

STEC, INC.
Form PRRN14A
May 14, 2013

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

SCHEDULE 14A
(Rule 14a-101)

INFORMATION REQUIRED IN PROXY STATEMENT

SCHEDULE 14A INFORMATION

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

(Amendment No. 2)

Filed by the Registrant

Filed by a Party other than the Registrant

Check the appropriate box:

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

STEC, INC.
(Name of Registrant as Specified in Its Charter)

Balch Hill Partners, L.P.
Balch Hill Capital, LLC
Simon J. Michael
Potomac Capital Partners L.P.
Potomac Capital Management, L.L.C.
Potomac Capital Partners II, L.P.
Potomac Capital Management II, L.L.C.
Potomac Capital Partners III, L.P.
Potomac Capital Management III, L.L.C.
Paul J. Solit
Eric Singer
Adam Leventhal
Clark Masters

(Name of Persons(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:

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PRELIMINARY COPY SUBJECT TO COMPLETION
DATED MAY 14, 2013
BALCH HILL PARTNERS, L.P.

May ___, 2013

Dear Fellow Shareholder:

Balch Hill Partners, L.P., a Delaware limited partnership and the other participants in this solicitation (collectively, “Balch Hill” or “we”) are the beneficial owners of an aggregate of 4,581,470 shares of common stock, par value \$0.001 per share (the “Common Stock”), of STEC, Inc., a California corporation (“STEC” or the “Company”), representing approximately 9.8% of the outstanding shares of Common Stock. We are seeking representation on the Board of Directors of the Company (the “Board”) because we believe that the Board could be improved with directors who have strong, relevant backgrounds and who are committed to fully exploring all opportunities to unlock shareholder value. Accordingly, we are seeking your support at the Company’s upcoming 2013 Annual Meeting of Shareholders scheduled to be held at 18000 Von Karman Avenue, Irvine, California 92612 on Tuesday, June 25, 2013 at 8:00 a.m., local time, including any adjournment or postponement thereof and any meeting which may be called in lieu thereof (the “Annual Meeting”), for the following:

1. To elect Balch Hill’s three (3) nominees (the “Nominees”) to the Board in opposition to three of the Company’s director nominees, to serve until the 2014 Annual Meeting of Shareholders and until their successors are duly elected and qualified or until their earlier resignation or removal;
2. To approve an amendment to the Company’s Second Amended and Restated Bylaws (the “Bylaws”) to increase the minimum and maximum size of the Board;
3. To approve the Company’s 2013 Executive Cash Incentive Plan;
4. To conduct an advisory vote to approve the compensation paid to the Company’s named executive officers;
5. To ratify the selection of Ernst & Young LLP as the Company’s independent registered public accounting firm for fiscal year ending December 31, 2013; and
6. To transact such other business as may properly come before the Annual Meeting.

The Board is currently composed of seven directors, all of whom are up for election at the Annual Meeting. At the Annual Meeting, the Board is asking shareholders to approve an amendment to the Bylaws to increase the size of the Board to eight directors. If the amendment to the Bylaws is approved by shareholders, the eight nominees receiving the highest number of affirmative votes will be elected. If the amendment to the Bylaws is not approved by shareholders, the seven nominees receiving the highest number of affirmative votes will be elected.

Through the attached Proxy Statement, we are soliciting proxies to elect not only our three Nominees, but also the candidates who have been nominated by the Company other than Manouch Moshayedi, Mark Moshayedi and []. This gives shareholders who wish to vote for our Nominees the ability to vote for a full slate of eight nominees in total, if Proposal No. 2 is approved by shareholders, or seven nominees in total if Proposal No. 2 is not approved by shareholders. The names, backgrounds and qualifications of the Company’s nominees, and other information about them, can be found in the Company’s proxy statement. There is no assurance that any of the Company’s nominees will serve as directors if our Nominees are elected. Further, since our Nominees would comprise less than a majority of the Board, if elected, there can be no assurance that any actions or changes proposed by our

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Nominees will be adopted or supported by the Board, or that any actions or changes proposed by our Nominees will enhance shareholder value. It is our hope, however, that if shareholders vote to elect our Nominees at the Annual Meeting, then the Board will give serious consideration to any ideas, plans or proposals for enhancing shareholder value that one or more of our Nominees may recommend to the full Board.

