

Peering into a Company's Equity Structure

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www.chaffe-associates.com

www.valrexmodel.com

What is an Equityholder?

- n Anyone who has an equity stake in a company, including the following:
 - Stockholders
 - Optionholders
 - Any other party that has a claim to the company's equity

What is a Company's Total Equity Value (TEV)?

- n The fair market value of a company's long term capital, excluding debt.
- n The sum of the fair market values of all of the outstanding shares of stock, options and other equity instruments.

Total Equity Value

Simple Equity Structure

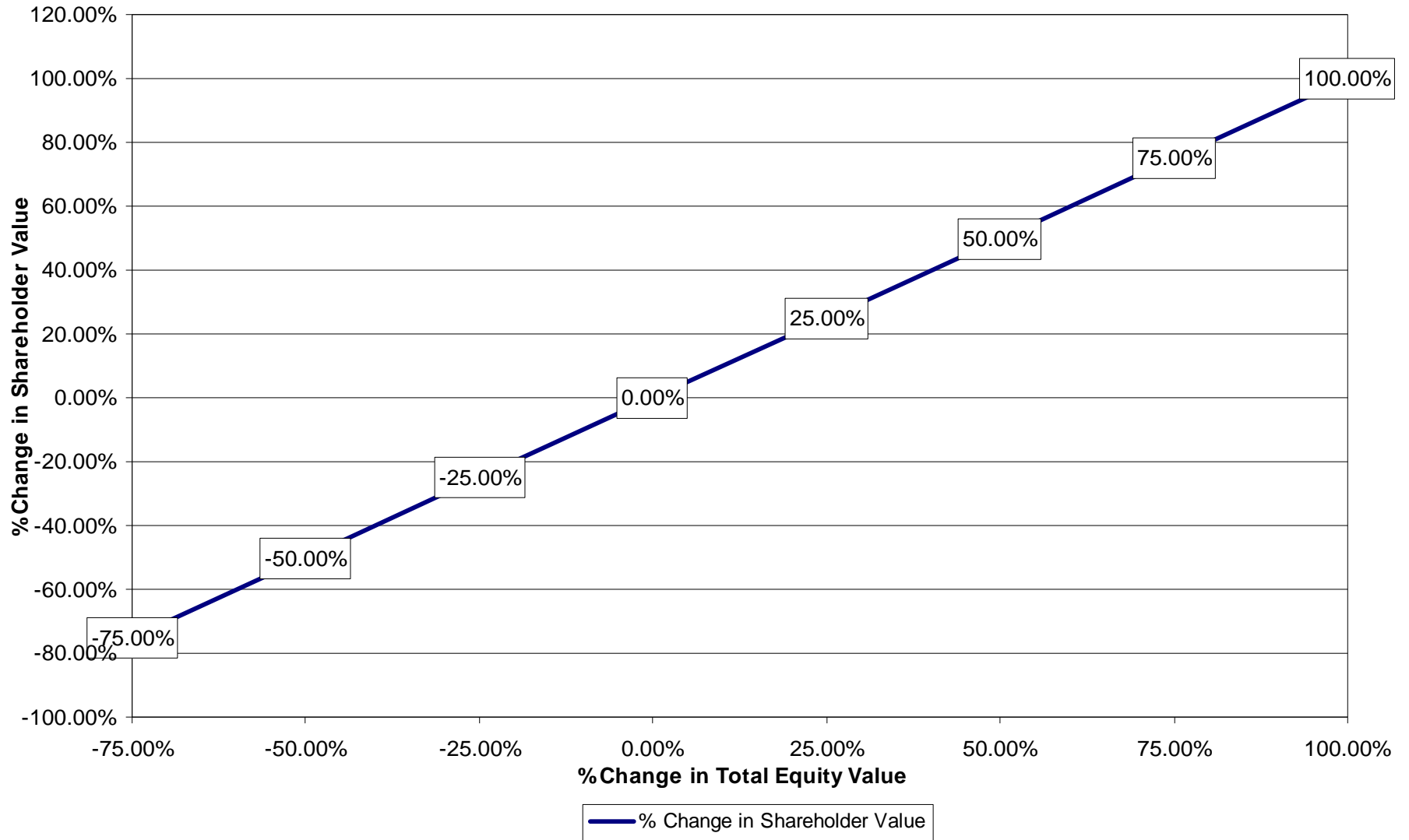
For companies with one class of stock and no outstanding options:

