Mr. Lewis has more than 20 years of experience in the pharmaceutical and finance industries both in the US and internationally. From 2011 to 2012, Mr. Lewis was a consultant and acted as a consultant to our Board from June 2012 until September 2012. From 2009 to 2011, Mr. Lewis was President of Aegerion Pharmaceuticals, Inc. (Nasdaq: AEGR) ("Aegerion"). In 2005, Mr. Lewis co-founded Aegerion and from 2005 to 2009, Mr. Lewis was the Chief Financial Officer of Aegerion. Prior to co-founding Aegerion, Mr. Lewis spent more than

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10 years working in the US and Europe in investment banking for JP Morgan, Robertson Stephens, and Wells Fargo. During his time in investment banking, he was involved in a broad range of domestic and international capital raising and advisory work. Mr. Lewis began his career as an Operations Officer with the Central Intelligence Agency. He earned a J.D. with Honors and an M.B.A. from Case Western Reserve University and a B.A. with Honors from Oberlin College.

**Key Attributes, Experience and Skills:** Mr. Lewis has more than 7 years of experience in the pharmaceutical industry and over 10 years of investment banking experience. The Board believes that Mr. Lewis brings significant qualifications including his experience as a seasoned entrepreneur and senior executive with a fast-growing biotechnology company. In addition, Mr. Lewis offers the Board significant insights and experience with financing, orphan drug technology, and international business development.

**THE BOARD RECOMMENDS THAT YOU VOTE "FOR" EACH OF THE DIRECTOR NOMINEES.**

**The Board of Directors**

Our Articles of Incorporation provide that our Board shall consist of not more than 12 directors, with the exact number to be prescribed by our Bylaws. Our Bylaws provide that the number of directors constituting our Board shall be designated by a resolution of the Board but shall be not less than six or more than ten. Our Board has adopted a resolution designating seven directors. The directors are divided into three classes Class I, Class II and Class III. Each class of directors serves for three years on a staggered term basis.

The Board has nominated three Class I directors, each of whom is currently a director with a term of office that expires at our 2013 Annual Meeting of Shareholders: Steinar J. Engelsen, M.D., Al Altomari, and Will Lewis. If re-elected, their term of office will expire at our 2016 Annual Meeting of Shareholders. The term of the Class II directors, Mr. Donald Hayden, Jr. and Mr. Richard S. Kollender, will expire at the 2014 Annual Meeting of Shareholders. The term of the Class III directors, Melvin Sharoky, M.D. and Randall W. Whitcomb, M.D. will expire at the 2015 Annual Meeting of Shareholders.

The following table sets forth the names of the directors nominated to be re-elected at the Annual Meeting and the names of the continuing directors not subject to re-election, the year each such person was first elected as a director, the positions currently held by each such person, the year such person's

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current term as a director will expire and the director class to which such person belongs or will belong:

Nominee's or Director's Name	Age	Position(s) with the Company	Year First Became Director and Year Current Term Will Expire	Class of Director
<b>Nominees for Class I Directors</b>				
Al Altomari(1)	54	Director	2012 - 2013	I
Steinar J. Engelsen, M.D.(1)(2)	62	Director	1999 - 2013	I
Will Lewis	44	President and Chief Executive Officer, and Director	2012 - 2013	I
<b>Continuing Directors:</b>				
Donald Hayden, Jr.	57	Chairman of the Board	2010 - 2014	II
Richard S. Kollender(1)(3)	43	Director	2011 - 2014	II
Melvin Sharoky, M.D.(2)(3)	62	Director	2001 - 2015	III
Randall W. Whitcomb, M.D.(2)(3)	58	Director	2001 - 2015	III

(1) Member of Audit Committee.

(2) Member of Nominations and Governance Committee.

(3) Member of Compensation Committee.

#### ***Incumbent Directors Whose Term Expires at the 2014 Annual Meeting of Shareholders (Class II Directors).***

**Donald Hayden, Jr.** Mr. Hayden has been a member of our Board since December 2010. Mr. Hayden has been the non-Executive Chairman of our Board since December 2010, except for the period from May 2012 to September 2012, when he acted as our Executive Chairman during a transition of senior level management. He previously served as the Executive Chairman of Transave from April 2006 until December 2010. Mr. Hayden is a senior advisor to Prospect Venture Partners, a venture capital firm. From 1981 to 2006, Mr. Hayden was an executive with Bristol-Myers Squibb Company and served in key executive roles including President of Global Pharmaceuticals; Executive Vice President and President, Americas; Executive Vice President of the Health Care Group; President of Oncology and Immunology; and Senior Vice President of Worldwide Franchise Management and Business Development. Mr. Hayden currently serves as lead independent director of Amicus Therapeutics (Nasdaq: FOLD). Mr. Hayden is also a director of Otsuka America Pharmaceuticals, Inc., a subsidiary of the Otsuka Group in Japan. Mr. Hayden also serves on the boards of directors for four privately-held companies: Alvine Pharmaceuticals; Nora Therapeutics; Satori Pharmaceuticals; and Vitae Pharmaceuticals. Mr. Hayden holds a B.A. from Harvard University and an M.B.A. from Indiana University.

**Key Attributes, Experience and Skills:** Mr. Hayden has more than 30 years of pharmaceutical industry experience, including roles in executive management, commercialization, business development, and financial and strategic planning. This extensive experience makes him a valuable asset to our Board. Furthermore, Mr. Hayden's leadership abilities and experiences make him particularly well qualified to be our Chairman.

**Richard S. Kollender.** Mr. Kollender has been a member of our Board since January 2011. Since 2005, Mr. Kollender has been a partner at Quaker Partners Management, L.P. (formerly Quaker BioVentures Management, L.P.), a venture capital and growth equity firm with a focus on the healthcare industry. From 2003 to 2005, Mr. Kollender was a principal with Quaker Partners

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Management, L.P. Mr. Kollender's prior experiences include a variety of sales, marketing and worldwide business development positions at GlaxoSmithKline, an Investment Manager at SR One and a Certified Public Accountant with KPMG LLP, with a significant emphasis on the healthcare and emerging businesses sectors. Mr. Kollender holds a B.A. in Accounting and Business Administration from Franklin and Marshall College, an M.B.A. from the University of Chicago and a certificate from the graduate program in Health Administration and Policy from the University of Chicago. Mr. Kollender currently serves on the board of directors and as chairman of the compensation committee of NuPathe Inc. (Nasdaq: PATH), having previously served from December 2007 to June 2011 on NuPathe's board of directors. Mr. Kollender currently serves as the chairman of the audit committee of Celator Pharmaceuticals, Inc. (a public company). Mr. Kollender also serves on the boards of directors of three privately-held companies, Precision Therapeutics, Inc., Rapid Micro Biosystems, Inc. and Corridor Pharmaceuticals, Inc. Beginning in 2005, he served as a member of the board of directors of TargetRx, Inc., and became its Chairman in 2008, until its acquisition in 2011. Mr. Kollender also served on the board of directors for Transport Pharmaceuticals, Inc., from 2004 to 2009 and the board of directors of Transave, Inc. (from 2007 to 2010) prior to its business combination with Insmmed in 2010.

**Key Attributes, Experience and Skills:** Mr. Kollender has more than 15 years of experience in the pharmaceutical and biotechnology industries. The Board believes that his diverse pharmaceutical and biotechnology background, including extensive accounting, financial, commercial, business development, and senior leadership experience, is an asset to our Board.

***Incumbent Directors Whose Term Expires at the 2015 Annual Meeting of Shareholders (Class III Directors).***

**Melvin Sharoky, M.D.** Dr. Sharoky has been a member of our Board since May 2001 and served as Chairman of our Board from June 2009 to December 2010. Since January 2008, Dr. Sharoky has been retired, but he continues to serve as a member of our Board and was a member of the board of directors of Par Pharmaceuticals from 2007 until October 2012 (NYSE:PRX). From January 2002 to March 2007, Dr. Sharoky was President and Chief Executive Officer of Somerset Pharmaceuticals, Inc. Dr. Sharoky continued as a consultant to Somerset until December 2007. From June 2001 to January 2002, Dr. Sharoky was retired. From July 1995 to June 2001, Dr. Sharoky served as President of Somerset Pharmaceuticals. From July 1995 through January 1998, Dr. Sharoky was President of Watson Pharmaceuticals, Inc., and from February 1993 to January 1998 he was President and CEO of Watson's wholly-owned subsidiary, Circa Pharmaceuticals, Inc. From 1988 to 1993 Dr. Sharoky held various senior executive positions with Circa Pharmaceuticals. From February 1986 to June 1988, Dr. Sharoky was Vice President and Chief Medical Officer of Pharmakinetix Laboratories, Inc. Dr. Sharoky received a B.A. in biology from the University of Maryland in Baltimore County and an M.D. from the University of Maryland School of Medicine.

**Key Attributes, Experience and Skills:** Dr. Sharoky has more than 25 years of experience in the pharmaceutical industry. The Board believes that, in addition to his medical experience as a physician, Dr. Sharoky's background as an executive of research and development pharmaceutical companies brings senior management, leadership, financial and strategic planning experience to our Board.

**Randall W. Whitcomb, M.D.** Dr. Whitcomb has been a member of our Board since November 2001, and he was designated our lead independent director in May 2012. Since 2008, Dr. Whitcomb has been a consultant to various companies and serves as a senior advisor to Frazier Healthcare, a venture capital firm. From 2001 to 2006, Dr. Whitcomb was Chief Medical Officer of Quatrux Pharmaceuticals, Inc., a privately-held, drug development company he founded. From 1992 through 2000, Dr. Whitcomb held various management positions with Parke-Davis Pharmaceutical Research, Inc., a division of Warner Lambert Company, serving as Vice President of Drug Development with particular responsibility for the development and approval of products for women's

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health care, metabolic diseases and diabetes. After Pfizer acquired Warner Lambert, Dr. Whitcomb was Vice President Global Project Management for Pfizer Global Research and Development. From 1987 through 1992, Dr. Whitcomb was on the faculty of Massachusetts General Hospital and Harvard Medical School. Dr. Whitcomb serves on the board of directors of Atterocor, a private drug development company. Dr. Whitcomb received his B.A from Tabor College and his M.D. from the University of Kansas.

**Key Attributes, Experience and Skills:** Dr. Whitcomb has more than 25 years of experience in the life sciences industry. The Board believes that, in addition to his medical experience as a physician, Dr. Whitcomb's experience in venture capital investing and extensive management experience bring leadership, financial and strategic planning strength to our Board.

### **Executive Officers**

The following table sets forth our current executive officers, their ages, the positions currently held by each such person as of the date of this Proxy Statement and the period holding such positions.

Name	Age	Position(s)	Period During Which Officer Served in Such Position(s)
Will Lewis	44	President and Chief Executive Officer	September 2012 Present
Andrew T. Drechsler	41	Chief Financial Officer	November 2012 Present
Dr. Renu Gupta	57	Executive Vice President of Development and Chief Medical Officer	December 2010 Present
Matthew Pauls	42	Chief Commercial Officer	April 2013 Present
Andrea Holtzman Drucker, J.D.	55	Senior Vice President, General Counsel and Corporate Secretary	July 2011 Present

*Will Lewis.* Mr. Lewis's biographical information is summarized above under "Information Relating to the Election of Directors."

*Andrew T. Drechsler.* Mr. Drechsler joined us as our Chief Financial Officer in November 2012. Mr. Drechsler has 15 years of financial and operational leadership experience in both public and private life sciences companies. From 2007 to 2012, Mr. Drechsler was Chief Financial Officer of VaxInnate Corporation. From 2005 to 2007, Mr. Drechsler was Chief Financial Officer of Valera Pharmaceuticals, a publicly traded specialty pharmaceutical company that was acquired by Indevus Pharmaceuticals, now part of Endo Pharmaceuticals. From 1997 to 2005, Mr. Drechsler held senior financial positions with i-STAT, now part of Abbott Laboratories, and Biomatrix, now part of Sanofi. From 1994 to 1997, Mr. Drechsler was a certified public accountant with Coopers & Lybrand. Mr. Drechsler serves on the board of Tivorsan Pharmaceuticals, a private biotech company. Mr. Drechsler graduated with a B.S. in accounting from Villanova University.

*Renu Gupta, M.D.* Dr. Gupta joined us as our Executive Vice President of Development and Chief Medical Officer in December 2010. From 2006 to 2010, Dr. Gupta served as the Executive Vice President of Development and Chief Medical Officer of Transave, Inc. From 2003 to 2006, Dr. Gupta was Senior Vice President of Development at Antigenics, Inc. Dr. Gupta's prior experience also includes executive clinical and development roles at Novartis and Bristol-Myers Squibb. Dr. Gupta received her bachelor and medical degrees from the University of Zambia and completed her medical and post-doctoral training at Albert Einstein Medical Center, the Wistar Institute of Anatomy and Biology, Children's Hospital of Philadelphia, and the University of Pennsylvania, where she was Adjunct Assistant Professor until 1997. Dr. Gupta has more than 25 years of development, regulatory and senior management experience with the biopharma industry. Her work has been published in leading

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peer-reviewed journals and she has been active in numerous relevant academic and professional societies. Dr. Gupta is a founding member of the Industrial Management Board at the Harvard Medical School, served as Chair of the Medical Advisory Council for Antigenics, is a board member of Aim at Melanoma (formerly Charlie Guild Melanoma Foundation) and was previously a member of the Scientific Advisory Board at Cerimon Pharmaceuticals and the Institute of Medicine Forum on Emerging Infections.

*Matthew Pauls.* Mr. Pauls joined us as our Chief Commercial Officer on April 1, 2013. From 2007 to 2013, Mr. Pauls served in various senior commercial positions at Shire Pharmaceuticals (LSE: SHP), most recently as Senior Vice President, Head of Global Commercial Operations, Shire Regenerative Medicine. From 2005 to 2007, Mr. Pauls served in the senior management of Bristol-Myers Squibb Company. From 1997 to 2005, Mr. Pauls held various positions at Johnson & Johnson, Inc. Mr. Pauls received his J.D. from Michigan State University College of Law and his M.B.A. and B.S. degrees from Central Michigan University.

*Andrea Holtzman Drucker, J.D.* Ms. Drucker joined Insmmed as our Senior Vice President, General Counsel and Corporate Secretary in July 2011. From 2006 to 2011, Ms. Drucker served as Senior Vice President, General Counsel and Secretary for PuriCore plc (LSE: PURI), a publicly traded biotechnology company. Ms. Drucker's prior experiences include two years with Practical Business Solutions, a private legal consulting firm, during which she served as Acting General Counsel for Novavax, Inc. (Nasdaq:NVAX), and as Interim Associate General Counsel for Auxilium Pharmaceuticals, Inc. (Nasdaq: AUXL), both publicly-traded biotechnology companies. Ms. Drucker also spent 17 years in a number of legal positions with FMC Corporation, a publicly traded diversified chemicals company. Ms. Drucker began her career as an associate with Ballard Spahr L.L.P. (formerly Ballard Spahr Andrews & Ingersoll). Ms. Drucker received her J.D. from the University of Pennsylvania Law School and a Bachelors of Science with Distinction in Environmental Studies from Cornell University.

## CORPORATE GOVERNANCE

### Corporate Governance Matters

*Code of Business Conduct and Ethics.* We adopted a Code of Conduct that applies to all of our directors, officers and employees. Our Code of Conduct contains written standards designed to communicate our expectations of our directors, officers and employees when making decisions and conducting themselves in corporate activities, including the ethical handling and use of confidential information; actual or apparent conflicts of interest; compliance with applicable governmental laws, rules and regulations; protection of our assets and proprietary information; the ethical handling of payments and gifts received in the normal course of business and of payments made to government personnel; prompt internal reporting of violations of our Code of Business Conduct and Ethics; and accountability for adherence to our Code of Business Conduct and Ethics. Our Code of Business Conduct and Ethics is posted on our website at [www.insmed.com](http://www.insmed.com) under the heading "Investor Relations Corporate Governance." We intend to satisfy the disclosure requirements regarding any amendment to, or waiver from, a provision of the Code of Conduct by making disclosures concerning such matters available on our website under the heading "Investor Relations Corporate Governance."

*Corporate Governance Guidelines.* We adopted Corporate Governance Guidelines to assist and guide the Board in the exercise of its responsibilities. The Corporate Governance Guidelines contain written standards pertaining to director qualifications, director responsibilities, structure of our Board, director access to management and independent advisors, director compensation, and performance evaluation of our Board and committees, among other things. Our Corporate Governance Guidelines are interpreted in accordance with all applicable laws and regulations, the Nasdaq Listing Rules, and our Articles of Incorporation and our Bylaws. Our Corporate Governance Guidelines and Bylaws are

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posted on our website at [www.insmed.com](http://www.insmed.com) under the heading "Investor Relations Corporate Governance."

**Meetings of the Board.** The Board held sixteen meetings during fiscal 2012, including five regularly scheduled meetings. Each director attended at least 75% of the Board meetings that occurred in 2012 while he was a director. No director missed more than one Board meeting in 2012 during his tenure as a director. Each director attended at least 75% of the committee meetings that occurred in 2012 during his tenure on such committees.

**Independence of the Directors and Director Nominees.** The Board has determined that the following members of the Board are independent, as that term is defined under the general independence standards in listing standards of the Nasdaq Marketplace Rules: Dr. Steinar J. Engelsen, Dr. Melvin Sharoky, Mr. Richard S. Kollender, Mr. Al Altomari, and Dr. Randall W. Whitcomb. Mr. Lewis is not considered independent because he currently is employed by the Company, and Mr. Hayden is not serving on any of our committees because he acted as our executive Chairman during 2012, but we plan to re-evaluate his independence given that such service was only on an interim basis. In assessing Mr. Kollender's independence, the Board considered Mr. Kollender's position at Quaker Partners Management, L.P. and the equity position in the Company of Quaker BioVentures II, L.P., Quaker BioVentures Capital II, L.P. and Quaker BioVentures Capital II, LLC (herein collectively referred to as "Quaker BioVentures").

**Director Nominating Process**

**The Nominations and Governance Committee.** Our Nominations and Governance Committee, which is described more fully below under "Corporate Governance Nominations and Governance Committee," performs the functions of a nominating committee and serves as an independent and objective party to identify and nominate qualified candidates for directorship, consistent with criteria approved by the Board, and establishes such criteria based on factors it considers appropriate. Among the factors that the Board considers are strength of character, maturity of judgment, career specialization, relevant technical skills, diversity, independence and the extent to which the candidate would fill a present need of the Board. The Committee takes a leadership role in shaping our corporate governance, including overseeing the evaluation of the Board and its committees. The Committee's Charter contains information concerning the Committee's responsibilities, including identifying and evaluating the director candidates. The Nominations and Governance Committee Charter and the Corporate Governance Guidelines are both available on our website at [www.insmed.com](http://www.insmed.com) under the heading "Investors Corporate Governance." The Board has determined that all members of the Nominations and Governance Committee are independent as defined in Rule 5605(a)(2) of the Nasdaq Listing Rules and our Corporate Governance Guidelines.

