

DEXCOM INC  
Form DEF 14A  
April 20, 2007  
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  x

Filed by a Party other than the Registrant  o

Check the appropriate box:

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

**DexCom, Inc.**

(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):

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

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| (1) | Amount Previously Paid:                       |
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| (3) | Filing Party:                                 |
| (4) | Date Filed:                                   |

April 20, 2007

To Our Stockholders:

You are cordially invited to attend the 2007 Annual Meeting of Stockholders of DexCom, Inc. to be held at DexCom's headquarters located at 5555 Oberlin Drive, San Diego, California 92121, on May 23, 2007, at 2:00 p.m. local time.

The matters expected to be acted upon at the meeting are described in detail in the following Notice of Annual Meeting of Stockholders and Proxy Statement.

It is important that you use this opportunity to take part in the affairs of DexCom, Inc. by voting on the business to come before this meeting. **WHETHER OR NOT YOU EXPECT TO ATTEND THE MEETING, PLEASE COMPLETE, DATE, SIGN, AND PROMPTLY RETURN THE ACCOMPANYING PROXY IN THE ENCLOSED POSTAGE-PAID ENVELOPE SO THAT YOUR SHARES MAY BE REPRESENTED AT THE MEETING.** Returning the proxy does not deprive you of your right to attend the meeting and to vote your shares in person.

We look forward to seeing you at the meeting.

Sincerely,

Andrew P. Rasdal  
Chief Executive Officer and President

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**DEXCOM, INC.**  
5555 Oberlin Drive  
San Diego, California 92121

**NOTICE OF ANNUAL MEETING OF STOCKHOLDERS  
TO BE HELD ON MAY 23, 2007**

Dear Stockholder:

You are cordially invited to attend the 2007 Annual Meeting of Stockholders of DexCom, Inc., a Delaware corporation. The meeting will be held on May 23, 2007 at 2:00 p.m. local time at DexCom's corporate headquarters located at 5555 Oberlin Drive, San Diego, California 92121, for the following purposes:

1. To elect three Class II directors to hold office until our 2010 Annual Meeting of Stockholders.
2. To approve an amendment to our 2005 Equity Incentive Plan that will provide discretion to the Board of Directors to determine the value and number of equity awards granted to non-employee directors from time to time.
3. To ratify the selection by the audit committee of our Board of Directors of Ernst & Young LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2007.
4. To conduct any other business properly brought before the meeting.

These items of business are more fully described in the proxy statement accompanying this notice.

The record date for the annual meeting is April 4, 2007. Only stockholders of record at the close of business on that date may vote at the meeting or any adjournment or postponement thereof.

By Order of the Board of Directors

Andrew P. Rasdal  
Chief Executive Officer and President

San Diego, California  
April 20, 2007

**You are cordially invited to attend the meeting in person. Whether or not you expect to attend the meeting, please complete, date, sign and return the proxy accompanying this notice as promptly as possible in order to ensure your representation at the meeting. A return envelope (which is postage prepaid if mailed in the United States) is enclosed for your convenience. Even if you have voted by proxy, you may still vote in person if you attend the meeting. Please note, however, that if your shares are held of record by a broker, bank or other agent and you wish to vote at the meeting, you must request and obtain a proxy issued in your name from that record holder.**

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**DEXCOM, INC.**  
5555 Oberlin Drive  
San Diego, California 92121

**PROXY STATEMENT  
FOR THE ANNUAL MEETING OF STOCKHOLDERS  
TO BE HELD MAY 23, 2007**

**QUESTIONS AND ANSWERS**

**Why am I receiving these proxy materials?**

We sent you this proxy statement and the accompanying proxy card because the Board of Directors of DexCom, Inc. is soliciting your proxy to vote at its 2007 Annual Meeting of Stockholders. You are invited to attend the annual meeting to vote on the proposals described in this proxy statement. However, you do not need to attend the meeting to vote your shares. Instead, you may simply complete, sign and return the accompanying proxy card.

We mailed this proxy statement, the accompanying proxy card and our annual report on or about April 20, 2007 to all stockholders of record entitled to vote at the annual meeting.

**Who can vote at the annual meeting?**

Only stockholders of record at the close of business on April 4, 2007, the record date for the annual meeting, will be entitled to vote at the annual meeting. At the close of business on the record date, there were 28,330,796 shares of common stock outstanding and entitled to vote.

*Stockholder of Record: Shares Registered in Your Name*

If at the close of business on the record date, your shares were registered directly in your name with our transfer agent, American Stock Transfer & Trust Company, then you are a stockholder of record. As a stockholder of record, you may vote in person at the meeting or vote by proxy. Whether or not you plan to attend the meeting, we urge you to fill out and return the accompanying proxy card to ensure your vote is counted.

*Beneficial Owner: Shares Registered in the Name of a Broker, Bank or Other Agent*

If at the close of business on the record date, your shares were held, not in your name, but rather in an account at a brokerage firm, bank or other agent, then you are the beneficial owner of shares held in street name and these proxy materials are being forwarded to you by your broker, bank or other agent. The broker, bank or other agent holding your account is considered to be the stockholder of record for purposes of voting at the annual meeting.

As a beneficial owner, you have the right to direct your broker, bank or other agent on how to vote the shares in your account. You are also invited to attend the annual meeting. However, since you are not the stockholder of record, you may not vote your shares in person at the meeting unless you request and obtain a valid proxy issued in your name from your broker, bank or other agent.

**What am I voting on?**

There are three matters scheduled for a vote at the annual meeting:

- the election of three Class II directors to hold office until our 2010 Annual Meeting of Stockholders,

- the approval of an amendment to our 2005 Equity Incentive Plan that will provide discretion to the Board of Directors to determine the value and number of equity awards granted to non-employee directors from time to time. If approved, we intend to provide the following equity-based compensation to our non-employee directors: (i) we intend to grant a number of options annually to non-employee directors, other than the Chairman of the Board, with a Black-Scholes value of \$125,000, rather than 20,000 options per year, which option grant is to vest in equal monthly installments over twelve months; (ii) we intend to grant a number of options annually to the Chairman of the Board with a Black-Scholes value of \$150,000, rather than 25,000 options per year, which option grant is to vest in equal monthly installments over twelve months; and (iii) we intend to grant a number of options to an incoming non-employee director with a Black-Scholes value of \$300,000, rather than an initial grant of 25,000 options, which option grant is to vest in equal monthly installments over thirty-six months, and
- the ratification of the selection by the audit committee of our Board of Directors of Ernst & Young LLP as our independent registered public accounting firm for the fiscal year ending December 31, 2007.

**How do I vote?**

For the election of directors, you may either vote  For the three nominees or you may  Withhold your vote for any nominee you specify. For any other matter to be voted on, you may vote  For or  Against or abstain from voting. The procedures for voting are as follows:

*Stockholder of Record: Shares Registered in Your Name*

If you are a stockholder of record, you may vote in person at the annual meeting. Alternatively, you may vote by proxy by using the accompanying proxy card. Whether or not you plan to attend the meeting, we urge you to vote by proxy to ensure your vote is counted. You may still attend the meeting and vote in person if you have already voted by proxy.

