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CREE INC
Form DEF 14A
September 22, 2004
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SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

SCHEDULE 14A INFORMATION

Proxy Statement Pursuant to Section 14(a) of the Securities Exchange Act of 1934

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

- Preliminary Proxy Statement
- Confidential, for use of the Commission Only (as permitted by Rule 14a-6(e)(2))
- Definitive Proxy Statement
- Definitive Additional Materials
- Soliciting Material Pursuant to Rule 14a-11(c) or Rule 14a-12

CREE, INC.

(Name of Registrant as Specified In Its Charter)

N/A

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

Payment of Filing Fee (Check the appropriate box):

No fee required.

Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

- 1) Title of each class of securities to which transaction applies: _____
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- 1) Amount Previously Paid: _____
- 2) Form, Schedule or Registration Statement No.: _____
- 3) Filing Party: _____
- 4) Date Filed: _____

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NOTICE OF ANNUAL MEETING OF SHAREHOLDERS

To the Shareholders:

The 2004 Annual Meeting of Shareholders of Cree, Inc. (the Company) will be held at the offices of the Company at 4425 Silicon Drive, Durham, North Carolina 27703, on Thursday, November 4, 2004, at 10:00 a.m. local time, to consider and vote upon the following matters and to transact such other business as may be properly brought before the meeting:

Proposal No. 1 Election of seven directors

Proposal No. 2 Approval of the 2004 Long-Term Incentive Compensation Plan

Proposal No. 3 Ratification of the appointment of Ernst & Young LLP as the Company's independent auditors for the fiscal year ending June 26, 2005

All shareholders are invited to attend the meeting in person. Only shareholders of record at the close of business on September 7, 2004 are entitled to notice of and to vote at the meeting.

By order of the Board of Directors,

Adam H. Broome

Secretary

Durham, North Carolina

September 17, 2004

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IMPORTANT: Whether or not you plan to attend the meeting in person, please submit voting instructions for your shares promptly using the directions on your proxy card to vote by one of the following methods: (1) by telephone, by calling the toll-free telephone number printed on your proxy card; (2) over the Internet, by accessing the website address printed on your proxy card; or (3) by marking, dating and signing your proxy card and returning it in the accompanying postage-paid envelope.

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CREE, INC.

PROXY STATEMENT

MEETING INFORMATION

The Board of Directors of Cree, Inc. (the Company) is asking for your proxy for use at the 2004 Annual Meeting of Shareholders and any adjournments of the meeting. The meeting will be held at the Company's offices at 4425 Silicon Drive, Durham, North Carolina 27703, on Thursday, November 4, 2004, at 10:00 a.m. local time, to conduct the following business and such other business as may be properly brought before the meeting: (1) election of seven directors; (2) approval of the 2004 Long-Term Incentive Compensation Plan; and (3) ratification of the appointment of Ernst & Young LLP as the Company's independent auditors for the fiscal year ending June 26, 2005.

The Board of Directors recommends that you vote FOR the election of the director nominees listed in this proxy statement, FOR approval of the 2004 Long-Term Incentive Compensation Plan and FOR ratification of the appointment of Ernst & Young LLP as the Company's independent auditors for the fiscal year ending June 26, 2005.

The Company intends to mail its 2004 Annual Report, this proxy statement and the accompanying proxy card to shareholders beginning on or about September 23, 2004. The annual report and proxy statement will also be available on the Internet at www.cree.com/annualmeeting. The annual report is not part of the Company's proxy soliciting materials.

VOTING PROCEDURES

Who Can Vote

Only shareholders of record at the close of business on September 7, 2004 are entitled to vote at the meeting and any adjournments of the meeting. At that time there were 73,829,873 shares of the Company's common stock outstanding, each of which is entitled to one vote on each matter submitted to a vote at the meeting. The common stock is the only class of securities of the Company having the right to vote at the meeting.

How You Can Vote

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You may vote shares by proxy or in person using one of the following methods:

Voting by Telephone. You can vote using the directions on your proxy card by calling the toll-free telephone number printed on the card. The deadline for voting by telephone is Wednesday, November 3, 2004, at 11:59 p.m. Eastern time. If you vote by telephone you need not return your proxy card.

Voting by Internet. You can vote over the Internet using the directions on your proxy card by accessing the website address printed on the card. The deadline for voting over the Internet is Wednesday, November 3, 2004 at 11:59 p.m. Eastern time. If you vote over the Internet you need not return your proxy card.

Voting by Proxy Card. You can vote by completing and returning your signed proxy card. To vote using your proxy card, please mark, date and sign the card and return it by mail in the accompanying postage-paid envelope. You should mail your signed proxy card sufficiently in advance for it to be received by Wednesday, November 3, 2004.

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Voting in Person. You can vote in person at the meeting if you are the record owner of the shares to be voted. You can also vote in person at the meeting if you present a properly signed proxy that authorizes you to vote shares on behalf of the record owner. If your shares are held by a broker, bank, custodian or other nominee, to vote in person at the meeting you must present a letter or other proxy appointment, signed on behalf of the broker or nominee, granting you authority to vote the shares.