**Director Candidate Recommendations and Nominations by Shareholders.** The Nominations and Governance Committee's Charter provides that the Committee will consider director candidate recommendations by shareholders. Shareholders should submit any such recommendations for the Nominations and Governance Committee through the method described under "Communications with the Board." In addition, in accordance with our Bylaws, any person who is a shareholder of record on the record date for the shareholder meeting, on the date of the shareholder meeting and on the date such person provides required notice to the Company may nominate persons for election to the Board if such shareholder complies with the notice procedures set forth in the Bylaws and summarized in this Proxy Statement under the heading "Proposals for 2014 Annual Meeting."

**Nominations and Governance Committee Process for Identifying and Evaluating Director Candidates.** The Nominations and Governance Committee evaluates all director candidates in accordance with the director qualification standards described in the Corporate Governance Guidelines and the Nominations and Governance Committee Charter, including the provision that diversity of backgrounds



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and experience should be emphasized in board composition, and seeks candidates with experience in the pharmaceutical and biotechnology industries, as well as business, management, accounting and financial experience. The Nominations and Governance Committee evaluates a candidate's qualifications to serve as a member of the Board based on the skills and characteristics of such individual Board members as well as the composition of the Board as a whole. In addition, the Nominations and Governance Committee will evaluate a candidate's independence, diversity, skills and experience in the context of the Board's needs.

**Communications with the Board**

The Board approved a process for shareholders to send communications to the Board. Shareholders can send communications to the Board and, if applicable, to the Nominations and Governance Committee or to specified individual directors in writing c/o Ms. Andrea Holtzman Drucker, Corporate Secretary, Insmmed Incorporated, 9 Deer Park Drive, Suite C, Monmouth Junction, New Jersey 08852-1923. All letters sent to Ms. Drucker will be forwarded, as appropriate, to the Board, the Nominations and Governance Committee or any specified individual directors.

**Director Attendance at Annual Meeting**

Our policy is that directors attend the annual meeting of shareholders. All directors attended the 2012 Annual Meeting of Shareholders in accordance with our policy.

**Board Leadership Structure**

Our Board does not have a policy on whether the same person should serve as both the Chief Executive Officer and Chairman of the Board or, if the roles are separate, whether the Chairman should be selected from the non-employee directors or should be an employee. The Board believes that it should have the flexibility to make these determinations in the way that it believes best provides appropriate leadership for us at a given time. The Board believes that its current leadership structure, with Mr. Lewis serving as Chief Executive Officer and Mr. Hayden serving as Chairman, is appropriate for the Company at this time. Both leaders are actively engaged on significant matters affecting us, such as long-term strategy. The Chief Executive Officer has overall responsibility for all aspects of our operation, while the Chairman has a greater focus on governance of the Company, including oversight of the Board. We believe this balance of shared leadership between the two positions is a strength for the Company. In addition, Dr. Whitcomb has been our lead independent director since May 2012 when Mr. Hayden became Executive Chairman for approximately four (4) months during a period of transition at the senior most levels of management. As the lead independent director, Dr. Whitcomb continues to serve as principal liaison with the Chairman and the CEO, presides at executive sessions of non-management and independent directors, has the authority to call meetings of independent directors, provides meaningful input into the agenda of Board meetings, authorizes the retention of outside advisors, consultants and legal counsel who report directly to the Board and consults frequently with other independent directors on issues as they arise.

**The Role of the Board in Risk Oversight**

The Board has primary responsibility for overseeing the Company's risk management. The Board administers its oversight responsibility for risk management directly and through its committees. Each committee chairman reports to the Board regarding the committee's considerations of management's processes for identifying, evaluating and controlling significant risks. In addition, the officers responsible for oversight of particular risks within the Company provide updates and information to our Board. The Board considers specific risk topics, including risks associated with our strategic plan, our capital structure, our research and development activities, our supply chain and our operations. Our Board believes that full and open communication between management and the Board is essential for

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effective risk management and oversight. Management routinely informs the Board of developments that could affect our risk profile or other aspects of our business and development. We face a number of risks, including those described under the "Risk Factors" section of our Annual Report on Form 10-K for the year ended December 31, 2012, which is available on our website at [www.insmed.com](http://www.insmed.com) under the heading "Investor Relations SEC Filings."

The Audit Committee periodically discusses with management our policies and guidelines regarding risk assessment and risk management as well as our major financial and operational risk exposures and the steps that management has taken to monitor and control such exposures. The Audit Committee oversees disclosure controls and procedures, including applicable internal control over financial reporting and meets with the Chief Financial Officer, the General Counsel, external audit personnel and other senior managers as appropriate to review issues regarding compliance with the applicable legal and regulatory requirements.

The Compensation Committee assesses and monitors whether any of our compensation policies and programs has the potential to encourage excessive risk taking. The Company believes that the risks arising from our overall compensation policies and practices for our employees are not reasonably likely to have a material adverse effect on the Company. During the last fiscal year, the Compensation Committee, with the assistance of its independent compensation consultant, reviewed the executive compensation program and determined that the design of the compensation policies, including the components, weightings and focus of the elements of executive compensation do not encourage management to assume excessive or inappropriate risks.

The Nominations and Governance Committee oversees the risks associated with our corporate governance and operating practices, including those relating to the composition of Board, the structure and function of Board committees and meeting logistics and policies. The Nominations and Governance Committee regularly reviews the Board's performance, oversees evaluation of each of the Board's committees, oversees our corporate governance and formulates and recommends corporate governance standards to our Board.

**Committees of the Board of Directors**

Our Bylaws provide that the Board may create one or more committees of the Board. Currently, the Board has three standing committees: the Audit Committee, the Compensation Committee, and the Nominations and Governance Committee.

**Audit Committee**

*Composition and Attendance.* Our Audit Committee consists of Mr. Kollender (Chairman), Dr. Engelsen, and Mr. Altomari. After being elected to the Board in August 2012, Mr. Altomari was appointed to serve on the Audit Committee, replacing Dr. Whitcomb who resigned from the Audit Committee. During 2012, the Audit Committee held six meetings. Mr. Kollender, Dr. Engelsen, Dr. Whitcomb, and Mr. Altomari each attended all meetings of the Audit Committee held during their respective time served on the Committee.

*Responsibilities and Duties.* The Audit Committee assists our Board in fulfilling its oversight responsibilities relating to the accounting, reporting and financial practices of the Company and seeking to ensure our compliance with applicable legal and regulatory requirements. The Committee reviews and oversees:

the financial statements, financial reports and other financial information which we provide to governmental bodies, our shareholders and others;

our systems of internal controls regarding finance and accounting;

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our auditing, accounting and financial reporting processes;

the qualifications and independence of our independent registered public accounting firm; and

the engagement and compensation of our independent registered public accounting firm to perform audit services and any permissible non-audit services.

Our Board has adopted a written charter for the Audit Committee, which is available on our website at [www.insmed.com](http://www.insmed.com) under the heading "Investor Relations Corporate Governance." Our Board amended the Audit Committee Charter on March 6, 2012 as part of its corporate governance review.

*Independence.* Rule 5605(c)(2) of the Nasdaq Listing Rules and Rule 10A-3 of the Exchange Act of 1934, as amended (the "Exchange Act"), each require that the members of our Audit Committee be independent. Our Board has determined that all three of the current Audit Committee members, Mr. Kollender, Dr. Engelsen, and Mr. Altomari, are "independent directors" within the meaning of Rule 5605(a)(2) of the Nasdaq Listing Rules, Rule 10A-3 of the Exchange Act and our Corporate Governance Guidelines. Our Board also determined that Dr. Whitcomb was an independent director under such standards during the portion of 2012 in which he was a member of the Audit Committee.

*Financial Literacy and Expertise.* Our Board determined that each of the members of the Audit Committee is able to read and understand fundamental financial statements, including our balance sheet, consolidated statement of operations and consolidated statement of cash flows, and has accounting or related financial management expertise, as such terms are interpreted by our Board. Our Board also has determined that Mr. Kollender is an "audit committee financial expert," as that term is defined in the rules promulgated by the Securities and Exchange Commission ("SEC") pursuant to the Sarbanes-Oxley Act of 2002, as amended.

### **Compensation Committee**

*Composition and Attendance.* Our Compensation Committee consists of Dr. Whitcomb (Chairman), Dr. Sharoky and Mr. Kollender. During fiscal 2012, the Compensation Committee held seven meetings. Mr. Kollender replaced Mr. Hayden on the Compensation Committee in May 2012. Each of Dr. Whitcomb, Dr. Sharoky, Mr. Kollender and Mr. Hayden attended all Compensation Committee meetings that occurred in 2012 during their respective time served on the Compensation Committee.

*Responsibilities and Duties.* The Compensation Committee develops and oversees the implementation of our compensation philosophy for our executive officers and is responsible for our executive and other compensation plans. The Committee's primary objectives are to develop and maintain an executive compensation policy that:

creates a direct relationship between pay levels and corporate performance and returns to shareholders;

provides overall competitive pay levels to effectively attract and retain executive talent;

creates proper incentives to enhance shareholder value; and

rewards performance.

Our Board has adopted a written charter for the Compensation Committee, a copy of which is available on our website at [www.insmed.com](http://www.insmed.com) under the heading "Investor Relations Corporate Governance." The Compensation Committee reviews and reassesses the adequacy of the charter at least annually.

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*Independence.* Rule 5605(d)(2) of the Nasdaq Listing Rules requires that the members of our Compensation Committee be independent. Our Board has determined that all three of the current Compensation Committee members, Dr. Whitcomb, Dr. Sharoky, and Mr. Kollender, are "independent directors" within the meaning of Rule 5605(a)(2) of the Nasdaq Listing Rules and our Corporate Governance Guidelines. Our Board also determined Mr. Hayden was an independent director under such standards during the portion of 2012 in which he was a member of the Compensation Committee.

**Nominations and Governance Committee**

*Composition and Attendance.* Our Nominations and Governance Committee consists of Dr. Sharoky (Chairman), Dr. Engelsen, and Dr. Whitcomb. During fiscal 2012, the Nominations and Governance Committee held three meetings. Dr. Whitcomb replaced Mr. Hayden on the Nominations and Governance Committee in May 2012. Each of Dr. Sharoky, Dr. Engelsen, Dr. Whitcomb and Mr. Hayden attended all meetings of the Nominations and Governance Committee that occurred in 2012 during his tenure on the Nominations and Governance Committee.

*Responsibilities and Duties.* The Nominations and Governance Committee identifies and nominates qualified candidates for directorship and serves in a leadership role in shaping our corporate governance and overseeing the evaluation of the Board and its committees. The Nominations and Governance Committee:

assists the Board by identifying and recruiting individuals qualified to become Board members and recommending to the Board the director nominees for the next annual meeting of shareholders;

recommends to the Board director nominees for each committee;

oversees our governance, including recommending to the Board Corporate Governance Guidelines;

leads the Board in its annual review of the Board's performance and oversees the evaluation of each of the Board's committees;

oversees the management continuity planning process;

ensures that the Board consists of a diversified group of individuals with strong business experience, good judgment and high integrity; and

seeks to ensure that directors, executive management and employees adhere to a high ethical standard in performing their duties.

Our Board has adopted a written charter for the Nominations and Governance Committee, a copy of which is available on our website at [www.insmed.com](http://www.insmed.com) under the heading "Investor Relations Corporate Governance."

*Independence.* Our Board has determined that all three of the current members of the Nominations and Governance Committee, Dr. Sharoky, Dr. Engelsen, and Dr. Whitcomb, are "independent directors" within the meaning of Rule 5605(a)(2) of the Nasdaq Listing Rules and our Corporate Governance Guidelines. Our Board also determined Mr. Hayden was an independent director under such standards during the portion of 2012 in which he was a member of the Nominations and Governance Committee.

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**AUDIT COMMITTEE REPORT\* AND INDEPENDENT AUDITOR FEES**

**Report of the Audit Committee**

The Audit Committee of the Board (the "Audit Committee") is comprised of three independent directors and operates under a written charter adopted by the Board. The Audit Committee reviews and reassesses the adequacy of the charter at least annually. The Audit Committee approves and recommends to the Board, the selection of the Company's independent registered public accounting firm. The Audit Committee meets with and holds discussions with management and Ernst & Young LLP, the Company's independent registered public accounting firm.

The Audit Committee oversees the Company's financial reporting process on behalf of the Board. Management has the primary responsibility for the financial statements and the reporting process including the systems of internal controls. In fulfilling its oversight responsibilities, the Audit Committee reviewed the audited financial statements in the Company's Annual Report on Form 10-K for the year ended December 31, 2012 (the "Annual Report") with management including a discussion of the quality, the accounting principles, the reasonableness of significant judgments, and the clarity of disclosures in the financial statements.

The Audit Committee reviewed with the independent registered public accounting firm, who are responsible for expressing an opinion on the conformity of those audited financial statements with generally accepted accounting principles, its judgments as to the quality, the Company's accounting principles, and such other matters as are required to be discussed with the Audit Committee by Public Company Accounting Oversight Board Standards.

In addition, the Audit Committee has discussed with the independent registered public accounting firm the independence of the independent registered public accounting firm from management and the Company, including the matters in the written disclosures and letter from the independent registered public accounting firm to the Audit Committee required by the applicable requirements of the Public Company Accounting Oversight Board regarding the independent accountant's communications with the Audit Committee concerning independence, and considered the compatibility of non-audit services with the independence of the independent registered public accounting firm.

In reliance on the reviews and discussions referred to above, the Audit Committee recommended to the Board (and the Board approved) that the audited financial statements be included in the Company's Annual Report on Form 10-K for the year ended December 31, 2012 for filing with the SEC. The Audit Committee and the Board also recommended, subject to ratification by our shareholders, the appointment of Ernst & Young LLP as the Company's independent registered public accounting firm for the year ending December 31, 2013.

**THE AUDIT COMMITTEE**

Richard S. Kollender, CPA, Chairman  
Steinar J. Engelsen, M.D., C.E.F.A.  
Al Altomari

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The foregoing report of the Audit Committee is not to be deemed "soliciting material" or deemed to be "filed" with the SEC (irrespective of any general incorporation language in any document filed with the SEC) or subject to Regulation 14A of the Exchange Act, or to the liabilities of Section 18 of the Exchange Act, except to the extent we specifically incorporate the text of such report by reference into a document filed with the SEC.

Table of Contents**Audit Committee Pre-Approval Policy**

In March 2012, as part of our corporate governance review, the Audit Committee adopted a revised Audit Committee Pre-Approval Policy for the pre-approval of audit services and permitted non-audit services by the Company's independent registered public accounting firm in order to assure that the provision of such services does not impair the independence of the independent registered public accounting firm from the Company and is consistent with the SEC's rules. The policy requires pre-approval by the Audit Committee of the terms and fees of all audit, review and attestation engagements and related services. The policy also requires the Audit Committee to determine that the provision of any audit-related services or non-audit services would not impair the independence of our independent registered public accounting firm. The policy also prohibits the Audit Committee from retaining our independent registered public accounting firm in connection with a transaction initially recommended by such firm, the purpose of which may be tax deferral or reduction. The policy delegates pre-approval authority to the Chair of the Audit Committee or, if the Chair is not available, to any of the Audit Committee's independent members, but any pre-approval decision must be reported to the full Audit Committee at its next scheduled meeting. All of the services performed by Ernst & Young LLP ("Ernst & Young") in the year ended December 31, 2012 were pre-approved in accordance with the applicable pre-approval policy.

**Independent Registered Public Accounting Firm Fee Disclosure**

The Audit Committee reviewed the aggregate fees billed by Ernst & Young for professional services rendered for the fiscal years ended December 31, 2012 and 2011, which were as follows:

	2012	2011
Audit Fees	\$ 414,000	\$ 307,000
Audit Related Fees		
Tax Fees		
Other Fees		
<b>Total Fees</b>	<b>\$ 414,000</b>	<b>\$ 307,000</b>

Audit Fees in 2012 and 2011 include fees for services performed to comply with Generally Accepted Auditing Standards. These services include the quarterly reviews, the integrated year end audit of our consolidated financial statements, review of documents filed with the SEC and accounting consultations on matters addressed during the audit or quarterly reviews. All of the Ernst & Young fees were pre-approved by the Audit Committee.

In considering the nature of the services provided by Ernst & Young, the Audit Committee determined that such services are compatible with the provision of independent audit services. The Audit Committee discussed these services with Ernst & Young and our management to determine that they are permitted under the rules and regulations concerning auditor independence promulgated by the SEC to implement the Sarbanes-Oxley Act of 2002, as well as by the American Institute of Certified Public Accountants.

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**CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS**

All of our directors and officers complete a directors and officers questionnaire at the beginning of each year, in which they are asked to disclose family relationships and other related party transactions. Our Audit Committee must review and approve or ratify all related party transactions, as defined in Item 404 of Regulation S-K promulgated under the Securities Act of 1933. In examining related party transactions, our Audit Committee considers whether any of our directors, officers, holders of more than five percent (5%) of our voting stock, or any immediate family members of the foregoing persons and any other persons whom the Audit Committee determines to be related parties, have a conflict of interest where an individual may have a private interest which interferes with or appears to interfere with our interests. In determining whether to approve or ratify a related party transaction, the Audit Committee will take into account, among other factors it deems appropriate, whether the related party transaction is on terms no less favorable to us than terms generally available to us from an unaffiliated third-party under the same or similar circumstances, and the extent of the related party's interest in the transaction. Any transaction which is deemed to be a related party transaction requires the approval, initially by a majority of the disinterested Audit Committee members, and finally by a majority of the disinterested Board members. Our Audit Committee's procedures for reviewing related party transactions are in writing.

The rules and regulations promulgated by the SEC require us to disclose in this Proxy Statement any transaction since January 1, 2012, or any currently proposed transaction, involving more than \$120,000 in which we are a participant and in which any related person has or will have a direct or indirect material interest. A related person is any executive officer, director, nominee for director, or holder of five percent (5%) or more of our Common Stock, or an immediate family member of any of those persons sharing the household of such person.

On September 28, 2012, we completed a registered direct public offering of 6,304,102 shares of our Common Stock for a price to the public of \$4.07 per share (which was equal to the last consolidated closing price of our Common Stock on the Nasdaq Capital Market prior to completion of the transaction). The net proceeds to us from the sale of the shares were \$25.7 million. Quaker BioVentures (as previously defined), a holder of more than 5% of our Common Stock, participated in this registered direct public offering by purchasing 737,100 shares for an aggregate purchase price of \$2,999,997. Richard Kollender, one of our directors, is a partner of Quaker Partners Management, L.P. and a managing member of Quaker BioVentures Capital II, LLC, the general partner of Quaker BioVentures Capital II, L.P., which is the general partner of Quaker BioVentures II, L.P. Affiliates of RA Capital Management, LLC ("RA Capital") became a holder of more than five percent (5%) of our Common Stock after participating in this registered direct public offering. RA Capital and its affiliates purchased 2,457,002 shares for an aggregate purchase price of \$9,999,998. The terms of this offering were reviewed and approved by the disinterested members of our Board but were not separately approved by a majority of the disinterested Audit Committee members.