$$\text{Total Equity Value} = \text{Stock Price} \times \text{Shares Outstanding}$$

Example:

\$10 stock price x 100,000,000 shares outstanding =
\$1 billion Total Equity Value

Simple Capital Structure



Option Valuation Methodology

The Valrex Model

Valrex values a non-traded option by stripping away a traded option's liquidity value.

Elements of a Traded Option's Value

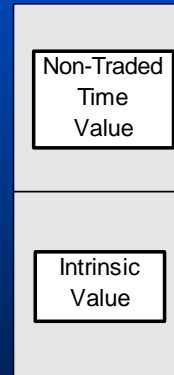
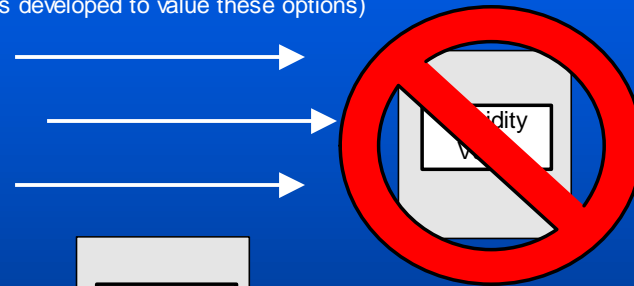
(Black-Scholes and Binomial models were developed to value these options)



$$\begin{array}{r}
 \text{Liquidity Value (1)} \\
 \text{Non-Traded Time Value (2)} \\
 + \text{ Intrinsic Value (3)} \\
 \hline
 \text{Traded Option Value}
 \end{array}$$

Elements of a Non-Traded Option's Value

(The Valrex model was developed to value these options)



$$\begin{array}{r}
 \text{Non-Traded Time Value (2)} \\
 + \text{ Intrinsic Value (3)} \\
 \hline
 \text{Valrex Value}
 \end{array}$$

- (1) Liquidity Value is measured by calculating the cost to hedge against the risk of loss in the option by using a put-on-call option formula.
 - (2) Non-Traded Time Value is the time value not attributable to the liquidity of an option.
 - (3) Intrinsic value for a call option is the difference between the current fair market value of the stock and the exercise price of the option.
- For more information on the Valrex model see www.valrexmodel.com.