- To vote in person, come to the annual meeting and we will give you a ballot when you arrive.
- To vote using the proxy card, simply complete, sign and date the accompanying proxy card and return it promptly in the envelope provided. If you return your signed proxy card to us before the annual meeting, we will vote your shares as you direct.

*Beneficial Owner: Shares Registered in the Name of Broker, Bank or Other Agent*

If you are a beneficial owner of shares registered in the name of your broker, bank or other agent, you should have received a voting instruction card and voting instructions with these proxy materials from that organization rather than from us. Simply complete and mail the voting instruction card to ensure that your vote is counted. To vote in person at the annual meeting, you must obtain a valid proxy from your broker, bank or other agent. Follow the instructions from your broker, bank or other agent included with these proxy materials, or contact your broker, bank or other agent to request a proxy form.

**How many votes do I have?**

On each matter to be voted upon, you have one vote for each share of common stock you owned as of the close of business on April 4, 2007, the record date for the annual meeting.

**What if I return a proxy card but do not make specific choices?**

If you return a signed and dated proxy card without marking any voting selections, your shares will be voted  For the election of the three nominees for director,  For the amendment to the 2005 Equity Incentive Plan and  For the ratification of the selection of Ernst & Young LLP as our independent



registered public accounting firm. If any other matter is properly presented at the meeting, one of the individuals named on your proxy card as your proxy will vote your shares using his best judgment.

**Who is paying for this proxy solicitation?**

We will pay for the entire cost of soliciting proxies. In addition to these mailed proxy materials, our directors, officers and employees may also solicit proxies in person, by telephone, or by other means of communication. Directors, officers, and employees will not be paid any additional compensation for soliciting proxies. We may also reimburse brokerage firms, banks and other agents for the cost of forwarding proxy materials to beneficial owners.

**What does it mean if I receive more than one proxy card?**

If you receive more than one proxy card, your shares are registered in more than one name or are registered in different accounts. Please complete, sign and return each proxy card to ensure that all of your shares are voted.

**Can I change my vote after submitting my proxy?**

Yes. You can revoke your proxy at any time before the applicable vote at the meeting. If you are the record holder of your shares, you may revoke your proxy in any one of three ways:

- you may submit another properly completed proxy with a later date,
- you may send a written notice that you are revoking your proxy to our Secretary at 5555 Oberlin Drive, San Diego, California 92121, or
- you may attend the annual meeting and vote in person (however, simply attending the meeting will not, by itself, revoke your proxy).

If your shares are held by your broker, bank or other agent, you should follow the instructions provided by them.

**When are stockholder proposals due for next year's annual meeting?**

To be considered for inclusion in next year's proxy materials, a stockholder proposal must be submitted in writing by December 22, 2007, to our Secretary at 5555 Oberlin Drive, San Diego, California 92121. If you wish to submit a proposal that is not to be included in next year's proxy materials, your proposal generally must be submitted in writing to the same address no later than February 23, 2008 but no earlier than January 25, 2008. Please review our bylaws, which contain additional requirements regarding advance notice of stockholder proposals.

**How are votes counted?**

Votes will be counted by the inspector of elections appointed for the meeting, who will separately count For and Withhold votes with respect to the election of directors and, with respect to any proposals other than the election of directors, For and Against votes, abstentions and broker non-votes. A broker non-vote occurs when a nominee holding shares for a beneficial owner does not vote on a particular proposal because the nominee does not have discretionary voting power with respect to that proposal and has not received instructions with respect to that proposal from the beneficial owner, despite voting on at least one other proposal for which it does have discretionary authority or for which it has received instructions. Abstentions will have no effect on the outcome. Broker non-votes have no effect and will not be counted towards the vote total for any proposal.

If your shares are held by your broker, bank or other agent as your nominee (that is, in street name), you will need to obtain a proxy form from the institution that holds your shares and follow the instructions included on that form regarding how to instruct your broker, bank or other agent to vote your shares. If you do not give instructions to your broker, bank or other agent, they can vote your shares with respect to discretionary items, but not with respect to non-discretionary items. Discretionary items are proposals considered routine, such as the election of directors, on which your broker, bank or other agent may vote shares held in street name in the absence of your voting instructions, such as the vote for directors and ratification of our independent registered public accounting firm. On non-discretionary items, such as the amendment to the 2005 Equity Incentive Plan, for which you do not give instructions to your broker, bank or other agent, the shares will be treated as broker non-votes.

**How many votes are needed to approve each proposal?**

- For the election of directors, the three nominees receiving the most For votes (among votes properly cast in person or by proxy) will be elected.
- To be approved, the amendment to the 2005 Equity Incentive Plan and the ratification of the selection of Ernst & Young LLP as our independent registered public accounting firm must receive a For vote from the majority of shares present and entitled to vote either in person or by proxy.

**What is the quorum requirement?**

A quorum of stockholders is necessary to hold a valid meeting. A quorum will be present if at least a majority of the outstanding shares as of the close of business on the record date are represented by stockholders present at the meeting or by proxy. At the close of business on the record date, there were 28,330,796 shares outstanding and entitled to vote. Therefore, in order for a quorum to exist, 14,165,399 shares must be represented by stockholders present at the meeting or by proxy.

Your shares will be counted towards the quorum only if you submit a valid proxy (or one is submitted on your behalf by your broker, bank or other agent) or if you vote in person at the meeting. Abstentions and broker non-votes will be counted towards the quorum requirement. If there is no quorum, a majority of the votes present at the meeting may adjourn the meeting to another date.

**How can I find out the results of the voting at the annual meeting?**

Preliminary voting results will be announced at the annual meeting. Final voting results will be published in our Quarterly Report on Form 10-Q for the second quarter of 2007.



**PROPOSAL 1****ELECTION OF DIRECTORS**

As of immediately prior to the annual meeting, our Board of Directors will consist of eight members and is divided into three classes, each of which has a three-year term. Class I consists of two directors, and classes II and III consist of three directors each as of immediately prior to the annual meeting. The Class II directors are to be elected at this annual meeting to serve until our 2010 Annual Meeting of Stockholders and until their successors are duly elected and qualified, or until their death, resignation or removal. The terms of the directors in Classes I and III expire at our 2009 and 2008 Annual Meetings of Stockholders, respectively.

The three nominees for Class II directors are Donald L. Lucas, Donald A. Lucas and Jay S. Skyler, M.D., MACP. Each of the nominees is currently a director of DexCom. Each nominee was elected by our stockholders in a stockholder meeting on March 21, 2005.

Directors are elected by a plurality of the votes present at the meeting or by proxy and entitled to vote at the meeting. The three nominees receiving the most For votes (among votes properly cast in person or by proxy) will be elected. If no contrary indication is made, shares represented by executed proxies will be voted For the election of the three nominees named above or, if any nominee becomes unavailable for election as a result of an unexpected occurrence, For the election of a substitute nominee designated by our Board of Directors. Each nominee has agreed to serve as a director if elected, and we have no reason to believe that any nominee will be unable to serve.