We urge you to carefully consider the information contained in the attached Proxy Statement and then support our efforts by signing, dating and returning the enclosed GOLD proxy card today. The attached Proxy Statement and the enclosed GOLD proxy card are first being mailed to shareholders on or about May ____, 2013.

If you have already voted for the management slate on the White card, you have every right to change your vote by signing, dating and returning a later dated GOLD proxy. Please vote each and every GOLD proxy card you receive.

If you have any questions or require any assistance with your vote, please contact Okapi Partners LLC, which is assisting us, at their address and toll-free numbers listed below.

Thank you for your support,

Simon J. Michael
Balch Hill Partners, L.P.

If you have any questions, require assistance in voting your GOLD proxy card, or need additional copies of Balch Hill Partnership's proxy materials, please contact Okapi Partners at the phone numbers or email listed below.

OKAPI PARTNERS LLC
437 Madison Avenue, 28th Floor
New York, N.Y. 10022
(212) 297-0720
Call Toll-Free at: (877) 566-1922
E-mail: info@okapipartners.com

PRELIMINARY COPY SUBJECT TO COMPLETION
DATED MAY 14, 2013

2013 ANNUAL MEETING OF SHAREHOLDERS
OF
STEC, INC.

PROXY STATEMENT
OF
BALCH HILL PARTNERS, L.P.

PLEASE SIGN, DATE AND MAIL THE ENCLOSED GOLD PROXY CARD TODAY

Balch Hill Partners, L.P., a Delaware limited partnership (“Balch Hill Partnership”), and the other participants in this solicitation (collectively, “Balch Hill” or “we”) are significant shareholders of STEC, Inc., a California corporation (“STEC” or the “Company”), owning approximately 9.8% of the outstanding shares of common stock, par value \$0.001 per share (the “Common Stock”), of the Company. We are seeking representation on the Board of Directors of the Company (the “Board”) because we believe that the Board could be improved with directors who have strong, relevant backgrounds and who are committed to fully exploring all opportunities to unlock shareholder value. Accordingly, we are seeking your support at the Company’s upcoming 2013 Annual Meeting of Shareholders scheduled to be held 18000 Von Karman Avenue, Irvine, California 92612 on Tuesday, June 25, 2013 at 8:00 a.m., local time, including any adjournment or postponement thereof and any meeting which may be called in lieu thereof (the “Annual Meeting”), for the following:

1. To elect Balch Hill’s director nominees, Adam Leventhal, Clark Masters, and Eric Singer (each a Nominee and collectively, the “Nominees”), to serve as directors of the Company until the 2014 Annual Meeting of Shareholders and until their successors are duly elected and qualified or until their earlier resignation or removal, in opposition to three of the Company’s director nominees whose terms expire at the Annual Meeting;
2. To approve an amendment to the Company’s Second Amended and Restated Bylaws (the “Bylaws”) to increase the minimum and maximum size of the Board;
3. To approve the Company’s 2013 Executive Cash Incentive Plan (the “Incentive Plan”);
4. To conduct an advisory vote to approve the compensation paid to the Company’s named executive officers (the “Say-On-Pay” vote);
5. To ratify the selection of Ernst & Young LLP as the Company’s independent registered public accounting firm for fiscal year ending December 31, 2013; and
6. To transact such other business as may properly come before the Annual Meeting.

This Proxy Statement is soliciting proxies to elect not only our three Nominees, but also the candidates who have been nominated by the Company other than Manouch Moshayedi, Mark Moshayedi and []. This gives shareholders who wish to vote for our Nominees the ability to vote for a full slate of eight nominees in total, if Proposal No. 2 is approved by shareholders, or seven nominees in total if Proposal No. 2 is not approved by shareholders. The names, backgrounds and qualifications of the Company’s nominees, and other information about them, can be found in the

Company's proxy statement. There is no assurance that any of the Company's nominees will serve as directors if our nominees are elected.