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**SECTION 16(A) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE**

Section 16(a) of the Exchange Act requires that our directors, executive officers and holders of more than 10% of our Common Stock report to the SEC their ownership of our Common Stock and changes in that ownership. Directors, executive officers and beneficial owners of more than 10% of our Common Stock are required by applicable regulations to furnish us with copies of all Section 16(a) forms they file. As a matter of practice, members of our staff assist our executive officers and directors in preparing initial ownership reports and reporting ownership changes and typically file these reports on their behalf. We reviewed copies of the reports filed pursuant to Section 16(a) of the Exchange Act. Based solely upon that review, we believe that during the year ended December 31, 2012, our officer, directors and holders of more than 10% of our Common Stock complied with applicable Section 16(a) requirements, except with respect to one Form 4 filed by Mr. Lewis on October 3, 2012 for one grant of stock options to acquire 186,170 shares, which he received on September 28, 2012.

**SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT**

The following table sets forth information about the beneficial ownership of our Common Stock as of the Record Date, March 28, 2013 (except as otherwise noted), by:

each person, or group of persons, who beneficially owns more than five percent (5%) of our capital stock;

each of our directors and director nominees;

each of our Named Executive Officers; and

all directors and executive officers as a group.

Beneficial ownership and percentage ownership are determined in accordance with the rules and regulations of the SEC and include voting or investment power with respect to shares of stock. This information does not necessarily indicate beneficial ownership for any other purpose. In computing the number of shares beneficially owned by a person and the percentage ownership of that person, shares of Common Stock subject to options held by that person that are currently exercisable or exercisable within 60 days of March 28, 2013 are deemed outstanding. Such shares, however, are not deemed outstanding for the purposes of computing the percentage ownership of any other person. Except as indicated in the footnotes to the following table or pursuant to applicable community property laws, each shareholder named in the table has sole voting and investment power with respect to the shares



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set forth opposite such shareholder's name. The percentage of beneficial ownership is based on 31,571,806 shares of Common Stock outstanding on the Record Date, March 28, 2013.

Name and Address	Shares Beneficially Owned(1)	
	Number	Percentage
<b>Greater Than Five Percent (5%) Shareholders</b>		
FMR LLC(2) 82 Devonshire Street Boston, Massachusetts 02109	4,418,083	14.0%
Quaker BioVentures II, L.P.(3) 2929 Arch Street, Cira Centre Philadelphia, PA 19104-2868	2,598,595	8.2%
RA Capital Management, LLC(4) 20 Park Plaza, Suite 1200 Boston, MA 02116	2,433,319	7.7%
TVM Capital GmbH(5) Maximilianstrasse 35/Eingang C, 80539 Munchen, Germany	1,627,854	5.2%
Prospect Venture Partners III, L.P.(6) 435 Tasso Street, Suite 200 Palo Alto, California 94301	1,604,940	5.1%

(1) Except as explicitly set forth in applicable footnotes, all information in this table, including the footnotes thereto, is derived from third-party filings made with the SEC, as described in the footnotes. We have not independently verified such information.

(2) As of December 31, 2012, as reported on Schedule 13G filed with the SEC on March 11, 2013 as adjusted in the manner described below. Fidelity Management & Research Company, Beacon Bioventures Limited Partnership, Beacon Bioventures Principals Limited Partnership, and Pyramis Global Advisors Trust Company are the beneficial owners of 2,807,200 shares, 1,869,084 shares, 12,668 shares, and 11,394 shares, respectively, of our Common Stock. Fidelity Management & Research Company is a wholly-owned subsidiary of FMR LLC. Pyramis Global Advisors Trust Company is an indirect wholly-owned subsidiary of FMR LLC. Beacon Bioventures Advisors Limited Partnership is the general partner of Beacon Bioventures Limited Partnership and Beacon Bioventures Principals Limited Partnership. The general partner of Beacon Bioventures Advisors Limited Partnership is Fidelity Biosciences Corp., a wholly-owned subsidiary of FMR LLC. Members of the family of Edward C. Johnson III, Chairman of FMR LLC, are the predominant owners, directly or through trusts, of Series B voting common shares of FMR LLC, representing 49% of the voting power of FMR LLC. The Johnson family group and all other Series B shareholders have entered into a shareholders' voting agreement under which all Series B voting common shares will be voted in accordance with the majority vote of Series B voting common shares. Accordingly, through their ownership of voting common shares and the execution of the shareholders' voting agreement, members of the Johnson family may be deemed, under the Investment Company Act of 1940, to form a controlling group with respect to FMR LLC. The reporting person's Schedule 13G includes 282,263 shares as beneficially owned that are subject to an indemnification holdback arising from the Company's merger with Transave. Such shares were retained by Insmmed at the time of the merger to satisfy any

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indemnification claims and which, as of the date of the proxy statement, have not been delivered to the reporting person. The reporting person does not have the right to vote such shares until they are delivered. As a result, we have not included such shares in the table above. If such shares are delivered in full to the reporting person, the reporting person would beneficially own 4,700,346 shares, representing approximately 14.9% of our shares.

(3)

As of December 31, 2012, as reported on Schedule 13G, as amended, filed with the SEC on February 14, 2013, as adjusted in the manner described below. 2,927,094 shares (the "Quaker Shares") are owned of record by Quaker BioVentures II, L.P., Quaker BioVentures Capital II, L.P. and Quaker BioVentures Capital II, LLC. Quaker BioVentures Capital II, L.P. ("Quaker Capital L.P.") is the general partner of Quaker BioVentures II, L.P., and Quaker BioVentures Capital II, LLC ("Quaker Capital LLC") is the general partner of Quaker Capital L.P. As a result of the control that Quaker Capital L.P. exercises over Quaker BioVentures II, L.P. and the control that Quaker Capital LLC exercises over Quaker Capital L.P., each of Quaker Capital L.P. and Quaker Capital LLC may be deemed to beneficially own the Quaker Shares. Richard S. Kollender, who is a director of Insmmed and a managing member of Quaker Capital LLC, holds 15,643 shares of Common Stock. Quaker Capital LLC may be deemed to beneficially own the shares held by Mr. Kollender. The reporting person's Schedule 13G includes 328,499 shares as beneficially owned that are subject to an indemnification holdback arising from the Company's merger with Transave. Such shares were retained by Insmmed at the time of the merger to satisfy any indemnification claims and which, as of the date of the proxy statement, have not been delivered to the reporting person. The reporting person does not have the right to vote such shares until they are delivered. As a result, we have not included such shares in the table above. If such shares are delivered in full to the reporting person, the reporting person would beneficially own 2,927,094 shares, representing approximately 9.3% of our shares.

(4)

As of December 31, 2012, as reported on Schedule 13G, as amended, filed with the SEC on February 14, 2013. RA Capital Healthcare Fund, L.P. is the beneficial owner of 1,467,926 shares. RA Capital Management, LLC, as the investment adviser and sole general partner of the RA Capital Management, LLC and investment adviser to an account owned by a separate investment vehicle which holds shares of our Common Stock, and Peter Kolchinsky as the manager of RA Capital Management, LLC, each may be deemed to beneficially own 2,433,319 shares of Common Stock.

(5)

As of March 1, 2011, as reported on Schedule 13G filed with the SEC on March 10, 2011. The joint statement on Schedule 13G was filed by TVM V Life Science Ventures GmbH & Co. KG ("TVM V"); TVM V Life Science Ventures Management GmbH & Co. KG ("TVM V LS Management"), the managing limited partner of TVM V; TVM IV GmbH & Co. KG ("TVM IV"); TVM IV Management GmbH & Co. KG, the managing limited partner of TVM IV ("TVM IV Management"); TVM Capital GmbH, the sole general partner of TVM V and TVM IV; Hans Schreck ("Schreck"), Friedrich Bornikoel ("Bornikoel"), John DiBello ("DiBello"), Alexandra Goll ("Goll"), and Helmut Schühlsler ("Schühlsler") who are limited partners of, and serve as members of the investment committee of TVM IV Management; and Hubert Birner ("Birner"), Mark Cipriano ("Cipriano"), Stefan Fischer ("Fischer"), Axel Polack ("Polack") and David Poltack ("Poltack"), who, together with DiBello, Goll and Schühlsler, are limited partners of, and serve as members of the investment committee of TVM V LS Management. The principal business address for TVM IV, TVM IV Management, TVM Capital, TVM V, TVM V Management, Birner, Bornikoel, Fischer,

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Goll, Polack, Schreck, and Schühsler is Maximilianstrasse 35/Eingang C, 80539 Munchen, Germany. The principal business address for Cipriano, DiBello and Poltack is 101 Arch Street, Suite 1950, Boston, MA 02110. . The reporting person's Schedule 13G excludes 287,269 shares as beneficially owned that are subject to an indemnification holdback in connection with the Transave merger, which shares were retained by Insmmed at the time of the merger to satisfy any indemnification claims and which, as of the date of the proxy statement, have not been delivered to the reporting person. The reporting person does not have the right to vote such shares until they are delivered. If such shares are delivered in full to the reporting person, the reporting person would beneficially own 1,915,122 shares, representing approximately 6.1% of our shares.

(6)

As of March 1, 2011, as reported on Schedule 13G filed with the SEC on March 8, 2011. Prospect Management Co. III, L.L.C. ("PMC III") serves as the sole general partner of Prospect Venture Partners III, L.P. ("PVP III"). As such, PMC III possesses power to direct the voting and disposition of the shares owned by PVP III and may be deemed to have indirect beneficial ownership of the shares held by PVP III. PMC III owns no securities of Insmmed directly. The reporting person's Schedule 13G excludes 283,225 shares as beneficially owned that are subject to an indemnification holdback in connection with the Transave merger, which shares were retained by Insmmed at the time of the merger to satisfy any indemnification claims and which, as of the date of the proxy statement, have not been delivered to the reporting person. The reporting person does not have the right to vote such shares until they are delivered. If such shares are delivered in full to the reporting person, the reporting person would beneficially own 1,888,165 shares, representing approximately 6.0% of our shares.

Name	Shares Beneficially Owned(1)	
	Number	Percentage
<b>Directors and Executive Officers</b>		
Donald Hayden, Jr.(2)	64,832	*
Melvin Sharoky, M.D.(3)	163,197	*
Steinar J. Engelsens, M.D.(4)	223,353	*
Randall W. Whitcomb, M.D.(5)	52,833	*
Al Altomari		*
Richard S. Kollender(6)	2,614,238	8.3%
Will Lewis	34,154	*
Andrew T. Drechsler		*
Renu Gupta, M.D.(7)	33,325	*
Andrea Holtzman Drucker, J.D.(8)	6,525	*
Timothy Whitten(9)	335,000	1.1%
Kevin P. Tully(10)	118,333	*
Nicholas A. LaBella, Jr.(11)	88,200	*
All current directors and executive officers as a group (11 persons)	3,192,457	10.1%

\*

Denotes ownership of less than 1% of the outstanding shares of our Common Stock.

(1)

Except as indicated otherwise in the footnotes below, each individual has sole voting and investment power with respect to the shares reported.

(2)

Includes 21,250 shares of our Common Stock that are subject to stock options that are currently exercisable or exercisable within 60 days after March 28, 2013.

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- (3) Includes 5,250 shares of our Common Stock that are subject to stock options that are currently exercisable or exercisable within 60 days after March 28, 2013. The number of shares listed opposite Dr. Sharoky's name includes 360 shares of our Common Stock that are owned by his spouse, 21 shares of our Common Stock that are owned by his son, and 62 shares of our Common Stock that are owned by his daughter. Dr. Sharoky disclaims beneficial ownership of the shares of our Common Stock held by his spouse, his daughter, and his son.
- (4) Includes 5,250 shares of our Common Stock that are subject to stock options that are currently exercisable or exercisable within 60 days after March 28, 2013.
- (5) Includes 5,250 shares of our Common Stock that are subject to stock options that are currently exercisable or exercisable within 60 days after March 28, 2013. The number of shares listed opposite Dr. Whitcomb's name includes 2,100 shares of our Common Stock that are owned by the Randall W. Whitcomb Living Trust. Dr. Whitcomb and his spouse, Rita K. Whitcomb, are trustees of the Randall W. Whitcomb Living Trust.
- (6) Includes 2,598,595 shares held by Quaker BioVentures II, L.P, Quaker BioVentures Capital II, L.P. and Quaker BioVentures Capital II, LLC, but excludes 328,499 shares reported as beneficially owned by Quaker BioVentures that are subject to an indemnification holdback arising from the Company's merger with Transave. Mr. Kollender disclaims beneficial ownership of all such shares, except to the extent of his pecuniary interest in such shares.
- (7) Includes 31,325 shares of our Common Stock that are subject to stock options that are currently exercisable or exercisable within 60 days after March 28, 2013.
- (8) Includes 6,525 shares of our Common Stock that are subject to stock options that are currently exercisable or exercisable within 60 days after March 28, 2013.
- (9) Includes 202,300 shares of our Common Stock that are subject to stock options that are currently exercisable.
- (10) Includes 24,800 shares of our Common Stock that are subject to stock options that are currently exercisable.
- (11) Includes 34,800 shares of our Common Stock that are subject to stock options that are currently exercisable.

**EXECUTIVE COMPENSATION**

**COMPENSATION DISCUSSION AND ANALYSIS**

This Compensation Discussion and Analysis (the "CD&A") explains our compensation philosophy, policies and decisions for 2012 for the following executives, who we refer to in this CD&A and in the following tables as our named executive officers:

1. Will Lewis, President and Chief Executive Officer ("CEO"), responsible for developing, in connection with the Board, our corporate mission and objectives and providing direction and leadership to ensure the execution of our corporate strategy and achievement of our objectives;
2. Andrew T. Drechsler, Chief Financial Officer, responsible for managing all financial and administration activities, including internal and external reporting, treasury, accounting, and information technology, and program management;



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3. Renu Gupta, M.D., Executive Vice President of Development and Chief Medical Officer, responsible for directing clinical, pre-clinical and regulatory departments, quality, development; and
4. Andrea Holtzman Drucker, J.D., Senior Vice President, General Counsel and Corporate Secretary, responsible for oversight of all corporate- and litigation- related legal matters and regulatory compliance and providing ongoing legal support for development, financing opportunities, business development initiatives, and intellectual property matters.

In addition to the above four named executive officers, the following four individuals were also named executive officers during 2012 and are referred to below, but were not serving as executive officers as of December, 31, 2012:

5. Donald Hayden, Jr., Executive Chairman, from May 14, 2012 to September 9, 2012. During this period, Mr. Hayden, was responsible for working closely with the Board on leadership development and key senior management transitions as well as working with the CEO on strategic and financial planning. Upon the hiring of Will Lewis as our President and Chief Executive Officer on September 10, 2012, Mr. Hayden transitioned back to serving as non-Executive Chairman of the Board, the position he held prior to being appointed Executive Chairman on May 14, 2012;
6. Timothy Whitten, our former President and CEO;
7. Kevin P. Tully, C.G.A., our former Executive Vice President and Chief Financial Officer; and
8. Nicholas A. LaBella, Jr., our former Chief Scientific Officer.

### **Executive Summary**

We are a biopharmaceutical company focused on developing and commercializing inhaled therapies for patients battling serious lung diseases that are often life threatening. Our lead product candidate, ARIKACE® or liposomal amikacin for inhalation, is an inhaled antibiotic treatment that delivers a proven and potent anti-infective directly to the site of serious lung infections to improve the efficacy, safety and convenience of this therapeutic approach for patients. Currently, we are conducting clinical trials of ARIKACE for two initial indications in orphan patient populations: a phase 3 clinical trial in cystic fibrosis (CF) patients who have lung infections caused by *Pseudomonas aeruginosa* (*Pseudomonas*) and a phase 2 clinical trial in patients who have lung infections caused by non-tuberculous mycobacteria (NTM).

We operate in a very competitive, rapidly changing and heavily regulated industry. The long term success of our business requires the ability to be resourceful, adaptable and innovative. As we transition from a development stage company to a commercial biopharmaceutical company, the skills, talent and dedication of our executive officers are critical components to the success of this transition. Therefore, our compensation program for our executive officers, including our named executive officers, is designed to attract, retain and motivate the best possible talent.

One of our primary compensation objectives is having a pay program that is highly correlated to our performance. Consistent with this objective, a significant portion of our named executive officers' total direct compensation (comprised of base salary, cash bonus and long-term equity) for 2012 was at-risk.

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***Compensation Objectives***

The compensation paid to our named executive officers in 2012 reflected our primary compensation objectives of:

providing a competitive total compensation opportunity that will enable us to attract, retain and motivate highly qualified executives;

aligning compensation opportunities with shareholder interests by making the executive compensation program highly correlated to our performance, which is defined in terms of milestones associated with achieving goals designed to enhance long-term profitability and creating shareholder value; and

providing a strong emphasis on equity-based compensation and equity ownership, creating a direct link between shareholder and management interests.

***2012 Company Performance***

We met or exceeded a number of our corporate objectives during 2012 including:

the completion of patient enrollment in our phase 3 clinical trial of ARIKACE in patients who have lung infection caused by *Pseudomonas aeruginosa*;

initiation of a Phase 2 clinical trial of ARIKACE in patients who have lung infections caused by non-tuberculous mycobacteria;

initiation of a dog toxicity study; and

maintenance of an appropriate level of capitalization to sustain our growth and development.

***2012 Compensation Decisions***

Key compensation decisions for 2012 (and 2013 where applicable) were as follows:

***Base salaries.*** Base salaries for Mr. Lewis and Mr. Drechsler, our named executive officers that commenced employment during 2012, were the result of arm's-length negotiations of their respective employment agreements at the time of their hire. For 2012, the Compensation Committee did not provide Mr. Whitten, our former CEO, with any change to his base salary. The other named executive officers employed during 2011 each received a 1.5% increase to their base salary in 2012 (pro-rated for Ms. Drucker since she was hired during 2011). The Compensation Committee believed that this was an appropriate balance given certain clinical challenges and the status of ARIKACE at the end of 2011.

