

DIGITAL ANGEL CORP
Form DEF 14A
April 01, 2005

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 Pursuant to §240.14a-12

Digital Angel Corporation
(Name of Registrant as Specified In Its Charter)

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

Payment of Filing Fee (Check the appropriate box):

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

DIGITAL ANGEL CORPORATION

490 Villaume Avenue
South St. Paul, Minnesota 55075
(651) 455-1621

**Notice of Annual Meeting of Stockholders
to Be Held May 3, 2005**

To the Stockholders of Digital Angel Corporation:

Notice is hereby given that the Annual Meeting of Stockholders (the Annual Meeting) of Digital Angel Corporation, a Delaware corporation (the Company), will be held on Tuesday, May 3, 2005 at 9:30 a.m. (local time) at the offices of Winthrop & Weinstine, P.A., 225 South Sixth Street, Suite 3500, Minneapolis, Minnesota 55402.

At the Annual Meeting, the Company s stockholders will be asked to:

1. Elect six (6) directors of the Company to serve until the next annual meeting of stockholders and until their successors are elected and qualified or until their earlier resignation, removal or death;
2. Approve an amendment to the Amended and Restated Digital Angel Corporation Transition Stock Option Plan (2002 Stock Plan) increasing the number of shares of Company common stock subject to the 2002 Stock Plan;

3. Ratify the appointment of Eisner LLP as independent auditors for the fiscal year ending December 31, 2005; and

4. Transact such other business as may properly come before the Annual Meeting or any adjournment thereof.

Only holders of record of the Company's common stock at the close of business on March 22, 2005 are entitled to notice of and to vote at the Annual Meeting or any adjournment thereof.

Each of you is invited to attend the Annual Meeting in person, if possible. Whether or not you plan to attend in person, please mark, date and sign the enclosed proxy, and mail it promptly. A return envelope is enclosed for your convenience.

By Order of the Board of Directors,

/s/ James P. Santelli

April 5, 2005

**Whether or not you expect to attend the Annual Meeting,
please sign the proxy and return it in the enclosed envelope or vote**

Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A
by telephone or through the Internet as instructed on the proxy card.

DIGITAL ANGEL CORPORATION

Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A

490 Villaume Avenue

South St. Paul, Minnesota 55075

(651) 455-1621

PROXY STATEMENT

SELECTION OF PROXIES

This proxy statement is being furnished to stockholders of Digital Angel Corporation, a Delaware corporation (the Company), in connection with the solicitation of proxies by and on behalf of the Board of Directors of the Company for use at the Annual Meeting of Stockholders (Annual Meeting) to be held on May 3, 2005 and any adjournment thereof. This proxy statement and the accompanying form of proxy are being mailed to stockholders beginning on or about April 5, 2005. This Proxy Statement and the accompanying Annual Report to Stockholders is for the year ended December 31, 2004.

The expense of the solicitation of proxies for the Annual Meeting, including the cost of mailing, has been or will be borne by the Company. Arrangements will be made with brokerage houses and other custodian nominees and fiduciaries to send proxies and proxy materials to their principals, and the Company will reimburse them for their expense in so doing. In addition to solicitation by mail, proxies may be solicited by telephone, telegraph or personally.

VOTING AND REVOCATION OF PROXY

Only holders of record of the Company's common stock, par value \$0.005 per share, at the close of business on March 22, 2005, the record date for the Annual Meeting, are entitled to notice of and to vote at the Annual Meeting. On the record date, 44,044,914 shares of the Company's common stock were outstanding. Each share of common stock entitles the holder thereof to one vote upon each matter to be presented at the Annual Meeting. A quorum, consisting of a majority of the shares of the Company's common stock entitled to vote at the Annual Meeting, must be present in person or by proxy before action may be taken at the Annual Meeting. Shares represented by a proxy with instructions to abstain on any matter or by a proxy that indicates that the broker does not have discretionary authority to vote on one or more proposals (that is, broker non-votes) will be counted for the purpose of determining the presence of a quorum at the Annual Meeting.

Each proxy returned to the Company will be voted according to the instructions indicated on the proxy. If no instructions are indicated, the shares will be voted (i) *for* the election of the nominees for the Board of Directors named in this proxy statement; (ii) *for* the amendment to increase the number of shares issuable under the Amended and Restated Digital Angel Corporation Transition Stock Option Plan (2002 Stock Plan); and (iii) *for* the ratification of the appointment of Eisner LLP as independent auditors for the fiscal year ending December 31, 2005. Although the Board of Directors knows of no other matters to be presented at the Annual Meeting or any adjournment thereof, all proxies returned to the Company will be voted on any such matter in accordance with the judgment of the proxy holders.

Instead of submitting a signed proxy card, stockholders may submit their proxies by telephone or through the Internet using the control number and instructions on the proxy card. Telephone and Internet

proxies must be used in conjunction with, and will be subject to, the information and terms contained on the proxy card. These procedures may not be available to stockholders who hold their shares through a broker, nominee, fiduciary or other custodian.

The election of the directors set forth in Proposal 1 requires a plurality of the votes of the shares of common stock present in person or represented by proxy at the Annual Meeting. If a quorum is present, those nominees receiving a plurality of the votes cast will be elected. With respect to Proposals 2 and 3, if a quorum is present, the affirmative vote of a majority of the shares of common stock present in person or represented by proxy at the Annual Meeting is required to approve such matters. If a proxy is returned and the stockholder has abstained from voting on any matter, the shares represented by such proxy will be included in the number of votes present and entitled to vote and will be treated as no votes with respect to that matter. Broker non-votes are not counted as shares present and entitled to be voted with respect to the matter on which the broker has expressly not voted. Thus, broker non-votes will not affect the outcome of any of the matters being voted on at the annual meeting. Generally, broker non-votes occur when shares held by a broker for a beneficial owner are not voted with respect to a particular proposal because the broker has not received voting instructions from the beneficial owner and the broker lacks discretionary voting power to vote such shares.

Any proxy given pursuant to this solicitation may be revoked by the person giving it at any time before it is voted. Proxies may be revoked by:

giving written notice of such revocation to the Assistant Secretary of the Company before or at the Annual Meeting before a vote is taken;

delivering another written proxy bearing a later date; or

attending the Annual Meeting and voting in person (although attendance at the Annual Meeting will not in and of itself constitute a revocation of a proxy).

At March 22, 2005, Applied Digital Solutions, Inc. owned 24,291,673 shares of the Company's outstanding common stock, representing approximately 55.2% of the Company's outstanding common stock and voting power. Applied Digital Solutions, Inc. controls the Company within the meaning of Section 801(a) of Part 8 of the Listing Standards, Policies and Requirements of the American Stock Exchange (AMEX Rules). Applied Digital Solutions, Inc. has indicated to the Company that it intends to vote for each proposal set forth in this Proxy Statement.

PROPOSAL 1

ELECTION OF DIRECTORS

The business and affairs of the Company are managed under the direction of its Board of Directors. The Company's Bylaws provide that the Board of Directors shall consist of at least three members. The Board of Directors currently consists of six members. Each Director is elected to serve until the next annual meeting of stockholders and until their successors are elected and qualified or until their earlier resignation, death or removal.

Stockholders will be asked at the Annual Meeting to elect six Directors. The Board has nominated the six individuals named below to serve as Directors of the Company. The nominees comprise the entire Board, and all nominees now serve as Directors of the Company.

All nominees have indicated a willingness to serve, if elected. If any nominee becomes unable to serve before the Annual Meeting, the proxies received in response to this solicitation will be voted for a replacement nominee selected in accordance with the best judgment of the proxy holders named in the proxy.

Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A

The following sets forth certain information as of March 31, 2005 regarding the nominees for the Board of Directors:

Name	Positions with the Company	Age
------	----------------------------	-----

Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A

Kevin N. McGrath	President, Chief Executive Officer and Director	52
Scott R. Silverman	Chairman of the Board	41
John R. Block	Director	70
Kevin H. McLaughlin	Director	63
Howard S. Weintraub, Ph.D.	Director	61

Stockholder Approval

The affirmative vote of a plurality of the shares of common stock of the Company represented at the Annual Meeting either in person or by proxy, assuming a quorum is present, is required for the election of a Director.

The Board of Directors recommends that the stockholders vote *for* the election of the nominees for the Board of Directors as set forth in Proposal 1.

INFORMATION CONCERNING DIRECTORS

AND EXECUTIVE OFFICERS

Directors

Each nominee for election to the Company's Board of Directors is presently serving as a Director of the Company. The following discussion sets forth information concerning the nominees for Directors of the Company.

Kevin N. McGrath has been Chief Executive Officer and President of the Company since January 2004. From 1987 until 2003, he was employed at Hughes Electronics Corp. in a number of senior level executive positions, including Corporate Vice President of DirectTV International, President of Hughes Communications, Inc. and the senior financial executive of Hughes Space and Communications Group. From 1996 to 2003, he was Chairman of DirecTV Latin America (a subsidiary of Hughes Electronics Corporation). In 2003-2004, DirecTV Latin America, LLC was reorganized under Chapter 11 of the United States Bankruptcy Code. Prior to his work at Hughes, Mr. McGrath spent two years as Chief Financial Officer for Electronic Data Systems, Asia and Pacific, and 10 years in various financial management positions at General Motors Corp. Mr. McGrath is a graduate of Princeton University and received a Masters of Business Administration from the Amos Tuck School at Dartmouth College.

Scott R. Silverman is Chairman of the Company's Board of Directors and has been a Director of the Company since July 2003. He has served since August 2001 as a special advisor to the Board of Directors of Applied Digital Solutions, Inc. (Nasdaq:ADSX) (ADSX). In March 2002, he was appointed to ADSX's Board of Directors and named President. In March 2003, Mr. Silverman was appointed Chairman of the Board and Chief Executive Officer of ADSX. From September 1999 to March 2002, Mr. Silverman operated his own private investment banking firm. From October 1996 to September 1999, he served in various capacities for ADSX, including positions related to business development, corporate development and legal affairs. From July 1995 to September 1996, Mr. Silverman

served as President of ATI Communications, Inc., a subsidiary of ADSX. He began his career as an attorney specializing in commercial litigation and communications law at the law firm of Cooper Perskie in Atlantic City, New Jersey, and Philadelphia, Pennsylvania. Mr. Silverman is a graduate of the University of Pennsylvania and the Villanova University School of Law.

John R. (Jack) Block joined the Board of Directors in January 2004. Mr. Block serves as Chairman of the Board's Government Relations Committee. He has served as the Executive Vice President of the Food Marketing Institute, a trade association in Washington, D.C., since January 2003, and for the past year has been President of its Wholesaler Division. From 1986 until December 2002, Mr. Block was President and Chief Executive Officer of Food Distributors International and the International Foodservice Distributors Association (NAWGA/IFDA). Mr. Block was appointed to President Reagan's Cabinet in 1981 and served for five years as the Secretary of the U.S. Department of Agriculture. As a member of the Reagan Cabinet and a key member of the Economic Policy Council, he dealt with a wide range of complex domestic farm program and tax issues. Under his leadership, the Department of Agriculture's Food for Peace Program was a primary resource in feeding the starving African continent. During his tenure as Secretary of Agriculture, Mr. Block visited more than 30 foreign countries, meeting with heads of state and agriculture ministers from all over the globe and negotiating sensitive agreements critical to U.S. farm interests. From 1977 to 1981, he served as Director of Agriculture for the State of Illinois. Mr. Block currently has a syndicated weekly radio commentary broadcast by more than 600 stations in 30 states. Mr. Block serves on a number of corporate boards, including those of NYSE-listed Deere & Co. and Hormel Foods Corporation. He is also a member of the Board of Advisors for the Retail Food Industry Center at the University of Minnesota, and he is President of the Board of Directors of the U.S. Friends of the World Food Programme, a joint initiative of the United Nations and the Food and Agricultural Organization, and Chairman of the Agribusiness Alliance of the Citizens Network for Foreign Affairs in Washington.

Kevin H. McLaughlin has been a Director since September 2003. He was the interim Chief Executive Officer of the Company from September 2003 through November 2003. Mr. McLaughlin has served as a director of InfoTech USA, Inc., a 52.5% owned subsidiary of ADSX, since April 2002. He was appointed President of ADSX in May 2003 and Chief Operating Officer in March 2003. From April 12, 2002 until March 10, 2003, Mr. McLaughlin served as a director and Chief Executive Officer of InfoTech USA, Inc. From September 2001 until January 2002, he served as Chief Executive Officer of Computer Equity Corporation, a wholly-owned subsidiary of ADSX. Mr. McLaughlin joined ADSX as Vice President of Sales and Marketing in June 2000. From June 1995 to May 2000, he served as Senior Vice President of Sales for SCB Computer Technology, Inc.

Howard S. Weintraub, Ph.D. has been a Director of the Company since March 2002. Dr. Weintraub retired from C. R. Bard, Inc., a medical device company, in 2003, where he was Vice President, R&D, Corporate Staff. From 1988 to 1998, he held a series of senior research and technology management positions at Bristol-Myers Squibb. Dr. Weintraub was previously associated with Ortho Pharmaceutical Corporation, a Johnson and Johnson company, from 1973 until 1988, where he held senior research management positions. He also has authored or co-authored over 50 scientific publications and abstracts. Dr. Weintraub previously served as chairman of the Industrial Pharmaceutical Technology Section of the AAPS (formerly APhA), and was the chairman of the Drug Metabolism sub-section of the Research and Pharmaceutical Manufacturers' Association. Dr. Weintraub earned a Bachelor of Science Degree in Pharmacy from Columbia University and his Ph.D. in biopharmaceutics from the State University of New York at Buffalo. He is a member of the Board of Directors of the privately-held biotechnology firm, Bioenergy, Inc., and a member of the Scientific Advisory Board of Polymerix Corporation, a specialty development-stage pharmaceutical company. He was also a Board Advisor to the Swiss Biotechnology firm, Modex Therapeutics, prior to its merger with IsoTis, NV, in 2002.

Michael S. Zarriello has been a Director of Digital Angel Corporation since September 2003. He has served as Senior Vice President and Chief Financial Officer for Rural/Metro Corporation in Scottsdale, Arizona, since July 2003. From 1998 to 2003, Mr. Zarriello was a Senior Managing Director of Jesup & Lamont Securities Corporation and President of Jesup & Lamont Merchant Partners LLC, both of which are investment banking firms. From 1989 to 1997, Mr. Zarriello was a Managing Director-Principal of Bear Stearns & Co., Inc., and from 1989 to 1991, he served as Chief Financial Officer of the Principal Activities Group that invested Bear Stearns' capital in middle market companies. Mr. Zarriello also serves as a member of the Board of ADSX.

Directors of the Company are elected annually to serve until the next annual meeting of stockholders and until their successors are elected and qualified or until their earlier resignation, death or removal. There is no family relationship between any of the directors or executive officers of the Company.

Board Actions and Committees

The Board held ten formal meetings and adopted resolutions by written action eighteen times during 2004. The Board has an Audit Committee, a Compensation Committee and a Government Relations Committee. The Company has no Nominating Committee and, under the AMEX Rules, it is not required to create such a committee as it is controlled by ADSX. The full Board of Directors considers and nominates candidates proposed for election.