Balch Hill Partnership, Balch Hill Capital, LLC, a Delaware limited liability company ("Balch Hill Capital"), Simon J. Michael ("Mr. Michael" and, together with the Balch Hill Partnership and Balch Hill Capital, the "Balch Hill Entities"), Potomac Capital Partners L.P., a Delaware limited partnership ("PCP I"), Potomac Capital Management, L.L.C., a New York limited liability company ("Potomac Management I"), Potomac Capital Partners II, L.P., a Delaware limited partnership ("PCP II"), Potomac Capital Management II, L.L.C., a Delaware limited liability company ("Potomac Management II"), Potomac Capital Partners III, L.P., a Delaware limited partnership ("PCP III"), Potomac Capital Management III, L.L.C., a Delaware limited liability company ("Potomac Management III"), Paul J. Solit ("Mr. Solit"), Eric Singer ("Mr. Singer" and, together with PCP I, Potomac Management I, PCP II, Potomac Management II, PCP III, Potomac Management III, and Mr. Solit, the "Potomac Entities"), and each of the other Nominees are members of a group (the "Group") formed in connection with this proxy solicitation and are deemed participants in this proxy solicitation.

The Company has set the close of business on May 13, 2013 as the record date for determining shareholders entitled to notice of and to vote at the Annual Meeting (the "Record Date"). The mailing address of the principal executive offices of the Company is 3001 Daimler Street, Santa Ana, CA 92705-5812. Shareholders of record at the close of business on the Record Date will be entitled to vote at the Annual Meeting. According to STEC, as of the Record Date, there were _____ shares of Common Stock (the "Shares") outstanding and entitled to vote at the Annual Meeting. As of the Record Date, the Group owned an aggregate of 4,581,470 Shares, which represents approximately 9.8% the Shares outstanding. We intend to vote such Shares FOR the election of the Nominees, FOR the amendment to the Bylaws to increase the minimum and maximum size of the Board, FOR the ratification of the appointment of Ernst & Young LLP, as described herein, and in a manner consistent with the recommendation of Institutional Shareholder Services Inc. ("ISS"), a leading proxy advisory firm, with respect to the proposal to approve the Incentive Plan and the Say-on-Pay vote, as described herein.

THIS SOLICITATION IS BEING MADE BY BALCH HILL AND NOT ON BEHALF OF THE BOARD OF DIRECTORS OR MANAGEMENT OF THE COMPANY. BALCH HILL IS NOT AWARE OF ANY OTHER MATTERS TO BE BROUGHT BEFORE THE ANNUAL MEETING OTHER THAN AS SET FORTH IN THIS PROXY STATEMENT. SHOULD OTHER MATTERS, WHICH BALCH HILL IS NOT AWARE OF A REASONABLE TIME BEFORE THIS SOLICITATION, BE BROUGHT BEFORE THE ANNUAL MEETING, THE PERSONS NAMED AS PROXIES IN THE ENCLOSED GOLD PROXY CARD WILL VOTE ON SUCH MATTERS IN THEIR DISCRETION.

BALCH HILL URGES YOU TO SIGN, DATE AND RETURN THE GOLD PROXY CARD IN FAVOR OF THE ELECTION OF THE NOMINEES.

IF YOU HAVE ALREADY SENT A PROXY CARD FURNISHED BY COMPANY MANAGEMENT OR THE BOARD, YOU MAY REVOKE THAT PROXY AND VOTE ON EACH OF THE PROPOSALS DESCRIBED IN THIS PROXY STATEMENT BY SIGNING, DATING AND RETURNING THE ENCLOSED GOLD PROXY CARD. THE LATEST DATED PROXY IS THE ONLY ONE THAT COUNTS. ANY PROXY MAY BE REVOKED AT ANY TIME PRIOR TO THE ANNUAL MEETING BY DELIVERING A WRITTEN NOTICE OF REVOCATION OR A LATER DATED PROXY FOR THE ANNUAL MEETING OR BY VOTING IN PERSON AT THE ANNUAL MEETING.

Important Notice Regarding the Availability of Proxy Materials for the Annual Meeting

This Proxy Statement and our GOLD proxy card are available at

IMPORTANT

Your vote is important, no matter how few Shares you own. We urge you to sign, date, and return the enclosed GOLD proxy card today to vote FOR the election of the Nominees.