**THE BOARD OF DIRECTORS RECOMMENDS A VOTE FOR THE ELECTION OF EACH NOMINEE NAMED ABOVE.**

The following is biographical information as of April 4, 2007 for each nominee for Class II director and each person whose term of office as a Class I or III director will continue after the annual meeting.

| <b>Name</b>          | <b>Age</b> | <b>Position</b>                                 |
|----------------------|------------|---|
| Andrew P. Rasdal     | 48         | President, Chief Executive Officer and Director |
| Donald L. Lucas      | 77         | Chairman of the Board of Directors              |
| Kim D. Blickenstaff  | 54         | Director  |
| Sean Carney          | 38         | Director  |
| Terrance H. Gregg    | 58         | Director  |
| Donald A. Lucas      | 44         | Director  |
| Jay S. Skyler, M.D.  | 60         | Director  |
| Glen D. Nelson, M.D. | 70         | Director  |

**Nominees for Election for a Three-year Term Expiring at the 2010 Annual Meeting**

*Donald L. Lucas* has served as Chairman of our Board of Directors since September 2002 and as a director since May 2002. In 1960, Mr. Lucas began a seven-year participation, including acting as both a general partner and a limited partner, with Draper, Gaither & Anderson, the first venture capital firm organized on the West Coast in the United States. Since 1967, Mr. Lucas has been actively engaged in venture capital activities as a private individual. Mr. Lucas currently serves as a director of Cadence Design Systems, Inc., Oracle Corporation, Vimicro Corporation and 51job, Inc. Mr. Lucas also serves as a director for several privately held companies. Mr. Lucas received a B.A. from Stanford University and an M.B.A. from the Stanford Graduate School of Business. Mr. Lucas is also trustee of Santa Clara University and Chairman Emeritus of the Stanford Institute for Economic Policy Research.

*Donald A. Lucas* has served on our Board of Directors since May 2002. Mr. Lucas, a second generation venture capitalist, co-founded RWI Ventures in 2000. Previously, Mr. Lucas spent over a decade with his father, Donald L. Lucas, investing in a number of venture backed companies in the technology and life sciences sectors, including Macromedia, Intuitive Surgical and Coulter Pharmaceutical. Mr. Lucas currently serves as a director of Response Analytics, Inc., and as a board observer of Paracor Medical, both privately held companies. Mr. Lucas also serves as a director of the Silicon Valley Chapter of the Juvenile Diabetes Research Foundation, the Richard M. Lucas Foundation, and is a member of the UCSF Diabetes Center Leadership Council. Mr. Lucas holds a B.A. from Santa Clara University.

*Jay S. Skyler, M.D., MACP* has served on our Board of Directors since September 2002. Dr. Skyler is a Professor of Medicine, Pediatrics and Psychology and Associate Director of the Diabetes Research Institute at the University of Miami in Florida, where he has been employed since 1976. Dr. Skyler also serves as the Chairman of the Planning Committee of the Clinical Research Institute, University of Miami Miller School of Medicine and as Study Chairman for the National Institute of Diabetes & Digestive & Kidney Diseases Type 1 Diabetes TrialNet clinical trials network. Dr. Skyler also serves as a director of Amylin Pharmaceuticals, Inc. Dr. Skyler received a B.S. from Pennsylvania State University and an M.D. from Jefferson Medical College.

**Directors Continuing in Office Until the 2008 Annual Meeting**

*Andrew P. Rasdal* has served as our President and Chief Executive Officer and on our Board of Directors since January 2002. From April 2000 to December 2001, Mr. Rasdal served as Senior Vice President of Medtronic, Inc., a medical technology company, and as President of Medtronic, Inc., Vascular Division. From February 1999 to April 2000, Mr. Rasdal served as General Manager of Medtronic, Inc., Vascular Division. Mr. Rasdal received a B.S. from San Jose State University and an M.B.A. from the Kellogg Graduate School of Management, Northwestern University.

*Sean Carney* has served on our Board of Directors since December 2004. Since 1996, Mr. Carney has been employed by Warburg Pincus LLC, a private equity firm, and has served as a Managing Director of Warburg Pincus LLC and General Partner of Warburg Pincus & Co. since January 2001. Mr. Carney also serves as a director of Arch Capital Group Ltd. Mr. Carney received an A.B. from Harvard College and an M.B.A. from Harvard Business School.

*Glen D. Nelson, M.D.* has served on our board of directors since October 2002. Since 2002, Dr. Nelson has served as Chairman of GDN Holdings, LLC, an aviation, health services and medical device company. From 1988 to 2002, Dr. Nelson served as Vice Chairman of Medtronic, Inc., a medical device company. Dr. Nelson also serves as a director of The St. Paul Travelers Companies, Inc. and Angiotech Pharmaceuticals, Inc. Dr. Nelson received a B.A. from Harvard University and an M.D. from the University of Minnesota.

**Directors Continuing in Office Until the 2009 Annual Meeting**

*Kim D. Blickenstaff* has served on our Board of Directors since June 2001. Mr. Blickenstaff is the co-founder of Biosite Incorporated, a medical technology company, where since October 2004, he has served as its Chairman and Chief Executive Officer, and from April 1988 to October 2004 served as its President, Chief Executive Officer and director. Mr. Blickenstaff received a B.A. and an M.B.A. from Loyola University.

*Terrance H. Gregg* has served on our Board of Directors since May 2005. In March 2007, Mr. Gregg assumed the role of Chief Executive Officer and President of Vasogen, Inc., an immunotherapy company focused on heart failure and neurodegenerative diseases, where he has served as a director since 1999 and as Chairman since March 2006. Since September 2004, Mr. Gregg has been a Special Venture Partner with



Galen Collaborative Capital, a private equity firm, and has operated THG Consulting LLC, a health care advisory firm. From July 2002 to September 2004, Mr. Gregg served as a senior adviser to the diabetes business of Medtronic, Inc., a medical technology company. Mr. Gregg served as President and Chief Operating Officer of MiniMed, Inc., a medical technology company focused on insulin pumps for people with diabetes, from October 1996 until its acquisition by Medtronic, Inc. in August 2001, and Mr. Gregg served as a Vice President of Medtronic and President of Medtronic MiniMed after the acquisition until July 2002. Mr. Gregg formerly served as the Chairman of the American Diabetes Association Research Foundation Board. He also serves as a director of LMS Medical Systems, Ltd. Mr. Gregg received a B.S. from Colorado State University.

Donald A. Lucas is the son of Donald L. Lucas. With the exception of such relationship, there are no family relationships among any of our directors and executive officers.

## **CORPORATE GOVERNANCE**

### **Independence of the Board of Directors and its Committees**

As required under NASDAQ Stock Market listing standards, a majority of the members of a listed company's Board of Directors must qualify as independent, as affirmatively determined by the board. Our Board of Directors consults with our counsel to ensure that the Board's determinations are consistent with all relevant securities and other laws and regulations regarding the definition of independent, including those set forth in applicable NASDAQ listing standards, as in effect from time to time.