Independent Directors

The Company's Board of Directors has determined that each of Messrs. Block, Weintraub and Zarriello are independent, as that term is defined in Section 121(A) of the AMEX Rules, except that Mr. Zarriello will not be considered independent with respect with deals between the Company and ADSX. Because the Company is controlled by ADSX, under the AMEX rules, it is not required to have a majority of independent directors.

Compensation Committee

Since April 30, 2004, the Compensation Committee consisted of Messrs. Howard S. Weintraub, Ph.D. (Chairman), Michael S. Zarriello and John R. Block. From November 6, 2003 to April 29, 2004, the Compensation Committee consisted of Messrs. Weintraub and Zarriello. The Compensation Committee determines compensation for senior management, advises the Board of Directors on the adoption and administration of employee benefit and compensation plans and administers the March 1998 Amended and Restated Employee and Directors Stock Plan (the 1998 Stock Plan) and the 2002 Stock Plan. The Compensation Committee is in the process of drafting a charter. The Compensation Committee met five times, and except for one meeting at which Mr. Block was absent, all members of the Compensation Committee attended each meeting.

Audit Committee

Since April 30, 2004, the Audit Committee consisted of Messrs. Michael S. Zarriello (Chairman), Howard S. Weintraub, Ph.D. and John R. Block. From November 6, 2003 to April 29, 2004, the Audit Committee consisted of Messrs. Zarriello and Weintraub. During 2004, the Audit Committee met six times, and except for two meetings at which Mr. Block was absent for one and Dr. Weintraub was absent for the other, all members of the Audit Committee attended each meeting.

The Audit Committee recommends annually to the Board of Directors the engagement of independent auditors, approves professional services provided by the independent auditors, considers the range of audit and any non-audit fees and reviews the adequacy of the Company's internal accounting controls and major accounting and financial reporting matters. The Audit Committee also reviews all reports and financial information submitted to the United States Securities and Exchange Commission and resolves any significant disagreements between management and the independent auditors in connection with the preparation of the Company's financial statements. The Audit Committee reviews with the Company's legal counsel all legal and regulatory matters which may have a significant impact on the Company's financial statements. The Audit Committee determined that the provision of non-audit services by the independent auditors in 2004 was compatible with maintaining the independent auditors' independence.

The Company's Board of Directors has determined that all members of the Audit Committee are independent under Section 121(A) of the AMEX Rules and Rule 10A-3 under the Securities Exchange Act of 1934 (Exchange Act). The Board has determined that Mr. Zarriello is qualified as an audit committee financial expert, as that term is defined in Item 401(h)(2)(i) of Regulation S-K under the Exchange Act.

The Audit Committee charter was included as an exhibit to the Company's Proxy Statement dated April 14, 2003.

Nominating Committee

The Company has no Nominating Committee and, under the AMEX Rules, it is not required to create such a committee as it is controlled by ADSX. The full Board of Directors considers and nominates candidates proposed for election.

Government Relations Committee

The Government Relations Committee was formed to assist the Company with the proposed national identification program for cattle and any other government-related matters. The Government Relations Committee consists of Mr. John R. Block. The Government Relations Committee is in the process of drafting a charter.

Executive Sessions of the Board

In 2004, the Board adopted a formal policy of meeting in executive session, with only independent directors being present, on a regular basis and at least two times each year. During 2004, the Board met in executive session six times, and all independent directors attended each meeting.

Compensation Committee Interlocks and Insider Participation

Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A

The members of the Compensation Committee for fiscal year 2004 were Messrs. Howard S. Weintraub, Ph.D. (Chairman), Michael S. Zarriello and John R. Block. During 2004, none of the members of the Compensation Committee served as an officer or employee of the Company, and none had any relationship requiring disclosure pursuant to Item 404 of Regulation S-K. Additionally, during 2004, none of the executive officers or directors of the Company served as a member of the board of directors, or any Compensation Committee thereof, of any other entity such that the relationship would be construed to constitute a committee interlock within the meaning of the rules of the Securities and Exchange Commission (SEC), except that Mr. Zarriello also served as a director and a member of the Compensation Committee for ADSX and Mr. Silverman served as a director and executive officer of ADSX.

Code of Business Conduct and Ethics

The Board has approved and the Company has adopted a Code of Business Conduct and Ethics that applies to all directors, officers and employees of the Company. This Code is available on the Company's website at www.digitalangelcorp.com. The Compensation Committee of the Board is responsible for overseeing the Code of Business Conduct and Ethics. In accordance with the AMEX Rules, any waivers of the Code for directors and executive officers must be approved by the Company's Board of Directors.

Qualifications of Candidates for Election to the Board

The Company's Directors take a critical role in guiding the Company's strategic direction, and they oversee the management of Company. When Board candidates are considered, they are evaluated based upon various criteria, such as their broad-based business and professional skills and experiences, experience serving as management or on the board of directors of companies such as the Company, concern for the long-term interests of the stockholders, financial literacy and personal integrity in judgment. In addition, director candidates must have time available to devote to Board activities. Accordingly, the Board seeks to attract highly-qualified directors who have sufficient time to attend to their duties and responsibilities to the Company. Recent developments in corporate governance and financial reporting have resulted in an increased demand for such highly-qualified and productive public company directors.

Director candidates for the Company's Board of Directors will be considered for vacant Board seats if they are able to read and understand fundamental financial statements, have at least 10 years of relevant business experience, have no identified conflicts of interest as a prospective Director of the Company, have not been convicted in a criminal proceeding other than traffic violations during the five years before the date of selection and are willing to comply with the Company's Code of Business Conduct and Ethics. The Company retains the right to modify these minimum qualifications from time to time. Exceptional candidates who do not meet all of these criteria may still be considered.

Process for Identifying and Evaluating Candidates for Election to the Board

The Board of Directors will review the qualifications and backgrounds of the Directors as well as the overall composition of the Board. In the case of any director candidates, the questions of independence and financial expertise are important to determine what roles can be performed by the candidate, and the Board of Directors will consider whether the candidate meets the applicable independence standards and the level of the candidate's financial expertise. Any new candidates would be interviewed, and the full Board would approve the final nominations. The Chairman of the Board, acting on behalf of the full Board, will extend the formal invitation to become a nominee of the Board of Directors.

Stockholder Nominations

Stockholders may nominate director candidates for consideration by the Board of Directors by writing to the Chairman and providing to the Chairman the candidate's name, biographical data and qualifications, including five-year employment history with employer names and a description of the employer's business; whether such individual can read and understand fundamental financial statements; other board memberships (if any); and such other information as is reasonably available and sufficient to enable the Board to evaluate the minimum qualifications stated above under the section of this proxy statement entitled "Qualifications of Candidates for Election to the Board." The submission must be accompanied by a written consent of the individual to stand for election if nominated by the Board of Directors and to serve

Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A

if elected by the stockholders. If a stockholder nominee is eligible, and if the nomination is proper, the Board then will deliberate and make a decision as to whether the candidate will be submitted to the Company's stockholders for a vote.

The Board will not change the manner in which it evaluates candidates, including the applicable minimum criteria set forth above, based on whether the candidate was recommended by a stockholder.

Communications with the Board

Stockholders can communicate directly with the Board, or with any Committee of the Board, by writing to Mr. James P. Santelli, the Company's Chief Financial Officer, by calling Mr. Santelli at (651) 455-1621 or via e-mail at jsantelli@digitalangelcorp.com. All communications will be reviewed by management and then forwarded to the appropriate director or directors or to the full Board, as appropriate.

Directors Compensation

Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A

The Board has determined to pay each member of the Company's Board of Directors who is not an employee or officer of the Company or an affiliate of the Company (as the term "affiliate" is defined in the Company's 2002 Stock Plan) \$5,000 per quarter for serving on the Board; \$5,000 per quarter for serving on the Audit Committee; \$1,250 per quarter for serving as the Audit Committee Chair; \$1,000 per quarter for serving on the Compensation Committee; \$4,000 per quarter for serving on the Government Relations Committee; and \$1,000 per quarter for serving as Chair of the Government Relations Committee. Effective January 1, 2005, the Board increased the compensation to \$5,000 per quarter for serving on the Compensation Committee and \$1,250 per quarter for serving as the Compensation Committee Chair. The Company also reimburses such directors for reasonable expenses incurred by them in rendering their duties as directors of the Company, subject to such reimbursement practices and procedures as the Company reasonably imposes.

Under these arrangements, the following non-employee Directors received the following cash amounts during 2004: Scott R. Silverman (\$0), Kevin H. McLaughlin (\$0), John R. Block (\$6,923), Howard S. Weintraub, Ph.D. (\$11,000) and Michael S. Zarriello (\$11,250). Information regarding options granted to the directors during 2004 under the 2002 Stock Plan is set forth below.

	Number of Shares Subject to Options Granted	Exercise Price	Grant Date	Expiration	Vesting(1)
Kevin N. McGrath	1,000,000(2)	\$ 3.92	1/13/2004	1/12/2014	(3)
John R. Block	250,000	\$ 4.00	1/26/2004	1/25/2014	1/25/2005
Scott R. Silverman	500,000(2)	\$ 3.43	2/18/2004	2/17/2014	2/18/2005
John R. Block	75,000(4)	\$ 3.79	3/16/2004	3/15/2014	(5)
Kevin H. McLaughlin	100,000	\$ 3.79	3/16/2004	3/15/2014	(6)
Howard S. Weintraub, Ph.D.	75,000(4)	\$ 3.79	3/16/2004	3/15/2014	(5)
Howard S. Weintraub, Ph.D.	100,000	\$ 3.79	3/16/2004	3/15/2014	(6)
Michael S. Zarriello	75,000(4)	\$ 3.79	3/16/2004	3/15/2014	(5)
Michael S. Zarriello	100,000	\$ 3.79	3/16/2004	3/15/2014	(6)

(1) All options have vested or will vest on these dates if the Director was or is a Director of the Company on such dates.

(2) Options were granted outside of the 2002 Stock Plan.

(3) Vests 33 1/3% on each 1/13/2005, 1/13/2006 and 1/13/2007.

(4) Options were issued in lieu of cash compensation.

(5) Vests 25% on each 6/30/2004, 9/30/2004, 12/31/2004 and 3/31/05.

(6) Vests 33 1/3% on each 3/16/2005, 3/16/2006 and 3/16/2007.

Executive Officers

Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A

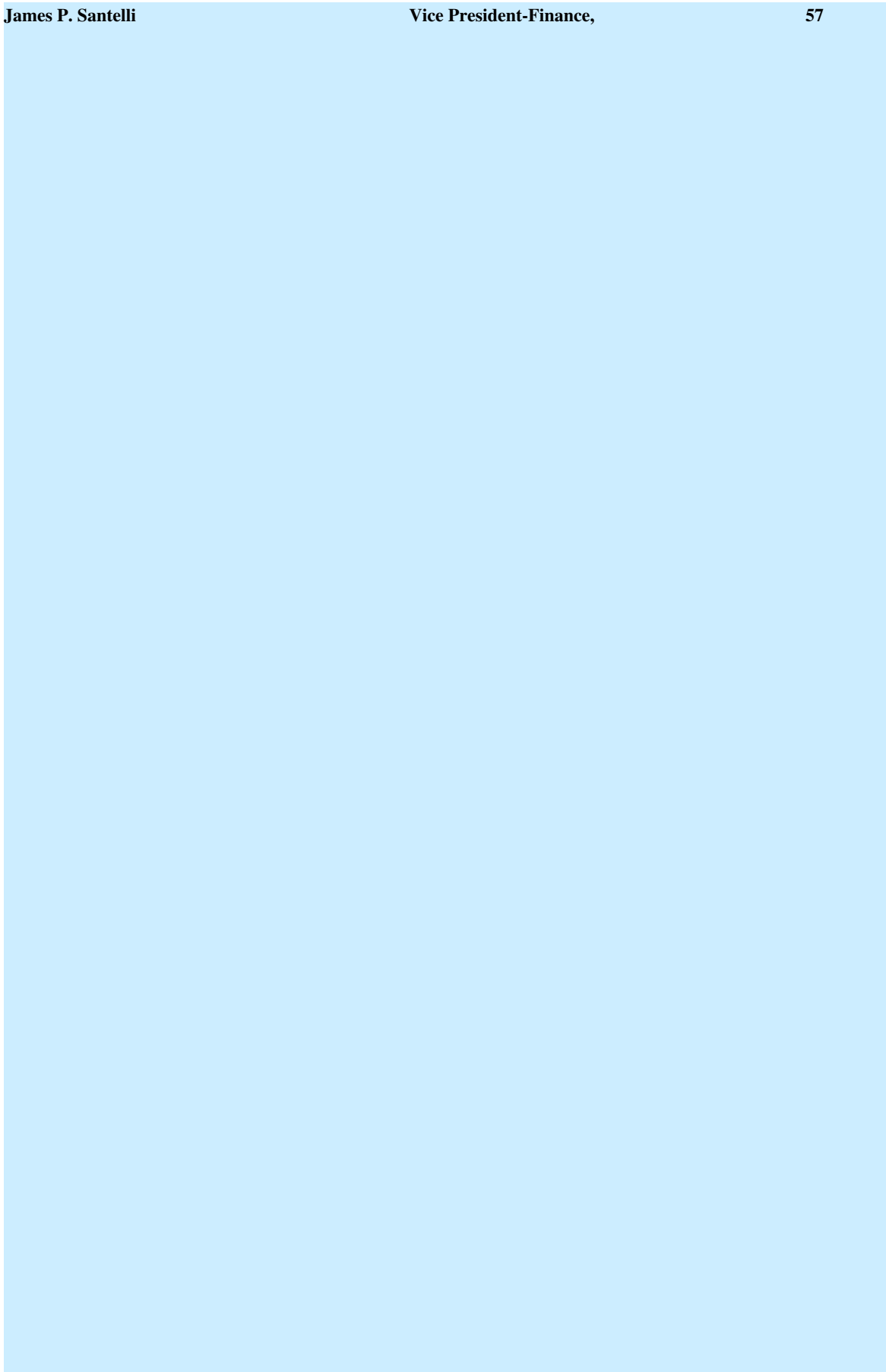
The following discussion sets forth information as of March 31, 2005 about Messrs. James P. Santelli, James G. Naro, Lasse Nordfeld and David M. Cairnie, who are executive officers but not Directors of the Company. Kevin L. Nieuwsma served as the Vice President from November 11, 2002 until he resigned on January 3, 2005 and accordingly is not listed.