How You Can Revoke Your Proxy and Change Your Vote

You can revoke your proxy and change your vote by: (1) attending the meeting and voting in person; (2) delivering written notice of revocation of your proxy to the Secretary at any time before voting is closed; (3) timely submitting another signed proxy card bearing a later date; or (4) timely submitting new voting instructions by telephone or over the Internet as described above.

How Your Proxy Will Be Voted

If you timely submit your proxy by telephone, over the Internet or by proxy card as described above and have not revoked it, your shares will be voted or withheld from voting in accordance with the voting instructions you gave. If you timely submit your proxy without giving contrary voting instructions, your shares will be voted **FOR** election of the director nominees listed in this proxy statement, **FOR** approval of the 2004 Long-Term Incentive Compensation Plan and **FOR** ratification of the appointment of Ernst & Young LLP as the Company's independent auditors for the fiscal year ending June 26, 2005.

How You Can Vote Shares Held by a Broker or Other Nominee

If your shares are held by a broker, bank, custodian or other nominee, you may have received a voting instruction form with this proxy statement instead of a proxy card. The voting instruction form is provided on behalf of the broker or other nominee to permit you to give directions to the broker or nominee on how to vote your shares. Please refer to the voting instruction form or contact the broker or nominee to determine the voting methods available to you.

Quorum Required

A quorum must be present at the meeting before business can be conducted. A quorum will be present if a majority of the shares entitled to vote are represented in person or by proxy at the meeting. Shares represented by a proxy with instructions to withhold authority to vote or to abstain from voting on any matter will be considered present for purposes of determining the existence of a quorum. Shares represented by a proxy as to which a broker, bank, custodian or other nominee has indicated that it does not have discretionary authority to vote on any matter (sometimes referred to as a broker non-vote) will also be considered present for purposes of determining the existence of a quorum.

Vote Required

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Directors will be elected by a plurality of the votes cast. Thus the seven nominees who receive the most votes will be elected to fill the available positions. Shareholders do not have the right to vote cumulatively in electing directors. Withholding authority in your proxy to vote for a nominee will result in the nominee receiving fewer votes.

The proposed 2004 Long-Term Incentive Compensation Plan and ratification of the appointment of Ernst & Young LLP as independent auditors for fiscal 2005 will be approved if the votes cast for approval exceed the votes cast against approval. Abstentions and broker non-votes will not be counted for purposes of determining whether these proposals received sufficient votes for approval.

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The graph below compares, for the five-year period ended June 27, 2004, the cumulative total return of the Company's common stock at each fiscal year end with a market index based on The Nasdaq Stock Market and an industry index based on Nasdaq-traded stocks of electronic components businesses. The market index is the Nasdaq Stock Market - U.S. Companies and the industry index is the Nasdaq Electronic Components. The graph assumes an investment of \$100 on June 27, 1999 in the Company's common stock and in each index and also assumes the reinvestment of all dividends during the period shown.

*Comparison of Five-Year Cumulative Total Return**Cree, Inc. Common Stock, Nasdaq Stock Market Index and**Nasdaq Electronic Components Index*

Performance Graph Data	June 1999	June 2000	June 2001	June 2002	June 2003	June 2004
Cree, Inc. Common Stock	\$ 100	\$ 478	\$ 133	\$ 79	\$ 99	\$ 132
Nasdaq Stock Market (U.S.)	\$ 100	\$ 193	\$ 69	\$ 58	\$ 56	\$ 76
Nasdaq Electronic Components	\$ 100	\$ 239	\$ 97	\$ 54	\$ 60	\$ 78

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All seven of the persons nominated for election to the Board of Directors at the annual meeting are currently serving as directors of the Company. Mr. William J. O'Meara, who has served on the Board since 2000, is not standing for re-election. The Company is not aware of any nominee who will be unable or will decline to serve as a director. If a nominee becomes unable or declines to serve, the accompanying proxy may be voted for a substitute nominee, if any, designated by the Board of Directors. The term of office of each person elected as a director will continue until the later of the next annual meeting of shareholders or until such time as his successor has been duly elected and qualified.

The following table lists the nominees for election and information about each.