***Cash Bonuses.*** Based upon our performance in 2012, including our achievement of the corporate goals summarized above, Mr. Lewis, our CEO, and Mr. Hayden, our former Executive Chairman, earned a cash bonus equal to 122.5% of their target bonus percentage (which was 50% of their base salaries), both pro-rated for their period of service during 2012. Dr. Gupta and Ms. Drucker each earned a cash bonus equal to 116.9% of their target bonus (which was 40% and 30% of their base salaries, respectively). As described in more detail below, for 2012, the Compensation Committee determined that due to changes in the executive management team, shifting priorities and responsibilities, and the executive management team's ability to manage through these changes, and based on the recommendation of our CEO, Dr. Gupta and Ms. Drucker each received 100% for their achievement against their individual objectives. The Compensation Committee believed that it was important for the executive team to work together to achieve critical operational and financial goals. The exception to this bonus structure was the amount of cash bonus paid to Mr. Drechsler, who joined the Company in the fourth quarter of 2012. His bonus was provided in recognition of the significant work that was accomplished for certain year-end financial activities.





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For 2013, the Compensation Committee has determined that the cash bonuses for our named executive officers other than Mr. Lewis will continue to be determined by reference to both corporate and individual goals, with 75% tied to corporate goals and 25% tied to individual goals. Mr. Lewis, in consultation with our senior vice president of human resources, established individual goals for each of our named executive officers at the beginning of 2013 that are specific to the executive officer's area of responsibility and are in support of our corporate objectives for 2013. These individual goals were then recommended to and approved by our Compensation Committee. Mr. Lewis's cash bonus will continue to be determined by reference to our corporate goals only. In addition, for 2013 the Compensation Committee modified the target bonus percentage of base salary for certain named executive officers as follows: (i) Mr. Lewis's target bonus percentage was increased from 50% to 55% of his base salary; (ii) Mr. Drechsler's target bonus percentage was increased from 30% to 40% of his base salary; and (iii) Ms. Drucker's target bonus percentage was increased from 30% to 35% of her base salary. The Compensation Committee made these modifications based on the market data highlighted by our 2012 peer group, which is described in more detail below.

While the Compensation Committee believes that achievement of our corporate goals should continue to be the dominant factor in determining bonus payouts because it best aligns our named executive officers' compensation with the interests of our shareholders, they also believe that some portion of the executives' compensation, except our CEO, should be linked to individual performance. The Compensation Committee believes that including the achievement of individual goals as a component of our 2013 bonus payouts is important to incentivize our officers during this pivotal time in our history as we transform the organization from a development stage company into a commercial biopharmaceutical company.

Given Mr. Lewis's substantial influence on the overall performance of the Company, the Compensation Committee believes it is appropriate and in the best interests of our shareholders to continue to have Mr. Lewis's cash bonus be based solely upon the achievement of corporate objectives.

*Long-term Incentives.* Equity compensation was granted to our existing named executive officers in December 2011. During 2012, we issued stock options to Mr. Lewis and Mr. Drechsler in accordance with their respective employment agreements. It was anticipated that the Compensation Committee would evaluate the potential issuance of additional equity awards to one or more named executive officers in December 2012. However, during the latter part of 2012, substantial analysis was conducted to evaluate the size of the current equity award pool, and the intermediate equity needs for current employees, new anticipated executive hires and current executives. Given such analysis and changes in several of our executive officer positions, the Compensation Committee determined that it should defer these grants until the first quarter of 2013.

As previously disclosed in the Company's Annual Report on Form 10-K for the year ended December 31, 2012, in connection with a recent review by us of equity compensation awards made under our Amended and Restated 2000 Stock Incentive Plan (the "2000 Stock Incentive Plan"), we determined that we had inadvertently exceeded the annual per-person sub-limits set forth in our 2000 Stock Incentive Plan. The awards that exceeded the per-person sub-limits included certain restricted stock, restricted stock unit and stock option awards made to certain of our current and past officers and directors. The amount of Common Stock represented by these awards in excess of the per-person annual sub-limits totaled approximately 1.6 million shares. The awards that exceeded the per-person sub-limits included several awards that were issued immediately following our business combination with Transave, several awards that were negotiated with new hires pursuant to employment agreements or offers of employment (including options to acquire 819,484 shares granted to Mr. Lewis and options to acquire 100,000 shares granted to Mr. Drechsler which were in excess of the per-person sub-limits), and certain other awards made subsequent to our 2011 one-for-ten reverse stock split. At no time did we exceed the aggregate maximum share limit approved by shareholders under the 2000 Stock

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Incentive Plan (currently 3,925,000 shares of Common Stock), whether as a result of previously-issued awards or currently outstanding awards.

As a result of the foregoing review, on March 7, 2013, the Board approved a remediation and compliance plan recommended by a special committee of the Board. As of March 15, 2013, each current employee and director who holds an affected equity compensation award that is currently unvested and/or unexercised, entered into a waiver and consent, pursuant to which, each affected current employee or director agreed that (1) the unvested portion of such awards (stock options and RSUs) in excess of the sub-limits shall not vest and shall not become exercisable, (2) any vested but unexercised portion of stock options in excess of the sub-limits shall not be exercisable, and (3) any vested RSUs and any previously granted restricted stocks in excess of sub-limits shall not be sold, in each case, unless our shareholders ratify and approve the portion of the affected awards that were in excess of the applicable sub-limits. If shareholders do not ratify and approve the affected portion of such awards, such portions would be deemed forfeited (see Proposal 3, "Ratification and Approval of Certain Equity Compensation Awards Previously Granted to Certain Employees and Directors Under Our 2000 Stock Incentive Plan" included in this Proxy Statement for additional information regarding these and other excess awards).

***Say on Pay and Say on Pay Frequency***

On May 18, 2011, at our 2011 Annual Meeting of Shareholders, we held our first shareholder advisory vote on executive officer compensation as required under the federal securities laws. More than 90% of the votes cast on such proposal were in favor of the compensation of the named executive officers. We disclosed the compensation of our named executive officers in the compensation discussion and analysis and the various compensation tables and narrative that appeared in our proxy statement dated April 18, 2011. The Compensation Committee considered these voting results and did not make any substantial changes to the executive compensation program. The Compensation Committee will continue to take into account future shareholder advisory votes on executive compensation in analyzing whether any subsequent changes to our executive compensation programs and policies would be warranted. Taking into account the voting preference of our shareholders, the frequency of future "say-on-pay" votes will be every three years. As a result, the next shareholder advisory vote on executive officer compensation will occur in 2014.

**Compensation Determination Process**

***Role of the Compensation Committee and the Board in Making Decisions.*** Our Compensation Committee has been delegated the authority to make determinations regarding all elements of compensation for our executive officers, except for our CEO. Our Compensation Committee recommends to our Board the compensation for Mr. Lewis, our President and CEO. The Board reviews those recommendations and determines the compensation for Mr. Lewis. As discussed in further detail below, in assessing and determining our compensation programs, our Compensation Committee conducts a peer group review and engages outside executive compensation consultants to assess the competitiveness of our programs on a periodic basis. A review of peer company data was conducted in September 2012. We conducted another review in January 2013 due to the Board's determination that the Company was now a pre-commercial pharmaceutical company and no longer a clinical stage pharmaceutical company. The outcome of the analysis conducted in January 2013 resulted in modifications to our 2013 peer group. Given the evolution of our organization to a pre-commercial biopharmaceutical company, we now anticipate conducting peer group and outside consultant review of our programs at least on an annual basis. (See "Selection of Peer Companies/Benchmarking" below for additional information regarding our Peer Group analysis).

***Compensation Evaluation Processes and Criteria.*** Given the high demand for experienced and well-qualified executives of the type we seek to employ, the Compensation Committee reviews data and

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information from a variety of sources such as outside surveys of compensation and benefits for executive officers in the biotechnology industry, as well as public information regarding executive compensation at peer biotechnology companies. The Compensation Committee, with the help of its independent Compensation Consultant, ExeQuity LLP, established a peer group to better align target compensation with competitive data. The Compensation Committee further draws upon the personal knowledge of its members with respect to executive compensation at comparable companies.

In determining the amount and composition of compensation elements (cash and non-cash elements and short and long-term elements), our Compensation Committee relies upon its judgment about the performance of each individual executive officer and not on rigid formulas or short-term changes in business performance. In setting final compensation levels for our executive officers for 2012 our Compensation Committee considered many factors, including, but not limited to the following (the "compensation factors"):

our achievement of certain product development, corporate partnering, financial, strategic planning and other goals;

each officer's individual performance using certain subjective criteria, including an evaluation of each officer's initiative, contribution to overall corporate performance and managerial ability;

the scope and strategic impact of each executive officer's responsibilities;

our past business performance and future expectations;

our long-term goals and strategies;

the experience of each individual;

past compensation levels of each individual and of the executives as a group;

relative levels of pay among the officers;

the amount of each element of compensation in the context of the executive officer's total compensation and other benefits;

for each executive officer, other than the President and CEO, the evaluations and recommendations of our President and CEO; and

the competitiveness of our compensation relative to the selected peer group companies and benchmarks (which are described below).

Consideration of the compensation factors is subjective; no relative weights or rankings are assigned to these factors (except as otherwise discussed in this CD&A).

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**Selection of Peer Companies/Benchmarking**

During 2012, the Compensation Committee, upon advice received from ExeQuity, selected the companies that comprise our 2012 peer group through a screening process that considered publicly traded biopharmaceutical companies that were similar to us in size, market capitalization and stage of development, and operate in geographic locations that generally have similar pay levels. The median size (based upon the number of employees) and market capitalization of the companies selected for our 2012 peer group was 45 employees and \$115.2 million, respectively. The number of employees at the companies in our 2012 peer group ranged from 7 to 121, and these companies had market capitalizations that ranged from \$45.5 million to \$331.4 million. The table below depicts our 2012 peer group:

Aegerion Pharmaceuticals, Inc.	Celsion Corporation	Northwest Biotherapeutics, Inc.
Agenus Inc.	Discovery Laboratories, Inc.	Rexahn Pharmaceuticals, Inc.
Amicus Therapeutics, Inc.	Immunomedics, Inc.	SIGA Technologies, Inc.
ArQule Inc.	Keryx Biopharmaceuticals, Inc.	Trius Therapeutics, Inc.
Callisto Pharmaceuticals, Inc.	MAP Pharmaceuticals, Inc.	Ventrus Biosciences, Inc.
CEL-SCI Corporation	Neuralstem, Inc.	Zalicus, Inc.

Based on the information it gathers, the Compensation Committee establishes benchmarks used for the purpose of evaluating appropriate compensation ranges for base salary, cash bonus and long-term incentives. Our Compensation Committee uses the benchmarks in various combinations in an effort to obtain comparative compensation information that reflects our particular facts and circumstances over the period of time for which the information is available. When reviewing benchmark data, our Compensation Committee generally targets compensation at or near the 50th percentile for companies of similar size and stage of development.

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**Components of Compensation**

In summary, the compensation paid to our executive officers includes the following components:

<b>Component</b>	<b>Purpose of Component</b>
Base Salary	Provide our executive officers with a level of stability and certainty each year.
Cash Bonuses	Motivate and reward executive officers for short-term individual and corporate performance.
Long-term Incentives (Stock Options, Restricted Stock and Restricted Stock Units)	Motivate and reward executive officers for long-term corporate performance. Encourage stock ownership by management, which is beneficial for aligning the interests of management and shareholders, thereby enhancing shareholder value.
Health, Welfare and Retirement Programs	Help to attract and retain talented employees. Provide market competitive benefits to protect employees' and their covered dependents' health and welfare. Provide a program to foster retirement savings.
Severance and Change in Control Benefits	Discourage turnover and cause executives to be better able to respond to the possibility of a change in control without being influenced by the potential effect of a change in control on their job security.

The components of our compensation program and compensation decisions for 2012 for each named executive officer are described in more detail below:

***Base Salary***

The Compensation Committee reviews and sets base salaries for executives, other than the President and CEO, on an annual basis during the first quarter of each fiscal year. The Compensation Committee reviews and recommends to our Board the base salary for our President and CEO and the Board determines the base salary for our President and CEO.

Our Board and Compensation Committee seek to establish and maintain base salaries for each position and level of responsibility that are competitive with those of executive officers at various other biotechnology companies of comparable size and stage of development. Salary levels for each of our executive officers are generally targeted at or near the 50th percentile of salaries that our Compensation Committee believes are paid to executive officers with comparable qualifications, experience and responsibilities within our peer group. When our compensation is benchmarked, our Compensation Committee reviews variances between the salary levels for each of our executive officers and those of the companies included in our peer group and determines, in its discretion, individual salary adjustments after considering the compensation factors described above, although no relative weights or rankings are assigned to these factors. In setting the base salary for our executive officers other than our CEO, the Compensation Committee also considers the recommendations of our CEO.

Due to corporate challenges we experienced during the second half of 2011, Mr. Whitten did not receive an increase to his base salary for 2012 and the base salary increases for Dr. Gupta, Mr. Tully

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and Ms. Drucker were 1.5% (pro-rated for Ms. Drucker since she was hired during 2011). The base salaries for Mr. Lewis and Mr. Drechsler were approved by the Board and Compensation Committee, respectively, as part of each of their hirings during 2012.

**Cash Bonus**

We maintain an annual cash bonus program for all of our employees to motivate and reward the attainment of annual corporate goals and individual goals. Cash bonuses for our executive officers are not guaranteed, but to date have been awarded from time to time, generally annually, only in the discretion of the Compensation Committee and the Board. We target the 50th percentile of cash bonuses provided to executive officers in similar positions at companies included in our peer group. The Compensation Committee sets guidelines for the bonuses potentially payable to our executive officers, except our President and CEO, whose bonus is determined by the Board based upon a recommendation from the Compensation Committee. For 2012, target bonus percentages were set at 50% of our CEO's and our Executive Chairman's base salaries, 40% of our Chief Medical Officer's salary, 35% of our Chief Financial Officer and Chief Scientific Officer's base salaries, and 30% of our General Counsel's base salary. Bonus payments can be increased beyond these target levels at the Compensation Committee's discretion, for example, in the event of exceptional performance by an individual officer.

At the beginning of each fiscal year, management recommends annual corporate objectives to the Compensation Committee for approval. These objectives serve as the basis for determining our performance against key strategic and operating parameters for the year. In the past, criteria for bonuses for executive officers ranged from success in attracting capital, to success in conducting clinical trials, obtaining US Food and Drug Administration (FDA) approvals, entering into new and expanded collaborations, licensing, acquisitions, divestitures, and establishing and expanding our manufacturing capabilities. When determining what bonus amounts, if any, would be paid for 2012, the Board, with respect to the President and CEO, and the Compensation Committee, with respect to the other executive officers, also took into account our overall financial condition at the time and our performance against our annual corporate objectives. For bonuses related to our 2012 performance, the Compensation Committee determined that we achieved a cash bonus payout percentage of 122.5% on our overall performance against our corporate objectives. The following table provides a breakdown of how we performed against each of our corporate objectives during 2012:

Corporate Objectives	Original Weighting (% of Corporate Objectives)	Actual Performance	Actual % of Corporate Objectives Earned
Completion of patient enrollment in our Phase 3 clinical trial of ARIKACE in patients with <i>Pseudomonas aeruginosa</i>	30%	Exceeded	45%
Initiation of a Phase 2 clinical trial of ARIKACE in patients with NTM	30%	Exceeded	45%
Maintenance of clinical supply in support of all of our clinical development programs	15%	Achieved	7.5%
Initiation of a dog toxicity study	10%	Achieved	10%
Maintenance of an appropriate level of capitalization	15%	Achieved	15%
Total	100%		122.5%

In addition to reviewing our performance against our corporate objectives, the President and CEO is evaluated by the Board and each executive officer is evaluated by the Compensation Committee regarding his or her individual performance, level of responsibility, leadership in relation to our overall

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performance and the other compensation factors described above. For 2012, due to changes in the executive management team, shifting priorities and responsibilities, the executive management team's ability to manage through these changes, and based on the recommendation of our CEO, the Compensation Committee determined that Dr. Gupta and Ms. Drucker would each receive 100% for their achievement against their individual objectives. Based on its overall evaluation, the Board approved the following cash bonus payments to the following named executive officers for 2012:

Name and Principal Position	Base Salary	Target Bonus %	Allocation of Bonus %		Actual Bonus % Achievement		2012 Cash Bonus
			Corporate Goals	Individual Goals	Corporate Goals	Individual Goals	
William H. Lewis(1) <i>President and Chief Executive Officer</i>	\$ 425,000	50%	100%	0%	122.5%	N/A	\$ 86,771
Andrew T. Drechsler(2) <i>Chief Financial Officer</i>	\$ 330,000	30%	N/A	N/A	N/A	N/A	\$ 35,000
Renu Gupta, M.D. <i>Executive Vice President of Development and Chief Medical Officer</i>	\$ 406,000	40%	75%	25%	122.5%	100.0%	\$ 189,805
Andrea Holtzman Drucker, J.D. <i>Senior Vice President, General Counsel and Corporate Secretary</i>	\$ 303,375	30%	75%	25%	122.5%	100.0%	\$ 106,371
Donald Hayden, Jr.(1) <i>Former Executive Chairman</i>	\$ 200,000	50%	100%	0%	122.5%	N/A	\$ 36,036

(1) Mr. Lewis's and Mr. Hayden's bonus payments were prorated for their respective period of service during 2012.

(2) Mr. Drechsler's employment began midway through the fourth quarter. As a result, his cash bonus was determined by the Compensation Committee based on its subjective assessment of the significant work he accomplished related to certain year-end financial activities.

As part of the Compensation Committee's review of our named executive officer's target bonus percentages that was completed during December 2012, it was determined that the target bonus percentages for certain of our named executive officers were below the 50<sup>th</sup> percentile of the target bonus percentages for executive officers within our 2012 peer group. In response to this finding, our Compensation Committee (and the Board for our CEO) approved increases to certain of our named executive officer target bonus percentages to align them with the 50<sup>th</sup> percentile of our 2012 peer group. For 2013, the target bonus percentage for certain of our named executive officers was increased as follows: Mr. Lewis's was increased to 55% of his base salary, Mr. Drechsler's was increased to 40% of his base salary, and Ms. Drucker's was increased to 35% of her base salary. In addition, in

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connection with this review, the Board approved our corporate objectives and assigned weightings for 2013 as follows:

	<b>Original Weighting (% of Corporate Objectives)</b>
<b>Corporate Goals</b>	
Actively pursue regulatory filings in the EU and US	40%
Expand our product supply chain in support of clinical development and commercialization	45%
Prepare for commercial launch of ARIKACE	15%
 Total	 100%

***Long-term Incentives***

Historically, we have granted stock options to all new employees upon commencement of employment. We plan to continue this practice. Shares of our Common Stock underlying these stock options typically vest over a four-year period, with 25% of the shares vesting on the first anniversary of the date of grant and 12.5% of the shares vesting on each sixth month anniversary thereafter until the fourth anniversary of the date of grant. The stock options granted typically expire ten years from the date of grant and the exercise price typically equals the fair market value of our Common Stock on the date of grant.