Name	Positions with the Company	Age
------	----------------------------	-----

James P. Santelli

Vice President-Finance,

57



Chief Financial Officer,



Treasurer and Assistant Secretary



Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A

James G. Naro	Vice President, General Counsel And Secretary	51
Lasse Nordfjeld	President of the Animal Applications Group	59
David M. Cairnie	Managing Director, Signature Industries, Ltd.	60

James P. Santelli has been Vice President-Finance, Chief Financial Officer and Treasurer of the Company since March 27, 2002. He was Secretary of the Company from March 27, 2002 to March 21, 2005, on which date he became Assistant Secretary of the Company. He is a manager (Chief Financial Officer) and one of two governors of Digital Angel Holdings, LLC. He was Vice President-Finance and Chief Financial Officer of the former Digital Angel Corporation since September 2000 (which is now named Digital Angel Technology Corporation and is a wholly-owned subsidiary of the Company). Mr. Santelli joined the former Digital Angel Corporation (then named Destron Fearing Corporation) in September 1999 as Vice President-Finance and Chief Financial Officer. From October 1998 until September 1999, he was Chief Operating Officer of Doorlite, Inc., a manufacturer of specialty door glass with approximately \$40 million in annual revenues. From November 1995 until October 1998, Mr. Santelli was Chief Financial Officer and Vice President, Finance of Hartzell Manufacturing, Inc., a manufacturer of custom plastic injected and metal die cast parts with approximately \$90 million in annual revenue. From December 1994 until November 1995, he was a Strategy Consultant for Continental Financial Management Corp., which was a start-up asset financing company. Mr. Santelli has a Bachelor's degree in Economics from Carleton College and an MBA in Finance from Cornell University.

James G. Naro has been Vice President, General Counsel and Secretary of the Company since March 21, 2005. From 2001 to June 2004, Mr. Naro was Senior Vice President and, from 1995 to 2004, General Counsel and Secretary of DirectTV Latin America, LLC, a provider of pay television services in 27 countries in Latin America and the Caribbean, with annual revenues exceeding \$600 million and over 3,000 employees. In 2003-2004, DirectTV Latin America, LLC was reorganized under Chapter 11 of the United States Bankruptcy Code. From 1995 to 2001, he served as Vice President of DirectTV Latin America, LLC. From 1986 to 1995, Mr. Naro was Senior Counsel for the Cisneros Group of Companies, a privately-held media, entertainment, technology and consumer products organization. Mr. Naro has a Bachelor of Arts degree from Niagara University, Niagara Falls, New York and a Juris Doctor degree from Boston University School of Law.

Lasse Nordfjeld has been the President of the Animal Applications Group of the Company since February 28, 2005. From May 2001 to February 2005, Mr. Nordfjeld was Chief Executive Officer, President and a member of the board of directors of DSD Holding A/S, which is the parent company of DigiTag A/S and Daploma International A/S, manufacturer of visual and electronic radio frequency identification tags for livestock. Mr. Nordfjeld has also been the Chairman for Daploma International A/S since May 1996, as well as the President for DigiTag A/S since May 2001 and a member of its board of directors since May 1998. Mr. Nordfjeld's son serves as the Chief Executive Officer of Daploma International A/S. Prior to this, Mr. Nordfjeld served as a technical director and was co-owner of UnoPlast, a manufacturer of single-use devices for the healthcare sector, and served as a Director of Production and held other senior level executive positions with Eskofot, a manufacturer of equipment for the graphics industry. Mr. Nordfjeld has a Bachelor's degree in Engineering and a Bachelor of Commerce in management and economy.

David M. Cairnie has been the Managing Director of our United Kingdom subsidiary, Signature Industries, Ltd., since March 27, 2002. Mr. Cairnie has been the Managing Director of Signature Industries, Ltd. since the management-led buy-out in 1993. Before the management led buy-out, Signature Industries, Ltd. was known as FKI Communications, a division of FKI plc, where Mr. Cairnie had been the Managing Director since 1990. Before joining FKI Communications, Mr. Cairnie worked for International Telephone and Telegraph (ITT). Mr. Cairnie completed the ITT Senior Management Development program at the London Business School and operated in various management roles before joining FKI.

Executive Compensation

The following table sets forth the compensation earned from the Company by Kevin N. McGrath, the President and Chief Executive Officer of the Company since January 12, 2004, and Van Chu, Chief Executive Officer of the Company from November 3, 2003 until January 12, 2004. The table below also provides information for each of the years ended December 31, 2004, 2003 and 2002 about the other four most highly compensated executive officers of the Company whose salary and bonus exceeded \$100,000 in 2004, including Thomas M. Hall, M.D., M.I.M., the Chief Executive Officer of the Company until March 27, 2002, who remains an employee of the Company. (The officers identified in the table are known as the Named Executive Officers.) Mr. Lasse Nordfjeld was appointed as the Company's President of the Animal Applications Group on February 28, 2005 and Mr. James G. Naro was appointed as the Company's Vice President, General Counsel and Secretary on March 21, 2005, and accordingly are not listed in the summary compensation table.

Summary Compensation Table

Name and Principal Position	Year	Annual Compensation		Other Annual Compensation (\$)	Long-Term Compensation Awards	
		Salary (\$)	Bonus (\$)		Shares of Stock Underlying Options (#)	All Other Compensation
Kevin N. McGrath	2004	240,384	324,318(1)	16,712(2)	1,000,000(3)	-0-
President and Chief Executive Officer	2003	-0-	-0-	-0-	-0-	-0-
	2002	-0-	-0-	-0-	-0-	-0-
Van Chu	2004	27,424	-0-	462(4)	-0-	64,763(5)
Former Chief Executive Officer	2003	33,654	-0-	1,615(4)	1,000,000	-0-
	2002	-0-	-0-	-0-	-0-	-0-
Thomas M. Hall, M.D., M.I.M.	2004	270,000	-0-	12,317(6)	-0-	-0-
Former Chief Executive Officer and Chief Physician	2003	260,000	-0-	10,615(6)	-0-	-0-
	2002	260,000	-0-	-0-	-0-	-0-
James P. Santelli (7)	2004	181,731	112,489(1)	-0-	150,000	-0-
Vice President-Finance and Chief Financial Officer	2003	171,634	-0-	-0-	100,000	-0-
	2002	175,000	-0-	-0-	250,000	-0-
Kevin L. Nieuwsma (8)	2004	155,769	-0-(9)	-0-	100,000	-0-
Vice President	2003	145,090	-0-	-0-	200,000	-0-
	2002	134,954	-0-	-0-	100,000	-0-
David M. Cairnie(10)	2004	220,850	124,500(11)	-0-	100,000	-0-
Managing Director, Signature Industries, Ltd.	2003	176,143	4,738	-0-	-0-	-0-
	2002	158,159	4,428	7,523(12)	50,000	-0-

- (1) Bonuses accrued during the fiscal year ended December 31, 2004 and were paid in 2005.
- (2) Consists of (i) \$12,077 for Mr. McGrath's vehicle allowance and (ii) \$4,635 paid for Mr. McGrath's life insurance.
- (3) Option was granted outside the Company's 2002 Stock Plan.
- (4) Consists of Mr. Chu's vehicle allowance.
- (5) Consists of (i) \$50,000 severance payment and (ii) reimbursement of COBRA premiums in the amount of \$14,763.
- (6) Consists of Dr. Hall's vehicle lease payments.
- (7) Mr. Santelli became Vice President-Finance and Chief Financial Officer on March 27, 2002.
- (8) Mr. Nieuwsma became Vice President on November 11, 2002 and resigned on January 3, 2005.
- (9) Does not include \$37,800 which is currently in dispute with Mr. Nieuwsma.
- (10) Mr. Cairnie was paid in Sterling. The table reflects the amounts converted into US dollars using the following exchange rates: 1.83 in 2004, 1.635 in 2003 and 1.528 in 2002.
- (11) Consists of (i) \$23,603 that was paid during the fiscal year ended December 31, 2004 and (ii) \$100,897 that accrued during the fiscal year ended December 31, 2004 but was paid in 2005.
- (12) Consists of Mr. Cairnie's vehicle allowance.

Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A

The following table sets forth information concerning grants of stock options in the year ended December 31, 2004 to the Named Executive Officers. Except as indicated, all grants of options were made under the Company's 2002 Stock Plan. No options were granted in 2004 under the Company's 1998 Stock Plan.

Stock Option Grants in 2004

Individual Grants

Name	Securities Underlying Options Granted (#)	Percent of Total Options Granted to Employees in Fiscal Year	Exercise or Base Price (\$/sh)	Expiration Date	Potential Realizable Value at Assumed Annual Rates of Stock Price Appreciation For Option Term	
					5% (\$)	10% (\$)
Kevin N. McGrath	1,000,000(1)	48.1%	\$ 3.92	1/12/2014	\$ 2,465,267	\$ 6,247,470
Van Chu		0.0%				
Thomas M. Hall, M.D., M.I.M.		0.0%				
James P. Santelli	150,000	7.2%	\$ 3.79	3/15/2014	\$ 357,527	\$ 906,043
Kevin L. Nieuwsma	100,000	4.8%	\$ 3.79	3/15/2014	\$ 238,351	\$ 604,028
David M. Cairnie	100,000	4.8%	\$ 3.79	3/15/2014	\$ 238,351	\$ 604,028

(1) Granted outside of the Company's 2002 Stock Plan.

The following table sets forth information concerning stock options exercised in the year ended December 31, 2004 and held as of December 31, 2004 by the Named Executive Officers.

Aggregated Option Exercises In Last Fiscal Year

and Fiscal Year-End Option Values

Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A

Name	Shares Acquired on Exercise(#)	Value Realized(\$)	Number of Unexercised Options at Fiscal Year End(#)		Value of Unexercised In-the-Money Options at Fiscal Year End\$(1)	
			Exercisable	Unexercisable	Exercisable	Unexercisable
Kevin N. McGrath			250,000	1,000,000	\$ 1,412,500	\$ 3,810,000
Van Chu						
Thomas M. Hall, M.D., M.I.M.			180,000		\$ 537,000	
James P. Santelli	385,375	\$ 861,791	100,000	150,000	\$ 384,000	\$ 591,000
Kevin L. Nieuwsma	132,291	\$ 481,319	200,000	133,334	\$ 768,000	\$ 538,670
David M. Cairnie	33,333	\$ 101,332		116,667		\$ 466,335

(1) Based on the difference between the December 31, 2004 closing price of \$7.73 per share as reported on The American Stock Exchange and the exercise prices of the options.

Personal Benefits

Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A

The Company seeks to maintain an egalitarian culture in its facilities and operations. The Named Executive Officers are not entitled to operate under different standards than other employees of the Company. As such, the Company does not provide the Named Executive Officers with separate dining or other facilities and does not have programs that provide personal benefit perquisites to Named Executive Officers, such as permanent lodging or defraying the cost of personal entertainment or family travel, except as described below. The Company's health care and other insurance programs are the same for all eligible employees including the Named Executive Officers.

It has been the practice of the Company to reimburse the Named Executive Officers for the expenses of cellular phones, blackberries and home internet which are used primarily for work. In the fiscal year ended December 31, 2004, the total aggregate amount of such expenses reimbursed was \$4,609.

401(k) Profit Sharing Plan and Trust

The Company maintains a 401(k) profit sharing plan for the benefit of eligible employees and their beneficiaries in which executive officers participate on the same basis as all other employees, subject to certain overall and specific anti-discrimination restrictions. An employee is eligible to participate in the 401(k) plan after completing 60 days of service. The plan is a defined contribution profit sharing plan designed to be funded with both Company and employee contributions. Employees may voluntarily contribute up to an annual dollar amount of \$13,000 in 2004, plus catch-up contributions for employees over the age of 50 up to an additional annual dollar amount of \$3,000. Employees may make contributions by payroll deductions. The Company has the option to make matching contributions each year for eligible employees. The amount of any matching contribution by the Company is determined by the Company. Distributions from the 401(k) plan are available only after reaching the age of 59-1/2 years (for salary deferral accounts) or termination of employment.

No amounts were paid or distributed during 2004 by the 401(k) plan to the Named Executive Officers, except that \$5,593 was distributed back to Messrs. Santelli and Nieuwsma who, it was determined, had made salary deferrals in the plan year ending December 31, 2003 that exceeded the amount allowed for highly compensated employees under the plan's non-discrimination testing. The Company contributed no benefit amounts under the plan for the Named Executive Officers during 2004, 2003 or 2002.

Stock Plans

Securities Authorized for Issuance Under Equity Compensation Plans

The following table sets forth certain information as of December 31, 2004 with respect to Company's 1998 Stock Plan and 2002 Stock Plan and certain options and warrants granted by the Company outside of the 1998 Stock Plan and 2002 Stock Plan:

Equity Compensation Plan Information

Plan category	Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)	Weighted-average exercise price of outstanding options, warrants and rights (b)	Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by security holders (1)	4,541,139	\$ 3.00	4,140,208
Equity compensation plans not approved by security holders (2)	2,706,582	\$ 3.99	272,010
Total	7,247,721	\$ 3.37	4,412,218

(1) Consists of only the 2002 Stock Plan, which is described below under the subheading 2002 Stock Plan.

(2) Consists of the 1998 Stock Plan, which is described below under the subheading 1998 Stock Plan, outstanding options to purchase 1,500,000 shares and outstanding warrants to purchase 719,762 shares.

2002 Stock Plan

The following is a summary of the terms of the 2002 Stock Plan and is qualified in its entirety by reference to the 2002 Stock Plan.

Effective April 11, 2002, the Company's Board of Directors adopted the 2002 Stock Plan, subject to approval by the stockholders of the Company, and reserved 5,195,312 shares of common stock for issuance under the 2002 Stock Plan. On June 27, 2002, the Board amended the 2002 Stock Plan to increase the number of shares reserved for issuance under the plan from 5,195,312 to 11,195,312 shares. On October 22, 2002, the Company's stockholders approved the 2002 Stock Plan and the amendment to the 2002 Stock Plan increasing the number of shares reserved for issuance to 11,195,312 shares and allowing the Company's Board to designate participants in the 2002 Stock Plan. On May 6, 2004, the Company's stockholders approved an amendment to the 2002 Stock Plan increasing the number of shares reserved for issuance to 16,195,312. As of March 22, 2005, 16,195,312 shares of common stock were reserved for issuance under the 2002 Stock Plan, of which 15,343,340 shares have been issued under the 2002 Stock Plan and 851,972 shares remain available to be issued under the 2002 Stock Plan. As of

March 22, 2005, awards consisting of options to purchase 7,827,375 shares of common stock were outstanding under the 2002 Stock Plan. As of March 22, 2005, there were outstanding options to purchase 1,500,000 shares of common stock which were granted outside the 2002 Stock Plan and the Company's 1998 Stock Plan. The Board of Directors and the Board's Compensation Committee administer the 2002 Stock Plan. Benefits under the 2002 Stock Plan may be granted to only employees and directors of the Company and its affiliates, consisting of approximately 245 individuals. The participants are those persons who are selected by the Board or the Committee.

The 2002 Stock Plan permits the Board or the Committee to grant benefits in the form of stock options, stock appreciation rights, restricted stock, cash awards, performance-based awards or any combination thereof. Any of such awards may, as determined by the Board or the Committee, be granted in a manner such that they qualify for the performance-based compensation exemption of Section 162(m) of the Code.

Options granted under the 2002 Stock Plan may be either incentive stock options which satisfy the requirements of Section 422 of the Code or non-qualified stock options which are not intended to meet such requirements. Incentive stock options may be granted only to participants who are employees of the Company or its affiliates as of the date of grant. The Board or the Committee determines the per share option exercise price subject to the requirements imposed by the Code and the 2002 Stock Plan. The 2002 Stock Plan and the Code provide that the exercise price for shares under any incentive stock option shall not be less than the fair market value of the shares at the time the option is granted. The 2002 Stock Plan provides that the exercise price for shares under non-qualified stock options shall not be less than 85% of the fair market value of the shares at the time the option is granted. Options may be exercised at such time or times and subject to such terms and conditions as are determined by the Board or the Committee. However, incentive stock options may not be exercised more than ten years after the date they are granted.