Total Equity Value

Complex Equity Structure

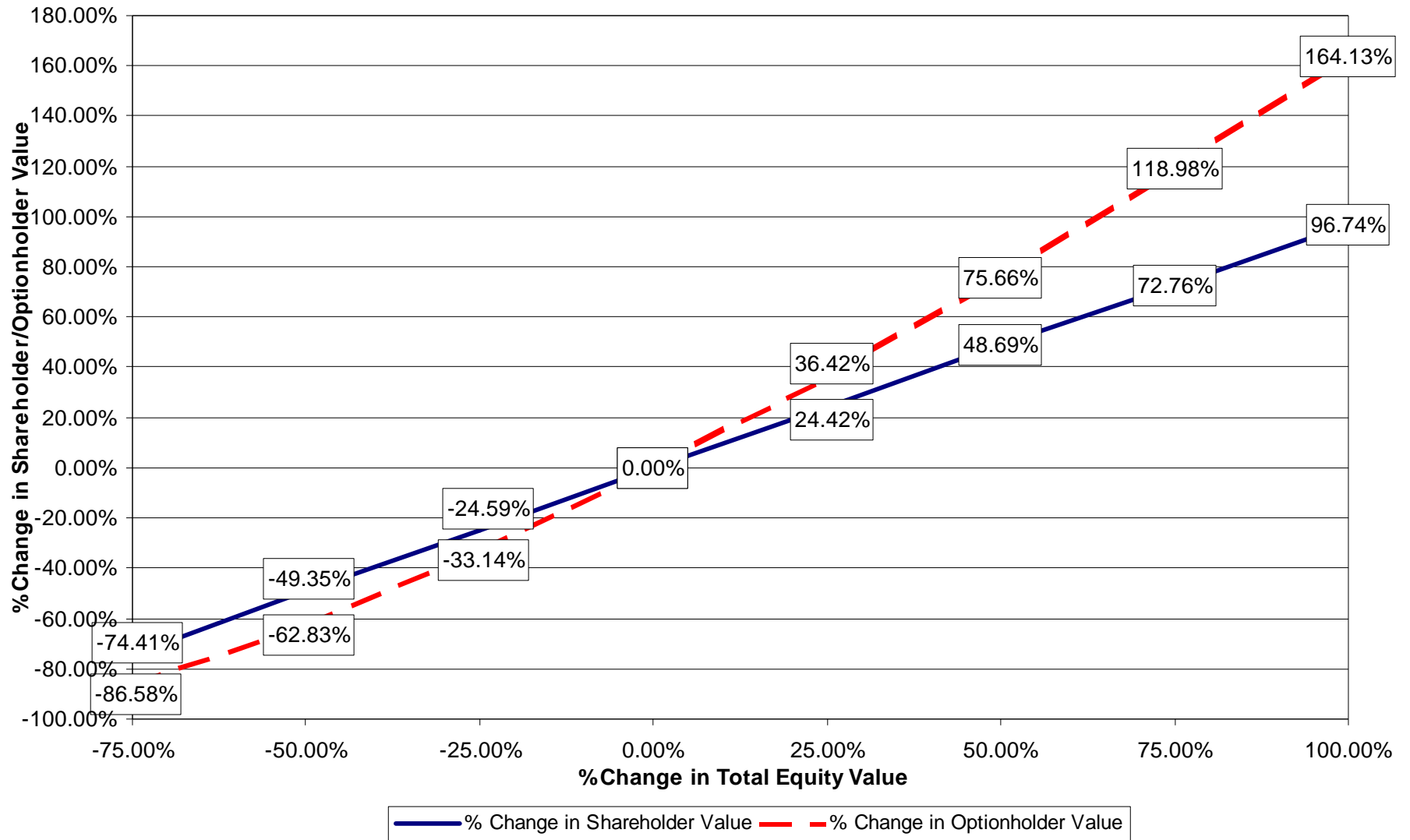
Verisign Inc

Valuation Date 3/31/02

Total Equity Capitalization

	Share Price		Shares Outstanding	=	Total	% of Total	
Shareholder Value	27.00	x	237,944,676	=	\$6,424,506,252	95.16%	
	Option Value		# of Options				Weighted Avg. Strike
Option Tranche 1	25.56	x	2,249,705	=	57,508,549	0.85%	1.65
Option Tranche 2	20.42	x	3,361,287	=	68,646,097	1.02%	7.21
Option Tranche 3	14.74	x	1,630,787	=	24,032,865	0.36%	12.90
Option Tranche 4	8.75	x	2,311,950	=	20,227,579	0.30%	27.16
Option Tranche 5	6.92	x	12,861,087	=	88,944,748	1.32%	34.84
Option Tranche 6	6.11	x	3,374,867	=	20,625,227	0.31%	43.65
Option Tranche 7	5.19	x	5,496,933	=	28,530,069	0.42%	68.75
Option Tranche 8	2.04	x	3,046,664	=	6,203,444	0.09%	126.95
Option Tranche 9	3.22	x	2,942,167	=	9,468,144	0.14%	160.77
Option Tranche 10	2.36	x	65,060	=	153,694	0.00%	237.81
ESPP Grants	5.74	x	433,524	=	2,487,495	0.04%	22.95
Total Option Value					326,827,911	4.84%	
Total Equity Value					\$6,751,334,163	100.00%	