The Compensation Committee may also grant stock options to executive officers from time to time in recognition of such executive officer's expanded duties and responsibilities or continuing contributions to the Company's performance. The Board approves all stock option grants to our President and CEO.

We may grant restricted stock and RSU awards to new employees upon their commencement of employment and to executive officers. The vesting criteria for the restricted stock or RSUs can be either time-based, performance-based or a combination of time-based and performance-based. We may grant stock options, restricted stock, and RSU awards to employees separately or in combination in the future as we deem beneficial and appropriate to fulfill the goals of our compensation program.

When granting stock options, restricted stock or RSUs, the Compensation Committee considers the compensation factors described above, as well as:

the existing levels of stock ownership among the executive officers relative to each other and to our employees as a whole;

previous grants of stock options, restricted stock or RSUs to such executive officers;

vesting schedules of previously granted stock options, restricted stock and RSUs;

personal knowledge of the Compensation Committee members regarding executive stock options and restricted stock awards at comparable companies; and

the impact of stock option, restricted stock and RSU awards on our results of operations.

Other than the stock options granted to Mr. Lewis and Mr. Drechsler in connection with their initial hire and pursuant to their employment agreements, none of the named executive officers were granted stock options, or restricted stock or RSU awards during 2012. The Compensation Committee made this determination due to the concern regarding the number of shares available for issuance under the 2000 Stock Incentive Plan and the need to attract new management into the organization during the course of 2012 and 2013. However, the Compensation Committee also recognizes that long





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term performance will be achieved through an ownership culture that rewards our executives for maximizing shareholder value over time and that aligns the interests of our employees and management with those of our shareholders. For this reason we are requesting approval of the 2013 Incentive Plan in order to maximize this form of compensation and support our long term incentive program (see Proposal 4, "Approval of the 2013 Incentive Plan" for additional information regarding our 2013 Incentive Plan).

The Compensation Committee believes that providing additional stock option grants beyond an initial new hire grant provides management with a strong link to long-term corporate performance and the creation of shareholder value, as well as providing continued retention via long-term and milestone driven vesting. We anticipate making semi-annual stock option grants to our named executive officers in connection with our Company-wide grants. The Compensation Committee believes that a semi-annual grant cycle spreads the incentives of the stock option grant across a broader time horizon and may mitigate the impact of the historical volatility of our stock.

***Other Benefits***

We maintain several other benefit programs that are offered to all employees, which include coverage for health insurance, dental insurance, life and disability insurance, and a 401(k) Plan. We do not have any defined benefit plans or non-qualified deferred compensation plans and we do not currently provide for any Company contributions or matching contributions under the 401(k) Plan.

***Severance and Change in Control Benefits***

As discussed in further detail below, we entered into employment agreements with each of our named executive officers that, in addition to other items, provide for certain severance and change in control payments. We believe that the existence of these potential benefits will discourage turnover and cause such executives to be better able to respond to the possibility of a change in control without being influenced by the potential effect of a change in control on their job security. We entered into separation agreements with Mr. Whitten, Mr. Tully and Mr. LaBella, as described in more detail below.

***Other Compensation Considerations***

***Section 162(m).*** In general, under Section 162(m) of the Internal Revenue Code of 1986, as amended (the "Code"), we cannot deduct, for federal income tax purposes, compensation in excess of \$1,000,000 paid to certain executive officers for any one calendar year. This deduction limitation does not apply, however, to certain "performance-based compensation" within the meaning of Section 162(m) of the Code and the regulations promulgated thereunder. We have considered the limitations on deductions imposed by Section 162(m) of the Code and generally seek to structure executive compensation to minimize application of the deduction limitations of Section 162(m) of the Code. However, we cannot assure you that all compensation will qualify for deductibility under Section 162(m), and we may, in our discretion, award non-deductible compensation.

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**COMPENSATION COMMITTEE REPORT\***

The Compensation Committee has reviewed and discussed the CD&A with management and based on the review and discussions with management of the CD&A, the Compensation Committee recommended to the Board that the CD&A be included in this Proxy Statement on Schedule 14A.

**THE COMPENSATION COMMITTEE**

Randall W. Whitcomb, M.D., Chairman

Richard S. Kollender, CPA

Melvin Sharoky, M.D.

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The foregoing report of the Compensation Committee is not to be deemed "soliciting material" or deemed to be "filed" with the SEC (irrespective of any general incorporation language in any document filed with the SEC) or subject to Regulation 14A of the Securities Exchange Act of 1934, as amended, or to the liabilities of Section 18 of the Securities Exchange Act of 1934, except to the extent we specifically incorporate it by reference into a document filed with the SEC.

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**Summary Compensation Table**

The following table sets forth information regarding compensation earned by the named executive officers in fiscal years 2012, 2011, and 2010.

<b>Name and Principal Position</b>	<b>Year</b>	<b>Salary</b>	<b>Bonus(1)</b>	<b>Stock Awards(2)</b>	<b>Option Awards(2)</b>	<b>All Other Compensation</b>	<b>Total</b>
Will Lewis(3) <i>President and Chief Executive Officer</i>	2012	\$ 125,397	\$ 86,771	\$	\$ 2,591,605	\$ 34,736	\$ 2,838,509
Andrew T. Drechsler(4) <i>Chief Financial Officer</i>	2012	\$ 52,673	\$ 35,000	\$	\$ 917,000	\$	\$ 1,004,673
Renu Gupta, M.D.(5) <i>Executive Vice President of Development and Chief Medical Officer</i>	2012	\$ 406,000	\$ 189,805	\$	\$	\$	\$ 595,805
	2011	\$ 400,000	\$ 102,800	\$ 475,540	\$ 229,371	\$	\$ 1,207,711
	2010	\$ 33,333	\$ 107,800	\$	\$	\$	\$ 141,133
Andrea Holtzman Drucker, J.D.(6) <i>Senior Vice President, General Counsel and Corporate Secretary</i>	2012	\$ 303,375	\$ 106,371	\$	\$	\$	\$ 409,746
	2011	\$ 137,500	\$ 31,106	\$ 513,450	\$ 79,083	\$	\$ 761,139
Donald Hayden, Jr.(7) <i>Former Executive Chairman</i>	2012	\$ 64,615	\$ 36,026	\$	\$	\$ 5,385	\$ 106,026
Timothy Whitten(8) <i>Former President and Chief Executive Officer</i>	2012	\$ 293,141	\$	\$ 442,680	\$ 199,280	\$ 939,798	\$ 1,874,899
	2011	\$ 425,000	\$ 106,250	\$ 1,353,460	\$ 312,393	\$	\$ 2,197,103
	2010	\$ 35,417	\$ 112,500	\$	\$	\$	\$ 147,917
Kevin P. Tully, C.G.A.(9) <i>Former Executive Vice President and Chief Financial Officer</i>	2012	\$ 302,386	\$	\$ 96,674	\$ 17,391	\$ 505,840	\$ 922,291
	2011	\$ 325,000	\$ 78,630	\$ 475,540	\$ 135,441	\$	\$ 1,014,611
	2010	\$ 278,173	\$ 111,269	\$	\$	\$	\$ 389,442
Nicholas A. LaBella, Jr.(10) <i>Former Chief Scientific Officer</i>	2012	\$ 253,750	\$	\$ 276,024	\$ 92,040	\$ 615,248	\$ 1,237,062
	2011	\$ 325,000	\$ 78,630	\$ 402,380	\$ 30,300	\$	\$ 836,310
	2010	\$ 214,711	\$ 72,000	\$ 115,000	\$	\$	\$ 401,711

(1) Amounts in this column represent cash bonus compensation paid to each executive officer as determined in the discretion of the Compensation Committee and our Board.

(2) Reflects grant date fair values of stock and option awards granted during the applicable fiscal year, calculated in accordance with FASB ASC Topic 718, except the assumptions of forfeitures is not made. See Note 10, "Stock-Based Compensation" of the consolidated financial statements in the Company's Form 10-K for 2012 regarding assumptions underlying valuation of equity awards.

(3) Mr. Lewis's 2012 salary covers the period from his date of hire on September 10, 2012 through December 31, 2012. Mr. Lewis's annual salary as of his hire date was \$425,000. Prior to entering into his employment agreement with the Company on September 10, 2012, Mr. Lewis was a consultant to the Company from the period June 21, 2012 to September 9, 2012 ("Mr. Lewis's consulting period"). During Mr. Lewis's consulting period, the Company paid Mr. Lewis consulting fees totaling \$34,736, which is the "All Other Compensation" included in the above table.

(4)

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Mr. Drechsler's 2012 salary covers the period from his date of hire on November 7, 2012 through December 31, 2012. Mr. Drechsler's annual salary as of his hire date was \$330,000.

(5) Dr. Gupta's salary in 2010 is for the month of December only. Dr. Gupta's annual salary as of her hire date was \$400,000.

(6) Ms. Drucker's 2011 salary covers the period from her date of hire on July 18, 2011 through December 31, 2011. Ms. Drucker's annual salary as of her hire date was \$300,000.

(7) Mr. Hayden's salary as our Executive Chairman covers the period from May 16, 2012 to September 9, 2012. Mr. Hayden's annual salary as of his hire date was \$200,000. The \$5,385 of "All Other Compensation" in the above table represents accrued vacation paid to Mr. Hayden during 2012.

(8) On September 10, 2012, Mr. Whitten resigned from employment with the Company. Pursuant to Mr. Whitten's letter agreement and general release with the Company dated September 10, 2012 ("Mr. Whitten's letter agreement"), the "All Other Compensation" amount of \$939,798 above consists of the following, all of which will be paid to Mr. Whitten within 9 months and a day following his last day of employment, except for the payment of monthly health insurance premiums; thirteen months of his annual base salary totaling \$460,417, a 2012 bonus of \$212,500, 100% of Mr. Whitten's annual target bonus of \$212,500 for 2012, accrued vacation of \$17,163, and the

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cost of health insurance premiums (net of Mr. Whitten's contribution while he was employed with the Company) for eighteen months at an estimated cost \$37,218. Also, pursuant to Mr. Whitten's letter agreement, all of Mr. Whitten's unvested RSUs and stock options became fully vested and the time to exercise these awards was extended to one year resulting in the 2012 compensation amounts of \$442,680 and \$199,280 under Stock Awards and Option Awards, respectively, in the above table. Mr. Whitten's salary for 2010 is for the month of December only.

(9)

On July 26, 2012, Mr. Tully entered into a letter of agreement and general release with the Company ("Mr. Tully's Separation Agreement") which provided that Mr. Tully's last day of employment with the Company was December 1, 2012, the date his employment agreement expired. Pursuant to Mr. Tully's Separation Agreement with the Company, the "All Other Compensation" amount of \$505,840 above consists of the following, all of which was paid to Mr. Tully on December 15, 2012, except for the payment of monthly health insurance premiums; nine months of annual base salary totaling \$247,407, his pro rata portion of his annual target bonus for 2012 of \$86,592, 100% of Mr. Tully's annual target bonus for 2012 of \$115,456, accrued vacation of \$13,956, and the cost of health insurance premiums (net of Mr. Tully's contribution while he was employed with the Company) for eighteen months at an estimated cost \$42,429. Also, pursuant to Mr. Tully's Separation Agreement, all of Mr. Tully's unvested RSUs and stock options granted to him at least one year prior to his last day of employment (December 1, 2012) became fully vested and the time to exercise these awards was extended to one year resulting in the 2012 compensation amounts of \$96,674 and \$17,391 under Stock Awards and Option Awards, respectively, in the above table.

(10)

On October 5, 2012, Mr. LaBella resigned from employment with the Company. Pursuant to Mr. LaBella's letter agreement and general release with the Company dated October 5, 2012 ("Mr. LaBella's letter agreement"), the "All Other Compensation" amount of \$615,248 above consists of the following, all of which will be paid to Mr. LaBella within 13 months following his last day of employment, except for the payment of monthly health insurance premiums; thirteen months of his annual base salary totaling \$357,365, a bonus for 2012 of \$115,456, 100% of Mr. LaBella's annual target bonus for 2012 of \$115,456, accrued vacation of \$8,247, and the cost of health insurance premiums (net of Mr. LaBella's contribution while he was employed with the Company) for twelve months at an estimated cost \$18,724. Also, pursuant to Mr. LaBella's letter agreement, all of Mr. LaBella's unvested RSUs and stock options became fully vested and the time to exercise these awards was extended to one year resulting in the 2012 compensation amounts of \$276,024 and \$92,040 under Stock Awards and Option Awards, respectively, in the above table.

Table of Contents**Grants of Plan-Based Equity Awards**

The following table sets forth certain information regarding the stock option grants made to our named executive officers during the fiscal year ended December 31, 2012. No other Plan-Based Awards were granted to any of our current or former named executive officers during 2012.

<b>Name and Principal Position</b>	<b>Grant Date</b>	<b>All Other Stock Awards: Number of Shares of Restricted Stock Units (RSUs) (#)</b>	<b>All Other Option Awards: Number of Securities Underlying Options (#)(1)</b>	<b>Exercise or Base Price of Option Awards (\$/Sh)</b>	<b>Grant Date Fair Value (\$)(2)</b>
William H. Lewis	9/10/2012		708,314	\$ 3.40	\$ 1,919,531
<i>President and Chief Executive Officer</i>	9/28/2012		186,170	\$ 4.55	\$ 672,074
Andrew T. Drechsler	11/7/2012		175,000	\$ 6.65	\$ 917,000
<i>Chief Financial Officer</i>					
Renu Gupta, M.D.					
<i>Executive Vice President of Development and Chief Medical Officer</i>					
Andrea Holtzman Drucker, J.D.					
<i>Senior Vice President, General Counsel and Corporate Secretary</i>					
Donald Hayden, Jr.					
<i>Former Executive Chairman</i>					
Timothy Whitten					
<i>Former President and Chief Executive Officer</i>					
Kevin P. Tully, C.G.A.					
<i>Former Executive Vice President and Chief Financial Officer</i>					
Nicholas A. LaBella, Jr.					
<i>Former Chief Scientific Officer</i>					

- (1) The amounts shown in this column reflect stock options granted to our named executive officers pursuant to our 2000 Stock Incentive Plan. These options have a vesting schedule of 25% on the first anniversary of the date of grant and 12.5% of the shares vesting on each six month anniversary thereafter until the fourth anniversary of the date of grant (see Proposal 3, "Ratification and Approval of Certain Equity Compensation Awards Previously Granted to Certain Employees and Directors Under Our 2000 Stock Incentive Plan" included in this Proxy Statement for additional information regarding these and other excess awards previously granted to employees and a director).
- (2) Reflects grant date fair values of stock option awards granted during the applicable fiscal year, calculated in accordance with FASB ASC Topic 718, except the assumptions of forfeitures is not made. See Note 10 of the consolidated financial statements in the Company's Form 10-K for 2012 regarding assumptions underlying valuation of equity awards.

**Narrative Disclosure to Summary Compensation Table and Grants of Plan-Based Awards Table**

**Employment Agreements**

*Will Lewis.* On September 10, 2012 we entered into an employment agreement with Mr. Lewis under which he is entitled to an annual base salary, which for fiscal 2012 was \$425,000, a target annual bonus opportunity equal to 50% of his base salary and participation in Company benefit plans generally provided to the Company's executive personnel, including participation in any equity incentive plans maintained by the Company. For 2013, Mr. Lewis's base salary was increased to \$445,000 and his target bonus percentage was increased to 55%.



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*Andrew T. Drechsler.* On November 7, 2012, we entered into an employment agreement with Mr. Drechsler under which he is entitled to an annual base salary, which for fiscal 2012 was \$330,000, a target annual bonus opportunity equal to 30% of his base salary and participation in Company benefit plans generally provided to the Company's executive personnel, including participation in any equity incentive plans maintained by the Company. For 2013, Mr. Drechsler's target bonus percentage was increased to 40%.

*Renu Gupta.* On January 31, 2011, we entered into an employment agreement with Dr. Gupta effective as of December 2, 2010 under which she is entitled to an annual base salary, which for fiscal 2012 was \$406,000, a target annual bonus opportunity equal to 40% of her base salary and participation in Company benefit plans generally provided to the Company's executive personnel, including participation in any equity incentive plans maintained by the Company. For 2013, Dr. Gupta's base salary was increased to \$422,240.

*Andrea Holtzman Drucker.* On June 7, 2011, we entered into an employment agreement with Ms. Drucker effective as of July 18, 2011 under which she is entitled to an annual base salary, which for fiscal 2012 was \$303,375, a target annual bonus opportunity equal to 30% of her base salary and participation in Company benefit plans generally provided to the Company's executive personnel, including participation in any equity incentive plans maintained by the Company. For 2013, Ms. Drucker's base salary was increased to \$321,578 and her target bonus percentage was increased to 35%.

*Donald Hayden, Jr.* On May 14, 2012, we entered into an employment agreement with Mr. Hayden effective as of that day under which he was entitled to an annual base salary, which for 2012 was \$200,000, a target annual bonus opportunity equal to 50% of his base salary and participation in Company benefit plans generally provided to the Company's executive personnel, including participation in any equity incentive plans maintained by the Company. In order to facilitate the Company's intent that Mr. Hayden's appointment be for an interim period, Mr. Hayden's employment agreement differed from the typical agreement which the Company utilizes for its executive officers. For example, Mr. Hayden's agreement included a 60-day termination provision and did not include any severance provisions. Additionally, equity compensation was not issued in relation to his employment. Upon the hiring of Will Lewis as our President and Chief Executive Officer on September 10, 2012, Mr. Hayden transitioned back to serving as our non-Executive Chairman of the Board, the position he held prior to being appointed Executive Chairman on May 14, 2012.

*Timothy Whitten.* Prior to his termination, Mr. Whitten's employment was governed by an employment agreement effective as of January 31, 2011. Pursuant to the terms of the employment agreement, Mr. Whitten was entitled to an annual base salary, which for fiscal 2012 was \$425,000, a target annual bonus opportunity equal to 50% of his base salary and participation in Company benefit plans generally provided to the Company's executive personnel, including participation in any equity incentive plans maintained by the Company.

*Kevin Tully.* Prior to his termination, Mr. Tully's employment was governed by an employment agreement effective as of January 31, 2011. Pursuant to the terms of the employment agreement, Mr. Tully was entitled to an annual base salary, which for fiscal 2012 was \$329,875, a target annual bonus opportunity equal to 35% of his base salary and participation in Company benefit plans generally provided to the Company's executive personnel, including participation in any equity incentive plans maintained by the Company.

*Nicholas A. LaBella.* Prior to his termination, Mr. LaBella's employment was governed by an employment agreement effective as of January 31, 2011. Pursuant to the terms of the employment agreement, Mr. Tully was entitled to an annual base salary, which for fiscal 2012 was \$329,875, a target annual bonus opportunity equal to 35% of his base salary and participation in Company benefit plans

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generally provided to the Company's executive personnel, including participation in any equity incentive plans maintained by the Company.