Unless permitted by the Board or the Committee, each benefit granted under the 2002 Stock Plan is not transferable other than by will or other laws of descent and distribution and is exercisable during the participant's lifetime only by the participant. Unless otherwise determined by the Board or the Committee, in the event of a change of control (as that term is defined in the 2002 Stock Plan), all options and other awards then outstanding under the 2002 Stock Plan will become fully vested.

The Board of Directors has the sole right and power to amend the 2002 Stock Plan at any time. However, it cannot amend the 2002 Stock Plan without approval of the Company's stockholders in a manner which would cause options which are intended to qualify as incentive stock options to fail to qualify as such, in a manner which would cause the 2002 Stock Plan to fail to meet the requirements of Rule 16b-3 under the Securities Exchange Act of 1934, or in a manner which would violate applicable law. The plan has no specific term and will continue in full force and effect until terminated. The 2002 Stock Plan may be terminated at any time by the Board.

1998 Stock Plan

Effective March 1, 1998, the Board of Directors of Medical Advisory Systems, Inc. adopted the 1998 Stock Plan. The 1998 Stock Plan and the Board's amendments to the 1998 Stock Plan were not submitted to the Company's stockholders for their approval. Only options that are not incentive stock options may be granted under the 1998 Stock Plan. The exercise price per share of common stock under each option granted under the 1998 Stock Plan must not be less than the fair market value of the common stock at the close of business on the date the option is granted. Under the 1998 Stock Plan, "fair market value" is the average of the highest and lowest price for a share of common stock as quoted on The American Stock Exchange on the last trading date immediately before the date of the grant. The exercise

price of an option may be paid with cash or a certified check, or with the surrender of shares of common stock having a fair market value on the date of exercise equal to that portion of the purchase price for which payment in cash or by certified check is not made.

Upon termination of employment except by death or in connection with a change of control, an employee has three months after cessation of employment to exercise his options under the 1998 Stock Plan to the extent that such employee is entitled to exercise them on the date of cessation of employment. Upon a change of control, all non-vested options immediately vest and are exercisable. The merger of the former Digital Angel Corporation with the wholly-owned subsidiary of the Company on March 27, 2002 triggered the vesting of options to purchase 600,000 shares under the 1998 Stock Plan. Upon an option holder's death while employed by the Company, or within three months after having retired with the consent of the Company, the employee's executors or administrators or the legatees or heirs of his estate have the right to exercise the options that are vested and not exercised to the extent that the deceased employee was entitled to exercise the options on the date of his death. However, no options are exercisable more than 10 years from the date they are granted. The plan expires on March 1, 2008. Under the 1998 Stock Plan, options may be granted to officers, directors, employees, advisors and consultants who render services to the Company. As of March 22, 2005, 1,650,000 shares of common stock were reserved for issuance under the 1998 Stock Plan, of which 1,377,990 shares have been issued under the 1998 Stock Plan and 272,010 remain available to be issued under the 1998 Stock Plan. As of March 22, 2005, awards consisting of options to purchase 476,820 shares were outstanding under the 1998 Stock Plan.

Employment Agreements

Employment Agreements with Former Executive Officers of Medical Advisory Systems, Inc.

Before March 27, 2002, the effective date of the merger, the Company entered into employment agreements with Ronald W. Pickett and Thomas M. Hall, M.D. On October 26, 2001, the Company signed amendments to the employment agreements with each of Mr. Pickett and Dr. Hall that reflected both certain prior oral amendments to the employment agreements and additional amendments. The amendments confirmed the extension of the term of each of Mr. Pickett's and Dr. Hall's employment agreement through October 31, 2006 and established that Mr. Pickett would receive an annual salary of at least \$180,000 and Dr. Hall would receive an annual salary of at least \$260,000 throughout the term of their employment agreements. The amendments also provide that if Mr. Pickett's or Dr. Hall's employment was terminated or they resigned at any time following a change of control of the Company, each of Mr. Pickett and Dr. Hall would be entitled to a \$250,000 payment, plus an amount equal to all salary and other benefits that would have been paid under the employment agreement for the remainder of the term of their agreements as though no termination or resignation occurred, plus an amount equal to the value of the fringe benefits, such as medical and dental insurance and use of an automobile, to which Mr. Pickett and Dr. Hall otherwise would have been entitled under their employment agreements for the remainder of the term, plus participation in any profit sharing, stock option or similar plans. These payments are due 30 days after termination of employment. The definition of change of control in the employment agreements also was amended to include any consolidation, merger or share exchange, regardless of whether the Company was the surviving corporation, in which any or affiliated person acquires in excess of 20.0% of the combined voting power of the then-outstanding securities of the Company.

Under the amended employment agreements, the March 27, 2002 merger of the Company's wholly-owned subsidiary with the former Digital Angel Corporation constituted a change of control. Therefore, each of Mr. Pickett and Dr. Hall is entitled to a \$250,000 payment from the Company plus the salaries and other benefits for the remaining term of their employment agreements upon the termination

of their employment with the Company. Mr. Pickett resigned his position with the Company on March 27, 2002, and the Company paid to him the \$250,000 amount due under his agreement. Because Dr. Hall remains an employee of the Company, the Company accrued for Dr. Hall's \$250,000 payment due to him under his agreement. During 2004, the Company paid a total of \$197,868 of salary and fringe benefits to Mr. Pickett and a total of \$282,317 of salary and fringe benefits to Dr. Hall due to them under their agreements.

Employment Agreements with the Company's Current Executive Officers

The Company does not have a formal written employment agreement with Kevin N. McGrath, its President and Chief Executive Officer. The terms of Mr. McGrath's employment provide that the Company will pay Mr. McGrath an initial base salary of \$250,000 per year and a bonus as determined by the Compensation Committee of the Board of Directors. Mr. McGrath's base salary was increased to \$300,000 per year effective on February 28, 2005. In addition, the Company has agreed to pay Mr. McGrath's life insurance premiums of approximately \$4,800 per year and a \$1,000 per month automobile allowance. On December 2, 2004, the Company entered into a Change of Control Agreement with Mr. McGrath. Upon a Change of Control (as defined in the agreement), Mr. McGrath would be entitled to receive three times his base salary and three times his average bonus paid to him for the three full years immediately prior to the Change of Control. Under the agreement, a Change of Control has occurred if: (i) any person or entity (or persons or entities acting as a group) other than Applied Digital Solutions, Inc., the Company's majority stockholder, acquires stock of the Company that, together with stock then held by such person, entity or group, results in such person, entity or group holding more than fifty (50%) percent of the fair market value or total voting power of the Company; or, (ii) a member of the Board of Directors of the Company is replaced by a director (or added to the Company's Board of Directors) and such director was not nominated and approved by the Board of Directors; or, (iii) a change of control occurs at Applied Digital Solutions, Inc., as such term is defined in the employment agreement between the Company's current Chairman of the Board, Scott R. Silverman, and Applied Digital Solutions, Inc.

Effective as of April 1, 2002, the Company entered into an employment agreement with Mr. James P. Santelli, its Vice President, Finance and Chief Financial Officer. The agreement has a term of three years. The term is automatically renewed for successive one-year terms on each anniversary date of the agreement, which is added at the end of the then existing term, unless either party notifies the other at least 60 days prior to such an anniversary date. The agreement provides that the Company shall pay Mr. Santelli an initial base salary of \$175,000 per year and that he is entitled to participate in any of the Company's benefit and deferred compensation plans or programs as are from time to time available to officers of the Company. Mr. Santelli's base salary was increased to \$205,000 per year effective on February 28, 2005. The agreement contains confidentiality, non-compete and assignment of invention clauses. The agreement also provides that if the Board of Directors terminates Mr. Santelli's employment with the Company because of his willful and material misconduct or because he has breached the agreement in any material respect, or if Mr. Santelli terminates his employment other than for Good Reason (as that term is defined in the agreement), he is entitled to salary and benefits accrued through the date of termination of employment. If Mr. Santelli dies or becomes disabled (as disabled is determined under the agreement), if the Company terminates his employment for reasons other than his misconduct or his breach of the agreement, or if he terminates his employment for Good Reason, the Company must pay him his accrued compensation and benefits for the remaining term of the agreement, including any extensions. The employment agreement provides that upon a change of control, Mr. Santelli may terminate his employment at any time within one year after the change of control upon 15 days' notice. Upon such termination, the Company must pay to Mr. Santelli a severance payment equal to the base amount as defined in Section 280G(b)(3) of the Internal Revenue Code minus \$1.00. Upon a change of control, all outstanding stock options held by Mr. Santelli would become fully exercisable.

The Company does not have a formal written employment agreement with James G. Naro, its Vice President, General Counsel and Secretary. The terms of Mr. Naro's employment provide that the Company will pay Mr. Naro an initial base salary of \$160,000 per year, a bonus as determined by the Compensation Committee of the Board of Directors and a ten-year option to purchase 200,000 shares of the Company's common stock. The option has an initial exercise price of \$4.64 per share and vests ratably over a three year period. Mr. Naro will also be entitled to participate in any of the Company's benefit and deferred compensation plans or programs as are from time to time available to officers of the Company.

Effective as of February 28, 2005, the Company entered into an employment agreement with Mr. Lasse Nordfjeld, its President of the Animal Applications Group. The agreement has an initial term of one year. The term is automatically renewed for successive one-year terms on each anniversary date of the agreement, which is added at the end of the then existing term, unless either party notifies the other at least 90 days prior to such an anniversary date. The agreement provides that the Company shall pay Mr. Nordfjeld a base salary of 1,200,000 Danish Kroner per year, a performance based annual bonus up to 50% of his base salary and a one time option to purchase 150,000 shares of the Company's common stock, and that he is entitled to participate in any of the benefit plans or programs as are from time to time available to officers of DSD Holding A/S, a wholly-owned subsidiary of the Company. The agreement contains confidentiality, non-compete and assignment of invention clauses. The agreement also provides that if the Board of Directors terminates Mr. Nordfjeld's employment with the Company because of his willful and material misconduct or because he has breached the agreement in any material respect, or if Mr. Nordfjeld terminates his employment other than for Good Reason (as that term is defined in the agreement), he is entitled to salary, bonus and benefits accrued through the date of termination of employment. If Mr. Nordfjeld dies, his estate is entitled to his salary, bonus and benefits accrued through the last day of the month in which his death occurs. If Mr. Nordfjeld becomes disabled (as determined under the agreement), Mr. Nordfjeld is entitled to salary, bonus and benefits accrued through 90 days after notice of termination. If the Company terminates his employment for reasons other than his misconduct or his breach of the agreement, or if he terminates his employment for Good Reason, the Company must pay him his accrued compensation and benefits for the remaining term of the agreement, including any extensions. The employment agreement provides that upon a change of control, Mr. Nordfjeld may terminate his employment at any time within one year after the change of control upon 15 days' notice. Upon such termination, the Company must pay to Mr. Nordfjeld a severance payment equal to the base amount as defined in Section 280G(b)(3) of the Internal Revenue Code minus \$1.00. Upon a change of control, all outstanding stock options held by Mr. Nordfjeld would become fully exercisable.

The Company has an employment agreement with David M. Cairnie effective April 13, 1993. The initial term of the agreement is one year until terminated by either party giving six months' notice or payment in lieu of such notice expiring on or at any time one year after the effective date of the agreement. The agreement provides that the Company will pay Mr. Cairnie an initial base salary of £75,000 per year, or a higher rate as to which the parties may from time to time agree. Mr. Cairnie's base salary was increased to £125,000 per year effective on April 1, 2004. The agreement also provides for a bonus based on the achievement of profits, as defined in the agreement. In addition, under the agreement, the Company is to provide an automobile to Mr. Cairnie. The agreement includes a non-compete provision.

The Company had an employment agreement with Kevin L. Nieuwsma effective between October 1, 2000 and January 3, 2005, the date Mr. Nieuwsma terminated his employment with the Company. The agreement provided that the Company would pay Mr. Nieuwsma an initial base salary of \$125,000 per year and that he was entitled to participate in any of the Company's benefit and deferred

compensation plans or programs that were available to its officers. The agreement contained confidentiality, non-compete and assignment of inventions clauses. The agreement also provided that if Mr. Nieuwsma terminated his employment other than for Good Reason (as that term is defined in the agreement), he would be entitled to salary and benefits accrued through the date of termination of employment. Mr. Nieuwsma terminated his employment with the Company on January 3, 2005 for reasons other than Good Reason. Therefore, the Company paid him his salary and benefits accrued through the date of termination.

Certain Transactions

In 2004, the Company paid \$24,038 to Richard J. Sullivan, a former Director and Chairman of the Company.

In 2004, the Company recognized \$87,000 of revenue under a Distribution and Licensing Agreement with Verichip Corporation, a wholly-owned subsidiary of Applied Digital Solutions, Inc.

REPORT OF THE COMPENSATION COMMITTEE

Notwithstanding anything to the contrary set forth in any of the Company's previous filings under the Securities Act of 1933 or the Exchange Act that might incorporate future filings or this proxy statement, the following report shall not be deemed to be incorporated by reference into any such filings. In addition, the following report shall not be deemed to be soliciting material or filed with the SEC.

The role of Compensation Committee is to determine the amount of compensation of, and incentives for, the Company's executive officers. The Compensation Committee also has the power to administer the 1998 Stock Plan and the 2002 Stock Plan.

The base salary, bonus and benefits payable to the executive officers of the Company for the year ended December 31, 2004 were fixed under written employment agreements, except for Kevin N. McGrath and Van Chu, who acted as Chief Executive Officer of the Company from November 3, 2003 until January 12, 2004. The terms of these agreements were determined before January 1, 2004 and before the appointment of the members of the Compensation Committee for 2004. These employment agreements provide as follows:

Dr. Hall was employed under an employment agreement that commenced on November 1, 1998 and provided for an initial annual salary of \$260,000 and bonuses and benefits based on the Company's internal policies.

Mr. Santelli's employment agreement is for a three-year term that commenced on April 1, 2002 and is automatically extended for an additional one-year term on each anniversary date of the agreement. It provides for an initial annual base salary of \$175,000. Mr. Santelli's base salary was increased to \$205,000 per year effective on February 28, 2005.

Mr. Nieuwsma's employment agreement was for a one-year term that commenced on October 1, 2000 and was automatically renewable for successive one-year periods. It provided for an initial annual base salary of \$125,000 per year. Mr. Nieuwsma terminated his employment with the Company on January 3, 2005 for reasons other than Good Reason, as that term was defined in his employment agreement.

Mr. Cairnie's employment agreement is for a one-year term that commenced on April 13, 1993 and is automatically renewable for successive one-year periods. It provides for an initial annual base salary of £75,000 per year. Mr. Cairnie's base salary was increased to £125,000 per year effective on April 1, 2004.

As described above in this proxy statement, the Company maintains the 1998 Stock Plan and the 2002 Stock Plan under which stock options may be granted to officers, directors, employees, advisors and consultants who render services to the Company.

Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A

Mr. McGrath's compensation, including his options, that he received during 2004 while he served as President and Chief Executive Officer of the Company was determined by the Company's Board of Directors. In making its determination, the Board considered the compensation, including the terms of options, of chief executive officers of comparable companies, as well as the availability of standard benefit packages and stock options at comparable companies. The Board also based Mr. McGrath's compensation on his expected performance and his achievement of expected performance goals.

Mr. Chu's compensation that he received during 2004 while he served as Chief Executive Officer of the Company was determined by the Company's Board of Directors. In making its determination, the Board considered the compensation of chief executive officers of comparable companies, as well as the availability of standard benefit packages and stock options at comparable companies. The Board also based Mr. Chu's compensation on his expected performance and his achievement of expected performance goals.

By the Compensation Committee

Howard S. Weintraub, Ph.D. (Chairman)

Michael S. Zarriello

John R. Block

REPORT OF THE AUDIT COMMITTEE

Notwithstanding anything to the contrary set forth in any of the Company's previous filings under the Securities Act of 1933 or the Securities Exchange Act of 1934 that might incorporate future filings or this proxy statement, the following report shall not be deemed to be incorporated by reference into any such filings. In addition, the following report shall not be deemed to be soliciting material or filed with the SEC.

The Audit Committee for the year ended December 31, 2004, whose members are identified below, has reviewed and discussed the audited financial statements as of and for the year ended December 31, 2004 with management of the Company and has discussed the matters required to be discussed by SAS 61 with the Company's independent auditors. The Audit Committee has also received the written disclosures and the letter from the Company's independent auditors required by Independent Standards Board Standard No. 1 and has discussed with the independent auditors the independent auditors' independence. Based upon its review of the foregoing materials and its discussions with the Company's management and independent auditors, the Audit Committee recommended to the Board of Directors that the audited financial statements be included in the Company's Annual Report on Form 10-K for the year ended December 31, 2004.

The Audit Committee has a written charter adopted by the Board on March 27, 2003 that was filed with the Company's Proxy Statement dated April 14, 2003. The Audit Committee established procedures for the receipt, retention and treatment of any complaints received by the Company regarding accounting, internal accounting controls or auditing matters and the confidential, anonymous submission by the Company's employees of any concerns regarding questionable accounting or auditing matters.

By the Audit Committee

Michael S. Zarriello (Chairman)
Howard S. Weintraub, Ph.D.
John R. Block

PERFORMANCE GRAPH

Notwithstanding anything to the contrary set forth in any of the Company's previous filings under the Securities Act of 1933 or the Securities Exchange Act of 1934 that might incorporate future filings or this proxy statement, the following performance graph and accompanying data shall not be deemed to be incorporated by reference into any such filings. In addition, they shall not be deemed to be soliciting material or filed with the SEC.

The Company's common stock is traded on The American Stock Exchange under the symbol DOC. The following graph shows changes during the period from December 31, 1999 to December 31, 2004 in the value of \$100 invested in: (1) the Company's common stock; (2) the Total Return Index for the American Stock Exchange (U.S.) (AMEX) compiled by the Center for Research in Securities Prices (CRSP) at the University of Chicago, Chicago, Illinois; and (3) the CRSP Total Return Index for AMEX Consumer Manufacturing Stocks. The values of each investment as of the dates indicated are based on share prices plus any dividends paid in cash, with the dividends reinvested on the date they were paid. The calculations exclude trading commissions and taxes.

	12/31/99	12/31/00	12/31/01	12/31/02	12/31/03	12/31/04
Digital Angel Corporation	\$ 100.00	\$ 33.15	\$ 37.69	\$ 19.62	\$ 36.46	\$ 59.46
CRSP Total Return Index for the AMEX Stock Market (U.S.)	\$ 100.00	\$ 92.76	\$ 86.34	\$ 70.57	\$ 95.52	\$ 110.38
CRSP Total Return Index for AMEX Consumer Manufacturing Stocks	\$ 100.00	\$ 90.00	\$ 119.73	\$ 127.58	\$ 169.42	\$ 256.50

BENEFICIAL OWNERSHIP OF COMMON STOCK

The following table sets forth information as of March 22, 2005 regarding the beneficial ownership of shares of common stock of the Company by (i) each person (including any group) who is known by the Company to beneficially own more than 5% of the Company's common stock, (ii) each Named Executive Officer, (iii) each Director of the Company as of March 22, 2004, and (iv) all Directors and executive officers of the Company as a group.

Name of Beneficial Owner (1)	Number of Shares Beneficially Owned	Percent of Outstanding Shares (2)
<i>Current Directors and Executive Officers:</i>		
Kevin N. McGrath	683,333(3)	1.5%
Scott R. Silverman	1,050,000(4)	2.3%
John R. Block	325,000(4)	*
Howard S. Weintraub, Ph.D.	358,333(4)	*
Michael S. Zarriello	358,333(4)	*
Kevin H. McLaughlin	283,333(4)	*
James P. Santelli	214,875(5)	*
James G. Naro	0	0%
Lasse Nordfjeld	0	0%
David M. Cairnie	33,333(4)	*
All current executive officers and Directors as a group (9 persons)	3,306,540(6)	7.0%
<i>Former Named Executive Officers:</i>		
Van Chu	0	0%
Thomas M. Hall, M.D., M.I.M	170,000(4)	*
Kevin L. Nieuwsma	0(7)	0%
<i>Certain Other Beneficial Owners:</i>		
Applied Digital Solutions, Inc. 1690 South Congress Avenue Suite 200 Delray Beach, FL 33445	24,291,673	55.2%

* Less than 1%.

(1) Unless otherwise indicated, the Company believes that the beneficial owners of the common stock described above, based on information furnished by such owners, have sole investment and voting power with respect to such shares, subject to community property laws where applicable.

(2) Based on 44,044,914 shares outstanding as of March 22, 2005, which does not include 10,523,957 shares of common stock subject to stock options and warrants outstanding as of March 22, 2005. However, as indicated, each figure showing the percentage of outstanding shares owned beneficially has been calculated by treating as outstanding and owned the shares which could be purchased by each beneficial owner within 60 days of March 22, 2005 upon the exercise of stock options and warrants.

(3) Consists of 100,000 shares owned by Mr. McGrath and 583,333 shares subject to options held by Mr. McGrath.

- (4) Consists of shares subject to options.
- (5) Consists of 114,875 shares owned by Mr. Santelli and 100,000 shares subject to options held by Mr. Santelli.
- (6) Consists of (i) 100,000 shares owned by Mr. McGrath, (ii) 114,875 shares owned by Mr. Santelli and (iii) 3,091,665 shares subject to options held by all current executive officers and Directors as a group.
- (7) Does not include an option to purchase 200,000 shares which is currently in dispute with Mr. Nieuwsma.

SECTION 16(a) BENEFICIAL OWNERSHIP

REPORTING COMPLIANCE

As required by rules adopted by the SEC under Section 16 of the Securities Exchange Act of 1934, directors and executive officers of the Company are required to file with the SEC an Initial Report of Beneficial Ownership on Form 3 within a certain period after becoming an executive officer or director stating the number of shares of common stock owned, a Report of Change in Beneficial Ownership on Form 4 to report certain transactions in the Company's common stock and an Annual Statement of Beneficial Ownership of Securities on Form 5 to report other transactions in securities of the Company that are not required to be reported on a Form 4. Based upon the Company's review of such Forms furnished to it by the directors and executive officers required to file such Forms with respect to the year ended December 31, 2004, the Company believes that all of these filing requirements were satisfied during 2004, except that Mr. Silverman filed a Form 4 on February 26, 2004 reporting one option grant on an untimely basis.

PROPOSAL 2

APPROVAL OF AMENDMENT TO 2002 STOCK PLAN

INCREASING NUMBER OF SHARES

As described above, the Board adopted the 2002 Stock Plan effective April 11, 2002. On June 27, 2002, the Board amended the 2002 Stock Plan to increase the number of shares reserved for issuance under the plan from 5,195,312 shares to 11,195,312 shares. The 2002 Stock Plan, as amended, was approved by the Company's stockholders on October 22, 2002. A further amendment to increase the number of shares reserved for issuance under the 2002 Stock Plan to 16,195,312 shares was approved by the Company's stockholders on May 6, 2004.

In order to grant additional future awards under the 2002 Stock Plan, on March 21, 2005, the Board amended the 2002 Stock Plan, subject to stockholder approval, to increase the number of reserved shares by 2,000,000 for a total of 18,195,312 reserved shares. The increase in the reserved shares would provide the Company the ability to grant future awards utilizing 2,851,972 remaining reserved shares under the 2002 Stock Plan.

Major Provisions of the 2002 Stock Plan

The following is a summary of the major provisions of the 2002 Stock Plan. For a complete description of the 2002 Stock Plan, please read it in its entirety. A copy of the 2002 Stock Plan, as amended, is included in this proxy statement as Appendix A.

Purpose

The purpose of the 2002 Stock Plan is to provide incentive that will retain, motivate and reward employees and directors of Company and to encourage ownership of the Company's common stock by them.

Administration

The 2002 Stock Plan provides that the committee administering the plan (Committee) may consist of the Board or a committee of two or more but less than all of the members of the Board. The Board's Compensation Committee currently acts as the Committee for the 2002 Stock Plan.

Shares Subject to 2002 Stock Plan

The Board initially reserved 5,195,312 shares of common stock for issuance under the 2002 Stock Plan. On June 27, 2002, the Board amended the 2002 Stock Plan to reserve 11,195,312 shares of common stock. The stockholders approved the 2002 Stock Plan as amended at the annual meeting of stockholders held on October 22, 2002. On March 12, 2004, the Board amended the 2002 Stock Plan to reserve 16,195,312 shares of common stock, and the stockholders approved the increase at the annual meeting of stockholders held on May 6, 2004. The maximum number of shares of common stock with respect to which benefits may be granted or measured to any participant under the 2002 Stock Plan is subject to adjustments made in accordance with the terms of the 2002 Stock Plan. As of March 22, 2005, 16,195,312 shares of common stock were reserved for issuance under the 2002 Stock Plan, of which 15,343,340 shares have been issued under the 2002 Stock Plan and 851,972 shares remain available to be issued under the 2002 Stock Plan. As of March 22, 2005, awards consisting of options to purchase 7,827,375 shares of common stock are outstanding under the 2002 Stock Plan.

Eligibility

The 2002 Stock Plan provides that the participants in the 2002 Stock Plan shall be those persons who are selected by the Committee subject to the approval of the Board if the Committee does not consist of the entire Board. Under the terms of the 2002 Stock Plan, benefits may be granted to only employees and directors of the Company and its affiliates, currently consisting of approximately 245 individuals.

Types of Benefits

The 2002 Stock Plan permits the Committee to grant benefits in the form of stock options, cash awards, restricted stock awards, stock appreciation rights, reload options or any combination thereof. The Committee may determine that stock awards consist of performance-based awards.

Options. Options granted under the 2002 Stock Plan may be either incentive stock options satisfying the requirements of Section 422 of the Internal Revenue Code of 1986 (the Code) or non-qualified stock options that are not intended to meet such requirements. Incentive stock options may be granted only to participants who are employees of the Company or its affiliates as of the date of grant. The Code places certain restrictions on the granting of incentive stock options to participants who own stock possessing over 10% of the total combined voting power of the Company or its affiliates.

The Committee determines the exercise price per share of options, subject to the requirements imposed by the Code and the 2002 Stock Plan. The 2002 Stock Plan and the Code provide that the exercise price for shares under any incentive stock option shall be no less than the fair market value of the shares at the time the option is granted. The 2002 Stock Plan provides that the exercise price for shares under each non-qualified stock option shall be no less than 85% of the fair market value of the shares at the time the option is granted.

Options may be exercised at such time or times and subject to such terms and conditions as are determined by the Committee. However, incentive stock options may not be exercised more than ten years after the date they are granted. Payment for shares of common stock purchased

Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A

upon exercise of an option or any other benefit granted under the 2002 Stock Plan that requires payment by a participant to the Company may be made in: (i) cash, including by means of a so-called "cashless exercise" of an option; (ii) by the surrender of all or part of a benefit, including the benefit being exercised; (iii) by the tender to the Company of shares of common stock owned by the optionee and registered in the optionee's name having a fair market value equal to the amount due to the Company; (iv) other property, rights and credits deemed acceptable by the Committee; or (v) by any combination of these methods. However, any

method of payment other than by cash or cashless exercise may be used only with the consent of the Committee unless and to the extent permitted in the agreement containing the terms of the option or benefit.

Stock Appreciation Rights. Under the 2002 Stock Plan, the Committee may grant stock appreciation rights entitling the holder to receive a payment in cash, common stock or a combination of cash and common stock in an amount equal to the appreciation in the fair market value of a specified number of shares of common stock measured from the date the stock appreciation right was granted to the date such right was exercised. Stock appreciation rights also may be granted in tandem with a stock option, in which case the holder would be entitled to receive a payment equal to the appreciation of the stock option during the same measurement period. The 2002 Stock Plan provides that when stock appreciation rights are granted in tandem with an incentive stock option, the rights must have such terms or conditions as shall be required for the incentive stock option to qualify as an incentive stock option. Each stock appreciation right is exercisable at the times and subject to the terms and conditions as determined by the Committee.

Restricted Stock. Under the 2002 Stock Plan, the Committee may grant benefits in shares of common stock, which would be treated as restricted stock. Shares of restricted stock are issued and delivered at the time of the grant or as otherwise determined by the Committee, but they are subject to forfeiture until otherwise provided in the applicable agreement or the 2002 Stock Plan. Each stock certificate evidencing shares of common stock granted as a restricted stock award must bear a legend referring to the 2002 Stock Plan and describing the risk of forfeiture of the shares of common stock and stating that such shares are non-transferable until all restrictions have been satisfied and the legend has been removed. At the discretion of the Committee, the grantee may or may not be entitled to full voting and dividend rights with respect to all shares of restricted stock from the date of grant. Unless otherwise determined by the Committee, grants of shares of restricted stock must be made at a per share cost to the participant equal to par value.

Cash Awards. Under the 2002 Stock Plan, the Committee may grant cash awards payable in cash in such amounts as it deems appropriate. However, the amount of any cash award granted in any fiscal year to any participant who is subject to Section 16 of the Securities Exchange Act of 1934 (generally consisting of the Company's executive officers, directors and 10% beneficial owners) shall not exceed the greater of \$100,000 or 100% of such person's cash compensation for such fiscal year. The Committee determines the conditions under which cash awards are granted.

Performance-Based Awards. Any benefits granted under the 2002 Stock Plan may be granted in a manner such that the benefits qualify for the performance-based compensation exemption of Section 162(m) of the Code.

Non-Transferability

Unless otherwise specified in an agreement containing the terms of the benefit granted under the 2002 Stock Plan or permitted by the Committee, each benefit granted under the 2002 Stock Plan is not transferable other than by will or other laws of descent and distribution and is exercisable during the participant's lifetime only by the participant. However, a participant may file with the Committee a written designation of a beneficiary or beneficiaries to exercise, in the event of the death of the participant, an option or to receive any benefits. The Committee has the

right to review and approve beneficiary designations.