Verisign, Inc. No New Grants



Factors That Change TEV Allocation

- n A change in the company's aggregate TEV
- n The grant of new options.
- n An option repricing or other transaction that involves changing the characteristics of outstanding options.
- n The company's issuance of new stock or the purchase of outstanding shares for the treasury.
- n A change in the company's dividend policy.
- n A change in the treasury yield curve.
- n A change in the company's stock price volatility.
- n The forfeiture of options.
- n The exercise of options.
- n The passage of time.

Verisign, Inc.

Potential Equity Structures

% Change in Total Equity Value	Total Equity Value	Total Optionholder Value	Total Shareholder Value	% Change in Optionholder Value	% Change in Shareholder Value	Valrex Overhang
-75.00%	1,688	44	1,644	-86.58%	-74.41%	2.60%
-50.00%	3,376	121	3,254	-62.83%	-49.35%	3.60%
-25.00%	5,064	219	4,845	-33.14%	-24.59%	4.32%
0.00%	6,751	327	6,425	0.00%	0.00%	4.84%
25.00%	8,439	446	7,993	36.42%	24.42%	5.28%
50.00%	10,127	574	9,553	75.66%	48.69%	5.67%
75.00%	11,815	716	11,099	118.98%	72.76%	6.06%
100.00%	13,503	863	12,639	164.13%	96.74%	6.39%

Verisign, Inc.

Effect of a New Option Grant

- n Issue 2,379,447 (a run rate of 1%) new at-the-money options with a total value of \$22 million.
- n Initial Result: Valrex Overhang increases from 4.84% to 5.15%.
- n Longer run result: the equity sharing structure changes.

Effect of a New Option Grant

Verisign Inc

Valuation Date	3/31/02
% Change in TEV	0.00%
Run Rate	1.00%
Term of New Grants	7.00

	Share Price		Shares Outstanding	=	Post-Grant Total	% of Total	Pre-Grant Total	% of Total	Post-Grant % Change
Shareholder Value	26.91	x	237,944,676	=	\$6,403,801,388	94.85%	\$6,424,506,252	95.16%	-0.32%
	Option Value		# of Options						
Option Tranche 1	25.48	x	2,249,705	=	57,312,790	0.85%	57,508,549	0.85%	-0.34%
Option Tranche 2	20.34	x	3,361,287	=	68,353,613	1.01%	68,646,097	1.02%	-0.43%
Option Tranche 3	14.65	x	1,630,787	=	23,890,962	0.35%	24,032,865	0.36%	-0.59%
Option Tranche 4	8.71	x	2,311,950	=	20,139,025	0.30%	20,227,579	0.30%	-0.44%
Option Tranche 5	6.88	x	12,861,087	=	88,541,617	1.31%	88,944,748	1.32%	-0.45%
Option Tranche 6	6.08	x	3,374,867	=	20,531,544	0.30%	20,625,227	0.31%	-0.45%
Option Tranche 7	5.17	x	5,496,933	=	28,405,872	0.42%	28,530,069	0.42%	-0.44%
Option Tranche 8	2.02	x	3,046,664	=	6,165,100	0.09%	6,203,444	0.09%	-0.62%
Option Tranche 9	3.20	x	2,942,167	=	9,418,965	0.14%	9,468,144	0.14%	-0.52%
Option Tranche 10	2.35	x	65,060	=	153,010	0.00%	153,694	0.00%	-0.45%
ESPP Grants	5.69	x	433,524	=	2,466,294	0.04%	2,487,495	0.04%	-0.85%
New Option Grants	9.31	x	2,379,447	=	22,153,984	0.33%		0.00%	
Total Option Value					347,532,775	5.15%	326,827,911	4.84%	
Total					\$6,751,334,163	100.00%	\$6,751,334,163	100.00%	0.00%

Verisign, Inc.

