3D ADVISORS

This 3DAdvisors Report Covers:
✓ **Insider Trading**: Insider Trading Behavior
✓ **Accounting**: Quality of Earnings Issues
✓ **Governance:** Corporate Governance Issues

Insiders Willing to Hold Fewer Shares As MSFT Looms
Symantec Corporation (NASDAQ:SYMC) Update

June 29, 2004

Contact: Bob Gabele (954) 779-3974 or bgabele@3DAdvisors.com

Symantec Corporation provides content and network security software and appliance solutions to enterprises, individuals and service providers. The Company provides client, gateway and server security solutions for virus protection, firewall and virtual private network (VPN), security management, intrusion detection, Internet content and e-mail filtering, remote management technologies and security services to enterprises and service providers worldwide. Symantec has offices in 36 countries worldwide. The Company views its business in five operating segments: enterprise security, enterprise administration, consumer products, services and other activities.

Summary of 3DAdvisors Findings for SYMC

- **Insider Trading:** Insiders willing to hold fewer shares as MSFT looms
- **Governance:** EPS-driven comp plans benefit from planned repurchases
- **Accounting:** Earnings from overseas subsidiaries not permanently invested
- **Accounting:** Goodwill treatment: stretching useful life too far?
- **Accounting:** Noteworthy miscellaneous items

Discussion of 3DAdvisors Findings

The most consistent theme, with regards to our analysis of Symantec, is that it seems that insiders are not willing to hold much of a stake in the Company and what stakes they do hold are being systematically reduced as the selling has outpaced the vesting of additional options from earlier grants. Aggressive selling in the shares became evident late last year, albeit at much lower share prices, when a number of key insiders filed 10b5-1 trading plans before reducing their holdings, some by large percentages. This selling has spread to a broader list of insiders as the shares have continued rising as demand for security software from consumers and businesses alike has remained strong in the wake of computer virus and general security concerns.

Not only has selling become the norm here, executives have also displayed certain other behaviors that suggest they'd rather be holding cash than Symantec shares. The Company's 2002 Executive Officers' Stock Purchase Plan, for instance, reserved 250,000 shares for issuance to insiders who wanted to apply a portion or all of their respective bonus payments (up to 10,000 shares per participant) towards the purchase of Symantec shares. In spite of the fact that executive bonuses have been running far in excess of base salaries since the plan's inception, as of 3/31/2004 there have been no takers and the entire 250,000 shares remain reserved.

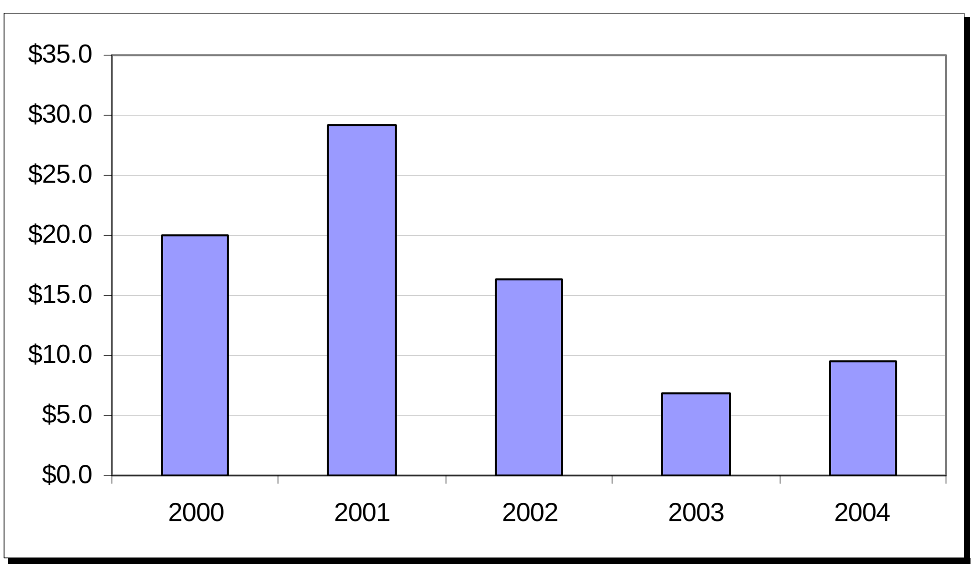
While the Stock Purchase Plan allows executives to take a portion of their bonuses in stock, executive compensation is also relying progressively less on stock option compensation and more on cash bonuses that are tied, in a large part, to EPS growth. Add to this the fact that an interesting number of executives are barely in compliance with the Company's executive ownership guidelines, which require that they hold at least 10,000 shares, and you are left to wonder why executives seem so unwilling to hold stock. With Microsoft looming as a major competitor in the market, this reluctance by Symantec insiders to hold shares isn't very reassuring for investors.