- If your Shares are registered in your own name, please sign and date the enclosed GOLD proxy card and return it to Balch Hill, c/o Okapi Partners LLC (“Okapi Partners”) in the enclosed postage-paid envelope today.
- If your Shares are held in a brokerage account or bank, you are considered the beneficial owner of the Shares, and these proxy materials, together with a GOLD voting form, are being forwarded to you by your broker or bank. As a beneficial owner, you must instruct your broker, trustee or other representative how to vote. Your broker cannot vote your Shares on your behalf without your instructions.
- Depending upon your broker or custodian, you may be able to vote either by toll-free telephone or by the Internet. Please refer to the enclosed voting form for instructions on how to vote electronically. You may also vote by signing, dating and returning the enclosed voting form.

Since only your latest dated proxy card will count, we urge you not to return any proxy card you receive from the Company. Even if you return the management proxy card marked “withhold” as a protest against the Company’s director nominees, it will revoke any proxy card you may have previously sent to us. Remember, you can vote for our Nominees only on our GOLD proxy card. So please make certain that the latest dated proxy card you return is the GOLD proxy card.

OKAPI PARTNERS LLC
437 Madison Avenue, 28th Floor
New York, N.Y. 10022
(212) 297-0720
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E-mail: info@okapipartners.com

BACKGROUND TO THE SOLICITATION

The following is a chronology of material events leading up to this proxy solicitation:

- On December 6, 2012, the Balch Hill Entities delivered a letter to the Board expressing their serious concerns about the strategic direction of the Company and its current performance. In the letter, the Balch Hill Entities recognized the substantial value of the Company's underlying technology, but noted that the Company's performance has declined significantly over the past two years, in the face of increasing competition. The Balch Hill Entities conveyed their belief that the Company's strategy, to increase its operating expenses, particularly in R&D spending, in order to gain scale and compete against larger industry players, has not resulted in commensurate growth in revenues. Accordingly, the Balch Hill Entities called upon the Company to immediately consider (i) a reduction in expenses, particularly in R&D or, greater disclosure to shareholders as to why such spending is justified, (ii) focusing the Company's efforts on its core products, particularly, the SAS market, and (iii) exploring all strategic alternatives, including a sale of the Company.
- On December 20, 2012, Mr. Michael met with Mark Moshayedi, President and Chief Executive Officer ("CEO") of the Company, Manouch Moshayedi, Founder and director of the Company, and Kevin C. Daly, interim Chairman of the Board, to discuss the concerns about the Company that were outlined in the Balch Hill Entities' December 6, 2012 letter.
- On January 25, 2013, the Balch Hill Entities and the Potomac Entities entered into a Joint Filing Agreement pursuant to which, among other things, (i) they agreed to the joint filing on behalf of each of them of statements on Schedule 13D, and any amendments thereto, with respect to the securities of the Company, (ii) they agreed to solicit proxies or written consents for the election of persons to be nominated by the Group to the Board at the Annual Meeting (the "Solicitation"), (iii) they agreed that all decisions and activities of the Group would require unanimous consent, (iv) Balch Hill Capital agreed to indemnify each of the Potomac Entities and hold each of them harmless against any and all third party claims of any nature arising from the Solicitation and any related activities, subject to certain exceptions, (v) the parties agreed that Balch Hill Capital shall have the right to pre-approve all expenses incurred in connection with the Solicitation, and (vi) Balch Hill Capital agreed to pay directly all expenses incurred in connection with the Solicitation.
- On February 8, 2013, Messrs. Michael and Singer met with Manouch Moshayedi, the Company's Founder, Mark Moshayedi, the Company's President and CEO, Kevin Daly, the Chairman of the Board, and Christopher Colpitts, an independent Board member. At this meeting, Mr. Michael expressed Balch Hill's belief that Manouch Moshayedi should resign from the Board and executive management team and the Company should search for a new, independent CEO with global experience in the industry to lead the Company forward. The Board did not respond to Mr. Michael at this meeting .
- Also on February 8, 2013, Balch Hill delivered a letter to the Company nominating Martin Colombatto, Adam Leventhal, Clark Masters, Mark Schwartz, Eric Singer, Dilip Singh, and Bernard Xavier for election to the Board at the Annual Meeting .
- Later in the day on February 8, 2013, Robert Saman, the Company's Chief Legal Officer, General Counsel and Secretary called Balch Hill's legal counsel. Mr. Saman and Balch Hill's legal counsel spoke on February 9, 2013. Mr. Saman expressed the Board's surprise by Mr. Michael's desire to seek the resignation of Manouch Moshayedi and replace Mark Moshayedi with a new CEO. Mr. Saman also informed Balch Hill's legal counsel that the Board would be meeting on February 11, 2013 to discuss the Nominees and would be in touch thereafter.