Consistent with these considerations, after review of all relevant transactions or relationships between each director, or any of his or her family members, and DexCom, our senior management and our independent registered public accounting firm, our Board of Directors has affirmatively determined that all of our directors are independent directors within the meaning of the applicable NASDAQ listing standards, except for Mr. Rasdal, our Chief Executive Officer and President. In making its independence determinations, the Board reviewed transactions and relationships between the director, or any member of his or her immediate family, and us or one of our subsidiaries or affiliates based on information provided by the director, our records and publicly available information. Specifically, the Board considered the following types of relationships and transactions: (i) principal employment of and other public company directorships held by each non-employee director; (ii) contracts or arrangements that are ongoing or which existed during any of the past three fiscal years between DexCom and its affiliates and any entity for which the non-employee director, or his or her immediate family member, is an executive officer or greater-than-10% shareholder; and (iii) contracts or arrangements that are ongoing or which existed during any of the past three fiscal years between DexCom and/or its subsidiaries or affiliates and any other public company for which the non-employee director serves as a director. The relationships and transactions reviewed by our Board included the following:

- the father and son relationship between Donald L. Lucas and Donald A. Lucas, in which case the Board determined that such relationship would not interfere with the exercise of independent judgment of either of them as directors; and
- the fact that two relatives of Terrance H. Gregg have been employed as an employee and as a consultant of DexCom, but neither has served as an executive officer of DexCom, in each case the Board determined that those relationships would not interfere with Mr. Gregg's exercise of independent judgment as a director.

As required under applicable NASDAQ listing standards, our independent directors meet in regularly scheduled executive sessions at which only independent directors are present. All of the committees of our Board of Directors are comprised entirely of directors determined by the Board to be independent within the meaning of applicable NASDAQ listing standards.

**Information Regarding the Board of Directors and its Committees**

Our Board of Directors has an audit committee, a compensation committee and a nominating and governance committee. The following is membership and meeting information for each of these committees during the fiscal year ended December 31, 2006, as well as a description of each committee and its functions.

| Name                               | Audit Committee | Compensation Committee | Nominating and Governance Committee |
|------------------------------------|-----------------|------------------------|-------------------------------------|
| Andrew P. Rasdal                   |                 |                        |                                     |
| Donald L. Lucas                    | X *             |                        | X                                   |
| Kim D. Blickenstaff                | X               |                        |                                     |
| Sean Carney                        | X               | X *                    |                                     |
| Terrance H. Gregg                  |                 |                        |                                     |
| Donald A. Lucas                    | X               | X                      |                                     |
| Glenn D. Nelson, M.D.              |                 | X                      | X *                                 |
| Jay S. Skyler, M.D.                |                 |                        | X                                   |
| Total meetings in fiscal year 2006 | 5               | 5                      | 3                                   |

\* Committee Chairperson

*Audit Committee*

The audit committee operates pursuant to a written charter that is available on our website at <http://www.dexcom.com>. The audit committee reviews and evaluates our financial statements, accounting practices and our internal accounting procedures, selects and engages the appointment of our independent registered public accounting firm and reviews the results and scope of the audit and other services provided by our independent registered public accounting firm.

*Audit Committee Financial Experts.* Our Board of Directors has determined that each of Kim Blickenstaff and Donald L. Lucas qualify as an audit committee financial expert, as defined in applicable Securities and Exchange Commission, or SEC, rules. In addition, each member of our audit committee possesses the financial qualifications required of audit committee members set forth in the rules and regulations of the NASDAQ Global Market. The Board made a qualitative assessment of the committee members' level of knowledge and experience based on a number of factors, including formal education and experience.

*Compensation Committee*

The compensation committee operates pursuant to a written charter that is available on our website at <http://www.dexcom.com>. The compensation committee reviews and determines the compensation and benefits of our executive officers, reviews and recommends to the Board concerning the compensation of our non-employee directors, reviews annually and recommends to our Board cash-based and equity-based incentive compensation under our equity compensation and employee benefits plans and reviews our general policies relating to compensation and benefits. Each member of this committee is a non-employee director, as defined in Rule 16b-3 promulgated under the Exchange Act and an outside director, as defined pursuant to Section 162(m) of the Internal Revenue Code of 1986.

*Compensation Committee Policies and Procedures.* The compensation committee reviews management's recommendations for compensation and benefits for executive officers. The compensation committee reviews and determines the amount and composition of executive compensation to be paid to the executive officers, including the Chief Executive Officer.

The compensation committee annually reviews and evaluates base salary and bonuses for all executive officers, and in conducting such reviews places primary consideration upon the recommendations by the Chief Executive Officer, along with the rationale for such recommendations, with the exception of the compensation review of the Chief Executive Officer himself. The Chief Executive Officer does not participate in the compensation committee's review or decision as to his compensation package. In establishing individual compensation levels, the compensation committee considers the Company's overall strategic objectives and performance, the Company's stock performance, peer group comparisons and individual performance. No formula is used to determine an executive's salary. The Company's overall performance and the achievement of financial and business objectives are considered.

*Management's Role in the Compensation-Setting Process.* Management, including named executive officers, plays some role in the compensation-setting process. The most significant aspects of management's role are: (1) evaluating employee performance, (2) assisting in establishing performance targets and objectives, and (3) recommending salary levels and equity awards. The Chief Executive Officer works with the compensation committee in establishing the agenda for compensation committee meetings. Management also prepares meeting information for each compensation committee meeting.

*Use of Compensation Consultants.* The compensation committee has in the past engaged compensation consultants to conduct a review and analysis of how the Company's compensation practices compare with its peer group of companies, including during 2006 and 2007.

#### *Nominating and Governance Committee*

The nominating and governance committee operates pursuant to a written charter that is available on our website at <http://www.dexcom.com>. The nominating and governance committee makes recommendations to our Board of Directors concerning candidates for election to our Board of Directors and other corporate governance matters.

The nominating and governance committee considers nominees recommended by directors, officers, employees, stockholders and others using the same criteria to evaluate all candidates. The nominating and governance committee reviews each candidate's qualifications, including whether a candidate possesses any of the specific qualities and skills desirable in certain members of the Board. Evaluations of candidates generally involve a review of background materials, internal discussions and interviews with selected candidates as appropriate. Upon selection of a qualified candidate, the nominating and governance committee recommends the candidate for consideration by the full Board. The nominating and governance committee may engage consultants or third-party search firms to assist in identifying and evaluating potential nominees, but has not done so to date.

Nominees for the Board should be committed to enhancing long-term stockholder value and must possess a high level of personal and professional ethics, sound business judgment and integrity. The Board's policy is to encourage selection of directors who will contribute to the company's overall corporate goals: responsibility to its stockholders, technology leadership in diabetes care, effective execution, high customer satisfaction and superior employee working environment. The nominating and governance committee may from time to time review the appropriate skills and characteristics required of Board members, including such factors as personal skills, diversity and professional experience in diabetes care, medical technology, finance, marketing, international business, financial reporting and other areas that are expected to contribute to an effective Board. In evaluating potential candidates for the Board, the nominating and governance committee considers these factors in the light of the specific needs of the Board at that time. Board members are expected to prepare for, attend and participate in meetings of the Board and committees on which they serve, and are strongly encouraged to attend the company's annual meetings of stockholders.

The nominating and governance committee will consider director candidates recommended by stockholders. The nominating and governance committee does not intend to alter the manner in which it evaluates candidates, including the minimum criteria set forth above, based on whether or not the candidate was recommended by a stockholder or not. Stockholders who wish to recommend individuals for consideration by the nominating and governance committee to become nominees for election to the Board at an annual meeting of stockholders must do so in accordance with the procedures set forth in "When are stockholder proposals due for next year's annual meeting?" on page three of this proxy statement. Each submission must set forth: the name and address of the stockholder on whose behalf the submission is made; the number of our shares that are owned beneficially by such stockholder as of the date of the submission; the full name of the proposed candidate; a description of the proposed candidate's business experience for at least the previous five years; complete biographical information for the proposed candidate; and a description of the proposed candidate's qualifications as a director. To date, the nominating and governance committee has not received a director nominee from a stockholder or stockholders holding more than five percent of our voting stock.