Name	Age	Principal Occupation and Background	Director Since
F. Neal Hunter	42	Mr. Hunter, one of the Company's founders, has served as Chairman of the Board of Directors since 1995 and as a member of the Board of Directors since the Company's inception in 1987. He was the Chief Executive Officer of the Company from August 1994 to June 2001 and President from 1994 to 1999. Prior to 1994, Mr. Hunter served as General Manager for the Company's optoelectronic products business and as Secretary and Treasurer.	1987
Charles M. Swoboda	37	Mr. Swoboda has served as the Company's Chief Executive Officer since June 2001, as a member of the Board of Directors since October 2000 and as President since January 1999. He was Chief Operating Officer of the Company from 1997 to June 2001 and Vice President for Operations from 1997 to 1999. Prior to his appointment as Chief Operating Officer, Mr. Swoboda served as Operations Manager from 1996 to 1997, as General Manager of the Company's former subsidiary, Real Color Displays, Incorporated, from 1994 to 1996 and as LED Product Manager from 1993 to 1994. He was previously employed by Hewlett-Packard Company.	2000
John W. Palmour, Ph.D.	43	Dr. Palmour, one of the Company's founders, has been a member of the Board of Directors since October 1995 and has served as the Company's Director of Advanced Devices since 1995 and as an Executive Vice President since August 2002. As Executive Vice President for Advanced Devices, Dr. Palmour is responsible for all aspects of the Company's wide bandgap RF, microwave and power switching device businesses and also manages the Company's contract research programs. He previously served on the Board of Directors from 1992 to 1993.	1995
Dolph W. von Arx	70	Mr. von Arx has been a member of the Board of Directors since October 1991 and is the former Chairman, President and Chief Executive Officer of Planters Lifesavers Company, an affiliate of RJR Nabisco, Inc. Since his retirement from Planters Lifesavers Company in 1991, Mr. von Arx has served as non-executive Chairman of Morrison Restaurants Inc., a publicly held family dining business, from 1996 to 1998, and is currently a director of Ruby Tuesday, Inc. and Northern Trust of Florida Corp.	1991

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Name	Age	Principal Occupation and Background	Director Since
James E. Dykes	66	Mr. Dykes has served on the Board of Directors since January 1992. He was formerly President and Chief Executive Officer of Signetics Company, a semiconductor manufacturer and wholly-owned subsidiary of North American Philips Corporation, from 1989 until his retirement in 1993, and from 1987 to 1988 served as the first President and Chief Executive Officer of Taiwan Semiconductor Manufacturing Company Ltd., a semiconductor foundry.	1992
Robert J. Potter, Ph.D.	71	Dr. Potter has served on the Board of Directors since April 2001. He is currently President and Chief Executive Officer of R. J. Potter Company, a business consulting firm based in Irving, Texas. Prior to establishing R. J. Potter Company, from 1987 to 1990, Dr. Potter was President and Chief Executive Officer of Datapoint Corporation, a producer of local area networking and video conferencing products. He held senior management positions in other information technology companies, including Nortel Networks Corporation where he served as Group Vice President responsible for the customer premises telecommunications equipment business. Previously, he was President of Xerox's Office Systems Division. He is currently a director of Molex Incorporated and Zebra Technologies Corporation.	2001
Harvey A. Wagner	63	Mr. Wagner has served on the Board of Directors since February 2004. He is currently Acting President and Chief Executive Officer and a member of the Board of Directors of Quovadx, Inc., a global software and services company. Prior to joining Quovadx, Mr. Wagner served as Executive Vice President and Chief Financial Officer of Mirant Corporation, an energy company, from January 2003 to April 2004, and as Executive Vice President of Finance, Secretary, Treasurer, and Chief Financial Officer of Optio Software, Inc., a software provider, from February 2002 to December 2002. From May 2001 to January 2002, he performed independent consulting services for various corporations. He was Chief Financial Officer, General Manager, and Chief Operating Officer for PaySys International, Inc., a provider of financial payment processing applications, from December 1999 to April 2001. He also served as Executive Vice President of Finance and Administration and Chief Financial Officer for Premiere Technologies, Inc. from April 1998 to September 1999.	2004

The Board of Directors recommends shareholders

vote FOR election of the nominees named above.

Retiring Director

William J. O Meara	67	Mr. O Meara, who has served on the Board of Directors since October 2000, is not standing for re-election. He previously served as President and Chief Executive Officer of C-Cube Microsystems, Inc., a semiconductor company supplying products for digital video applications, until his retirement in 1995 and thereafter served as its Vice Chairman until 1997. Before joining C-Cube Microsystems Mr. O Meara was Chairman, Chief Executive Officer and President of Headland Technology, Inc., an entity affiliated with LSI Logic Corporation, a semiconductor company he co-founded in 1981, and served as Vice President of Worldwide Sales and Marketing for LSI Logic. Mr. O Meara also served as a member of the Board of Directors of Cisco Systems, Inc. from 1987 to 1993.	2000
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Executive Officers

Mr. Hunter, Mr. Swoboda and Dr. Palmour serve as both executive officers of the Company and members of the Board of Directors. The executive officers of the Company also include Cynthia B. Merrell (age 43), who has served as Chief Financial Officer and Treasurer of the Company since 1998 and previously served as the Company's Controller from 1996 to 1998 after joining the Company in 1996. Her prior financial experience includes service in various capacities with The Times Mirror Company, Tropicana Products, Inc. and an international public accounting firm. She is licensed as a certified public accountant in the state of Florida.