- On February 12, 2013, Mr. Saman and the Company's outside legal counsel had a call with Balch Hill's legal counsel. The Company proposed expanding the Board to nine, agreeing to interview four of the Nominees (Messrs. Colombatto, Leventhal, Masters and Singh), and selecting two of the four Nominees to be added to the Company's slate of directors for election at the Annual Meeting. The Company requested that Balch Hill respond to the settlement offer prior to the filing of its Schedule 13D amendment which was due that same day as a result of Balch Hill's nomination of the Nominees. Balch Hill responded that the Company's initial settlement offer would not result in meaningful change to the Company, if Manouch Moshayedi remained in effective control of the Company. Balch Hill instead proposed that Manouch Moshayedi resign immediately, the Board be expanded by two, the Board appoint three of the Nominees, and that the Company engage in a search for a truly independent CEO with global experience and industry contacts to help the Company regain some of its market share loss.
- On February 12, 2013, Balch Hill filed a Schedule 13D amendment announcing its nomination of the Nominees for election to the Board at the Annual Meeting. Balch Hill also expressed its belief that meaningful change to the Board and executive management team were necessary to restore trust to the Company. Balch Hill indicated that it remained willing to engage in constructive discussions with management and the Board regarding the nomination of directors at the Annual Meeting and the composition of the Board in order to avoid a protracted and costly proxy contest, but that it believed shareholder value is at risk without a reconstituted Board.
- Later in the day on February 12, 2013, the Company issued a press release responding to Balch Hill's nomination. The Company argued that Balch Hill had discounted the Company's 2013 strategic plan and rejected what they considered a good faith effort to engage in constructive dialogue, in order to pursue a proxy contest aimed at taking control of the Company and potentially seeking the sale of the Company.
- From February 21, 2013 to March 12, 2013, the Company's outside legal counsel and Balch Hill's legal counsel engaged in discussions regarding the composition of the Board in order to avoid a proxy contest. The Company and Balch Hill were in verbal agreement that Manouch Moshayedi would resign immediately from the Board, Eric Singer would be appointed to fill the resulting vacancy, the Board would form a four person special committee to search for a new CEO, of which Eric Singer would be a member, Mark Moshayedi would not stand for election at the Annual Meeting, the Company would propose amending the Bylaws to expand the Board by two directors, one additional Nominee would be supported by the Company for election at the Annual Meeting, one Board seat would be reserved for the new CEO, and the final seat would be reserved for a new independent director to be selected by the Board. However, the Board disagreed on the timing of the announcement of Mark Moshayedi's intended departure from the Board and the announcement of the search for a new CEO and would not memorialize these material terms of our verbal agreement in a written settlement agreement.
- On March 14, 2013, Balch Hill Partnership and PCP II issued an open letter to shareholders and a press release announcing that settlement discussions with the Company had broken down. Balch Hill Partnership and PCP II also expressed their belief that in order to move the Company forward, both Manouch and Mark Moshayedi should resign from the Board immediately .