#### **Meetings of the Board of Directors and Board and Committee Member Attendance**

Our Board of Directors met five times during the last fiscal year. Each Board member attended 75% or more of the aggregate of the meetings of the Board and of the committees on which he served, held during the period for which he was a director or committee member, respectively, except Kim Blickenstaff who attended three of five meetings.

We encourage all of our directors and nominees for director to attend our annual meeting of stockholders. Directors who attended our 2006 annual meeting of stockholders on May 15, 2006 included Andrew Rasdal, Terrance Gregg, Donald A. Lucas and Donald L. Lucas.

#### **Compensation Committee Interlocks and Insider Participation**

None of the members of our compensation committee has at any time been one of our officers or employees. None of our executive officers serves or in the past has served as a member of the Board of Directors or compensation committee of any entity that has one or more of its executive officers serving on our Board of Directors or our compensation committee.

#### **Code of Business Conduct and Ethics**

We have adopted a Code of Conduct and Ethics for Employees and Directors that applies to all of our officers, directors and employees. We have also adopted an additional written code of ethics, the Code of Conduct and Ethics for Chief Executive Officer and Senior Finance Department Personnel, for financial employees that applies to our principal executive officer, principal financial officer, principal accounting officer, controller and other employees of the finance department designated by our Chief Financial Officer. These codes are available on our website at <http://www.dexcom.com>. If we make any substantive amendments to the codes or grant any waiver from a provision of the codes to any executive officer or director, we will promptly disclose the nature of the amendment or waiver on our website, as well as via any other means then required by NASDAQ listing standards or applicable law.

#### **Stockholder Communications With The Board Of Directors**

Should stockholders wish to communicate with the Board, such correspondences should be sent to the attention of the Company's Secretary, at 5555 Oberlin Drive, San Diego, California 92121. Our Secretary will forward the communication to the other Board members.

**DIRECTOR COMPENSATION****Director Compensation Table**

The following table provides information for 2006 regarding all compensation awarded to, earned by or paid to each person who served as a director for some portion or all of 2006. Other than as set forth in the table and the narrative that follows it, to date we have not paid any fees to or reimbursed any expenses of our directors, made any equity or non-equity awards to directors, or paid any other compensation to directors.

| Name                | Fees Earned or Paid in Cash(2) | Option Awards(3) | Non-Equity Incentive Plan Compensation | All Other Compensation | Total      |
|---------------------|--------------------------------|------------------|--|------------------------|------------|
| Brent Ahrens(1)     | \$ 4,500                       | \$ 135,864       |  |                        | \$ 140,364 |
| Kim Blickenstaff    | 26,000                         | 103,396          |  |                        | 129,396    |
| Sean Carney         | 45,866                         | 102,146          |  |                        | 148,012    |
| Terrance Gregg      | 28,833                         | 110,541          |  |                        | 139,374    |
| Donald A. Lucas(4)  | 40,836                         | 102,146          |  |                        | 142,982    |
| Donald L. Lucas     | 72,250                         | 141,992          |  |                        | 214,242    |
| Glen D. Nelson      | 38,250                         | 103,290          |  |                        | 141,540    |
| Andrew P. Rasdal(5) |                                |                  |  |                        |            |
| Jay S. Skyler       | 31,953                         | 103,426          |  |                        | 135,379    |

- (1) Mr. Ahrens did not stand for re-election at our 2006 annual meeting of stockholders on May 15, 2006.
- (2) Our non-employee directors, at their discretion, can elect to be paid in stock in lieu of cash for retainer and meeting fees.
- (3) These amounts reflect the dollar amount recognized for financial statement reporting purposes for the year ended December 31, 2006 in accordance with FAS 123(R), with the exception that estimated forfeitures related to service-based vesting were disregarded in these amounts, for awards pursuant to our 2005 Equity Incentive Plan. Assumptions used in the calculation of this amount for years ended December 31, 2004, 2005 and 2006 are included in footnote one to our audited financial statements for the year ended December 31, 2006 included in our annual report on Form 10-K filed with the Securities and Exchange Commission on February 28, 2007. The grant date fair value of options granted during 2006 to Messrs. Blickenstaff, Carney, Donald. A. Lucas, Nelson and Skyler is \$231,813. The grant date fair value of options granted to Mr. Ahrens is \$111,852. The grant date fair value of options granted to Mr. Gregg is \$230,446. The grant date fair value of options granted to Mr. Donald L. Lucas is \$287,739. As of December 31, 2006, Mr. Blickenstaff had options outstanding for 107,500 shares, Mr. Carney had options outstanding for 45,000 shares, Mr. Gregg had options outstanding for 45,000 shares, Mr. Donald A. Lucas had options outstanding for 45,000 shares, Mr. Donald L. Lucas had options outstanding for 62,500 shares, Dr. Nelson had options outstanding for 60,886 shares, Mr. Rasdal had options outstanding for 1,036,000 shares, none of which were received as compensation as a director, and Dr. Skyler had options outstanding for 45,000 shares.
- (4) All board compensation received by Mr. Lucas is subsequently delivered to RWI Ventures.
- (5) Mr. Rasdal receives no compensation as a director.

**Cash Compensation Paid to Directors.** During 2006, each of our non-employee directors received an annual retainer of \$20,000. In addition, each non-employee director received \$1,750 per meeting and \$1,250 per telephone meeting of the Board and committees on which they serve, and each committee chair received an additional \$1,750 per meeting and \$1,250 per telephone meeting of their respective committees. The Chairman of the Board, the Chairman of the audit committee, the Chairman of the





compensation committee and the Chairman of the nominating and governance committee also received additional annual retainers of \$20,000, \$15,000, \$5,000 and \$5,000, respectively. Our non-employee directors, at their discretion, can elect to be paid in stock in lieu of cash for retainer and meeting fees. All of our directors, including our non-employee directors, are reimbursed for their reasonable expenses in attending Board of Directors and Board of Directors committee meetings. As of March 15, 2007, each of our non-employee directors will receive an annual retainer of \$30,000. Payment to non-employee directors for attending Board or committee meetings and telephone meetings was eliminated. The Chairman of the Board, the Chairman of the audit committee, the Chairman of the compensation committee and the Chairman of the nominating and governance committee will also receive additional annual retainers of \$10,000, \$20,000, \$15,000 and \$10,000, respectively. Directors shall be paid at least 50% of the annual retainer in shares of stock, and may elect to be paid up to 100% of the annual retainer in shares of stock.