Board Composition and Independence of Directors

The size of the Board of Directors was fixed at nine members in 1988 by shareholder action pursuant to the Company's Bylaws. Generally only seven or eight persons have served on the Board at any one time. Mr. O'Meara is not standing for re-election and only seven persons have been nominated for election at the annual meeting. Under the rules of the Securities and Exchange Commission, the accompanying proxy cannot be voted for more than seven nominees.

A majority of the Board of Directors must be comprised of independent directors for the Company to comply with the listing requirements of The Nasdaq Stock Market, Inc. (Nasdaq). The Board has determined that five of the present directors Messrs. Dykes, von Arx, O'Meara, Potter and Wagner are each an independent director within the meaning of the applicable Marketplace Rules of Nasdaq. Of the seven nominees proposed for election at the annual meeting, four of the nominees Messrs. Dykes, von Arx, Potter and Wagner are independent directors.

Attendance at Meetings

The Board of Directors held eight meetings during the fiscal year ended June 27, 2004. Each director attended or participated in 75% or more of all meetings of the Board of Directors held in fiscal 2004 during the period he served as a director. Each director also attended or participated during the year in 75% or more of all meetings of committees on which he served that were held during the period of his service.

The Company expects all directors to attend each annual meeting of shareholders absent good reason. All directors then holding office attended the 2003 Annual Meeting of Shareholders.

Standing Committees

The Board has three standing committees: the Audit Committee, the Governance and Nominations Committee and the Compensation Committee. Each of these committees operates under a written charter adopted by the Board and is composed solely of independent directors. Copies of the committee charters are reproduced in the appendices to this proxy statement. The Executive Committee, which was previously a standing committee of the Board, was dissolved in August 2004. The following is a brief description of the responsibilities of each of the existing standing committees and their composition.

Audit Committee

The Audit Committee is appointed by the Board to oversee the accounting and financial reporting processes of the Company and audits of the Company's financial statements. The responsibilities of the Audit Committee include acting on the Board's behalf in providing oversight with respect to: (i) the quality and integrity of the Company's financial statements and internal accounting and financial controls; (ii) all audit, review and attest services relating to the Company's financial statements and internal controls, including the appointment, compensation, retention and oversight of the work of the auditors engaged to provide audit services to the Company; and (iii) the Company's compliance with legal and regulatory requirements.

The members of the Audit Committee are Messrs. Wagner, Dykes, von Arx, O'Meara and Potter. The Board has determined that all members of the Committee are independent directors within the meaning of the

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applicable Nasdaq Marketplace Rules, including the special independence requirements applicable to Audit Committee members. Mr. Wagner is Chairman of the Audit Committee and has served in that capacity since August 2004, when he succeeded Mr. von Arx, who had served as Chairman since fiscal 2001. The Board has determined that Mr. Wagner is an audit committee financial expert as defined in Item 401 of Regulation S-K of the Securities and Exchange Commission. During fiscal 2004, the Audit Committee held nine meetings.

Governance and Nominations Committee

The Governance and Nominations Committee is appointed by the Board to assist the Board in fulfilling its responsibilities to shareholders by: (i) identifying individuals qualified to become directors and selecting, or recommending that the Board select, the candidates for all directorships to be filled by the Board or by the shareholders; (ii) developing and recommending to the Board corporate governance principles for the Company; and (iii) otherwise taking a leadership role in shaping the corporate governance of the Company.

The members of the Governance and Nominations Committee are Messrs. von Arx, Dykes, O Meara, Wagner and Potter. The Board has determined that all members of the Committee are independent directors within the meaning of the applicable Nasdaq Marketplace Rules. Mr. von Arx is Chairman of the Governance and Nominations Committee and has served in that capacity since August 2004. The Governance and Nominations Committee charter establishes a policy with regard to the consideration of director candidates recommended by shareholders and in accordance with that policy the Committee will consider written nominations properly submitted by shareholders. For a description of the policy regarding nominations submitted by shareholders see Procedures for Director Nominations and 2005 Annual Meeting of Shareholders below. The Governance and Nominations Committee was established in May 2004 and held no meetings during fiscal 2004. The Compensation Committee served as the nominating committee for evaluating and nominating candidates for election as directors before the Governance and Nominations Committee was established.

Compensation Committee

The Compensation Committee is appointed by the Board to assist the Board in discharging its overall responsibility relating to executive and director compensation and to oversee and report to the Board as appropriate on the Company's compensation policies, programs and plans, including its stock-based compensation programs. The Compensation Committee determines the compensation of the chief executive officer, approves compensation of all other executive officers, oversees compensation of other senior members of the management team, administers the Company's stock-based compensation programs and recommends compensation for non-employee directors to the Board for approval.

The members of the Compensation Committee are Messrs. Dykes, von Arx, O Meara, Wagner and Potter. The Board has determined that all members of the Committee are independent directors within the meaning of the applicable Nasdaq Marketplace Rules. Mr. Dykes is Chairman of the Compensation Committee and has served in that capacity since 1992. During fiscal 2004, the Compensation Committee held four meetings. The Compensation Committee also often takes action by unanimous written consent in lieu of holding a meeting.