- Also on March 14, 2013, the Company filed its earnings release for the fourth quarter and 2012 fiscal year, disclosing operating losses of over \$103 million, a 510% decline from the prior year. The Company separately issued a press release acknowledging that settlement discussion with Balch Hill had broken down.
- On March 18, 2013, Balch Hill Partnership and PCP II issued an open letter to shareholders and a press release stating that it believes STEC has tremendous value to be realized but that the Board and executive management team must be reconstituted for this underlying value to be realized. Balch Hill Partnership and PCP II argued that the current Board and executive management team have presided over a massive loss of revenue and market share in the Company's core OEM enterprise SSD market even as that market grows strongly, because they have misallocated corporate funds (through a share buy back program at a premium more than double the closing price of the stock just eight months later and increased research and development spending that has not resulted in increased revenues) and are pursuing a misguided business strategy of customer diversification instead of focusing on the Company's business on SAS SSD sales to large storage OEM customers. Balch Hill Partnership and PCP II reiterated their belief that in order for the Company to move forward, the Board and management team has to be reconstituted without Manouch or Mark Moshayedi in control .
- On March 20, 2013, the Company issued an open letter to shareholders responding to our March 18, 2013 letter. The Company reiterated its confidence in and commitment to its new business strategy focused on diversifying its customer base and argued that its Board and management have the track record to create shareholder value.
- On March 29, 2013, the Company requested that Balch Hill execute a non-disclosure agreement in order to resume settlement discussions.
- On April 1, 2013, Balch Hill's legal counsel sent a letter to the Company's outside legal counsel indicating that Balch Hill would be willing to keep such discussions private while they were negotiating in good faith and that a non-disclosure agreement in order to reach a negotiated settlement was unnecessary.
 - On April 4 and 5, 2013, Balch Hill and the Company discussed signing a limited non-disclosure agreement.
- On April 9, 2013, Balch Hill's legal counsel called the Company's outside legal counsel to request a meeting between Balch Hill and the independent members of the Board.
- On April 15, 2013, Messrs. Michael and Singer had a conference call with all of the independent members of the Board. On this call, Mr. Michael requested an in person meeting to discuss the framework for settlement without a non-disclosure agreement.
- On April 19, 2013, Messrs. Michael and Singer had an in-person meeting with Kevin Daly and Matthew Witte; Rajat Bahri and Christopher Colpitts participated telephonically. At the meeting, the parties discussed the framework for settlement. Mr. Michael agreed to put forth in writing a proposal for settlement.
- On April 22, 2013, Balch Hill Partnership and PCP II sent the independent members of the Board a letter expressing their encouragement by the progress made to reach a mutually agreeable resolution of the proxy contest. The letter also set forth Balch Hill's terms for settlement, which Balch Hill believed would adequately address the significant concerns and issued it had raised and result in meaningful change to the Board.
- On April 28, 2013, Mr. Daly sent Mr. Michael an email indicating that in order to preclude any possibility of miscommunication, the Board had determined it would be best for it to respond formally to Balch Hill's proposal for settlement. Later that day, outside legal counsel to the Company called Balch Hill's legal counsel indicating that the

Board had no interest in the Group's proposal for settlement and that we should proceed with a proxy contest.

· On May 1, 2013, Balch Hill Partnership issued an open letter to the Board's Nominating and Corporate Governance Committee (the "Nominating Committee") urging the Nominating Committee not to renominate Manouch or Mark Moshayedi to the Board in light of the SEC's action against Manouch Moshayedi for insider trading. Balch Hill Partnership argued that the insider trading charges brought by the SEC against Manouch Moshayedi represent a significant cloud over not just Manouch Moshayedi but also over his brother, Mark Moshayedi, who has not been charged, but who has been investigated by the SEC, who served as Chief Operating Officer for the Company during the events in question, and who sold stock alongside Manouch Moshayedi. Balch Hill Partnership also expressed its belief that the SEC's recent action seeking to amend its original complaint against Manouch Moshayedi was particularly concerning.

REASONS FOR THE SOLICITATION

We believe that change is needed now on the Board. Therefore, we are soliciting your support to elect our Nominees at the Annual Meeting. We believe our Nominees would bring significant and relevant experience, new insight and fresh perspectives to the Board. If elected, our Nominees are committed to working constructively with the other members of the Board and using their experience to help effect more prudent and thoughtful decision making, thus helping management to reverse the recent significant underperformance and execute a successful strategic plan for STEC for the benefit of all shareholders. However, since the Nominees would comprise less than a majority of the Board, if elected, there can be no assurance that any actions or changes proposed by the Nominees will be adopted or supported by the Board, or that any actions or changes proposed by the Nominees will enhance shareholder value if adopted by the Board. It is our hope, however, that if shareholders vote to elect our Nominees at the Annual Meeting, then the Board will give serious consideration to any ideas, plans or proposals for enhancing shareholder value that one or more of the Nominees may recommend to the full Board.