Status as Unfunded Plan

The 2002 Stock Plan is intended to constitute an unfunded plan for incentive and deferred compensation. All payments made under the 2002 Stock Plan will be paid from the general funds of the Company, and no special or separate fund has been established and no segregation of assets will be made to assure payment of such amounts. However, the Committee may authorize the creation of trusts or other arrangements to meet the obligations created under the 2002 Stock Plan to deliver shares of common stock or payments under the 2002 Stock Plan. The 2002 Stock Plan is not intended to be subject to the Employee Retirement Income Security Act of 1974, as amended.

Change of Control

Unless otherwise determined by the Committee, in the event of a change of control (as that term is defined in the 2002 Stock Plan), the following will occur:

all outstanding options will become fully exercisable, except to the extent that the right to exercise the option is subject to restrictions established in connection with a stock appreciation right that is issued in tandem with the option;

all outstanding stock appreciation rights will become immediately payable, except to the extent that the right to exercise the stock appreciation right is subject to restrictions established in connection with an option that is issued in tandem with the stock appreciation rights;

all shares of restricted stock will become fully vested;

all performance shares will be deemed to be fully earned and shall be paid out in such matter as determined by the Committee; and

all cash awards, other stock-based awards and other benefits will become fully vested and/or earned and paid out in such manner as determined by the Committee.

Amendment or Termination

Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A

The Board of Directors has the sole right and power to amend the 2002 Stock Plan at any time. However, it cannot amend the 2002 Stock Plan without approval of the Company's stockholders in a manner which would cause options which are intended to qualify as incentive stock options to fail to qualify as such, in a manner which would cause the 2002 Stock Plan to fail to meet the requirements of Rule 16b-3 under the Securities Exchange Act of 1934 or in a manner which would violate applicable law. The Committee may convert, modify, forfeit or cancel any benefit granted under the 2002 Stock Plan, in whole or in part, if and to the extent permitted in the 2002 Stock Plan or the applicable agreement or with the consent of the participant to whom such benefit was granted. Except as may be provided in an agreement, the Committee may, in whole or in part, waive any restrictions or conditions that apply to, or accelerate the vesting of, any benefit granted under the 2002 Stock Plan. The plan has no specific term and, subject to the terms of the 2002 Stock Plan, including those requiring approval by the Company's stockholders and those limiting the period over which incentive stock options or any other benefits may be granted, will continue in full force and effect until terminated. The 2002 Stock Plan may be terminated at any time by the Board.

Federal Income Tax Consequences

The federal income tax treatment for the two types of options that can be granted under the 2002 Stock Plan is as follows:

Incentive Stock Options

Under the Code, an employee generally recognizes no regular taxable income as the result of the grant or the exercise of an incentive stock option. However, an amount equal to the difference between the fair market value of the stock on the date of exercise and the exercise price must be included in the employee's alternative minimum taxable income (which may cause the employee to be liable for alternative minimum tax in that year).

The tax treatment of a sale or disposition of shares acquired under an incentive stock option will depend on whether the holding period requirements are satisfied. The holding period requirements will generally be satisfied if an optionee does not sell or dispose of such shares until after the later of one year after the exercise of such an option or two years after the date such option is granted.

If the holding period requirements are satisfied and an employee sells or disposes of shares acquired upon exercise of an incentive stock option, the optionee will recognize gain or loss equal to the difference between the sale price and the exercise price. Such gain or loss will be characterized for federal income tax purposes as long-term capital gain or loss.

If the holding period requirements are not satisfied and an employee sells or disposes of such shares, then the overall gain or loss on such sale or disposition is bifurcated into compensation and capital elements. The overall gain or loss is an amount equal to the difference between the sale price of the shares and the exercise price. With respect to the compensation element, the optionee must recognize as ordinary compensation income upon such sale or disposition an amount equal to the difference between (a) the lower of the fair market value of the shares at the date of the option exercise or the sale price of the shares and (b) the exercise price. With respect to the capital element, the optionee must recognize as capital gain or loss the difference between the overall gain (or loss) and the compensation element. If the shares have been held for more than 12 months, then any such gain or loss will be long-term capital gain or loss.

Generally, the Company will not be entitled to any deduction for federal income tax purposes in connection with the grant or exercise of an incentive stock option, regardless of the applicability of the alternative minimum tax to the optionee. However, if the holding period requirements are not satisfied with respect to the sale or disposition of any shares acquired under an incentive stock option, then the Company will be entitled to a tax deduction in the year of such sale or disposition equal to the compensation element recognized by the optionee as a result of such sale or disposition. Optionees will not be subject to withholding on the compensation element.

Non-Qualified Stock Options

An optionee generally recognizes no taxable income as a result of the grant of a non-qualified stock option, provided that such option does not have a readily ascertainable fair market value at the time it is granted. Upon exercise of a non-qualified stock option, an optionee will normally recognize ordinary compensation income for federal tax purposes equal to the excess, if any, of the fair market value of the shares over the exercise price. Optionees who are employees will be subject to withholding with respect to income recognized upon exercise of a non-qualified stock option.

The Company will be entitled to a tax deduction in the amount and in the year that any such ordinary income is recognized by the optionee, provided that the optionee's total compensation is deemed reasonable in amount.

Upon a sale of shares acquired pursuant to the exercise of a non-qualified stock option, any difference between the sale price and the fair market value of the shares on the date of exercise will be treated as a capital gain or loss and will qualify for long-term capital gain or loss treatment if the shares have been held for more than 12 months.

Stock Appreciation Rights and Stock Awards

Generally, the grantee of a stock appreciation right or stock award recognizes no taxable income as a result of such grant.

Upon exercise of a stock appreciation right, the grantee will normally recognize ordinary compensation income for federal tax purposes equal to the payment due under such stock appreciation right. Upon the acquisition of shares under a stock award, a grantee will normally recognize ordinary compensation income equal to the excess, if any, of the fair market value of the shares at the time of acquisition over the purchase price of such shares.

Upon a subsequent sale of any shares acquired pursuant to a stock award, any difference between the sale price and the fair market value of the shares upon the date of acquisition or the vesting date will be treated as a capital gain or loss and will qualify for long-term capital gain or loss treatment if the shares have been held for more than 12 months.

Grantees who are employees will be subject to withholding with respect to income recognized upon exercise of a stock appreciation right or under a stock award.

The Company will be entitled to a tax deduction in the amount and in the year that any ordinary income is recognized by the grantee pursuant to a stock appreciation right or stock award, provided that the grantee's total compensation is deemed reasonable in amount.

Market Price of Common Stock

The closing price of the Company's Common Stock as traded on The American Stock Exchange was \$4.45 per share on March 22, 2005. As of such date, the approximate aggregate market value of the shares of the Company's Common Stock available for issuance under the 2002 Stock Plan was \$3,791,275.

Stockholder Approval

The Code requires that the amendment to the 2002 Stock Plan be submitted to the Company's stockholders for approval. The affirmative vote of a majority of the shares of Common Stock of the Company represented at the Annual Meeting either in person or by proxy, assuming a quorum is present, is required to amend the 2002 Stock Plan. If the stockholders do not approve of the amendment, the amendment will not be effective.

The Board of Directors recommends that the stockholders vote *for* the approval of the amendment to the 2002 Stock Plan as set forth in Proposal 2.

PROPOSAL 3

**RATIFICATION OF THE APPOINTMENT OF
INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

The Audit Committee of the Board of Directors has appointed and the Board affirmed the appointment of the firm of Eisner LLP as independent auditors for the fiscal year ending December 31, 2005, subject to the ratification of the holders of the Company's common stock. If the holders of the common stock do not ratify the selection of Eisner LLP, other independent accountants may be considered and selected by the Audit Committee, or the Audit Committee may affirm its selection of Eisner LLP as the Company's independent auditors. All proxies received in response to this solicitation will be voted in favor of the ratification of the appointment of Eisner LLP as the Company's independent auditors, unless other instructions are indicated thereon. No representative of Eisner LLP will be present at the Annual Meeting.

The Company engaged Eisner LLP on May 23, 2002 as its independent auditors to audit its financial statements for the fiscal year ending December 31, 2002. During 2000 and 2001 and in the subsequent interim period from January 1, 2002 through May 23, 2002, the Company did not consult with Eisner LLP on items which concern the application of accounting principles generally, or as to a specific transaction or group of either completed or proposed transactions, or as to the type of audit opinion that might be rendered on the Company's financial statements. Eisner LLP did not prepare a report on the Company's financial statements for fiscal 2000 or 2001. Therefore, no report was issued by Eisner LLP that could contain an adverse opinion or disclaimer of opinion, or a qualification or modification, as to uncertainty, audit scope or accounting principles.

Audit and Non-Audit Fees

Fees billed to the Company by Eisner LLP for the years ended December 31, 2004 and 2003 were as follows:

Audit Fees. The aggregate fees billed and to be billed for the audit of the Company's annual financial statements for the fiscal years ended December 31, 2004 and 2003, for the reviews of the financial statements included in the Company's Quarterly Reports on Form 10-Q, and for other services that generally only an independent auditor reasonably can provide, such as comfort letters, statutory audits, attest services, consents and assistance with and review of documents filed with the SEC, were \$413,775 in 2004 and \$278,115 in 2003.

Audit-Related Fees. The aggregate fees billed for audit-related services for the fiscal years ended December 31, 2004 and 2003 were \$103,290 and \$1,500, respectively. These fees included any employee benefit plan audit, due diligence related to mergers and acquisitions, accounting consultations and audits in connection with acquisitions, internal control reviews, attest services not required by statute or regulation, and consultation concerning accounting and reporting standards for the fiscal years ended December 31, 2004 and December 31, 2003.

Financial Information Systems Design and Implementation Fees. The aggregate fees billed for financial information systems

design and implementation services for the fiscal years ended December 31, 2004 and 2003 were \$0 and \$0, respectively. These fees would have included any services regarding operating, or supervision of the operating of, the Company's information system or managing the Company's local area network, or designing or implementing a hardware or software system that aggregates source data underlying the financial statements or generates information that is significant to the Company's financial statements or other financial information systems taken as a whole for the fiscal years ended December 31, 2004 and December 31, 2003.

Tax Fees. The aggregate fees billed for tax services for the fiscal years ended December 31, 2004 and 2003 were \$0 and \$0, respectively. These fees would have related to tax compliance, tax planning and tax advice for the fiscal years ended December 31, 2004 and December 31, 2003. Tax compliance generally involves preparation of original and amended tax returns, claims for refund and tax payment and planning services. Tax planning and tax advice encompass a diverse range of services, including assistance with tax audits and appeals, tax advice related to mergers and acquisitions, employee benefit plans and requests for rulings or technical advice from taxing authorities.

All Other Fees. The aggregate fees for services not included above for the fiscal years ended December 31, 2004 and 2003 were \$0 and \$0, respectively. The fees would have related to services that do not meet the above category descriptions.

The Company has also agreed in its engagement letter with Eisner LLP to not hire Eisner LLP personnel at the manager or partner level who have been directly involved in performing auditing procedures or providing accounting advice to the Company.

The Company's Audit Committee is responsible for appointing the Company's independent auditor and approving the terms of the independent auditor's services. The Audit Committee has established a policy for the pre-approval of all audit and permissible non-audit services to be provided by the independent auditor, as described below.

Before the beginning of each fiscal year, a description of the services anticipated to be performed by the independent auditor in each of the above specified categories in the ensuing fiscal year is presented to the Audit Committee for approval. Services provided by the independent auditor during the ensuing fiscal year are pre-approved in accordance with procedures of the Audit Committee.

Any request for audit, audit-related, tax and other services not contemplated must be submitted to the Audit Committee for specific pre-approval, irrespective of the amount, and cannot commence until such approval has been granted. Normally, pre-approval is provided at regularly scheduled meetings of the Audit Committee. However, the authority to grant specific pre-approval between meetings, as necessary, has been delegated to the Chairman of the Audit Committee. The Chairman will update the full audit Committee at the next regularly scheduled meeting for any interim approval granted.

On a quarterly basis, the Audit Committee reviews the status of services and fees incurred year-to-date as compared to the original list of services and the forecast of remaining services and fees for the fiscal year.

The services performed by the independent auditor in 2004 were pre-approved in accordance with procedures followed by the Audit Committee.

Stockholder Approval

Although stockholder action on this matter is not required, the appointment of Eisner LLP is being recommended to the stockholders for ratification. Pursuant to applicable Delaware law, the ratification of the appointment of auditors of the Company requires the affirmative vote of the holders of a majority of the shares of common stock present, in person or by proxy, and entitled to vote at the Meeting. Abstentions and broker non-votes will be counted and will have the same effect as a vote against this proposal.

The Board of Directors recommends that the stockholders vote *for* the ratification of the appointment of Eisner LLP as independent auditors as set forth in Proposal 3.

PROPOSALS OF STOCKHOLDERS

Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A

Any stockholder of the Company who wishes to present a proposal at the 2006 Annual Meeting of Stockholders and who wishes to have such proposal included in the Company's proxy statement for that meeting must deliver a copy of such proposal to the Company at 490 Villaume Avenue, South St. Paul, Minnesota 55075, Attention: Corporate Assistant Secretary, for receipt not later than December 16, 2005. The Company reserves the right to decline to include in the Company's proxy statement any stockholder's proposal that does not comply with the rules of the SEC for inclusion therein.

For any proposal that is not submitted for inclusion in next year's proxy statement but is instead sought to be presented directly at the 2006 Annual Meeting of Stockholders, management will be able to vote proxies in its discretion if the Company: (1) receives notice of the proposal before the close of business on February 28, 2006 and advises stockholders in the 2006 Proxy Statement about the nature of the matter and how management intends to vote on such matters; or (2) does not receive notice of the proposal before the close of business on February 28, 2006. Notices of intention to present proposals at the 2006 Annual Meeting of Stockholders should be addressed to: Digital Angel Corporation, 490 Villaume Avenue, South St. Paul, Minnesota 55075, Attention: Corporate Assistant Secretary.

OTHER BUSINESS

At the date of this Proxy Statement, management knows of no other business that may properly come before the Annual Meeting. However, if any other matters properly come before the meeting, the persons named in the enclosed form of proxy will vote the proxies received in response to this solicitation in accordance with their best judgment on such matters.

ANNUAL REPORTS

The Company is mailing a copy of its Annual Report to Stockholders with this proxy statement. However, the Annual Report is not to be considered part of the proxy solicitation materials.

The Company's Annual Report on Form 10-K is available without charge upon written request to Mr. James P. Santelli, Digital Angel Corporation, 490 Villaume Avenue, South St. Paul, Minnesota 55075.

HOUSEHOLDING

As permitted by the Securities Exchange Act of 1934, only one copy of this proxy statement is being delivered to stockholders residing at the same address, unless such stockholders have notified the Company of their desire to receive multiple copies of the proxy statement. The Company will promptly deliver, upon oral or written request, a separate copy of the proxy statement to any stockholder residing at an address to which only one copy was mailed. Requests for additional copies should be directed to: Digital Angel Corporation, 490 Villaume Avenue, South St. Paul, Minnesota 55075, Attention: Corporate Assistant Secretary.