### **Outstanding Equity Awards at Year-End**

The following table sets forth certain information regarding the stock options and RSUs held by each of our named executive officers as of December 31, 2012.

Name and Principal Position	Option Awards			Option Expiration Date	Stock Awards		Equity Incentive Plan Awards		
	Number of Securities Underlying Unexercised Options (#) Exercisable	Number of Securities Underlying Unexercised Options (#) Unexercisable	Exercise Price (\$)		Number of Shares or Units of Stock That Have Not Vested	Market Value of Stock That Have Not Vested	Number of Shares, Units or Rights That Have Not Vested (#)	Market or Payout Value of Unearned Shares, Units or Rights That Have Not Vested (\$)	
William H. Lewis <i>President and Chief Executive Officer</i>		708,314	\$ 3.40	9/10/2022	(1)(3)				
		186,170	\$ 4.55	9/28/2022	(1)(3)				
Andrew T. Drechsler <i>Chief Financial Officer</i>		175,000	\$ 6.55	11/7/2022	(1)(3)				
Renu Gupta, M.D. <i>Executive Vice President of Development and Chief Medical Officer</i>	9,300	15,500	\$ 5.90	1/31/2021	(1)(3)	27,900	\$ 186,651(3)(4)	27,900	\$ 186,651(3)(5)
	18,925	56,775	\$ 3.03	12/21/2021	(1)(3)				
Andrea Holtzman Drucker, J.D. <i>Senior Vice President, General Counsel and Corporate Secretary</i>	6,525	19,575	\$ 3.03	12/21/2021	(1)	22,500	\$ 150,525(3)(4)	22,500	\$ 150,525(3)(5)
Donald Hayden, Jr. <i>Former Executive Chairman</i>	21,250	63,750	\$ 3.03	12/21/2021	(1)(3)	15,988	\$ 106,960(3)(6)		
Timothy Whitten <i>Former President and Chief Executive Former President and Chief Executive Officer</i>	99,200		\$ 5.90	9/10/2013	(2)(3)				
	103,100		\$ 3.03	9/10/2013	(2)(3)				
Kevin P. Tully, C.G.A. <i>Former Executive Vice President and Chief Financial Officer</i>	24,800		\$ 5.90	12/1/2013	(2)				
Nicholas A. LaBella, Jr. <i>Former Chief Scientific Officer</i>	24,800		\$ 5.90	10/5/2013	(2)				
	10,000		\$ 3.03	10/5/2013	(2)				

(1) These stock options have a vesting schedule of 25% on the first anniversary of the date of grant and 12.5% of the shares vesting on each six month anniversary thereafter until the fourth anniversary of the date of grant.

(2) Pursuant to the individual letter/separation agreements entered into by each of Mr. Whitten, Mr. Tully and Mr. LaBella and the Company, these stock options became fully vested on each former employee's last date of employment with the Company and each employee has one year from their respective last date of employment with the Company to exercise these stock options.

(3) With regard to these stock option and RSU grants, during the first quarter of calendar year 2013, we determined that we inadvertently exceeded the annual per-person sub-limits of 75,000 stock options per-person per calendar year and 12,500 RSUs per-person per calendar year that were in place

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when these awards were granted. (See Proposal 3, "Ratification and Approval of Certain Equity Compensation Awards Previously Granted to Certain Employees and Directors Under Our 2000 Stock Incentive Plan" included in this Proxy Statement for additional information regarding these and other excess awards previously granted to employees and directors).

- (4) These RSUs vest on the third anniversary of the date of grant.
- (5) These RSUs vest (if at all) on the date on which our Board determines that ARIKACE (our lead product candidate) has achieved its primary endpoint in a Phase 3 clinical trial provided that the grantee continues to be employed by the Company on such date.
- (6) These RSUs have a vesting schedule of 100% on the first anniversary of the date of grant, provided that Mr. Hayden attends at least 75% of the Board meetings.

Table of Contents**Stock Options Exercised and Stock Vested**

The following table sets forth information with respect to stock options exercised and stock awards vested by the named executive officers during the fiscal year ended December 31, 2012.

<b>Name and Principal Position</b>	<b>Number of Shares Acquired on Exercise (#)</b>	<b>Value Realized on Exercise (\$)</b>	<b>Number of Shares Acquired on Vesting (#)</b>	<b>Value Realized on Vesting \$(1)</b>
William H. Lewis <i>President and Chief Executive Officer</i>				
Andrew T. Drechsler <i>Chief Financial Officer</i>				
Renu Gupta, M.D. <i>Executive Vice President of Development and Chief Medical Officer</i>				
Andrea Holtzman Drucker, J.D. <i>Senior Vice President, General Counsel and Corporate Secretary</i>				
Donald Hayden, Jr. <i>Former Executive Chairman</i>			8,594	\$ 29,306
Timothy Whitten <i>Former President and Chief Executive Officer</i>			130,200	\$ 442,680
Kevin P. Tully, C.G.A. <i>Former Executive Vice President and Chief Financial Officer</i>			55,800	\$ 399,528
Nicholas A. LaBella, Jr. <i>Former Chief Scientific Officer</i>			43,400	\$ 276,024

- (1) Calculated by multiplying the number of shares acquired on vesting date by the closing price of our Common Stock on the date the RSUs vested.

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**Potential Payments Upon Termination or Change in Control**

Our named executive officers, except for Mr. Hayden whose employment agreement did not contain any change in control benefits, are entitled to certain benefits in connection with certain terminations or as a result of a change in control. We believe that the existence of these potential benefits will discourage turnover and cause such executives to be better able to respond to the possibility of a change in control without being influenced by the potential effect of a change in control on their job security.

If Mr. Lewis's employment is terminated by us without cause or by Mr. Lewis for good reason within twelve months after a change in control of the Company, Mr. Lewis will receive payment of accrued obligations, a lump sum payment equal to the sum of two times his annual base salary and target bonus, a pro-rata portion of his annual target bonus, full vesting of all time-vested equity awards, and up to eighteen months continuation of health benefits provided Mr. Lewis elects continued coverage under COBRA.

If Mr. Drechsler's employment is terminated by us without cause or by Mr. Drechsler for good reason within twelve months after a change in control of the Company, Mr. Drechsler will receive payment of accrued obligations, a lump sum payment equal to the sum of one times his annual base salary, a pro-rata portion of his annual target bonus, full vesting of all time-vested equity awards, and up to one year continuation of health benefits provided Mr. Drechsler elects continued coverage under COBRA.

If the employment of Dr. Gupta or Ms. Drucker is terminated by us without cause or by the executive officers for good reason within twelve months after a change in control of the Company, Dr. Gupta or Ms. Drucker, as applicable, will receive payment of accrued obligations, a lump sum payment equal to the sum of one times her respective annual base salary and pro-rata portion of her annual target bonus for the year of termination, 100% of her annual target bonus, full vesting of all equity awards, and up to two years continuation of health benefits provided the executive officers elect continued coverage under COBRA.

The employment of each of our executive officers may be terminated by us with or without cause, or by the executive officers with or without good reason. If the employment of one of our executive officers is terminated by us without cause or by the executive officers for good reason prior to the date of a change in control or following the one year period after a change in control, the executive officers (other than Mr. Drechsler) will receive payment of accrued obligations, a pro rata portion of their annual target bonus for the year of termination, twelve months continuation of his or her respective annual base salary, 100% of his or her annual target bonus, full vesting of all equity awards in place for one year or longer (or, in the case of Mr. Lewis, full vesting of all time-vested equity awards in place for one year or longer), and Company-paid health insurance for the officer and his or her dependents for up to eighteen months so long as they are eligible for COBRA coverage under the Company's health and welfare plans. If Mr. Drechsler's employment is terminated by us without cause or by Mr. Drechsler for good reason prior to the date of a change in control or following the one year period after a change in control, Mr. Drechsler will receive payment of accrued obligations, a pro rata portion of his annual target bonus for the year of termination, six months continuation of his annual base salary, an additional six months of option vesting, and Company-paid health insurance for the officer and his or her dependents for up to six months so long as he is eligible for COBRA coverage under the Company's health and welfare plans.

In addition, if we decide, without cause, to not renew one of the employment agreements at the end of its term, then the executive (other than Mr. Lewis and Mr. Drechsler) will receive payment of accrued obligations, twelve months continuation of his or her respective annual base salary less the amount of base salary that was paid to him or her during the 120 day notice period for non-renewal of the term, 100% of his or her annual target bonus less the pro rata portion of the annual target bonus

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paid to him or her with respect to the 120 day notice period for non-renewal of the term, full vesting of all equity awards in place for one year or longer, and Company-paid health insurance for the officer and his or her dependents for up to eight months so long as they elect COBRA coverage under Company's health and welfare plans.

To protect our business and goodwill, for a period of twelve months after the termination of an executive's employment with us, the executive agrees that he or she will not:

1. engage in any activity in material competition with the business in which we engaged while the executive was employed by us;
2. directly or indirectly recruit or solicit any person who is then an employee of us or was an employee of us at any time within six months prior to such solicitation; or
3. solicit, divert or take away, or attempt to divert or to take away, the business or patronage of any of our clients or customers, or prospective clients or customers.

Pursuant to the RSU award agreements entered into in connection with the respective employment of Dr. Gupta and Ms. Drucker, the restrictions imposed on such RSUs held by such executives shall lapse upon a change in control. Upon a change in control, the value of the accelerated awards as of December 31, 2012 would have been \$373,302 for Dr. Gupta and \$301,050 for Ms. Drucker.

The severance benefits that executives may be entitled to receive under these agreements and other benefits that the executives are entitled to receive under other plans, may constitute parachute payments that are subject to the "golden parachute" rules of Section 280G of the Code and the excise tax of Code Section 4999. If these payments are determined to be parachute payments, as calculated by our independent registered public accounting firm, the parachute payments will be reduced if, and only to the extent that, a reduction will allow the executives to receive a greater net after tax amount than the executives would receive absent a reduction. All severance benefits are also subject to the execution and non-revocation of a general release of claims against the Company.

The table below summarizes the hypothetical payments that could be incurred for each of the named executive officers at the time assuming that a qualified termination under the applicable agreement occurred on December 31, 2012 as a result of a change in control.

	Cash Severance(1)	Pro-Rata Bonus(2)	Benefits	Value of Accelerated Equity(3)	Total
Will Lewis	\$ 1,275,000	\$ 212,500	\$ 46,295	\$ 2,728,757	\$ 4,262,552
Andrew T. Drechsler	\$ 330,000	\$ 99,000	\$ 30,863	\$ 7,000	\$ 466,863
Renu Gupta, M.D.	\$ 568,400	\$ 162,400	\$ 74,423	\$ 593,344	\$ 1,398,566
Andrea Holtzman Drucker, J.D.	\$ 394,388	\$ 91,013	\$ 43,847	\$ 372,695	\$ 901,941

- (1) These payments and other benefits would be payable to the executive upon a qualified termination under the applicable agreement. The cash severance figure for Mr. Lewis includes salary for two years plus the target bonus for two years. The cash severance figure for Mr. Drechsler includes salary for one year. The cash severance figures for other executive officers include salary for one year plus the target bonus for one year.
- (2) The pro-rata bonus would be payable based on actual performance for the year pro-rated for the number of days worked in the year of termination. The value used in the table assumes the full target bonus for the year.
- (3) For all four (4) named executive officers listed in this table, these figures include certain Excess Awards as defined and described in more detail under "Proposal 3 Ratification and Approval of Certain Equity Compensation Awards Previously Granted to Certain Employees and Directors"



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Under Our 2000 Stock Incentive Plan" included herein. For Messrs. Lewis and Drechsler, the value represents the acceleration of all time-based equity awards outstanding as of December 31, 2012 and the value shown is equal to the number of stock options multiplied by the difference between the stock price as of December 31, 2012 (\$6.69 per share) and the exercise price of the options. For Dr. Gupta and Ms. Drucker, the value represents the acceleration of all equity awards outstanding as of December 31, 2012 and the value is equal to (1) for stock options, the number of stock options multiplied by the difference between the stock price as of December 31, 2012 (\$6.69 per share) and the exercise price of the options, and (2) for RSUs, the number of RSUs multiplied by the stock price as of December 31, 2012.

The table below summarizes the hypothetical payments that could be incurred for each of the named executive officers at the time assuming that a qualified termination under the applicable agreement occurred on December 31, 2012 as a result of termination without cause or for good reason prior to the date of a change in control or following the one year period after a change in control.

	Cash Severance(1)	Pro-Rata Bonus(2)	Benefits	Value of Accelerated Equity(3)	Total
Will Lewis	\$ 637,500	\$ 212,500	\$ 46,295	\$	\$ 896,295
Andrew T. Drechsler	\$ 264,000	\$	\$ 20,576	\$	\$ 284,576
Renu Gupta, M.D.	\$ 568,400	\$ 162,400	\$ 55,817	\$ 593,344	\$ 1,379,961
Andrea Holtzman Drucker, J.D.	\$ 394,388	\$ 91,013	\$ 32,885	\$ 372,695	\$ 890,980

- (1) These payments and other benefits would be payable to the executive upon a qualified termination under the applicable agreement. The cash severance figures for all of the executive officers (except Mr. Drechsler) include salary for one year plus the target bonus for one year. The figure for Mr. Drechsler includes salary for six months.
- (2) The pro-rata bonus would be payable based on actual performance for the year pro-rated for the number of days worked in the year of termination. The value used in the table assumes the full target bonus for the year.
- (3) For Dr. Gupta and Ms. Drucker, these figures include certain Excess Awards as defined and described in more detail under "Proposal 3 Ratification and Approval of Certain Equity Compensation Awards Previously Granted to Certain Employees and Directors Under Our 2000 Stock Incentive Plan" included herein. For Mr. Lewis, the value represents the acceleration of all time-vested equity outstanding as of December 31, 2012 granted at least one year prior to the termination date. For Mr. Drechsler, the value represents an additional six months of vesting of his outstanding options as of December 31, 2012. For Dr. Gupta and Ms. Drucker, the values represent the acceleration of all equity outstanding as of December 31, 2012 that was granted at least one year prior to the termination date and the value is equal to (1) for stock options, the number of stock options multiplied by the difference between the stock price as of December 31, 2012 (\$6.69 per share) and the exercise price of the options, and (2) for RSUs, the number of RSUs multiplied by the stock price as of December 31, 2012.

For purposes of the employment agreements, the term "cause" generally includes:

- (a) a conviction of the executive, or a plea of nolo contendere, to a felony involving moral turpitude; or
- (b) willful misconduct or gross negligence by the executive resulting, in either case, in material economic harm to the Company or any related entities; or



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- (c) a willful failure by the executive to carry out the reasonable and lawful directions of the Board and failure by the executive to remedy the failure within thirty (30) days after receipt of written notice of same, by the Board; or
- (d) fraud, embezzlement, theft or dishonesty of a material nature by the executive against the Company or any related entity, or a willful material violation by the executive of a policy or procedure of the Company or any related entity, resulting, in any case, in material economic harm to the Company or any related entity; or
- (e) a willful material breach by the executive of their employment agreement and failure by the executive to remedy the material breach within 30 days after receipt of written notice of same, by the Board.

For purposes of the employment agreements, the term "change in control" generally includes:

- (a) the acquisition by another person of beneficial ownership of 40% or more of our Common Stock;
- (b) a proxy contest that results in the replacement of a majority of the members of our Board;
- (c) a merger after which our shareholders own less than 60% of the surviving corporation's stock; or
- (d) approval by our shareholders of a complete liquidation or dissolution of our Company.

For purposes of the employment agreements, the term "good reason" generally includes:

- (a) a material diminution in the executive's base compensation;
- (b) a material diminution in the executive's authority, duties, or responsibilities;
- (c) a material diminution in the authority, duties, or responsibilities of the supervisor to whom the executive is required to report;
- (d) the Company's or related entity's requiring the executive to be based at any office or location outside of 50 miles from the location of employment or service as of the effective date of their employment agreement, except for travel reasonably required in the performance of the executive's responsibilities; or
- (e) any other action or inaction that constitutes a material breach by the Company of their employment agreement.

Messrs. Whitten, LaBella and Tully terminated their employment with us on September 10, 2012, October 5, 2012, and December 1, 2012, respectively. In connection with the termination of Mr. Whitten's employment, we entered into a letter agreement dated September 10, 2012 pursuant to which (i) Mr. Whitten received a lump sum payment of \$726,042, (ii) Mr. Whitten will receive an aggregate of \$159,375 payable in three monthly installments commencing six months and one day after his resignation date, (iii) otherwise unvested equity awards held by Mr. Whitten became vested, (iv) all stock options held by Mr. Whitten will remain outstanding for one year, (v) Mr. Whitten and his eligible dependents will receive subsidized COBRA coverage for up to 18 months, and (vi) Mr. Whitten became eligible to receive up to \$15,000 on or before September 1, 2013 for the cost of outplacement services. The letter also includes a customary release by Mr. Whitten of claims against the Company and its affiliates and a mutual commitment by the parties not to disparage each other.

In connection with the termination of Mr. LaBella's employment, we entered into a letter agreement dated October 5, 2012 pursuant to which (i) Mr. LaBella received a payment of \$115,456, (ii) Mr. LaBella will receive an aggregate of \$445,331 payable in twelve monthly installments commencing within 30 days following his resignation date, (iii) otherwise unvested equity awards held



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by Mr. LaBella became vested, (iv) all stock options held by Mr. LaBella will remain outstanding for one year, (v) Mr. LaBella and his eligible dependents will receive subsidized COBRA coverage for up to 12 months, and (vi) Mr. LaBella became eligible to receive up to \$15,000 on or before September 1, 2013 for the cost of outplacement services. The letter also includes a customary release by Mr. LaBella of claims against the Company and its affiliates and a mutual commitment by the parties not to disparage each other.

In connection with the termination of Mr. Tully's employment, we entered into a separation agreement dated July 26, 2012 pursuant to which Mr. Tully received the following severance benefits: (i) a lump sum payment of \$449,454.67, (ii) the continuation of health and certain other fringe benefits for up to eighteen months following December 1, 2012, and (iii) full vesting of outstanding equity awards held by Mr. Tully immediately prior to the December 1, 2012 that had not vested and were granted at least one (1) year prior to such date. All stock options held by Mr. Tully will remain outstanding for one year. Mr. Tully also became eligible to receive up to \$15,000 on or before August 20, 2013 for the cost of outplacement services. In addition, the separation agreement includes a general release of claims by Mr. Tully against the Company arising out of or related to Mr. Tully's employment with the Company and a mutual commitment by the parties not to disparage each other.

### **COMPENSATION COMMITTEE INTERLOCKS AND INSIDER PARTICIPATION**

The Compensation Committee is comprised entirely of independent directors and none of our executive officers served on the Compensation Committee or on the board of any company that employed any member of our Compensation Committee or our Board.