New Grant at 1% Run Rate

% Change in Total Equity Value	Total Equity Value	Total Optionholder Value	Total Shareholder Value	% Change in Optionholder Value	% Change in Shareholder Value	Valrex Overhang
-75.00%	1,688	48	1,640	-86.32%	-74.39%	2.82%
-50.00%	3,376	130	3,246	-62.57%	-49.32%	3.85%
-25.00%	5,064	233	4,831	-33.02%	-24.56%	4.60%
0.00%	6,751	348	6,404	0.00%	0.00%	5.15%
25.00%	8,439	474	7,965	36.34%	24.38%	5.61%
50.00%	10,127	611	9,516	75.73%	48.60%	6.03%
75.00%	11,815	763	11,052	119.47%	72.59%	6.46%
100.00%	13,503	922	12,581	165.34%	96.45%	6.83%

Verisign, Inc.

Effect of a 1 for 1 Option Exchange

- n Cancel 30,098,728 underwater options and issue the same number of new at-the-money options.
- n Initial Result: Valrex Overhang increases from 4.84% to 6.30%.
- n Longer run result: the equity sharing structure changes.

Verisign, Inc.

1 for 1 Option Exchange

Verisign Inc

Valuation Date 3/31/02

Set Strike to \$27/Share and Extend Term to 7 Years

Total Capitalization

	Share Price	x	Shares Outstanding	=	Post-Exchange Total	% of Total	Pre-Exchange Total	% of Total	Post-Exchange % Change	Original Strike
Shareholder Value	26.59	x	237,944,676	=	\$6,325,960,107	93.70%	\$6,424,506,252	95.16%	-1.53%	
	Option Value		# of Options							
Option Tranche 1	25.15	x	2,249,705	=	56,576,821	0.84%	57,508,549	0.85%	-1.62%	ITM
Option Tranche 2	20.01	x	3,361,287	=	67,254,000	1.00%	68,646,097	1.02%	-2.03%	ITM
Option Tranche 3	14.32	x	1,630,787	=	23,357,465	0.35%	24,032,865	0.36%	-2.81%	ITM
Option Tranche 4	9.16	x	2,311,950	=	21,184,681	0.31%	20,227,579	0.30%	4.73%	27.16
Option Tranche 5	9.16	x	12,861,087	=	117,847,713	1.75%	88,944,748	1.32%	32.50%	34.84
Option Tranche 6	9.16	x	3,374,867	=	30,924,319	0.46%	20,625,227	0.31%	49.93%	43.65
Option Tranche 7	9.16	x	5,496,933	=	50,369,069	0.75%	28,530,069	0.42%	76.55%	68.75
Option Tranche 8	9.16	x	3,046,664	=	27,916,955	0.41%	6,203,444	0.09%	350.02%	126.95
Option Tranche 9	9.16	x	2,942,167	=	26,959,436	0.40%	9,468,144	0.14%	184.74%	160.77
Option Tranche 10	9.16	x	65,060	=	596,153	0.01%	153,694	0.00%	287.88%	237.81
ESPP Grants	5.51	x	433,524	=	2,387,443	0.04%	2,487,495	0.04%	-4.02%	
Total Option Value					425,374,056	6.30%	326,827,911	4.84%	30.15%	
Total					<u>\$6,751,334,163</u>	100.00%	<u>\$6,751,334,163</u>	100.00%	0.00%	

Verisign, Inc.