Compensation of Directors

Directors who are also employed by the Company are not separately compensated for their service on the Board. Non-employee directors are compensated for Board service through a combination of cash meeting fees and grants of non-qualified stock options to purchase shares of the Company's common stock. The Company also reimburses directors for expenses incurred in serving as a director.

The Company grants each continuing non-employee director annually an option corresponding to the term of service following election as a director at the annual meeting of shareholders. Non-employee directors appointed to fill a vacancy between annual meetings of shareholders are generally granted an option that corresponds to the remaining term of service before the next annual meeting. The exercise price of all grants is

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equal to the fair market value on the grant date, vesting of the option is subject to continued service to the Company and the maximum term of the option is seven years. The options generally vest during the term of service as a director following election, vesting in equal increments on the last day of each calendar quarter following election or, if earlier, upon the election of directors at the next annual meeting. With the exception of Mr. Wagner, each non-employee director presently serving on the Board was granted, in October 2003, an option to purchase 16,000 shares of common stock at an exercise price of \$19.88 per share, the closing market price on the grant date. The option terms provided for vesting in equal increments on the last day of each calendar quarter following election as a director at the 2003 Annual Meeting or, if earlier, upon the election of directors at the 2004 Annual Meeting. Upon election to the Board in February 2004, Mr. Wagner was granted an option to purchase 12,000 shares of common stock at an exercise price of \$24.33 per share, the closing market price on the grant date. The option terms provided for vesting in equal increments on the last day of each calendar quarter following election as a director or, if earlier, upon the election of directors at the 2004 Annual Meeting.

For Board meetings, non-employee directors are paid \$2,500 for each meeting attended in person and \$1,000 for each meeting attended by telephone or other means. For committee meetings, including ad hoc or special committees, non-employee directors serving on the committee are paid \$1,000 for each meeting attended (whether in person or by telephone) except that the person serving as the committee chair, if any, is paid \$2,000 per meeting. The aggregate meeting fees paid to any director for meetings of the Board and standing Board committees during any fiscal year cannot exceed \$40,000 unless the excess is approved by the Board. During fiscal year 2004, the following amounts were earned by non-employee directors as cash meeting fees: Mr. Dykes, \$45,500; Mr. von Arx, \$54,000; Mr. O Meara, \$43,000; Dr. Potter, \$51,500; and Mr. Wagner \$11,000.

Certain Transactions and Legal Proceedings

In June 2004 the Company paid \$326,351 to Mr. Hunter as reimbursement of expenses incurred in connection with the defense of claims asserted against him as an officer and director of the Company in a lawsuit filed in June 2003 in the U.S. District Court for the Middle District of North Carolina. The plaintiffs dismissed the claims against Mr. Hunter in his corporate capacities with prejudice in November 2003. The reimbursement to Mr. Hunter was approved by the Audit Committee.

Mr. Wagner served as Executive Vice President and Chief Financial Officer of Mirant Corporation, an international energy company based in Atlanta, Georgia (Mirant), from January 2003 through April 2004. In July 2003, Mirant and certain of its wholly-owned subsidiaries in the United States filed voluntary petitions for relief under Chapter 11 of the U.S. Bankruptcy Code. Additionally, certain of Mirant's Canadian subsidiaries filed an application for creditor protection under the Companies Creditors Arrangement Act in Canada. The Canadian subsidiaries emerged from creditor protection in May 2004. The proceedings in the United States are still pending.

Section 16(a) Beneficial Ownership Reporting Compliance

Section 16(a) of the Securities Exchange Act of 1934, as amended, requires that the Company's directors and executive officers, and persons who own more than ten percent of a registered class of the Company's equity securities, file with the Securities and Exchange Commission initial reports of ownership and reports of changes in ownership of common stock and other equity securities of the Company. Directors, officers and greater-than-ten-percent (10%) beneficial owners are required by Commission rules to furnish the Company with copies of all reports they file under Section 16(a). To the Company's knowledge, based solely on its review of the copies of such reports furnished to the Company and written representations that no other reports were required, all Section 16(a) filing requirements applicable to its directors, officers and beneficial owners were complied with on a timely basis during the fiscal year ended June 27, 2004, except that Mr. von Arx reported gifts of the Company's common stock made in calendar 2000 and 2001 on a Form 4 filed October 15, 2003 and Mr. O Meara reported an open market purchase of the Company's common stock on April 29, 2004 one day late.

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**PROPOSAL NO. 2 APPROVAL OF 2004 LONG-TERM
INCENTIVE COMPENSATION PLAN**

Overview and Reasons for Approval

We are requesting that shareholders approve adoption of the Company's proposed 2004 Long-Term Incentive Compensation Plan (the Proposed Plan), which was unanimously approved by the Board of Directors on August 19, 2004. If adopted, the Proposed Plan will replace the Company's Amended and Restated Equity Compensation Plan (the Equity Compensation Plan) and will be the sole plan for providing stock-based incentive compensation to eligible employees and non-employee directors.