### **DIRECTOR COMPENSATION**

Our Board determines the compensation of our non-employee directors in conjunction with recommendations made by the Compensation Committee. The Compensation Committee evaluates the appropriate level and form of compensation for non-employee directors at least annually and recommends changes to our Board when appropriate. The Compensation Committee did not recommend any changes in compensation for our non-employee directors for fiscal 2012. Our board of directors is compensated through fees, grants of stock options and grants of restricted stock.

#### **Fees Earned or Paid in Cash**

During 2012, each non-employee director was paid an annual retainer fee of \$25,000, except for the Chairman of the Board, who was paid an annual fee of \$44,097, pro-rated for his period of service, which was less than the full year due to Mr. Hayden's appointment to Executive Chairman of the Company for the period from May 14, 2012 to September 9, 2012, and Mr. Altomari who was paid an annual retainer fee of \$6,250, pro-rated for his period of service. Mr. Whitcomb was also paid \$15,797, pro-rated for his period of service as our lead independent director, a role he assumed when Mr. Hayden was appointed Executive Chairman on May 14, 2012. The Chairman of each of the Compensation Committee and the Nominations and Governance Committee was paid an annual fee of \$10,000, and the Chairman of the Audit Committee was paid an annual fee of \$15,000. These annual fees were paid quarterly. In addition to these annual fees, each director received a general Board meeting fee of either \$1,000 (if attending by phone) or \$2,000 (if attending in person) with respect to each meeting they attend. With respect to each meeting of the Audit Committee, each director received \$1,500 for each meeting he attends, and with respect to each meeting of each of the Compensation Committee and the Nominations and Governance Committee, each director will receive \$1,000 for each meeting he attends.

Table of Contents**Grant of Restricted Stock Units**

During 2012, each non-employee director, except for the Chairman of the Board and Mr. Altomari, received an annual equity-based grant with a grant date value of \$35,000 in the form of RSUs with a one year vesting period from the date of the award, provided that the director attend at least 75% of the meeting of the Board. The annual equity-based grant for 2012 for each of the directors, other than the Chairman and Mr. Altomari, was 10,174 RSUs, which was based on the closing price of \$3.44 per share of our Common Stock on the Nasdaq Capital Market on January 12, 2012. The Chairman of the Board also received an annual equity-based grant with a grant date value of \$55,000 in the form of RSUs with a one year cliff vesting period from the date of the award, provided that he attends at least 75% of the Board meetings. The Chairman's annual equity-based grant for 2012 was 15,988 RSUs, which was based on the closing price of \$3.44 per share of our Common Stock on the Nasdaq Capital Market on January 12, 2012. Following his election to the Board, the Company made an equity-based grant to Mr. Altomari with a grant date value of \$14,582 in the form of RSUs with a one year cliff vesting period from the date of the award, provided that he attend at least 75% of the meetings of the Board. The equity-based grant for 2012 for Mr. Altomari was 4,327 RSUs, which was based on the closing price of \$3.37 per share of our Common Stock on the Nasdaq Capital Market on August 2, 2012. The RSU awards will be settled on vesting by the issuance of one share of Common Stock for each RSU.

The following table sets forth a summary of the compensation we paid to our non-employee directors in 2012.

	<b>Fees Earned or Paid in Cash(1)</b>	<b>Restricted Stock Units(2)(3)</b>	<b>Total</b>
Donald J. Hayden Jr.	\$ 53,097	\$ 55,000	\$ 108,097
Steinar J. Engelsen, M.D.	\$ 57,000	\$ 35,000	\$ 92,000
Richard S. Kollender	\$ 73,000	\$ 35,000	\$ 108,000
Melvin Sharoky, M.D.	\$ 65,000	\$ 35,000	\$ 100,000
Randall Whitcomb, M.D.	\$ 83,797	\$ 35,000	\$ 118,797
Al Altomari(4)	\$ 20,250	\$ 14,582	\$ 34,832

- (1) The amounts in this column reflect the actual fees earned and paid during fiscal 2012.
- (2) Reflects grant date fair values of RSUs granted during the fiscal year, calculated in accordance with FASB ASC Topic 718, except the assumptions of forfeitures is not made. See Note 10 of the consolidated financial statements in the Company's Form 10-K for fiscal year 2012 regarding assumptions underlying valuation of equity awards.
- (3) Each Director received 10,174 RSUs, except for the Chairman of the Board who received 15,988 RSUs and Al Altomari, who received 4,327 RSUs. These figures represent the number of outstanding stock awards each director had as of the end of 2012, except for Mr. Hayden, who in addition to his RSUs, also had 85,000 stock options outstanding as of the end of 2012, of which 21,250 were exercisable as of the end of 2012.
- (4) The figures for Mr. Altomari cover the period from the date of his election to the Board on August 2, 2012 until December 31, 2012.

**Director Compensation Changes for 2013**

At the end of 2012, the Compensation Committee, in accordance with its charter, undertook a review of our director compensation with the assistance of ExeQuity. Based on market data and ExeQuity's findings, the Compensation Committee determined and recommended to the Board, that a

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greater percentage of directors' compensation be equity-based and proposed a new compensation structure for directors. As a result, beginning in 2013, we implemented a new director compensation policy which discontinues cash payment to directors for meeting attendance and replaces them with equity-based compensation. Our directors will now receive an annual cash retainer fee of \$35,000, except for our Chairman of the Board who will receive an annual cash retainer fee of \$75,000. Each director will also receive an annual equity-based with a grant date value of \$60,000 in the form of RSUs that vest one year from the grant date, provided that the director attend at least 75% of the meetings of the Board. The lead independent director will also receive an annual cash retainer of \$25,000, the Audit Committee Chairman will also receive an annual cash retainer fee of \$15,000, and each of the Compensation Committee Chairman and the Nominating and Governance Chairman will receive an annual cash retainer fee of \$10,000. The Board believes these changes were necessary to further align our non-employee director compensation practices with the best interests of our shareholders. ExeQuity has also recommended, and the Board has agreed, that the total compensation to be paid to each director for the services noted above for 2013 will be comparable to the total compensation paid to each director for these same services in 2012.

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**PROPOSAL NO. 2**

**RATIFICATION OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

**Information Relative to Ratification of Independent Registered Public Accounting Firm**

The Audit Committee has designated Ernst & Young LLP, independent registered public accounting firm, as our independent registered public accounting firm for the fiscal year ending December 31, 2013. A representative of Ernst & Young LLP is expected to be present at the Annual Meeting and will have an opportunity to make a statement and respond to appropriate questions.

Ernst & Young LLP's principal function is to audit our consolidated financial statements and, in connection with that audit, to review certain related filings with the Securities and Exchange Commission and to conduct limited reviews of the consolidated financial statements included in each of our quarterly reports. The aggregate fees billed for each of the last two fiscal years for professional services rendered by Ernst & Young LLP, as well as information relating to the Audit Committee's pre-approval policies and procedures, are detailed in the "Audit Committee Report."

**Vote Not Required for Approval**

Shareholder ratification of our independent registered public accounting firm is not required under Virginia law, our Articles of Incorporation or our Bylaws. However, the Board is submitting the expected appointment of Ernst & Young to the shareholders for ratification as a matter of good corporate practice. In the event that a majority of the votes cast are against the ratification of Ernst & Young LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2013, the Audit Committee will consider the vote and the reasons therefor in future decisions on the selection of our independent registered public accounting firm.

**Recommendation**

**THE BOARD RECOMMENDS THAT YOU VOTE "FOR" THE RATIFICATION OF ERNST & YOUNG LLP AS OUR INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM.**

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**PROPOSAL NO. 3**

**RATIFICATION AND APPROVAL OF CERTAIN EQUITY COMPENSATION AWARDS  
PREVIOUSLY GRANTED TO CERTAIN EMPLOYEES AND DIRECTORS UNDER OUR  
2000 STOCK INCENTIVE PLAN**

**Introduction**

This proposal seeks ratification and approval by shareholders of certain equity compensation awards previously granted to certain employees and directors under our Amended and Restated 2000 Stock Incentive Plan, as amended (the "2000 Stock Incentive Plan").

As disclosed in our most recent Form 10-K, in connection with a recent review by us of equity compensation awards made by us under the 2000 Stock Incentive Plan, we determined that we had inadvertently exceeded the annual per-person sub-limits of 75,000 stock options and 12,500 performance shares per individual per calendar year set forth in the 2000 Stock Incentive Plan in connection with awards previously made to certain of our current and past officers and directors (the "Recipients"). The aggregate amount of Common Stock represented by these awards in excess of the per person annual sub-limits, which consisted of restricted stock, RSUs and stock options, is approximately 1.6 million shares (referred to as the "Excess Grants"). The Excess Grants included certain awards issued immediately following our business combination with Transave, awards negotiated with new hires pursuant to employment agreements or offers of employment, and certain other awards made subsequent to our 2011 one-for-ten reverse stock split. We have not exceeded the aggregate maximum share limit approved by shareholders under the 2000 Stock Incentive Plan (currently 3,925,000 shares of Common Stock), whether as a result of previously-issued awards or currently outstanding awards. Proposal 3 asks that you ratify and approve the Excess Grants.

**Additional Information**

On March 12, 2013, we notified Nasdaq of the Excess Grants. We believe that a decision by us to increase the annual sub-limits would have constituted an immaterial amendment to the 2000 Stock Incentive Plan, which amendment would not have required shareholder approval under applicable Nasdaq guidance. However, because the grant of certain awards exceeded the sub-limits applicable at the time the grants were made, it was possible that Nasdaq would conclude that we issued securities pursuant to the 2000 Stock Incentive Plan without shareholder approval in violation of Nasdaq Listing Rule 5635(c). In a March 13, 2013 letter to Nasdaq, we submitted a remediation and compliance plan, which we refer to as our remediation plan, to address the grants made in excess of the 2000 Stock Incentive Plan sub-limits. Among other items, our remediation plan conditions (1) the sale of the portion of any vested shares of restricted stock or RSUs or any shares received upon exercise of the vested portion of stock options, and (2) the continued vesting and exercise of the portion of stock options and RSUs issued to our current employees and directors in each case in excess of the 2000 Stock Incentive Plan's sub-limits on approval by shareholders of such portion of the affected grants.

Nasdaq took into account our remediation plan and, in connection therewith, each of our current employees and directors who currently hold Excess Grants have executed waivers providing that such employee's or director's right to exercise, transfer, and/or dispose of the Excess Grants (and any shares of Common Stock received upon grant, vesting, settlement or exercise of the Excess Grants) is conditioned upon shareholder ratification and approval of the Excess Grants and that such Excess Grants shall be deemed forfeited if shareholders do not ratify and approve their Excess Grants. However, none of the Excess Grants made to our prior employees or directors shall be deemed forfeited if shareholders do not ratify and approve such Excess Grants.

In this proposal, we ask that you ratify and approve all of the Excess Grants made to the Recipients. The following table shows the number of stock options, RSUs and shares of restricted stock

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held by our current employees and directors, which Excess Grants are subject to ratification and approval by shareholders:

Name and Position	Number of Stock Options or Performance Shares Granted in Excess of Sub-limits to Current Employees and Directors				
	Grant Date(s)	Number of Stock Options	Stock Option Exercise Price	Number of Restricted Stock Units	Number of Shares of Restricted Stock
Will Lewis <i>President and CEO</i>	9/10/2012	633,314	\$ 3.40		
	9/28/2012	186,170	\$ 4.55		
Andrew T. Drechsler <i>Chief Financial Officer</i>	11/7/2012	100,000	\$ 6.65		
Renu Gupta, M.D. <i>Executive Vice President of Development and Chief Medical Officer</i>	1/31/2011			43,300	
	12/21/2011	25,500	\$ 3.03		
Andrea Holtzman Drucker, J.D. <i>Senior Vice President, General Counsel, and Corporate Secretary</i>	7/18/2011			32,500	
Nicole Schaeffer <i>Senior Vice President, Human Resources and Corporate Services</i>	1/2/2013	10,000	\$ 6.96		
Walter Perkins, Ph.D. <i>Chief Technology Officer</i>	1/31/2011			9,200	
Steinar J. Engelsen, M.D. <i>Director</i>	5/20/2009				962
Donald Hayden, Jr. <i>Director</i>	12/21/2011	10,000	\$ 3.03		
	1/12/2012			3,488	
Melvin Sharoky, M.D. <i>Director</i>	5/20/2009				962
Randall W. Whitcomb, M.D. <i>Director</i>	5/20/2009				962
All current executive officers as a group		944,984		75,800	
All current directors who are not executive officers as a group		10,000		3,488	2,886
All employees, including all current officers who are not executive officers, as a group		10,000		9,200	



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In addition to the Excess Grants described above, the following table shows the number of stock options, RSUs and shares of restricted stock held by our former employees and directors, for which we are also seeking ratification and approval by shareholders:

Name and Position	Number of Stock Options or Performance Shares Granted in Excess of Sub-limits to Former Employees and Directors				
	Grant Date(s)	Number of Stock Options	Stock Option Exercise Price	Number of Restricted Stock Units	Number of Shares of Restricted Stock
Geoffrey Allan	5/29/2008				53,522
<i>Chairman of the Board, Chief Executive Officer and President</i>	3/31/2009				12,258
Douglas Farrar	5/29/2008				10,424
<i>Vice President, Insmed Therapeutic Proteins</i>					
Steve Glover	5/29/2008				16,385
<i>Chief Business Officer</i>					
Nicholas Gurreri	1/31/2011			27,800	
<i>Senior Vice President, Commercial Operations and Business Development</i>					
Glen Kelley	5/29/2008				10,424
<i>Vice President, Regulatory Affairs</i>					
Nicholas LaBella	1/31/2011			30,900	
<i>Chief Scientific Officer</i>					
Kevin Tully	5/29/2008				
<i>Executive Vice President and Chief Financial Officer</i>	1/31/2011			43,300	
Timothy Whitten	1/31/2011	24,200	\$ 5.90		
<i>President and Chief Executive Officer</i>	1/31/2011			117,700	
	12/21/2011	103,100			
Kenneth Condon	5/20/2009				962
<i>Director</i>					
Graham Crooke	5/20/2009				962
<i>Director</i>					
Denny Lanfear	5/20/2009				962
<i>Director</i>					
All former employees as a group					
		127,300		219,700	115,730
All former directors as a group					2,886

### **Why You Should Vote for Ratification of the Excess Grants**

The Board recommends that our shareholders ratify and approve all of the Excess Grants made to our prior and current officers and directors. Our executive officers and directors did not intend to receive awards in excess of the 2000 Stock Incentive Plan's sub-limits. We have not exceeded the aggregate maximum share limit approved by shareholders under the 2000 Stock Incentive Plan (currently 3,925,000 shares of Common Stock), whether as a result of previously-issued awards or currently outstanding awards. In fact, with respect to Mr. Lewis, Mr. Drechsler, Ms. Drucker, Dr. Gupta (with respect to her RSU grants) and Ms. Schaeffer, the Excess Grants were awarded in connection with their initial hire by us and the grants were agreed upon prior to the commencement of their employment with us. In addition, the Board believes, particularly at this very important time for the Company as we prepare for regulatory approvals and potential commercialization of ARIKACE, that appropriate equity incentives are very important to attract and retain the highest caliber of employees, to link incentive reward to Company performance, to encourage employee and director ownership in our Company and to align the interests of recipients to those of our shareholders.

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to ratify and approve the Excess Grants would result in a loss to us and shareholders of these benefits in respect of the Excess Grants and could require us to adopt an alternative compensation program, which may include the payment of cash compensation, or grant additional equity awards to replace the lost retention, alignment and other benefits to us from the Excess Grants. Any forfeitures resulting from a failure to ratify and approve the Excess Grants also may reduce the morale of the current employees and directors and may cause a more widespread reduction in employee morale, which could make it difficult for us to retain these and other qualified employees and to hire additional qualified employees in the future.

We are determined to try to ensure that this kind of error does not happen again. Accordingly, a special committee of the Board conducted the review of equity compensation awards made by us under the 2000 Stock Incentive Plan described above with the assistance of outside counsel and has begun to implement the remediation plan described in our recent Annual Report on Form 10-K.

**Summary of Excess Grants**

The following is a description of the material features of the Excess Grants. As noted above, the Excess Grants were granted pursuant to and are subject to all of the terms and conditions of our 2000 Stock Incentive Plan. The Excess Grants consisted of awards of stock options, restricted stock and restricted stock granted under the 2000 Stock Incentive Plan.

**Stock Options.** The Excess Grants awarded in the form of stock options include both non-qualified stock options and incentive stock options under Section 422 of the Code. The exercise price of these stock options equaled 100% of the fair market value of a share of our Common Stock on the applicable date of grant. The option exercise price must be paid in full either in cash or a cash equivalent acceptable to the plan administrator or by delivery of shares of Common Stock. Subject to applicable law, the exercise price may also be delivered to us by a broker pursuant to irrevocable instructions to the broker from the holder thereof. The stock options become exercisable in installments determined by the plan administrator at the time of grant and have a maximum term of ten years from the date of grant.

**Restricted Stock and Restricted Stock Units.** The Excess Grants awarded in the form of restricted stock and RSUs provide that the vesting and/or settlement of such awards will occur at such time and is subject to such terms and conditions as determined by the plan administrator at the time of grant or under criteria established by the plan administrator at the time of grant, which may include conditions based on continued employment, passage of time, attainment of age and/or service requirements, and /or satisfaction of performance conditions.

**Federal Income Tax Treatment**

The following discussion summarizes the material U.S. federal income tax consequences to us and the Recipients in connection with the Excess Grants under existing applicable provisions of the Code and the accompanying regulations. The discussion is general in nature and does not address issues relating to the income tax circumstances of any individual Recipient. The discussion is based on federal income tax laws in effect on the date of this Proxy Statement and is, therefore, subject to possible future changes in the law. The discussion does not address the consequences of state, local or foreign tax laws.

*Nonqualified Options* An employee will not recognize any income upon receipt of a nonqualified stock option, and we will not be entitled to a deduction for federal income tax purposes in the year of grant. Ordinary income will be realized by the holder at the time the nonqualified stock option is exercised and the shares are transferred to the employee. The amount of such taxable income, in the

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case of a nonqualified stock option, will be the difference, if any, between the option price and the fair market value of the shares on the date of exercise.

