

March 15, 2006

Silicon Valley's Tech Revival Spurs New Fever for Cashing In Options

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Stock options are back in Silicon Valley.

For the first time in years, many Silicon Valley technology executives are seeing their stock options move into profitable territory, and they are cashing in at levels not seen since the end of the tech-stock boom in 2000. That's helping restore, for a while at least, a once-major source of wealth for the local economy and California's coffers.

In just the past two years, **Yahoo Inc.** Chief Executive Officer Terry Semel has cashed in about \$400 million in stock options. Incomes overall are up in the area. Multimillion-dollar homes are changing hands at a faster clip, real-estate agents say. And people are pouring more money into home remodeling.


In the late 1990s, stock options became a favored form of compensation among Silicon Valley companies -- relatively cheap for the companies to dole out and a potentially huge windfall for employees in a sector growing by leaps and bounds. But after the collapse of the tech-heavy Nasdaq Composite Index in 2000, many executives' stock options languished valueless. Stock options gain value only when the company's share price rises above the "strike" or "exercise" price at which the holder has the option to buy the shares (and then, ostensibly, sell them for a profit).

Now, many of the long-moribund Silicon Valley options are back in the money as tech shares have rebounded. The Nasdaq Composite Index is up around 13% since the start of 2004. Not only are executives at companies such as Yahoo, **Cisco Systems Inc.** and **Symantec Corp.** working through a big overhang of options held since the boom days; newer stock options also are starting to vest at younger companies such as **Google Inc.**

According to an analysis for The Wall Street Journal by compensation-research firm Equilar Inc., the named executive officers at Silicon Valley's 150 biggest public companies by revenue cashed in \$1.55 billion of options in their fiscal 2004, the most recent year for which comprehensive data are available. That was up 50% from 2003 and up 177% from 2002. It's the highest value of options cashed in since 2000, when Silicon Valley executives sold \$3.6 billion in stock options.

Repriced options are probably contributing to the trend. As tech stocks plunged, many tech companies repriced their options to maintain the viability of equity compensation. Equilar estimates that roughly one-third of Silicon Valley's 150 biggest companies repriced options

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between 1997 and 2005.

Tech executives are also cashing in a bigger proportion of their vested options, suggesting many want to take profits while they can. In their fiscal 2004, top Silicon Valley executives exercised 32.7% of their total vested options, up from 22.2% in 2003, according to Equilar. The 2004 level hadn't been seen since fiscal 2000, when tech executives sold 47.1% of their vested options.



But the cash-ins don't necessarily suggest a lack of faith in the sector's performance. Charles Wolf, a technology analyst at Needham & Co., says the resurgence in stock-option sales simply reflects the overhang built up in recent years. "With sales now, it's not a signal that tech companies are about to fall apart," he says. "Executives want to diversify away from having their money being tied up in one asset."

The options revival so far isn't coaxing more start-ups to go public; young companies these days are required to meet much higher hurdles in terms of profitability and other measures before completing an initial public offering. Likewise, new accounting rules are damping the incentive to continue using compensation programs that include stock options.

For now, though, the trend has broad implications for the Silicon Valley economy, which depends heavily on the tech industry. Stock-option proceeds are adding to

income at many households in the area, economists say, driving consumer spending and potentially spurring the creation of new jobs. The region's real per capita income rose to \$53,633 last year from \$49,724 in 2003, according to a study by Joint Venture Silicon Valley, a nonprofit group representing businesses and government agencies in the area.

In addition, stock-option exercises will help juice government coffers. Recent data from the California Department of Finance show that tax revenue from stock-option proceeds climbed to \$3.2 billion last year from \$2 billion in 2002. While that is short of the \$7.1 billion the state reaped at the peak of the tech boom in 2000, California's revenue from options sales is projected to rise further this year, to \$3.4 billion.

Economists say people are putting their options profits into such areas as new investments and home improvements. The Construction Industry Research Board, a nonprofit construction-research firm, calculates that residents in Silicon Valley's Santa Clara County spent \$416 million last year on home remodeling, compared with \$331 million in 2001.