1 for 1 Option Exchange

% Change in Total Equity Value	Total Equity Value	Total Optionholder Value	Total Shareholder Value	% Change in Optionholder Value	% Change in Shareholder Value	Valrex Overhang
-75.00%	1,688	66	1,621	-84.40%	-74.37%	3.93%
-50.00%	3,376	168	3,207	-60.45%	-49.30%	4.98%
-25.00%	5,064	289	4,774	-31.98%	-24.53%	5.71%
0.00%	6,751	425	6,326	0.00%	0.00%	6.30%
25.00%	8,439	573	7,866	34.77%	24.34%	6.79%
50.00%	10,127	740	9,387	73.87%	48.39%	7.30%
75.00%	11,815	930	10,885	118.65%	72.06%	7.87%
100.00%	13,503	1,139	12,363	167.82%	95.44%	8.44%

Verisign, Inc.

Effect of an Even Value Exchange

- n Cancel 30,098,728 underwater options and issue 18,626,422 new 7 year at-the-money options (an amount that is equal in value to those cancelled).
- n Initial Result: Valrex Overhang remains constant at 4.84%.
- n Longer run result: the equity sharing structure changes slightly.

Verisign, Inc.

Even Value Exchange

Verisign Inc
Valuation Date

3/31/02

Total Capitalization

	Share Price		Shares Outstanding		Post-Exchange Total	% of Total	Pre-Exchange Total	% of Total	Post-Exchange % Change
Shareholder Value	27.00	x	237,944,676	=	\$6,424,506,252	95.16%	\$6,424,506,252	95.16%	0.00%
	Option Value		# of Options						
Option Tranche 1	25.56	x	2,249,705	=	57,508,549	0.85%	57,508,549	0.85%	0.00%
Option Tranche 2	20.42	x	3,361,287	=	68,646,097	1.02%	68,646,097	1.02%	0.00%
Option Tranche 3	14.74	x	1,630,787	=	24,032,865	0.36%	24,032,865	0.36%	0.00%
Option Tranche 4	-	x	-	=	-	0.00%	20,227,579	0.30%	
Option Tranche 5	-	x	-	=	-	0.00%	88,944,748	1.32%	
Option Tranche 6	-	x	-	=	-	0.00%	20,625,227	0.31%	
Option Tranche 7	-	x	-	=	-	0.00%	28,530,069	0.42%	
Option Tranche 8	-	x	-	=	-	0.00%	6,203,444	0.09%	
Option Tranche 9	-	x	-	=	-	0.00%	9,468,144	0.14%	
Option Tranche 10	-	x	-	=	-	0.00%	153,694	0.00%	
ESPP Grants	5.74	x	433,524	=	2,487,495	0.04%	2,487,495	0.04%	0.00%
New Options	9.35	x	18,626,422	=	174,152,905	2.58%	-	0.00%	
Total Option Value					<u>326,827,911</u>	4.84%	<u>326,827,911</u>	4.84%	0.00%
Total					<u>\$6,751,334,163</u>	100.00%	<u>\$6,751,334,163</u>	100.00%	0.00%

Verisign, Inc.

Even Value Exchange

% Change in Total Equity Value	Total Equity Value	Total Optionholder Value	Total Shareholder Value	% Change in Optionholder Value	% Change in Shareholder Value	Valrex Overhang
-75.00%	1,688	49	1,639	-85.00%	-74.49%	2.90%
-50.00%	3,376	127	3,248	-61.05%	-49.44%	3.77%
-25.00%	5,064	221	4,842	-32.25%	-24.63%	4.37%
0.00%	6,751	327	6,425	0.00%	0.00%	4.84%
25.00%	8,439	440	7,999	34.73%	24.50%	5.22%
50.00%	10,127	567	9,560	73.36%	48.81%	5.59%
75.00%	11,815	709	11,105	117.04%	72.86%	6.00%
100.00%	13,503	867	12,636	165.25%	96.68%	6.42%

Conclusion

- n An understanding of the economics of employee stock options requires an understanding of the following:
 - How the company's value is divvied up among stockholders and optionholders at the present. (Valrex overhang)
 - How certain events and transactions (e.g. option grants and exchanges) change the equity structure at the point of occurrence and beyond. (changes in the relationship between TEV and Valrex overhang)