*Incentive Stock Options* An employee who receives an incentive stock option ("ISO") will not recognize any income for federal income tax purposes upon receipt of the ISO, and we will not realize a deduction for federal income tax purposes. The optionee generally will not be taxed upon exercise, but the difference between the fair market value of the stock on the date of exercise and the option exercise price is an item that may subject the optionee to the alternative minimum tax. If the optionee does not dispose of the ISO shares within two years from the date the option was granted or within one year after the shares were transferred to him on exercise of the option, then that portion of the gain on the sale of the shares that is equal to the difference between the sales price and the option exercise price will be treated as a long-term capital gain. We will not be entitled to a deduction either at the time the employee exercises the ISO or subsequently sells the ISO shares. However, if the employee sells the ISO shares within two years after the date the ISO is granted or within one year after the date the ISO is exercised, then the sale is considered a disqualifying sale, and the spread on exercise will be taxed as ordinary income. The balance of the gain will be treated as long- or short-term capital gain depending on the length of time the employee held the stock. If the shares decline in value after the date of exercise, the compensation income will be limited to the difference between the sale price and the amount paid for the shares. The tax will be imposed in the year the disqualifying sale is made. We will be entitled to a deduction equal to the ordinary income recognized by the employee.

With respect to both nonqualified stock options and ISOs, special rules apply if an employee uses shares already held by the employee to pay the exercise price or if the shares received upon exercise of the option are subject to a substantial risk of forfeiture by the employee.

*Restricted Stock* Employees receiving restricted stock will not recognize any income upon receipt of the restricted stock. Ordinary income will be realized by the holder at the time that the restrictions on transfer are removed or have expired. The amount of ordinary income will be equal to the fair market value of the shares on the date that the restrictions on transfer are removed or have expired. We will be entitled to a deduction at the same time and in the same amount as the ordinary income the employee is deemed to have realized. However, no later than 30 days after an employee receives the restricted stock, the employee may elect to recognize taxable ordinary income in an amount equal to the fair market value of the shares at the time of receipt. Provided that the election is made in a timely manner, when the restrictions on the shares lapse, the employee will not recognize any additional income. If the employee forfeits the shares to us, the employee may not claim a deduction with respect to the income recognized as a result of the election.

Generally, when an employee disposes of shares acquired under the Excess Grants, the difference between the sales price and his or her basis in such shares will be treated as long- or short-term capital gain or loss depending upon the holding period for the shares.

*Restricted Stock Units* Employees who are granted RSUs do not recognize income at the time of the grant. When the award vests or is paid, Recipients generally recognize ordinary income in an amount equal to the fair market value of the units at such time, and we will receive a corresponding deduction.

*Federal Income Tax Consequences to the Company* To the extent that a Recipient recognizes ordinary income in the circumstances described above, we will be entitled to a corresponding deduction provided that, among other things, the income meets the test of reasonableness, is an ordinary and necessary business expense, is not an "excess parachute payment" within the meaning of Section 280G of the Code and is not disallowed by the \$1,000,000 limitation on certain executive compensation under Section 162(m) of the Code.

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*Potential Limitation on Deductions* Special rules limit the deductibility of compensation paid to our Chief Executive Officer and to each of the next three most highly compensated executive officers, other than our Chief Financial Officer. Under Section 162(m), unless various conditions are met that enable compensation to qualify as "performance-based," the annual compensation paid to any of these specified executives will be deductible only to the extent that it does not exceed \$1,000,000. The Excess Grants will not qualify as "performance-based."

*Tax Withholding* To the extent required by applicable federal, state, local or foreign law, a Recipient will be required to satisfy, in a manner satisfactory to us, any withholding tax obligations that arise by reason of the award.

The ratification and approval of the Excess Grants requires the affirmative vote of a majority of the votes cast, in person or by proxy, at the Annual Meeting. **THE BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT YOU VOTE "FOR" RATIFICATION AND APPROVAL OF CERTAIN EQUITY COMPENSATION AWARDS PREVIOUSLY GRANTED TO CERTAIN EMPLOYEES AND DIRECTORS UNDER OUR 2000 STOCK INCENTIVE PLAN.**

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**PROPOSAL NO. 4**

**APPROVAL OF THE 2013 INCENTIVE PLAN**

**Introduction**

On April 17, 2013, the Board unanimously adopted and approved the 2013 Incentive Plan and is submitting the 2013 Incentive Plan to shareholders for their adoption and approval at the 2013 Annual Meeting. The Board believes our interests are best advanced by providing equity-based incentives to certain individuals responsible for our long-term success by encouraging such persons to remain in the service of the Company and to align the financial objectives of such individuals with those of our shareholders.

The Company currently administers its equity-based compensation programs under the Amended and Restated 2000 Stock Incentive Plan (the "2000 Stock Incentive Plan"). As of the Record Date, 455,583 shares remained available for issuance under the 2000 Stock Incentive Plan. Because the Company anticipates that its equity-based compensation needs will soon exceed the remaining shares available under the 2000 Stock Incentive Plan, the Board of the Company adopted the 2013 Incentive Plan.

The 2013 Incentive Plan, if approved, will provide for the issuance of 3,000,000 shares, plus any shares of Common Stock that were authorized for issuance under the 2000 Stock Incentive Plan that, as of the effective date of the 2013 Incentive Plan, remain available for issuance under the 2000 Stock Incentive Plan. As of the Record Date, this represents 10.9% of the Company's outstanding shares of Common Stock. Shares subject to outstanding awards under the 2000 Stock Incentive Plan that are cancelled, expired, forfeited or otherwise not issued under such awards (including as a result of being withheld to pay withholding taxes in connection with such awards or settled in cash) will also be added to the number of shares available under the 2013 Incentive Plan. If the 2013 Incentive Plan is approved, no additional awards will be granted under the 2000 Stock Incentive Plan.

**Items Considered By the Board in Connection With This Proposal**

Equity-based compensation is a vital part of our compensation program, for our named executive officers, our other key employees, and our non-employee directors. Equity-based compensation creates an ownership culture that rewards our executives for maximizing shareholder value over time and aligns the interests of our employees and directors with those of our shareholders. We have traditionally granted stock options to new hires in connection with their commencement of employment and stock options, as well as other forms of equity-based compensation, to key employees as part of their ongoing compensation packages. We believe that providing additional stock option grants beyond an initial new hire grant provides management with a strong link to long-term corporate performance and the creation of shareholder value, as well as providing continued retention via long-term and milestone driven vesting. In addition, we grant RSUs to non-employee directors annually as part of their compensation for service on the Board.

We anticipate making Company-wide semi-annual stock option grants. The Compensation Committee believes that a semi-annual grant cycle spreads the incentives of the stock option grant across a broader time horizon and may mitigate the impact of the historical volatility of our stock.

The Board currently intends that the 3,000,000 shares requested, along with the shares remaining under the 2000 Stock Incentive Plan, will be sufficient to fund the Company's semi-annual stock option grants to current employees as well as stock option grants to new hires for approximately the next 12 to 18 months, which it believes appropriate taking into account the current phase of the Company's development as it plans towards commercialization. In addition, as part of our on-going compensation analysis, the Compensation Committee reviewed total employee ownership and determined that it was below market. The Compensation Committee has taken steps to try to ensure grants for 2013 will be

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made at levels competitive with the market as we believe that providing competitive equity awards are critical in attracting and retaining talent as we progress towards commercialization. The increase in the shares available for equity awards is necessary to provide us with the ability to make grants at these market competitive levels.

In determining the appropriate number of shares to request, the Board considered a dilution and overhang analysis prepared by ExeQuity, the Compensation Committee's independent compensation consultant. The ExeQuity analysis compared our ISS burn rate percentage, our overhang percentage, and our run rate percentage to our 2013 peer group, which was formed during January 2013 after our Compensation Committee reevaluated our 2012 peer group given increases in our market capitalization and the Company's increased focus on its preparations for commercialization. In summary, with recommendations from ExeQuity, the Compensation Committee removed six companies, including Callisto Pharmaceuticals, CEL-SCI Corporation, Neuralstem, Inc., Northwest Biotherapeutics, Inc., Rexhn Pharmaceuticals, Inc., and Ventrus Biosciences, Inc., added back five companies that were included in our 2011 peer group, including Celldex Therapeutics, Curis, Inc., Dyax Corp, Sunesis Pharmaceuticals, Inc., and Vical Incorporated, and added one new company, XenoPort, Inc. The Compensation Committee intends to continue to review and revise our peer group at least annually in an effort to ensure it continues to reflect companies of similar size, market capitalization and stage of development. The table below depicts our 2013 Peer Group:

Aegerion Pharmaceuticals, Inc	Curis, Inc.	SIGA Technologies, Inc.
Agenus Inc.	Discovery Laboratories, Inc.	Sunesis Pharmaceuticals, Inc.
Amicus Therapeutics, Inc	Dyax Corp.	Trius Therapeutics, Inc.
ArQule Inc.	Immunomedics, Inc.	Vical Incorporated
Celldex Therapeutics	Keryx Biopharmaceuticals, Inc	XenoPort, Inc.
Celsion Corporation	MAP Pharmaceuticals, Inc.	Zalicus, Inc.

ExeQuity did not make a recommendation regarding the number of additional shares to request with respect to the 2013 Incentive Plan. When approving the 2013 Incentive Plan, the Compensation Committee reviewed preliminary figures that included:

the Company's ISS burn rate percentage, which is equal to the total number of equity awards the Company granted in a fiscal year (adjusted by a multiplier for full value awards based on 200-day volatility), which is then divided by the weighted average common stock outstanding during the year,

the Company's simple overhang percentage, which is equal to the total number of equity awards outstanding plus the total number of shares available for grant under the Company's equity plans, each as of the end of the most recent fiscal year divided by total Common Stock outstanding at the end of the year, and

the Company's run rate percentage, which is equal to the total number of equity awards granted by the Company during a year divided by the weighted average common stock outstanding during the most recent fiscal year.

The Company's three-year average ISS burn rate percentage, at the time the Board approved the 2013 Incentive Plan, was approximately 5.0%, which is higher than the median three-year average ISS burn rate percentage of 3.7% for the Company's 2013 peer group. This higher burn rate was primarily due to the stock option grants made to Mr. Lewis in connection with his hire and our registered direct public offering in September 2012 (see Proposal 3, "Ratification and Approval of Certain Equity Compensation Awards Previously Granted to Certain Employees and Directors Under Our 2000 Stock Incentive Plan" included in this Proxy Statement for additional information regarding this and other Excess Awards previously granted to employees and directors). The Company's simple overhang percentage as of the end of 2012 was 8.8%, which was well below the median simple overhang of the

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peer group of 19.7%. The Company's three-year average run rate percentage, at the time the Board approved the 2013 Incentive Plan, was 3.4%, which equals the median three-year average run rate percentage of 3.4% for the Company's 2013 peer group. If the 2013 Incentive Plan is approved, the Company's simple overhang percentage would increase to 18.3%, which is comparable to the median simple overhang percentage of 19.7% for the Company's 2013 peer group. Our Compensation Committee intends to track our annual run rate percentage, as well as our dilution and overhang levels, in order to track the dilutive effect that equity grants have on our current shareholders and to evaluate the risks and benefits of issuing equity-based awards under the 2013 Incentive Plan.

**Why You Should Vote for the 2013 Incentive Plan**

The Board recommends that our shareholders approve the 2013 Incentive Plan because it believes appropriate equity incentives are important to attract and retain the highest caliber of employees, to link incentive reward to Company performance, to encourage employee and director ownership in our Company, and to align the interests of participants to those of our shareholders. The approval of the 2013 Incentive Plan will enable us to continue to provide such incentives.

If the 2013 Incentive Plan is not approved, we will be permitted to continue to grant awards under the 2000 Stock Incentive Plan up to the 455,583 shares that remained available for issuance as of the Record Date. This limited number of shares will not permit us to make the grants of equity-based compensation that we believe are necessary to attract and retain key employees and could negatively impact our shareholders.

**Promotion of Good Corporate Governance Practices**

The Board of Directors believes the use of share-based incentive awards promotes best practices in corporate governance by aligning participants' interests with maximizing shareholder value. Specific features of the 2013 Incentive Plan that are consistent with good corporate governance practices include, but are not limited to:

1. options and stock appreciation rights generally may not be granted with exercise prices lower than the fair market value of the underlying shares on the grant date;
2. there can be no repricing of options or stock appreciation rights without shareholder approval, either by canceling the award in exchange for cash or a replacement award at a lower price or by reducing the exercise price of the award, other than in connection with a change in our capitalization;
3. dividends and dividend equivalents may not be paid during the performance period with respect to unearned performance-based awards of restricted stock or RSUs; and
4. awards are not transferrable except by will or the laws of descent and distribution.

**Section 162(m) of the Code**

The Board believes that it is in our best interests and the best interests of our shareholders to provide for an equity incentive plan under which compensation awards made to our executive officers can qualify for deductibility by us for federal income tax purposes. Accordingly, the 2013 Incentive Plan has been structured in a manner such that we may grant certain awards under it that have the potential to satisfy the requirements for "performance-based" compensation within the meaning of Section 162(m) of the Code, subject to our ability to comply with the requirements of Section 162(m). In general, under Section 162(m), in order for us to be able to deduct compensation in excess of \$1,000,000 paid in any one year to our Chief Executive Officer or any of our three other most highly compensated executive officers (other than our Chief Financial Officer), such compensation must qualify as "performance-based." One of the requirements of "performance-based" compensation for



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purposes of Section 162(m) is that the material terms under which the compensation is to be paid, including the performance goals under which compensation may be paid, be disclosed to and approved by majority vote of our shareholders. If we do not satisfy the disclosure and approval requirement or the other requirements of Section 162(m), we may be unable to deduct compensation in excess of the \$1,000,000 threshold. For purposes of Section 162(m), the material terms include (i) the employees eligible to receive compensation, (ii) a description of the business criteria on which the performance goal is based and (iii) the maximum amount of compensation that can be paid to an employee under the performance goal. With respect to the various types of awards under the 2013 Incentive Plan, each of these aspects is discussed below, and shareholder approval of the 2013 Incentive Plan will be deemed to constitute approval of each of these aspects of the 2013 Incentive Plan for purposes of the approval requirements of Section 162(m).

**Key Data**

The following table includes information regarding all of our outstanding equity awards and shares available for future awards under our equity plans and equity award agreements as of March 28, 2013 (and without giving effect to this Proposal No. 4):

Total shares underlying all outstanding options	2,027,919
Weighted average exercise price of outstanding options	\$4.40
Weighted average remaining contractual life of outstanding options	7.90 Years
Total shares underlying all outstanding and unvested restricted share and restricted share unit awards	200,452
Total shares currently available for grant	455,583

**2013 Incentive Plan Summary**

The following is a description of the material features of the 2013 Incentive Plan. The complete text of the 2013 Incentive Plan is attached hereto as Appendix A to this Proxy Statement. The following discussion is qualified in all respects by reference to Appendix A. The term "employees" in the following discussion is used to refer to officers and directors and other employees of the Company and its affiliates.

**Purpose and Eligibility**

The purpose of the 2013 Incentive Plan is to advance the interests the Company by aligning the individual interests of employees, officers, non-employee directors and other service providers, in each case who are selected to be participants to those of Company shareholders and by providing such individuals with an incentive to continue working toward and contributing to the success and progress of the Company. Employees of the Company and its affiliates, members of the Board, and all other non-employee advisors or service providers will be eligible to be considered for the grant of awards under the 2013 Incentive Plan. As of the Record Date, approximately 6 nonemployee directors, 5 executive officers and 42 other employees of the Company were so eligible.

**Shares Subject to the 2013 Incentive Plan and to Awards**

The maximum number of shares of Common Stock that may be issued pursuant to awards granted under the 2013 Incentive Plan is 3,000,000, plus any shares of Common Stock that were authorized for issuance under the 2000 Stock Incentive Plan that, as of May 23, 2013, remain available for issuance under the 2000 Stock Incentive Plan (not including any shares that are subject to, as of May 23, 2013, outstanding awards under the 2000 Stock Incentive Plan), and subject to adjustments to prevent dilution. Shares of Common Stock subject to outstanding awards under the 2000 Stock Incentive Plan as of May 23, 2013 (such awards the "2000 Stock Incentive Plan Awards") that, after May 23, 2013, are

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canceled, expired, forfeited or otherwise not issued under a 2000 Stock Incentive Plan Award (including as a result of being withheld to pay withholding taxes in connection with any such awards) or settled in cash shall be added to the number of shares of Common Stock issuable under the 2013 Incentive Plan.

Shares of Common Stock issued under the 2013 Incentive Plan may either be authorized and unissued shares or previously issued shares acquired by the Company, including shares purchased in the open market. To the extent that an award terminates, expires, or lapses for any reason, or an award is settled in cash without the delivery of shares to the participant, then any shares of common stock subject to the award shall again be available for the grant of an award pursuant to the 2013 Incentive Plan. Any shares of common stock tendered or withheld to satisfy the grant or exercise price or tax withholding obligation pursuant to any award (or any 2000 Stock Incentive Plan Award) shall again be available for the grant of an award pursuant to the 2013 Incentive Plan. The payment of dividend equivalents in cash in conjunction with any outstanding awards shall not be counted against the shares available for issuance under the 2013 Incentive Plan.

The aggregate number of shares of Common Stock that may be issued pursuant to the exercise of incentive stock options granted under the 2013 Incentive Plan shall not exceed 3,000,000, plus any shares of Common Stock that were authorized for issuance under the 2000 Stock Incentive Plan that, as of the date of the Annual Meeting (May 23, 2013) and proposed approval of the 2013 Incentive Plan, remain available for issuance under the 2000 Stock Incentive Plan. The aggregate number of shares of Common Stock subject to awards granted under the 2013 Incentive Plan during any calendar year to any one participant may not exceed 1,500,000 (not including any tandem stock appreciation rights as described below). The maximum cash amount payable pursuant to the portion of an incentive bonus granted in any calendar year to any participant that is intended to satisfy the requirements for "performance-based compensation" under Section 162(m) of the Code shall not exceed \$5,000,000.

Awards granted or shares issued by the Company in assumption of, or in substitution or exchange for, awards previously granted, or the right or obligation to make future awards, by a company acquired by the Company or with which the Company combines shall not reduce the shares authorized for issuance under the 2013 Incentive Plan or authorized for grant to a participant during a calendar year. In addition, in the event that a company acquired by the Company, or with which the Company combines, has shares available under a pre-existing equity compensation plan, the shares available for grant pursuant to such pre-existing plan (as adjusted in connection with such acquisition or combination) may be used for awards under the 2013 Incentive Plan and will not reduce the shares authorized for issuance under the 2013 Incentive Plan, provided that the awards using such available shares will not be made after the date awards could have been made under the terms of the pre-existing plan and will only be made to individuals who were employees of such acquired or combined company before such acquisition or combination.

**Administration**

The 2013 Incentive Plan will be administered by the Compensation Committee (the "Committee"), or, in the absence of the Committee, the Board itself. Any power of the administrator may also be exercised by the Board, except to the extent that the grant or exercise of such authority would cause an award intended to qualify as performance-based compensation under Section 162(m) of the Code not to qualify for such treatment. To the extent that any permitted action taken by the Board conflicts with action taken by the administrator, the Board action will control. The Committee may by resolution authorize one or more officers of the Company to perform any or all things that the administrator is authorized and