**Equity Awards Granted to Directors.** Each of our directors receives an initial stock option grant of 25,000 shares of our common stock upon joining our Board of Directors. The shares subject to the option vest monthly over a three-year period from the date of grant. Currently, on the date of our annual meeting, our directors will receive an additional stock option grant of 20,000 shares of our common stock that will vest monthly over a three-year period from the date of grant. Proposal Two of this Proxy Statement requests stockholder approval to provide the Board of Directors with discretion to determine the method used in granting equity awards to our non-employee directors from time to time. If approved, we intend to provide the following equity-based compensation to our non-employee directors: (i) we intend to grant a number of options annually to non-employee directors, other than the Chairman of the Board, with a Black-Scholes value of \$125,000, rather than 20,000 options per year, which option grant is to vest in equal monthly installments over twelve months; (ii) we intend to grant a number of options annually to the Chairman of the Board with a Black-Scholes value of \$150,000, rather than 25,000 options per year, which option grant is to vest in equal monthly installments over twelve months; and (iii) we intend to grant a number of options to an incoming non-employee director with a Black-Scholes value of \$300,000, rather than an initial grant of 25,000 options, which option grant is to vest in equal monthly installments over thirty-six months.

## PROPOSAL 2

### APPROVAL OF AMENDMENT TO THE 2005 EQUITY INCENTIVE PLAN

The Board of Directors approved the adoption of the 2005 Equity Incentive Plan (the 2005 Plan ) in January 2005 and our stockholders approved it in March 2005. It was subsequently amended by our Board and stockholders effective on May 15, 2006.

The Board believes it is important to the continued success of DexCom that we adequately compensate non-employee directors in order to attract and retain highly qualified board members.

Stockholders are being asked to approve amendments to our 2005 Equity Incentive Plan that will provide discretion to the Board of Directors to determine the value and number of equity awards granted to non-employee directors from time to time. The 2005 Plan, as proposed to be amended, is attached hereto as Annex A. If approved, we intend to provide the following equity-based compensation to our non-employee directors: (i) we intend to grant a number of options annually to non-employee directors, other than the Chairman of the Board, with a Black-Scholes value of \$125,000, rather than 20,000 options per year, which option grant is to vest in equal monthly installments over twelve months; (ii) we intend to grant a number of options annually to the Chairman of the Board with a Black-Scholes value of \$150,000, rather than 25,000 options per year, which option grant is to vest in equal monthly installments over twelve months; and (iii) we intend to grant a number of options to an incoming non-employee director with a Black-Scholes value of \$300,000, rather than an initial grant of 25,000 options, which option grant is to vest in equal monthly installments over thirty-six months. The board approved this amendment on March 15, 2007.

#### 2005 Equity Incentive Plan

**Background.** The 2005 Plan became effective on the date of our initial public offering and will terminate on April 19, 2015, unless terminated earlier by our Board of Directors. The plan authorizes the award of stock options, restricted stock awards, stock appreciation rights, restricted stock units and stock bonuses.

**Administration.** Our 2005 Plan is administered by the compensation committee of our Board of Directors, each member of which is an outside director as defined under Section 162(m) of the Internal Revenue Code. Our compensation committee has the authority to interpret this plan and any agreement entered into under the plan, grant awards and make all other determinations for the administration of the plan. Our compensation committee may at any time reprice or exchange stock options or stock appreciation rights, but not other types of awards without prior stockholder approval, provided that the terms of any repricing satisfy the requirements of Section 409A of the U.S. Internal Revenue Code and any other applicable legal requirements.

**Eligibility.** Our employees, consultants and directors are eligible to receive awards under the 2005 Plan. As of the record date, there were approximately 259 employees and 7 non-employee directors who would be eligible to participate in the 2005 Plan. Our compensation committee determines which of our employees, consultants and directors will be granted awards. No employee or consultant is entitled to participate in the 2005 Plan as a matter of right nor does any such participation constitute assurance of continued employment. Only those employees, directors (apart from our non-employee directors) and consultants who are selected to receive grants by our compensation committee may participate in the 2005 Plan.

**Discretionary Stock Option Awards.** With respect to stock options, our 2005 Plan provides for the grant of both incentive stock options that qualify for favorable tax treatment under Section 422 of the Internal Revenue Code for their recipients and nonqualified stock options. Incentive stock options may be

granted only to our employees or employees of any of our subsidiaries. Initially, no more than 3,000,000 shares may be issued pursuant to the exercise of incentive stock options under the 2005 Plan, which number of shares is subject to automatic annual increases as described below. Nonqualified stock options, and all awards other than incentive stock options, may be granted to our employees, officers, directors, consultants, independent contractors and advisors and those of any of our subsidiaries. The exercise price of incentive stock options must be at least equal to the fair market value of our common stock on the date of grant. The exercise price of incentive stock options granted to 10% stockholders must be at least equal to 110% of the fair market value of our common stock on the date of grant. Nonqualified stock options and restricted stock generally will, but need not, be granted with an exercise price at least equal to the fair market value of our common stock on the date of grant. The maximum permitted term for stock options granted under our 2005 Plan is ten years.

**Automatic Grants to Non-Employee Directors.** Currently, our non-employee directors are eligible for the grant of awards under the 2005 Plan. To simplify administration with respect to their compensation the 2005 Plan provides for automatic grants of stock options to our non-employee directors. Automatic stock option grants currently occur as follows:

- An option to purchase 25,000 shares is granted to a non-employee director on first becoming a member of our Board.
- An option to purchase 20,000 shares (previously 10,000 shares) is granted to a non-employee director on each anniversary of first becoming a non-employee director except that automatic grants made to non-employee directors on the board on the date of our initial public offering shall occur on April 13 of each year.
- An option to purchase 12,500 shares is granted to a non-employee director on first being appointed to serve as Chairman of our Board and while in service as Chairman of our Board an additional option to purchase 5,000 shares will be granted on each anniversary of the date of appointment except that automatic grants made to the non-employee director who was our Chairman of the Board on the date of our initial public offering shall occur on April 13 of each year.

Each of these automatic stock option grants has an exercise price per share equal to the fair market value of a share on the date of grant, a 3-year vesting schedule, and a term of 10 years (subject to earlier termination on ceasing to be a director or a consultant to us). Vesting is accelerated in full immediately prior to a Corporate Transaction (see the description under Adjustments Upon Changes in Capitalization ).

Stockholders are being asked to approve amendments to our 2005 Plan that will provide discretion to the Board of Directors to determine the value and number of equity awards granted to non-employee directors from time to time. Assuming approval of Proposal 2, we intend to provide the following equity-based compensation to our non-employee directors:

- an option to purchase a number of shares equal to \$300,000, using a Black-Scholes valuation, at the time a non-employee director first becomes a member of our Board. If this option had been granted on April 4, 2007, when the closing price of our stock was \$7.66, the number of shares would have been 72,816.
- an option to purchase a number of shares equal to \$125,000 (previously 20,000 shares), using a Black-Scholes valuation, on each anniversary of first becoming a non-employee director to each non-employee director other than the Chairman of the Board. If this option had been granted on April 4, 2007, when the closing price of our stock was \$7.66, the number of shares would have been 30,340.

- with respect to the Chairman of the Board, an option to purchase a number of shares equal to \$150,000 (previously 25,000 shares), using a Black-Scholes valuation, on each anniversary of first becoming Chairman of the Board. If this option had been granted on April 4, 2007, when the closing price of our stock was \$7.66, the number of shares would have been 36,408.