Adoption of the Proposed Plan would increase the pool of common stock authorized for future option grants and other stock-based awards by 1,200,000 shares or approximately 1.6% of the shares outstanding on September 7, 2004. The Proposed Plan would also enable the Company to utilize various types of stock-based awards, including restricted stock, stock units and stock appreciation rights. The existing Equity Compensation Plan authorizes only incentive (statutory) and non-qualified (non-statutory) stock option awards. Historically we have granted only non-qualified stock options. Although we presently have no plans to utilize other types of awards, the Proposed Plan will give us more flexibility to make future awards designed to best serve the Company's needs.

We believe that a broad-based stock option program is an essential employee incentive and retention tool that benefits all of our shareholders. Stock-based compensation has been a key element of our incentive compensation programs since the Company's inception and we believe has contributed to the Company's success. In our view, long-term incentive compensation should be closely aligned with shareholders' interests. We seek to achieve that goal through grants of fixed-price stock options. Our option grants align employees' interests directly with those of other shareholders because the employee has the opportunity to realize value only if the stock price increases after the option is awarded.

We have granted stock options to all regular, full-time employees in connection with their initial hiring and annually, depending on performance and other factors. At September 7, 2004, employees other than executive officers and directors held options to purchase 9,920,371 shares, which represented approximately 77% of all shares subject to options then outstanding. We believe that our option program helps motivate employees throughout the organization to act with the shareholders' perspective in mind and complements our cash-based incentives that are directed to achieving revenue, earnings and other financial goals. We also believe that our option program over the years has enabled us to recruit and retain the talent needed to develop new technologies and to grow our business with lower base pay and cash incentive compensation than otherwise would have been required. Without stock options, we would find it necessary to consider offering higher levels of cash compensation to provide competitive compensation packages necessary to recruit and retain essential personnel.

We recognize that options and other stock-based awards must be judiciously managed with consideration given to the potential dilution such awards represent. One measure of this potential dilution or overhang is the proportion, expressed as a percentage, that the pool of shares which may be issued under outstanding and future awards bears to the sum of the pool plus shares presently outstanding. We have worked to reduce the potential dilution or overhang of our stock option program from 19.6% at the end of fiscal 2001 to 17.5% at the end of fiscal 2004. As of September 7, 2004, the overhang stood at 16.8%. We achieved these reductions in large part by reducing the size of option grants. Beginning in 2001 we also reduced the maximum term of our option awards from ten to seven years in part to reduce the adverse impact of the longer option term on overhang. In addition, a portion of the existing overhang is attributable to options with exercise prices significantly higher than the current market price. These options may have no actual dilutive effect unless the market price rises above the exercise price before the option expires and the option is exercised. Of the shares subject to options outstanding at September 7, 2004, approximately 20% had exercise prices in the range of \$34 to \$72 per share, as compared to the closing market price of \$24.29 reported by Nasdaq for that day. The potential dilution from our option program has also been offset through the Company's stock repurchases. During the three fiscal years that ended in June 2004, we

repurchased

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approximately 3.2 million shares of common stock. By comparison, during the same period there were approximately 2.8 million in net option grants (*i.e.*, shares subject to options awarded net of options forfeited).

In requesting approval for additional shares in the Proposed Plan, we have proposed the minimum amount we believe necessary to allow us to continue to make stock-based awards, at levels consistent with our current practices, through at least calendar 2005. We expect to seek shareholder approval again at the 2005 Annual Meeting, and annually thereafter, for additional shares to replenish the reserves to the levels we consider prudent. This approach will enable shareholders to consider each year, and to approve or disapprove, our proposed plans for use of stock-based incentive compensation.

As of September 7, 2004, there were outstanding options to purchase 12,880,571 shares and there remained 2,041,590 shares authorized for future awards under the Equity Compensation Plan. The outstanding options had a weighted average exercise price of \$22.60 per share and a weighted average remaining term of approximately 4.9 years. If the Proposed Plan is approved, no further awards may be made under the Equity Compensation Plan but shares authorized for future awards under the Equity Compensation Plan, including shares subject to outstanding options that are later forfeited, may thereafter be used for awards under the Proposed Plan. The Proposed Plan would also authorize an additional 1,200,000 shares for future awards, of which no more than 600,000 shares could be subject to awards granted as restricted stock, stock units or performance units. We have included this sublimit of 600,000 shares to limit the potential dilutive effect of such awards, which can be greater than that of non-discounted options that require participants upon exercise to pay at least the fair market value established at the grant date.