Stockholders residing at the same address and currently receiving only one copy of the proxy statement may contact the Corporate Assistant Secretary at the address set forth above to request multiple copies of proxy statements in the future. Stockholders residing at the same address and currently receiving multiple copies of proxy statements may contact the Corporate Assistant Secretary to request that only a single copy of proxy statements be mailed in the future.

Dated: April 5, 2005.

By Order of the Board of Directors,

/s/ James P. Santelli
James P. Santelli, *Assistant Secretary*

Exhibit A

Amended and Restated

Digital Angel Corporation

Transition Stock Option Plan, as amended

1. NAME AND PURPOSE

1.1 *Name.*

The name of this Plan is the *Digital Angel Corporation Transition Stock Option Plan.*

1.2 *Purpose.*

The Company has established this Plan to retain, motivate and reward Employees and Directors of Digital Angel Corporation, a Delaware corporation acquired by the Company as a result of a merger completed on March 27, 2002 and to encourage ownership of the Company's Common Stock by them.

2. DEFINITIONS OF TERMS AND RULES OF CONSTRUCTION

2.1 *General Definitions.*

The following words and phrases, when used in the Plan, unless otherwise specifically defined or unless the context clearly otherwise requires, shall have the following respective meanings:

2.1.1. *Affiliate.*

A Parent or Subsidiary of the Company.

2.1.2. *Agreement.*

The document which evidences the grant of any Benefit under the Plan and which sets forth the Benefit and the terms, conditions and provisions of, and restrictions relating to, such Benefit.

2.1.3. *Benefit.*

Any benefit granted to a Participant under the Plan.

2.1.4. *Board.*

The Board of Directors of the Company.

2.1.5. *Cash Award.*

A Benefit payable in the form of cash.

2.1.6. *Change of Control.*

If any *person* (as such term is used in Sections 13(d) and 14(d)(2) of the Exchange Act) is or becomes the *beneficial owner* (as defined in Rule 13d-3 promulgated under the Exchange Act), directly or indirectly, of securities of the Company representing 20% or more of the combined voting power of the Company's then outstanding securities; upon the first purchase of the Common Stock pursuant to a tender or exchange offer (other than a tender or exchange offer made by the Company); upon the approval by the Company's stockholders of a merger or consolidation, a sale or disposition of all or substantially of the Company's assets or a plan of liquidation or dissolution of the Company; or if during an period of 2 consecutive years, individuals who at the beginning of such period constitute the Board cease for any reason to constitute at least a majority thereof, unless the election or nomination for the election by the Company's stockholders of each new director was approved by a vote of at least $\frac{2}{3}$ of the Board then still in office who were members of the Board at the beginning of the period. Notwithstanding the foregoing, a Change in Control shall not be deemed to occur if the Company either merges or consolidates with or into another company or sells or disposes of all or substantially all of its assets to another company, if such merger, consolidation, sale or disposition is in connection with a corporate restructuring wherein the stockholders of the Company immediately before such merger, consolidation, sale or disposition own, directly or indirectly, immediately following such merger, consolidation, sale or disposition of at least 80% of the combined voting power of all outstanding classes of securities of the Company resulting from such merger or consolidation, or to which the Company sells or disposes of its assets, in substantially the same proportion as their ownership in the Company immediately before such merger, consolidation, sale or disposition.

2.1.7. *Code.*

The Internal Revenue Code of 1986, as amended. Any reference to the Code includes the regulations *promulgated* pursuant to the Code.

2.1.8. *Company.*

Digital Angel Corporation

2.1.9. *Committee.*

The Committee described in Section 5.1.

2.1.10. *Common Stock.*

The Company's common stock, par value \$.005 per Share.

2.1.11. *Director.*

A member of the Board or a member of the Board of Directors of an Affiliate.

A-2

2.1.12. *Effective Date.*

April 11, 2002.

2.1.13. *Employee.*

Any person employed by the Employer.

2.1.14. *Employer.*

The Company and all Affiliates.

2.1.15. *Exchange Act.*

The Securities Exchange Act of 1934, as amended.

2.1.16. *Fair Market Value.*

The last sale price, regular way, or, in case no such sale takes place on such date, the average of the closing bid and asked prices, regular way, of the Shares, in either case as reported in the principal consolidated transaction reporting system with respect to securities listed or admitted to trading on the New York Stock Exchange, Inc. (the *NYSE*) or, if the Shares are not listed or admitted to trading on the NYSE, as reported in the principal consolidated transaction reporting system with respect to securities listed on the principal national securities exchange on which the Shares are listed or admitted to trading or, if the Shares are not listed or admitted to trading on any national securities exchange, the last quoted sale price on such date or, if not so quoted, the average of the high bid and low asked prices in the over-the-counter market on such date, as reported by the National Association of Securities Dealers, Inc. Automated Quotations System or such other system then in use, or, if on any such date the Shares are not quoted by any such organization, the average of the closing bid and asked prices on such date as furnished by a professional market maker making a market in the Shares selected by the Committee. If the Shares are not publicly held or so listed or publicly traded, the determination of the Fair Market Value per Share shall be made in good faith by the Committee.

2.1.17. *Fiscal Year.*

The taxable year of the Company which is the calendar year.

2.1.18. *ISO*.

An Incentive Stock Option as defined in Section 422 of the Code.

2.1.19. *NQSO*.

A non-qualified stock Option, which is an Option that does not qualify as an ISO.

A-3

2.1.20. *Option.*

An option to purchase Shares granted under the Plan.

2.1.21. *Other Stock Based Award.*

An award under Section 18 that is valued in whole or in part by reference to, or is otherwise based on, Common Stock.

2.1.22. *Parent.*

Any corporation (other than the Company or a Subsidiary) in an unbroken chain of corporations ending with the Company, if, at the time of the grant of an Option or other Benefit, each of the corporations (other than the Company) owns stock possessing 50% or more of the total combined voting power of all classes of stock in one of the other corporations in such chain.

2.1.23. *Participant.*

An individual who is granted a Benefit under the Plan. Benefits may be granted only to Employees and Directors.

2.1.24. *Performance Based Compensation.*

Compensation which meets the requirements of Section 162(m)(4)(C) of the Code.

2.1.25. *Performance Share.*

A Share awarded to a Participant under Section 16 of the Plan.

2.1.26. *Plan.*

The Digital Angel Corporation Transition Stock Option Plan and all amendments and supplements to it.

2.1.27. *Reload Option.*

An Option to purchase the number of Shares used by a Participant to exercise an Option and to satisfy any withholding *requirement* incident to the exercise of such Option.

2.1.28. *Restricted Stock.*

Shares issued under Section 16 of the Plan.

A-4

2.1.29. *Rule 16b-3.*

Rule 16b-3 promulgated by the SEC, as amended, or any successor rule in effect from time to time.

2.1.30. *SEC.*

The Securities and Exchange Commission.

2.1.31. *Share.*

A share of Common Stock.

2.1.32. *SAR.*

A stock appreciation right, which is the right to receive an amount equal to the appreciation, if any, in the Fair Market Value of a *Share* from the date of the grant of the right to the date of its payment.

2.1.33. *Subsidiary.*

Any corporation, other than the Company, in an unbroken chain of corporations beginning with the Company if, at the time of grant of an Option or other Benefit, each of the corporations, other than the last corporation in the unbroken chain, owns stock possessing 50% or more of the total combined voting power of all classes of stock in one of the other corporations in such chain.

2.2. *Other Definitions.*

In addition to the above definitions, certain words and phrases used in the Plan and any Agreement may be defined in other portions of the Plan or in such Agreement.

2.3. *Conflicts.*

In the case of any conflict in the terms of the Plan relating to a Benefit, the provisions in the section of the Plan which specifically grants such Benefit shall control those in a different section. In the case of any conflict between the terms of the Plan relating to a Benefit and the terms of an Agreement relating to a Benefit, the terms of the Plan shall control.

3. COMMON STOCK

3.1. *Number of Shares.*

The number of Shares which may be issued or sold or for which Options, SARs or Performance Shares may be granted under the Plan shall be 18,195,312. Such Shares may be authorized but unissued Shares, Shares held in the treasury, or both. The full number of Shares available may be used for any type of Option or other Benefit.

3.2. *Reusage.*

If an Option or SAR expires or is terminated, surrendered, or canceled without having been fully exercised, if Restricted Shares or Performance Shares are forfeited, or if any other grant results in any Shares not being issued, the Shares covered by such Option or SAR, grant of Restricted Shares, Performance Shares or other grant, as the case may be, shall again be available for use under the Plan. Any Shares which are used as full or partial payment to the Company upon exercise of an Option or for any other Benefit that requires a payment to the Company shall be available for purposes of the Plan.

3.3. *Adjustments.*

If there is any change in the Common Stock of the Company by reason of any stock dividend, spin-off, split-up, spin-out, recapitalization, merger, consolidation, reorganization, combination or exchange of shares, or otherwise, the number of SARs and number and class of shares available for Options and grants of Restricted Stock, Performance Shares and Other Stock Based Awards and the number of Shares subject to outstanding Options, SARs, grants of Restricted Stock which are not vested, grants of Performance Shares which are not vested, and Other Stock Based Awards, and the price thereof, as applicable, shall be appropriately adjusted by the Committee.

4. ELIGIBILITY

4.1. *Determined By Committee.*

The Participants in this Plan shall be those persons who received options to purchase Digital Angel Corporation common stock pursuant to the Digital Angel.net, Inc. Restated Flexible Stock Plan on or prior to March 27, 2002.

5. ADMINISTRATION

5.1. *Committee.*

The Plan shall be administered by the Committee. The Committee shall consist of the Board, unless the Board appoints a Committee of two or more but less than all of the Board. If the Committee does not include the entire Board, it shall serve at the pleasure of the Board, which may from time to time appoint members in substitution for members previously appointed and fill vacancies, however caused, in the Committee. The Committee may select one of its members as its Chairman and shall hold its meetings at such times and places as it may determine. A majority of its members shall constitute a quorum. All determinations of the Committee made at a meeting at which a quorum is present shall be made by a majority of its members present at the meeting. Any decision or determination reduced to writing and signed by a majority of the members shall be fully as effective as if it had been made by a majority vote at a meeting duly called and held.

5.2. *Authority.*

Subject to the terms of the Plan, the Committee shall have discretionary authority to:

A-6

(a) determine the individuals to whom Benefits are granted, the type and amounts of Benefits to be granted and the date of issuance and duration of all such grants;

(b) determine the terms, conditions and provisions of, and restrictions relating to, each Benefit granted;

(c) interpret and construe the Plan and all Agreements;

(d) prescribe, amend and rescind rules and regulations relating to the Plan;

(e) determine the content and form of all Agreements;

(f) determine all questions relating to Benefits under the Plan;

(g) maintain accounts, records and ledgers relating to Benefits;

(h) maintain records concerning its decisions and proceedings;

(i) employ agents, attorneys, accountants or other persons for such purposes as the Committee considers necessary or desirable;

(j) take, at any time, any action required or permitted by Section 9.1 or 9.2(a), respectively, irrespective of whether any Change of Control has occurred or is imminent;

(k) determine, except to the extent otherwise provided in the Plan, whether and the extent to which Benefits under the Plan will be structured to conform to the requirements applicable to Performance-Based Compensation, and to take such action, establish such procedures, and impose such restrictions at the time such Benefits are granted as the Committee determines to be necessary or appropriate to conform to such requirements; and

(l) do and perform all acts which it may deem necessary or appropriate for the administration of the Plan and carry out the purposes of the Plan.

5.3. *Delegation.*

Except as required by Rule 16b-3 with respect to grants of Options, Stock Appreciation Awards, Performance Shares, Other Stock Based Awards, or other Benefits to individuals who are subject to Section 16 of the Exchange Act or as otherwise required for compliance with Rule 16b-3 or other applicable law, the Committee may delegate all or any part of its authority under the Plan to any Employee, Employees or committee.

5.4. *Determination.*

All determinations of the Committee shall be final.

A-7

6. AMENDMENT

6.1. *Power of Board.*

Except as hereinafter provided, the Board shall have the sole right and power to amend the Plan at any time and from time to time.

6.2. *Limitation.*

The Board may not amend the Plan, without approval of the stockholders of the Company:

(a) in a manner which would cause Options which are intended to qualify as ISOs to fail to qualify;

(b) in a manner which would cause the Plan to fail to meet the requirements of Rule 16b-3; or

(c) in a manner which would violate applicable law.

7. TERM AND TERMINATION

7.1. *Term.*

The Plan shall commence as of the Effective Date and, subject to the terms of the Plan, including those requiring approval by the stockholders of the Company and those limiting the period over which ISOs or any other Benefits may be granted, shall continue in full force and effect until terminated.

7.2. *Termination.*

The Plan may be terminated at any time by the Board.

8. MODIFICATION OR TERMINATION OF BENEFITS

8.1. *General.*

Subject to the provisions of Section 8.2, the amendment or termination of the Plan shall not adversely affect a Participant's right to any Benefit granted prior to such amendment or termination.

8.2. *Committee's Right.*

Any Benefit granted may be converted, modified, forfeited or canceled, in whole or in part, by the Committee if and to the extent permitted in the Plan or applicable Agreement or with the consent of the Participant to whom such Benefit was granted. Except as may be provided in an Agreement, the Committee may, in its sole discretion, in whole or in part, waive any restrictions or conditions applicable to, or accelerate the vesting of, any Benefit.

9. CHANGE OF CONTROL

9.1. *Vesting and Payment.*

In the event of a Change of Control:

(a) all outstanding Options shall become fully exercisable, except to the extent that the right to exercise the Option is subject to restrictions established in connection with an SAR that is issued in tandem with the Option;

(b) all outstanding SARs shall become immediately payable, except to the extent that the right to exercise the SAR is subject to restrictions established in connection with an Option that is issued in tandem with the SAR.

(c) all Shares of Restricted Stock shall become fully vested;

(d) all Performance Shares shall be deemed to be fully earned and shall be paid out in such manner as determined by the Committee; and

(e) all Cash Awards, Other Stock Based Awards and other Benefits shall become fully vested and/or earned and paid out in such manner as determined by the Committee.

9.2. *Other Action.*

In the event of a Change of Control, the Committee, in its sole discretion, may, in addition to the provisions of Section 9.1 above and to the extent not inconsistent therewith:

(a) provide for the purchase of any Benefit for an amount of cash equal to the amount which could have been attained upon the exercise or realization of such Benefit had such Benefit been currently exercisable or payable;

(b) make such adjustment to the Benefits then outstanding as the Committee deems appropriate to reflect such transaction or change; and/or

(c) cause the Benefits then outstanding to be assumed, or new Benefits substituted therefor, by the surviving corporation in such change.

10. AGREEMENTS AND CERTAIN BENEFITS

10.1. *Grant Evidenced by Agreement.*

The grant of any Benefit under the Plan may be evidenced by an Agreement which shall describe the specific Benefit granted and the terms and conditions of the Benefit. The granting of any Benefit shall be subject to, and conditioned upon, the recipient's execution of any Agreement required by the Committee. Except as otherwise provided in an Agreement, all capitalized terms used in the Agreement shall have the same meaning as in the Plan, and the Agreement shall be subject to all of the terms of the Plan.