The automatic stock option grant at the time a non-employee director first becomes a member of our Board has an exercise price per share equal to the fair market value of a share on the date of grant, a 36-month vesting schedule, and a term of 10 years (subject to earlier termination on ceasing to be a director or a consultant to us). Each annual automatic stock option grant has an exercise price per share equal to the fair market value of a share on the date of grant, a 12-month vesting schedule, and a term of 10 years (subject to earlier termination on ceasing to be a director or a consultant to us). In all cases, vesting is accelerated in full immediately prior to a Corporate Transaction (see the description under Adjustments Upon Changes in Capitalization ).

**Restricted Stock Awards.** A restricted stock award is an offer by us to sell shares of our common stock subject to restrictions. The price of a restricted stock award will be determined by the compensation committee. Unless otherwise determined by the compensation committee at the time of award, vesting ceases on the date the participant no longer provides services to us and unvested shares are forfeited to us.

**Stock Bonuses.** Stock bonuses are granted as additional compensation for performance, and therefore, are not issued in exchange for cash.

**Stock Appreciation Rights.** Stock appreciation rights provide for a payment, or payments, in cash or shares of common stock, to the holder based upon the difference between the fair market value of our common stock on the date of exercise over the stated exercise price up to a maximum amount of cash or number of shares. Stock appreciation rights may vest based on time or achievement of performance conditions.

**Restricted Stock Units.** Restricted stock units represent the right to receive shares of our common stock at a specified date in the future, subject to forfeiture of such right due to termination of employment or failure to achieve certain performance conditions. If the restricted stock unit has not been forfeited, then on the date specified in the restricted stock unit agreement, we will deliver to the holder of the restricted stock unit whole shares of our common stock, cash or a combination of our common stock and cash.

**Transferability of Awards.** Awards granted under the 2005 plan generally may not be transferred in any manner other than by will or by the laws of descent and distribution. Our compensation committee, however, may permit nonqualified stock options to be transferred by domestic relations order or, in limited circumstances, by gift.

**Shares Subject to the 2005 Plan.** As of December 31, 2006, there were options to purchase 3,990,848 shares of our common stock outstanding under the 2005 Plan and 2,059,657 shares reserved for future issuance. The number of shares is increased by any shares that are forfeited or no longer issuable under stock options still outstanding under our now-terminated 1999 Stock Option Plan. In addition, under the terms of our 2005 Plan, the number of shares of our common stock reserved for grant and issuance under the plan increases automatically on January 1 of each of the years starting from 2006 through 2015 by an amount equal to the lesser of 3% of our total issued and outstanding shares as of the immediately preceding December 31st or the number of shares determined by our Board of Directors. Our Board of Directors or compensation committee may reduce the amount of any increase in any particular year. In 2007, the automatic increase equaled 3%, or 844,910 shares. As of March 31, 2007, we had a total of 259 employees who are eligible to participate in the 2005 Plan. The closing price of our stock on April 4, 2007 was \$7.66.

Shares available for grant and issuance under our 2005 Plan include:

- shares of our common stock issuable upon exercise of an option or stock appreciation right granted under this plan that is terminated or cancelled before the option or stock appreciation right is exercised;
- shares of our common stock subject to awards granted but forfeited or repurchased by us at the original issue price; and
- shares of our common stock subject to awards granted under this plan that otherwise terminate without shares being issued.

During any calendar year, no person will be eligible to receive more than 500,000 shares, or, in the case of new employees during their first fiscal year of employment, 1,000,000 shares under our 2005 Plan.

**Adjustments Upon Changes in Capitalization.** In the event of any dividend, stock split, combination or exchange of shares, merger, consolidation, spin-off, recapitalization or other distribution (other than normal cash dividends) of assets to our stockholders or any other change affecting our common stock, our compensation committee will make appropriate adjustments in the number and type of shares of stock subject to the 2005 Plan, the terms and conditions of any award outstanding under the 2005 Plan, and the grant or exercise price of any such award.

In the event of a Corporate Transaction, each outstanding award may be assumed or an equivalent option or right may be substituted by the successor corporation. The vesting of each outstanding award shall accelerate (in other words, become exercisable immediately in full) if the successor corporation refuses to assume the awards, or to substitute substantially equivalent awards or there is no successor corporation. Under the 2005 Plan, a Corporate Transaction is generally defined as:

- a merger or consolidation in which we are not the surviving corporation (other than a merger or consolidation with a wholly-owned subsidiary, our reincorporation in a different jurisdiction, or other transaction in which there is no substantial change in our stockholders and awards granted under the 2005 Plan are assumed or replaced by the successor corporation); or
- the sale of all or substantially all of our assets; or
- a merger or consolidation in which we are the surviving corporation but after which our stockholders immediately prior to such merger (other than any stockholder that merges, or which owns or controls another corporation that merges, with us in such merger) cease to own their shares or other equity interest in us; or
- any other transaction (including a dissolution or liquidation) which qualifies as a corporate transaction under Section 424(a) of the U.S. Internal Revenue Code wherein our stockholders give up all of their equity interest in us (except for the acquisition, sale or transfer of all or substantially all of our outstanding shares).

**Amendment and Termination of the 2005 Plan.** Our Board may suspend or terminate the 2005 Plan, or any part thereof, at any time and for any reason. Our compensation committee may also amend the 2005 Plan from time to time, except that we may not amend the 2005 Plan in any manner which would require stockholder approval to comply with any applicable laws, regulations or rules without obtaining such stockholder approval. No action by our Board of Directors, our compensation committee or our stockholders may impair the terms of any award previously granted under the 2005 Plan without the consent of the holder of such award. Unless terminated earlier, the 2005 Plan shall terminate on April 19, 2015.

**Federal Income Tax Consequences Associated with the 2005 Plan.** The following is a general summary under current law of the material federal income tax consequences to participants in the 2005



Plan. This summary deals with the general tax principles that apply and is provided only for general information. Some kinds of taxes, such as foreign, state and local income taxes, are not discussed. Tax laws are complex and subject to change and may vary depending on individual circumstances and from locality to locality. The summary does not discuss all aspects of income taxation that may be relevant in light of a holder's personal investment circumstances. This summarized tax information is not tax advice.

*Non-Qualified Stock Options ( NSOs )* For federal income tax purposes, if an optionee is granted NSOs under the 2005 Plan, the optionee will not have taxable income on the grant of the option. Generally, on exercise of NSOs the optionee will recognize ordinary income, and we will be entitled to a deduction at that time, in an amount equal to the difference between the aggregate fair market value of the shares for which each such option is exercised and the aggregate exercise price for such shares.

*Incentive Stock Options ( ISOs )* There is no taxable income to an optionee when an optionee is granted an ISO or when that option is exercised. However, the amount by which the fair market value of the shares at the time of exercise exceeds the option price will be an item of adjustment for the optionee for purposes of the alternative minimum tax. Gain realized by the optionee on the sale of an ISO is taxable at capital gains rates, and no tax deduction is available to us, unless the optionee disposes of the shares within either of: (1) two years after the date of grant of the ISO or (2) within one year of the date the shares were transferred to the optionee. If the common shares are sold or otherwise disposed of before the end of the two-year and one-year periods specified above, the difference between the option exercise price and the fair market value of the shares on the date of the option's exercise will be taxed at ordinary income rates, and we will be entitled to a deduction to the extent the optionee recognizes ordinary income. If such a sale or disposition takes place in the year in which the optionee exercises the option, the income the optionee recognizes upon sale or disposition of the shares will not directly affect whether the optionee is subject to the federal alternative minimum tax.