Insider Trading: Insiders willing to hold fewer shares as MSFT looms

Since last year we've been closely monitoring insider activity at Symantec. We reported in three prior reports (see SYMC reports dated 09/05/03, 12/12/03, and 01/12/04) the persistent dispersion of stock by Symantec's rank and file employees. The final tally for insider sales during 2003 was 2.27 million shares, more than they had sold during any prior year dating back to 1997. From what we've observed so far, insiders are on track to outpace last year's activity, having already sold 1.3 million shares through the first six months of 2004. Most recently nine executives and directors sold a total of 708,629 shares between March 1st and June 10th as the issue climbed from right around \$42 a share to an all-time high of \$49.35 (close on April 22nd).

Symantec insider sales, which accelerated in late 2003, have continued to the point where a growing number of executives have been selling at a much higher clip than their options (which vest monthly) are vesting, resulting in significant holdings reductions (common stock plus vested options). At the same time, new grants are

Figure 1. SYMC Annual Option Grants (Millions of $). Source: SYMC SEC Filings



also slowing as shown in Figure 1. In fact, in 2003, new options were granted to just 2 of the 5 named executives listed in the proxy. After monthly vesting, for instance, holdings for **Gail Hamilton**, Symantec's EVP, Product Delivery and Response, remain over 40% lighter than they stood late last year. Ditto for CFO **Greg Meyers**, whose holdings, even after new option vestings, are 27% lighter. The list of those reducing their positions, since the initial 10b5-1 filings of late last year, has grown with each subsequent earnings window.

- **Stephen Cullen** (age not disclosed) – Senior V.P., Security Products and Solutions. In January of 2004, Cullen was promoted to lead Symantec's Security Products and Solutions Group, making him a filing insider for the first time. We find it interesting that he wasted little time cashing out of stock following the filing of his Form 3 (Initial Statement of Ownership) in January 2004. Since his appointment he has unloaded 48,718 shares, **dropping 51% of his position**. In the process, he exercised five separate series of options, which weren't set to expire until April of 2009 at the earliest. It is somewhat uncommon to see newly promoted executives selling aggressively like this.

- **Kris Halvorsen** (52) – Director. While most of his peers were busy selling during the past year, Halvorsen refrained from any activity. Apparently he made up for lost time when he sold 30,000 shares on May 4th at $47.03, **reducing his holdings by 54%**. In order to acquire the shares to sell he exercised four series of non-expiring options (expiration dates: 9/12, 4/13, 4/17 @ 12.82, and 4/17 @ $13.14), which was the first time since joining the board in 2000 that we've ever seen him exercise more than one series at a time.

- **Donald Frischman** (61) – Senior V.P., Communications and Brand Management. Though Frischman had been a fairly consistent seller going back to 2002, he picked up his selling pace after filing a 10b5-1 plan in December. Between March 10th and June 10th, he has sold 90,000 shares, **dropping his holdings by 41%** in the process.

- **Rebecca Ranninger** (44) – Senior V.P., Human Resources. Though Ranninger has been with the Company since 1991, she has only been a Section 16 filing insider since 2000. Between 2000 and 2002, she sold just over 190,000 shares, less than the 210,143 shares she has now sold over the past year-and-a-half. Most recently she sold 49,000 shares on May 3rd between $45.40 and $47. Not only does her presence in the recent round help substantiate the convergence of execs, but she too has sold a sizeable amount of her holdings – **36% since December**.

- **John Thompson (55)** – Chairman, CEO. Thompson was the most aggressive seller in the recent round; having sold 325,000 shares on May 3rd at $46.97 a share. Since joining the Company in 1999, we've watched him sell 200,000 shares each quarter since early 2002. The recent activity was part of a newly established 10b5-1 trading plan, which probably implies similar sales will follow. After the sale, Thompson still has a sizeable ownership stake (over 3 million shares), most in the form of options.

- **John Schwarz (53)** – President, COO. As noted above, Schwarz established a 10b5-1 trading plan in December 2003. On March 1st he sold 43,000 shares at $40.95, which were not part of the trading plan. He then sold an additional 101,008 shares, this time as a 10b5-1 transaction, on May 3rd and June 7th as the stock climbed to $46.38. Schwarz reported holding a mere 3,024 shares in common stock, which leaves him below the 10,000 he is required to own. Schwarz has only a few more months to shore up his common stock holdings considering he joined the company in 2002.