Catherine Marcus, a real-estate agent in Menlo Park, Calif., says homes priced from \$2.5 million to \$7 million are selling briskly, partly driven by buyers using stock-option profits. "It's the stock-option people...that are buying," Ms. Marcus says.

Such ripple effects may continue for the next few years: Many of the options granted during the boom are set to expire soon, which means executives must exercise them or lose the chance to profit. "So many stock-option grants were made at the peak of the market that we'll be working

our way through these sales for some time," says Patrick McGurn, an executive vice president at proxy advisory firm Institutional Shareholder Services.

Yahoo is one company where executives recently realized a hefty hunk of stock options. Named executive officers at the Sunnyvale, Calif., Internet company exercised \$338 million in stock options in 2004 and \$296 million last year, according to the company and to public filings. Those numbers compare with \$89 million in 2003. Yahoo's stock has risen about 40% since early 2004.

Mr. Semel, the chief executive, exercised \$173 million in stock options last year and \$229 million in 2004, compared with \$25.4 million in 2003, according to the company and public filings. According to Equilar, Mr. Semel's 2004 options sales represented 36.5% of the total number of vested options he would have held at year end had he not exercised them, up from 11.3% in 2003. Equilar didn't analyze 2005 figures because Yahoo's proxy for last year isn't out yet. A Yahoo spokeswoman says the stock-options sales are "a standard part of the executives' portfolio diversification."

Symantec CEO John Thompson pulled in \$69 million from stock options in the year ended March 31, 2005, more than three times the \$21.1 million he hauled in the prior fiscal year. During those two years, the share price of the Cupertino, Calif., security-software maker rose 118%. (The shares have since traded down.)

In total, Mr. Thompson took slightly more than a third of his stock options off the table that would have been available for the fiscal year ended March 2005, up from 18.4% in the prior fiscal year, according to Equilar.

A Symantec spokeswoman says the value of Mr. Thompson's stock options benefited from stock splits and share appreciation. She adds that the CEO's options sales took place under a 10b5-1 plan that started in July 2002 and expired in December 2004. Under such a plan, executives sell stock at preset times regardless of valuation.

Cisco CEO John Chambers reaped \$61.2 million from options sales in the year ended July 2005, up from \$38.3 million in the prior fiscal year. In total, the options Mr. Chambers sold last fiscal year represented 13.4% of his total available for the year, up from 6.2% a year earlier. Mr. Chambers sold none of his options in fiscal 2003, 2002 and 2001 as the San Jose, Calif., networking company's stock nose-dived.

A Cisco spokeswoman says Mr. Chambers began to sell more options after he adopted a 10b5-1 stock plan in August 2004 "on the recommendation of his financial advisers, as part of his individual long-term strategy for gradual asset diversification and liquidity." She adds that Mr. Chambers adopted the plan also because many of his options were set to expire between 2004 and 2008.

While **eBay** Inc. CEO Meg Whitman hasn't cashed in any stock options during the past five years, her colleagues have. eBay executives other than the CEO reaped \$98.3 million in 2004, according to company filings. In 2003, the total was \$46.8 million. The San Jose-based Internet auctioneer's stock is up around 20% since the beginning of 2004. An eBay spokesman declined to comment.

Stock-option exercises are up even as stock options are being used less as compensation. Because of new accounting rules that require companies to tally stock-option grants as an expense on their balance sheets, many tech companies have shifted from options to issuing restricted shares.

Microsoft Corp., for instance, stopped issuing stock options in 2003 and switched to giving out restricted stock.

Overall, the median burn rate at Silicon Valley's top 150 companies -- the percentage of a company's shares outstanding that are being given away in stock-option grants -- is down. In fiscal 2004, the rate fell to 3.4% from 4.5% two years earlier, Equilar says.

With the popularity of stock options fading, economists say California and other states must be wary of becoming overreliant on tax revenue from stock-option profits. "When this revenue goes away, it goes away fast and completely," says Nicholas Jenny, a senior policy analyst at the Nelson A. Rockefeller Institute of Government, a public research group in Albany, N.Y. "California experienced the downside of this in 2001, and needs to watch how much of this revenue is real and sustainable this time."

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