*Stock Appreciation Rights ( SARs )* In the case of SARs granted with an exercise price equal to the fair market value of our common stock on the date of grant, no taxable income is realized upon the receipt of the SAR, but upon exercise of the SAR, the fair market value of the shares received, determined on the date of exercise of the SAR, or the amount of cash received in lieu of shares, must be treated as compensation taxable as ordinary income to the recipient in the year of such exercise. We will be entitled to a deduction for compensation paid in the same amount which the recipient realized as ordinary income.

*Restricted Stock Awards.* A participant receiving restricted stock may be taxed in one of two ways: the participant (i) pays tax when the restrictions lapse (in other words, the shares become vested) or (ii) makes a special election to pay tax in the year the shares are issued. At either time the value of the award for tax purposes is the excess of the fair market value of the shares at that time over the amount (if any) paid for the shares. This value is taxed as ordinary income and is subject to income tax withholding. We receive a tax deduction at the same time and for the same amount taxable to the participant. If a participant elects to be taxed at grant, then, when the restrictions lapse, there will be no further tax consequences attributable to the awarded stock until the recipient sells or otherwise disposes of the stock.

*Restricted Stock Units.* In general, no taxable income is realized upon the grant of a restricted stock unit award. The participant will generally include in ordinary income the fair market value of the award of stock at the time shares of stock are delivered to the participant or at the time the restricted stock unit is otherwise settled. We generally will be entitled to a tax deduction at the time and in the amount that the participant recognizes ordinary income.

*Stock Bonus Awards.* The participant will realize ordinary income when shares are transferred to him or her unless the shares are subject to restrictions (in which case the tax treatment is as described above under Restricted Stock Awards). The amount of such income will be equal to the fair market value of such transferred shares on the date of transfer. We will be entitled to a deduction for federal income tax





purposes at the same time and in the same amount as the participant is considered to have realized ordinary income as a result of the transfer of shares.

*Section 162(m) of the Code.* In general, under Section 162(m), income tax deductions of publicly-held corporations may be limited to the extent total compensation (including base salary, annual bonus, stock option exercises and non-qualified benefits paid) for specified executive officers exceeds \$1 million (less the amount of any excess parachute payments as defined in Section 280G of the Code) in any one year. However, under Section 162(m), the deduction limit does not apply to certain performance-based compensation as provided for by the Code and established by an independent compensation committee which is adequately disclosed to, and approved by, stockholders. In particular, stock options and SARs will satisfy the performance-based compensation exception if the awards are made by a qualifying compensation committee, the underlying plan sets the maximum number of shares that can be granted to any person within a specified period and the compensation is based solely on an increase in the stock price after the grant date (in other words, the option exercise price is equal to or greater than the fair market value of the stock subject to the award on the grant date). To meet the maximum number of shares requirement, the 2005 Plan limits awards to individual participants as follows: no person may receive more than 500,000 shares issuable as awards in any calendar year, other than new employees, who may receive up to a maximum of 1,000,000 shares issuable as awards granted in the calendar year in which they first commence employment. Other awards granted under the 2005 Plan may qualify as qualified performance-based compensation for purposes of Section 162(m) if such awards are granted or vest upon any of the following types of pre-established objective performance goals:

- Net revenue and/or net revenue growth;
- Earnings per share and/or earnings per share growth;
- Earnings before income taxes and amortization and/or earnings before income taxes and amortization growth;
- Operating income and/or operating income growth;
- Net income and/or net income growth;
- Total stockholder return and/or total stockholder return growth;
- Return on equity;
- Operating cash flow return on income;
- Adjusted operating cash flow return on income;
- Economic value added;
- Individual business objectives; and
- Company-specific operational metrics.

To the extent that an award under the 2005 Plan is designated as a performance award, but is not intended to qualify as performance-based compensation under Section 162(m), the performance criteria can include the achievement of strategic objectives as determined by the compensation committee.

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Notwithstanding satisfaction of any performance criteria described above, to the extent specified at the time of grant of an award, the number of shares of common stock or other benefits granted, issued, and/or vested under an award on account of satisfaction of performance criteria may be reduced by the compensation committee on the basis of such further considerations as the compensation committee in its sole discretion determines.

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*Section 409A.* Section 409A of the U.S. Internal Revenue Code imposes certain requirements on non-qualified deferred compensation arrangements and additional taxes on non-qualified deferred compensation arrangements that do not meet such requirements. These requirements affect the timing of an individual's election to defer compensation and the timing of when changes can be made to the timing and form of distribution of the deferred compensation. Also, Section 409A generally provides that distributions must be made on or following the occurrence of certain events (i.e., the individual's separation from service, a predetermined date, or the individual's death). For certain individuals (generally, but not exclusively, our officers) Section 409A requires that such individual's distribution, when triggered by a separation from service, commence no earlier than six months after the date of such separation from service.

Certain types of awards under the 2005 Plan are automatically subject to the requirements of Section 409A. For example, restricted stock units are treated as deferred compensation subject to Section 409A. Stock options granted with an exercise price of not less than fair market value on the date of grant, and with no other feature for the deferral of compensation, are not treated as deferred compensation subject to Section 409A.

If a 2005 Plan award is subject to and fails to satisfy the requirements of Section 409A, the recipient of that award may recognize ordinary income on the amounts deferred under the award, to the extent vested, which may be prior to when the compensation is actually received. Also, if an award that is subject to Section 409A fails to comply, Section 409A imposes an additional 20% federal income tax on compensation recognized as ordinary income, as well as interest on such deferred compensation. At the time we were drafting this proposal, the Internal Revenue Service had not issued final regulations under Section 409A. Accordingly, the requirements of Section 409A may yet be enlarged or restricted in such a way as to materially affect the accuracy of this description of Section 409A's application to awards granted under the 2005 Plan.

**New Plan Benefits.** The following table shows in the aggregate, the options that will be automatically granted to non-employee directors under the 2005 Plan in 2007, assuming that all directors at the close of the 2007 Annual Meeting remain directors until the next annual meeting and that there are no new board appointees if the amendment to the 2005 Plan is approved by stockholders.

| Name and Position | Black-Scholes<br>Dollar Value (\$) | Number of Units |
|-------------------|------------------------------------|-----------------|
| Kim Blickenstaff  | \$ 125,000                         | (1)             |
| Sean Carney       | 125,000                            | (1)             |
| Terrance Gregg    | 125,000                            | (1)             |
| Donald A. Lucas   | 125,000                            | (1)             |
| Donald L. Lucas   | 150,000                            | (1)             |
| Glen Nelson       | 125,000                            | (1)             |
| Jay Skyler        | 125,000                            | (1)             |

(1) We cannot currently determine the number of shares subject to awards that will be granted in the future to non-employee directors under the 2005 Plan.

Future awards to executive officers and employees and any additional future awards to non-employee directors under the 2005 Plan are discretionary and cannot be determined at this time. We have therefore not included a table reflecting any such awards.

**THE BOARD OF DIRECTORS RECOMMENDS A VOTE *FOR* THE APPROVAL OF THE AMENDMENT TO THE 2005 EQUITY INCENTIVE PLAN.**

**PROPOSAL 3**