10.2. *Provisions of Agreement.*

Each Agreement shall contain such provisions that the Committee shall determine to be necessary, desirable and appropriate for the Benefit granted which may include, but not necessarily be limited to, the following with respect to any Benefit: description of the type of Benefit; the Benefit's duration; its transferability; if an Option, the exercise price, the exercise period and the person or persons who may exercise the Option; the effect upon such Benefit of the Participant's death, disability, changes of duties or termination of employment; the Benefit's conditions; when, if, and how any Benefit may be forfeited, converted into another Benefit, modified, exchanged for another Benefit, or replaced; and the restrictions on any Shares purchased or granted under the Plan.

10.3. *Transferability.*

Unless otherwise specified in an Agreement or permitted by the Committee, each Benefit granted shall be not transferable other than by will or the laws of descent and distribution and shall be exercisable during a Participant's lifetime only by him.

11. REPLACEMENT AND TANDEM AWARDS

11.1. *Replacement.*

The Committee may permit a Participant to elect to surrender a Benefit in exchange for a new Benefit.

11.2. *Tandem Awards.*

Awards may be granted by the Committee in tandem. However, no Benefit may be granted in tandem with an ISO except SARs.

12. PAYMENT, DIVIDENDS, DEFERRAL AND WITHHOLDING

12.1. *Payment.*

Upon the exercise of an Option or in the case of any other Benefit that requires a payment by a Participant to the Company, the amount due the Company is to be paid:

(a) in cash, including by means of a so-called *cashless exercise* of an Option;

(b) by the surrender of all or part of a Benefit (including the Benefit being exercised);

(c) by the tender to the Company of Shares owned by the optionee and registered in his name having a Fair Market Value equal to the amount due to the Company;

(d) in other property, rights and credits deemed acceptable by the Committee, including the Participant's promissory note;

(e) by any combination of the payment methods specified in (a), (b), (c) and (d) above.

A-10

Notwithstanding, the foregoing, any method of payment other than (a) may be used only with the consent of the Committee or if and to the extent so provided in an Agreement. The proceeds of the sale of Shares purchased pursuant to an Option and any payment to the Company for other Benefits shall be added to the general funds of the Company or to the Shares held in treasury, as the case may be, and used for the corporate purposes of the Company as the Board shall determine.

12.2. *Dividend Equivalents.*

Grants of Benefits in Shares or Share equivalents may include dividend equivalent payments or dividend credit rights.

12.3. *Deferral.*

The right to receive any Benefit under the Plan may, at the request of the Participant, be deferred for such period and upon such terms as the Committee shall determine, which may include crediting of interest on deferrals of cash and crediting of dividends on deferrals denominated in Shares.

12.4. *Withholding.*

The Company may, at the time any distribution is made under the Plan, whether in cash or in Shares, or at the time any Option is exercised, withhold from such distribution or Shares issuable upon the exercise of an Option, any amount necessary to satisfy federal, state and local income and/or other tax withholding requirements with respect to such distribution or exercise of such Options. The Committee or the Company may require a participant to tender to the Company cash and/or Shares in the amount necessary to comply with any such withholding requirements.

13. OPTIONS

13.1. *Types of Options.*

It is intended that both ISOs and NQSOs, which may be Reload Options, may be granted by the Committee under the Plan.

13.2. *Grant of ISOs and Option Price.*

Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A

Each ISO must be granted to an Employee and granted within ten years from the earlier of the date of adoption by the Board or the Effective Date. The purchase price for Shares under any ISO shall be no less than the Fair Market Value of the Shares at the time the Option is granted.

13.3. *Other Requirements for ISOs.*

The terms of each Option which is intended to qualify as an ISO shall meet all requirements of Section 422 of the Code.

A-11

13.4. *NQSOs.*

The terms of each NQSO shall provide that such Option will not be treated as an ISO. The purchase price for Shares under any NQSO shall be no less than 85% of the Fair Market Value of the Shares at the time the Option is granted.

13.5. *Determination by Committee.*

Except as otherwise provided in Section 13.2 through Section 13.4, the terms of all Options shall be determined by the Committee.

14. SARS

14.1. *Grant and Payment.*

The Committee may grant SARs. Upon electing to receive payment of a SAR, a Participant shall receive payment in cash, in Shares, or in any combination of cash and Shares, as the Committee shall determine.

14.2. *Grant of Tandem Award.*

The Committee may grant SARs in tandem with an Option, in which case: the exercise of the Option shall cause a correlative reduction in SARs standing to a Participant's credit which were granted in tandem with the Option; and the payment of SARs shall cause a correlative reduction of the Shares under such Option.

14.3. *ISO Tandem Award.*

When SARs are granted in tandem with an ISO, the SARs shall have such terms and conditions as shall be required for the ISO to qualify as an ISO.

14.4. *Payment of Award.*

SARs shall be paid by the Company to a Participant, to the extent payment is elected by the Participant (and is otherwise due and payable), as soon as practicable after the date on which such election is made.

15. ANNUAL LIMITATIONS

15.1. *Limitation on Options and SARs.*

The number of (a) Shares covered by Options where the purchase price is no less than the Fair Market Value of the Shares on the date of grant plus (b) SARs which may be granted to any Participant in any Fiscal Year shall not exceed 1,000,000.

15.2. *Computations.*

For purposes of Section 15.1: Shares covered by an Option that is canceled shall count against the maximum, and, if the exercise price under an Option is reduced, the transaction

shall be treated as a cancellation of the Option and a grant of a new Option; and SARs covered by a grant of SARs that is canceled shall count against the maximum, and, if the Fair Market Value of a Share on which the appreciation under a grant of SARs will be calculated is reduced, the transaction will be treated as a cancellation of the SARs and the grant of a new grant of SARs.

16. RESTRICTED STOCK AND PERFORMANCE SHARES

16.1. *Restricted Stock.*

The Committee may grant Benefits in Shares available under Section 3 of the Plan as Restricted Stock. Shares of Restricted Stock shall be issued and delivered at the time of the grant or as otherwise determined by the Committee, but shall be subject to forfeiture until provided otherwise in the applicable Agreement or the Plan. Each certificate representing Shares of Restricted Stock shall bear a legend referring to the Plan and the risk of forfeiture of the Shares and stating that such Shares are nontransferable until all restrictions have been satisfied and the legend has been removed. At the discretion of the Committee, the grantee may or may not be entitled to full voting and dividend rights with respect to all shares of Restricted Stock from the date of grant.

16.2. *Cost of Restricted Stock.*

Unless otherwise determined by the Committee, grants of Shares of Restricted Stock shall be made at a per Share cost to the Participant equal to par value.

16.3. *Non-Transferability.*

Shares of Restricted Stock shall not be transferable until after the removal of the legend with respect to such Shares.

16.4. *Performance Shares.*

Performance Shares are the right of an individual to whom a grant of such Shares is made to receive Shares or cash equal to the Fair Market Value of such Shares at a future date in accordance with the terms and conditions of such grant. The terms and conditions shall be determined by the Committee, in its sole discretion, but generally are expected to be based substantially upon the attainment of targeted profit and/or performance objectives.

16.5. *Grant.*

The Committee may grant an award of Performance Shares. The number of Performance Shares and the terms and conditions of the grant shall be set forth in the applicable Agreement.

A-13

17. CASH AWARDS

17.1. *Grant.*

The Committee may grant Cash Awards at such times and (subject to Section 17.2) in such amounts as it deems appropriate.

17.2. *Rule 16b-3.*

The amount of any Cash Award in any Fiscal Year to any Participant who is subject to Section 16 of the Exchange Act shall not exceed the greater of \$100,000 or 100% of his cash compensation (excluding any Cash Award under this Section 17) for such Fiscal Year.

17.3. *Restrictions.*

Cash Awards may be subject or not subject to conditions (such as an investment requirement), restricted or nonrestricted, vested or subject to forfeiture and may be payable currently or in the future or both.

18. OTHER STOCK BASED AWARDS AND OTHER BENEFITS

18.1. *Other Stock Based Awards.*

The Committee shall have the right to grant Other Stock Based Awards which may include, without limitation, the grant of Shares based on certain conditions, the payment of cash based on the performance of the Common Stock, and the grant of securities convertible into Shares.

18.2. *Other Benefits.*

The Committee shall have the right to provide types of Benefits under the Plan in addition to those specifically listed, if the Committee believes that such Benefits would further the purposes for which the Plan was established.

19. MISCELLANEOUS PROVISIONS

19.1. *Underscored References.*

The underscored references contained in the Plan are included for convenience only, and they shall not be construed as a part of the Plan or in any respect affecting or modifying its provisions.

19.2. *Number and Gender.*

The masculine and neuter, wherever used in the Plan, shall refer to either the masculine, neuter or feminine; and, unless the context otherwise requires, the singular shall include the plural and the plural the singular.

A-14

19.3. *Unfunded Status of Plan.*

The Plan is intended to constitute an *unfunded* plan for incentive and deferred compensation. With respect to any payments or deliveries of Shares not yet made to a Participant by the Company, nothing contained herein shall give any rights that are greater than those of a general creditor of the Company. The Committee may authorize the creation of trusts or other arrangements to meet the obligations created under the Plan to deliver Shares or payments hereunder consistent with the foregoing.

19.4. *Termination of Employment.*

If the employment of a Participant by the Company terminates for any reason, except as otherwise provided in an Agreement, all unexercised, deferred, and unpaid Benefits may be exercisable or paid only in accordance with rules established by the Committee. These rules may provide, as the Committee may deem appropriate, for the expiration, forfeiture, continuation, or acceleration of the vesting of all or part of the Benefits.

19.5. *Designation of Beneficiary.*

A Participant may file with the Committee a written designation of a beneficiary or beneficiaries (subject to such limitations as to the classes and number of beneficiaries and contingent beneficiaries as the Committee may from time to time prescribe) to exercise, in the event of the death of the Participant, an Option, or to receive, in such event, any Benefits. The Committee reserves the right to review and approve beneficiary designations. A Participant may from time to time revoke or change any such designation of beneficiary and any designation of beneficiary under the Plan shall be controlling over any other disposition, testamentary or otherwise; provided, however, that if the Committee shall be in doubt as to the right of any such beneficiary to exercise any Option or to receive any Benefit, the Committee may determine to recognize only an exercise by the legal representative of the recipient, in which case the Company, the Committee and the members thereof shall not be under any further liability to anyone.

19.6. *Governing Law.*

This Plan shall be construed and administered in accordance with the laws of the State of Delaware, without giving effect to conflict of laws principles.

19.7. *Purchase for Investment.*

The Committee may require each person purchasing Shares pursuant to an Option or other award under the Plan to represent to and agree with the Company in writing that such person is acquiring the Shares for investment and without a view to distribution or resale. The certificates for such Shares may include any legend that the Committee deems appropriate to reflect any restrictions on transfer. All certificates for Shares delivered under the Plan shall be subject to such stock-transfer orders and other restrictions as the Committee may deem advisable under all applicable laws, rules and regulations, and the Committee may cause a legend or legends to be put on any such certificates to make appropriate

references to such restrictions.

A-15

19.8. *No Employment Contract.*

Neither the adoption of the Plan nor any Benefit granted hereunder shall confer upon any Employee any right to continued employment nor shall the Plan or any Benefit interfere in any way with the right of the Employer to terminate the employment of any of its Employees at any time.

19.9. *No Effect on Other Benefits.*

The receipt of Benefits under the Plan shall have no effect on any benefits to which a Participant may be entitled from the Employer, under another plan or otherwise, or preclude a Participant from receiving any such benefits.

DIGITAL ANGEL CORPORATION

PROXY SOLICITED BY BOARD OF DIRECTORS

For Annual Meeting of Stockholders

May 3, 2005

DIGITAL ANGEL CORPORATION

PROXY

The undersigned, revoking all prior proxies, hereby appoints Kevin N. McGrath and James P. Santelli, and either of them, as proxy or proxies, with full power of substitution and revocation, to vote all shares of common stock of Digital Angel Corporation (the Company) of record in the name of the undersigned at the close of business on March 22, 2005, at the Annual Meeting of Stockholders (the Annual Meeting) to be held on Tuesday, May 3, 2005, or at any adjournment thereof, upon the following matters:

See reverse for voting instructions

There are three ways to vote your Proxy

Your telephone or Internet vote authorizes the Named Proxies to vote your shares in the same manner as if you marked, signed and returned your proxy card.

VOTE BY PHONE TOLL FREE 1-800-560-1965 QUICK * EASY *** IMMEDIATE**

Use any touch-tone telephone to vote your proxy 24 hours a day, 7 days a week until 12 noon (CT) on May 2, 2005.

Please have your proxy card and the last four digits of your Social Security Number available. Follow the simple instructions the Voice provides you.

VOTE BY INTERNET <http://www.eproxy.com/doc/> QUICK * EASY *** IMMEDIATE**

Use the Internet to vote your proxy 24 hours a day, 7 days a week until 12 noon (CT) on May 2, 2005.

Please have your proxy card and the last four digits of your Social Security Number available. Follow the simple instructions to obtain your records and create an electronic ballot.

VOTE BY MAIL

Mark, sign and date your proxy card and return it in the postage-paid envelope we've provided or return it to **Digital Angel Corporation**, c/o Shareowner Services,SM P.O. Box 64873, St. Paul, MN 55164-0873.

If you vote by Phone or Internet, please do not mail your Proxy Card

- | | | | | | |
|--------------------------------------|------------------------|-------------------------------|--------------------------------------------|---|---------------------------------|
| 1. Electing the following directors: | 01 John R. Block | 04 Scott R. Silverman | o Vote FOR all nominees (except as marked) | o | Vote WITHHELD from all nominees |
| | 02 Kevin N. McGrath | 05 Howard S. Weintraub, Ph.D. | | | |
| | 03 Kevin H. McLaughlin | 06 Michael S. Zarriello | | | |
| | | | | | |

Edgar Filing: DIGITAL ANGEL CORP - Form DEF 14A

(Instructions: To withhold authority to vote for any indicated nominee, write the number(s) of the nominee(s) in the box provided to the right.)

2. Approving an amendment to the Amended and Restated Digital Angel number of Corporation Transition Stock Option Plan (*2002 Stock Plan*) increasing the shares of Company common stock subject to the plan. For Against Abstain
3. Ratifying the appointment to Eisner LLP as independent auditors for the fiscal year ending December 31, 2005. For Against Abstain

In their discretion, the Proxies are authorized to vote upon any other matters as may properly come before the Annual Meeting or any adjournments thereof.

Please mark, date, sign, and mail this proxy promptly in the enclosed envelope.

This proxy, when properly executed, will be voted in the manner directed herein by the undersigned stockholder. If no direction is made, this proxy will be voted **FOR** Proposals 1, 2 and 3. The Board of Directors recommends a vote **for** Proposals 1, 2 and 3.

Address Change? Mark Box

Indicate changes below:

Date:

Signature(s) in Box

Please sign your name exactly as it appears below. In the case of shares owned in joint tenancy or as tenants in common, all should sign. Fiduciaries should indicate their title and authority.