Our overhang would increase from 16.8% to 17.9% if the Proposed Plan were approved as of September 7, 2004. We believe this increase is reasonable and compares favorably to other companies of a similar size in the semiconductor field. We reviewed the overhang from option programs at 18 other publicly-traded companies engaged in semiconductor manufacturing or related businesses, with reported revenues for the most recent twelve months as of September 7, 2004 ranging from \$212 million to \$468 million and median revenues of \$322 million. Overhang at these companies, as of the end of the most recent fiscal year for which financial statements were published, ranged from 9.9% to 24.9% with a median overhang of 19.3%, which is above both our current overhang level and that which would result from approval of the Proposed Plan.

The Proposed Plan would also implement features designed to address concerns expressed by investors in recent years about options and other stock-based incentive compensation. It prohibits granting stock options and stock appreciation rights with an exercise price less than the fair market value on the date of grant. Subject to exceptions for death, disability, retirement and certain other events, the Proposed Plan requires a minimum vesting or restriction period of at least three years for awards of restricted stock or stock units, except that awards with restrictions based on achievement of performance goals or to non-employee directors must have a restriction period of at least one year. The Proposed Plan also prohibits repricing of stock options and stock appreciation rights, including granting an award in replacement of a canceled award with a lower exercise price. In addition, the Proposed Plan requires shareholder approval of any material amendments to the plan independently of whether such approval is required under applicable law or listing standards applicable to the Company.

We consider adoption of the Proposed Plan essential to the Company's future success and encourage all shareholders to vote in favor of its approval.

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**The Board of Directors recommends
shareholders vote FOR Proposal No. 2.**

Key Terms of Proposed Plan

The following table highlights key terms of the Proposed Plan. This table and the description of the Proposed Plan in this proxy statement are merely summaries of material features of the plan and are qualified in their entirety by the full text of the plan, a copy of which is included in Appendix D to this proxy statement.

<i>Plan Term:</i>	From the date of shareholder approval through June 28, 2009
<i>Predecessor Plan:</i>	Cree, Inc. Amended and Restated Equity Compensation Plan (the "Equity Compensation Plan"). No further grants may be made under the Equity Compensation Plan following shareholder approval of the Proposed Plan.
<i>Eligible Participants:</i>	All employees of the Company and its subsidiaries, where legally eligible to participate, and non-employee directors of the Company
<i>Shares Authorized:</i>	1,200,000 shares, plus the number of shares previously authorized for issuance under the Equity Compensation Plan and not issued pursuant to awards under that plan, subject to adjustment to reflect stock splits and similar events
<i>Award Types:</i>	<ol style="list-style-type: none"> (1) Non-qualified and incentive stock options (2) Stock appreciation rights (3) Restricted stock (4) Stock units (5) Performance units
<i>Limits on Certain Awards:</i>	<ol style="list-style-type: none"> (1) No more than 600,000 shares may be issued pursuant to awards of restricted stock, stock units or performance units. (2) Awards to non-employee directors during any fiscal year may not exceed 16,000 shares for awards in the form of non-qualified stock options or stock appreciation rights or 5,000 shares for awards in the form of restricted stock or stock units.
<i>Award Terms:</i>	<ol style="list-style-type: none"> (1) Stock options and stock appreciation rights cannot be granted at a price below fair market value on the date of grant. (2) Stock options and stock appreciation rights will have a term no longer than seven years. (3) Repricing or reducing the exercise price of a stock option or stock appreciation right, including granting an award in replacement of a canceled award with a lower exercise price, is prohibited without shareholder approval except for adjustments made in connection with stock splits or similar events. (4) Restricted stock and stock units may not vest in less than three years except that awards in which vesting is based on the achievement of performance criteria and awards to non-employee directors may not vest in less than one year. These minimum periods may be shortened in connection with

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death, disability, retirement and certain corporate transactions (acquisitions in which the successor does not assume or replace the awards).

162(m) Share Limits:

So that awards may qualify under Section 162(m) of the Internal Revenue Code, the Proposed Plan limits awards to individual participants to:

- (1) no more than 300,000 shares subject to stock options or stock appreciation rights granted to an individual participant in any fiscal year,
- (2) no more than 100,000 shares subject to restricted stock or stock unit awards granted to an individual participant in any fiscal year, and
- (3) no more than the fair market value of 100,000 shares in the form of performance unit awards granted to an individual participant in any fiscal year.

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Description of Proposed Plan

Nature and Purpose. The Proposed Plan provides for grants to eligible participants in the form of non-qualified stock options, incentive stock options, stock appreciation rights (SARs), restricted stock, stock units and performance units. The objectives of the plan are to (i) attract and retain employees for the Company and its affiliates and directors of the Company by providing competitive compensation opportunities; (ii) provide incentives to those individuals who contribute significantly to the long-term performance and growth of the Company and its affiliates; and (iii) align the long-term financial interests of employees and directors with those of the Company's shareholders.

The Proposed Plan is not generally subject to the provisions of the Employee Retirement Income Security Act of 1974, as amended. The Proposed Plan is not a qualified plan under Section 401 of the Internal Revenue Code of 1986, as amended (the Code).