We believe that the Company is suffering significant reputational damage by the continued presence of Manouch and Mark Moshayedi.

In 2009, the SEC commenced a formal investigation of the Company, Manouch Moshayedi, the Company's Founder, and Mark Moshayedi, the Company's CEO and President, involving trading in the Company's securities, which ultimately led to an SEC action brought against Manouch Moshayedi for insider trading. Various shareholder class actions and shareholder derivative actions have also been brought against the Company alleging that the Company and certain of its senior officers and directors, including Manouch Moshayedi and Mark Moshayedi, made materially false or misleading public statements. In addition to the legal costs that have resulted for the Company (for the year ended December 31, 2012, STEC recorded approximately \$21.8 million of settlement costs and legal fees in excess of its insurance deductible under its director and officer insurance coverage, \$15 million of which relates to the settlement of a federal shareholder class action, which is subject to court approval), we believe the Company has suffered considerable reputational damage that, when compounded with increasing competition, has resulted in incredible market share loss for the Company.

While Manouch Moshayedi recently stepped down in July 2012 as Chairman of the Board and CEO pending the resolution of the civil complaint filed against him by the SEC for insider trading, we believe his change in title to Founder and continuation as a director of the Company are merely cosmetic changes. Why, for example, did Manouch Moshayedi continue to receive the same salary and benefits following his resignation as Chairman and CEO until both Mark and Manouch Moshayedi decided to reduce their salaries to \$1.00, effective December 1, 2012, shortly after the filing of our initial Schedule 13D in November 2012? Also, rather than appointing an outside candidate as CEO to replace Manouch Moshayedi to energize the business and represent a new direction for the Company, why did the Board appoint Mark Moshayedi, Manouch Moshayedi's brother, to the role of CEO? Did the Board believe that Mark Moshayedi was the best candidate for the position? Was he appointed after a full and robust process to identify the best candidate to lead the Company forward? We believe the Company's continuing underperformance clearly indicates that Mark Moshayedi is the wrong man for the job. Would he really have been appointed to CEO if he had not been the brother of Manouch Moshayedi?

We believe the continued presence of Manouch Moshayedi and the appointment of his brother to continue at the helm of STEC are the actions of a Board that is too heavily influenced by its founders. We believe the Board must be reconstituted with truly independent directors that will hold management accountable for the Company's poor financial performance and work to restore the reputational harm caused by the continued presence of the Moshayedi brothers.

We are concerned with the Company's poor stock price performance.

In just over three (3) years, the current Board and management team have overseen the destruction of over \$509 million in shareholder value, from a closing price of \$13.42 on the day the Company filed its Annual Report on Form 10-K for the year ended December 31, 2009 to a recent closing price of \$3.54 on May 10, 2013. STEC's share price has declined over 60% in the year preceding our initial filing of a Schedule 13D on November 16, 2012, and approximately 70% since the Company first announced, in its Annual Report on Form 10-K for the year ended December 31, 2009, that the SEC had commenced a formal investigation involving trading in the Company's securities by Manouch Moshayedi, the Company's Founder, and Mark Moshayedi, the Company's CEO and President. We believe that the entire Board must be held accountable for this significant destruction of shareholder value.

We are concerned with the Company's poor capital allocation and growing size of its operating expenses.

We believe the Company has a strong but eroding balance sheet due to the current Board and executive management team's poor capital allocation and financial performance. For example, the Company spent approximately \$55 million to repurchase 1,546,700 shares of common stock at an average price per share of \$9.72 and 4,063,911 shares of common stock at an average price per share of \$9.86, from August 9, 2011 until March 30, 2012. Less than eight months later, the stock closed at a low of \$4.07 on the trading day immediately preceding the filing of our initial Schedule 13D on November 16, 2012.