Eligible Participants. Only employees of the Company and its subsidiaries, and non-employee directors of the Company, are eligible to receive awards under the Proposed Plan. As of September 15, 2004, there were approximately 1,381 employees (including 27 part-time and 167 temporary employees) and five non-employee directors who would be eligible to participate in the Proposed Plan. The Company in the past generally has not made stock-based awards to part-time or temporary employees and does not currently have plans to do so in the future.

Administration. The Proposed Plan will be administered by a committee (the Committee) consisting of two or more non-employee directors appointed by the Board. The Committee has the exclusive right to interpret, construe and administer the Proposed Plan, to select the persons eligible to receive awards, and to act in all matters pertaining to the granting of awards and the contents of agreements evidencing awards, except that awards to non-employee directors must also be approved by the Board. The Committee's decisions are conclusive, final and binding upon all parties.

Unless the Board directs otherwise, the Compensation Committee of the Board shall serve as the Committee. The charter adopted by the Board for the Compensation Committee provides that all members of the Compensation Committee must be (i) independent directors who meet the independence requirements of Nasdaq's Marketplace Rules, (ii) non-employee directors as defined by Rule 16b-3 under the Securities Exchange Act of 1934, as amended (the Exchange Act), and (iii) outside directors as defined by Section 162(m) of the Code. The Board, in its sole discretion, may exercise any authority of the Committee under the plan. To the extent permitted by law and the Company's Bylaws, and subject to the applicable rules of any securities exchange or quotation or trading system on which the Company's shares are traded, the Committee may delegate authority under the plan to one or more Committee members or executive officers of the Company, except that the Committee may not delegate such authority with respect to awards to directors or executive officers. The Committee may also delegate authority for certain administrative functions under the Proposed Plan to an officer or officers of the Company.

Securities to be Offered. The Company would be authorized to issue shares of the Company's common stock, with a par value \$0.00125 per share (the Shares), pursuant to awards under the Proposed Plan. Shares subject to awards under the plan will be made available from the authorized and unissued Shares of the Company's common stock. The last sale price of the common stock on September 17, 2004 was \$28.37 per share, as reported by The Nasdaq Stock Market, Inc.

The aggregate number of Shares which may be issued pursuant to awards under the plan is: (i) 1,200,000 plus (ii) the number of Shares which, immediately prior to the date of shareholder approval of the Proposed Plan (the Effective Date), were authorized for issuance under the Equity Compensation Plan and are not thereafter used for awards under the Equity Compensation Plan. The number of authorized Shares include Shares which, immediately prior to the Effective Date, were authorized for issuance under the Equity Compensation Plan and

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either were not subject to then outstanding awards or were subject to then outstanding awards that subsequently expire, are canceled or otherwise terminate unexercised for any reason. No more than an aggregate of 600,000 Shares may be issued pursuant to awards of restricted stock, stock units or performance units under the Proposed Plan. If for any reason any Shares awarded or subject to purchase under the Proposed Plan are not delivered or purchased, or are reacquired by the Company, such Shares will again be available for issuance pursuant to an award under the Proposed Plan. The determination of the number of Shares that may again become available for issuance with respect to grants of incentive stock options will be made in accordance with the requirements of applicable regulations under the Code.

The Committee will determine the individuals to whom awards will be granted, the number of Shares subject to an award, and the other terms and conditions of an award. Except to the extent the Committee determines that an award shall not comply with the performance-based compensation provisions of Section 162(m) of the Code, (i) the aggregate number of Shares subject to options or SARs granted in any one fiscal year to any one participant shall not exceed 300,000; (ii) the aggregate number of Shares subject to restricted stock or stock unit awards granted in any one fiscal year to any one participant shall not exceed 100,000; and (iii) the aggregate value of performance unit awards (valued as of the grant date) that may be granted in any one fiscal year to any one participant shall not exceed the fair market value of 100,000 Shares.

The Committee will make equitable adjustments upon the occurrence of certain events that result in changes in the outstanding shares of the Company's common stock or that result in exchanges of shares of common stock for a different number or class of common stock or other securities of the Company or another corporation. These events include changes in corporate capitalization, such as a stock split, reverse stock split, or stock dividend, or any corporate transaction such as a reorganization, reclassification, merger or consolidation or separation, including a spin-off, of the Company or sale or other disposition by the Company of all or a portion of its assets, any other change in the Company's corporate structure, or any distribution to shareholders (other than a cash dividend). Under such circumstances, adjustments may be made by the Committee in the number of Shares that may be awarded under the Proposed Plan, the limitations on the aggregate number of Shares that may be awarded to any one participant, the number and class of Shares that may be subject to an award and which have not been issued or transferred under an outstanding award, the exercise price under outstanding options and the number of Shares to be transferred in settlement of outstanding SARs, and the terms, conditions or restrictions of any award and award agreement, including the price payable for the acquisition of Shares.