Governance: EPS-driven comp plans benefit from planned repurchases

Symantec's bonus plan for key executives, put in place the same year CEO Thompson joined the company (Variable Incentive Plan) is uncapped: bonus can exceed salary if assigned, but undisclosed metrics are passed. For the past five years, Symantec CEO's bonus has been determined 50% by EPS growth and 50% by revenue growth. Others have had bonus payout tied to an even split between EPS and revenue growth plus a smaller component consisting of individual objectives. This structure paid off handsomely for Thompson in 2003 when he received a $2.1 million bonus in addition to his $750,000 salary, and no new option grants. Others from the top management group received bonuses that far exceeded salaries. The Company's justification for the compensation fell short of defining exactly what metrics allowed for bonuses to exceed salaries to such an extent: "Specific performance thresholds for each metric had to be exceeded before the portion of the bonus associated with the respective metric was paid."

Clearly, options grants have slowed for Symantec. It appears that Symantec plans to make up for the reduced options compensation through a heightened emphasis on the bonus plan. With the cutting back on its options compensation, or as Symantec puts it, its "careful management of option grants", the Company is clearly expanding the number of executives who, like Thompson in 2003, will receive cash bonuses, instead of option grants, with the bonus payments driven significantly by EPS growth.

Table 1. Authorized Participants in Variable Incentive Plan. (BU=Business Unit)
Source: SYMC SEC Filings

Fiscal 2001	Fiscal 2002	Fiscal 2003	Fiscal 2004	Fiscal 2005
President/CEO[1]	President/CEO[1]	CEO[3]	CB/CEO[3]	CB/Chief Salesman[3]
VPs (no BU)[5]	VPs (no BU)[5]	President/COO[3]	President/COO[3]	President/COO[3]
VPs (w/BU)[4]	VPs (w/BU)[4]	VPs[2]	VPs[2]	SVPs (no BU)[3]
				VP Sales[2]
				VPs (w/BU)[1]
				VPs[2]

[1] 30% of bonus tied to earnings per share
[2] 35% of bonus tied to earnings per share
[3] 50% of bonus tied to earnings per share
[4] 50% of bonus tied to revenue growth and earnings per share
[5] 75% of bonus tied to revenue growth and earnings per share

It should come as no surprise then that Symantec's plans to significantly increase the pace of its share repurchases in 2004 is behavior that immediately gets our attention. After buying back just $60 million worth of stock in 2003 and $64 million in 2002, Symantec, in January of 2004, increased its authorized share repurchase program by $240 million (to $940 million). The Company plans to buy back $240 million worth of shares in the current fiscal year, just in time to help juice the EPS components of its new executive bonus packages. It should also be noted that these planned repurchases are taking place while the stock is trading at or near all-time highs.

Accounting: Earnings from overseas subsidiaries not permanently invested

Symantec has been building a cache of unremitted earnings from foreign subsidiaries that the Company claims to keep reinvested permanently offshore. These earnings, for which no provision for U.S. taxes has been recorded, have grown from $287 million as of 3/31/2002 to $740 million as of 3/31/2004. The Company has disclosed that the unrecognized deferred tax liability related to these earnings to be at $221 million.

It seems that there is a risk that at least some of these earnings, where U.S. taxes have not been paid, may be in jeopardy of becoming repatriated. We say this because Symantec has been quietly recording deferred tax liabilities associated with some of its unremitted earnings of foreign subsidiaries and the amount has been moving up each year. The 2004 10-K reveals a deferred tax liability increase from $14 million to $51.7 million related to the unremitted earnings of foreign subsidiaries. In a first-time disclosure, the Company reveals, in a separate section of the K, that this deferred tax liability is "attributable to unremitted foreign earnings that are not intended to be indefinitely reinvested." This represents clear evidence that, in spite of company assurances, not all expatriated earnings have been indefinitely reinvested and pressure exists for providing for tax liability for earnings that have already been reported in past periods where no U.S. tax had been paid. One wonders if future planning strategies will dictate that more unremitted earnings will be brought back to the U.S. thereby generating additional tax liabilities. It is not clear why certain amounts are to be remitted while the major amounts are not.

Accounting: Goodwill treatment: stretching useful life too far?

Symantec benefited greatly from SFAS 142 as it had been amortizing its Goodwill over 4 to 5 years prior to the rule's adoption. Symantec's acquisition pace after it changed auditors a couple of years ago has served to significantly expand its Goodwill numbers. Four deals totaling $375.2 million were closed soon after the arrival of the new auditors, adding $308 million to Symantec's existing $526 million total. The total Goodwill number has since swelled to $1,080 million and, after two annual impairment tests, none has yet to be charged.

We note this primarily because before its auditor switch, Symantec was required to write its Goodwill off very aggressively while now, with two years passed, the pressure doesn't seem to exist to write some down. We would say that it appears the Company is in somewhat of a tight spot here treating goodwill as it suddenly has continuing value beyond the estimated useful life previously used. Perhaps it is equally interesting how all reference to the old 4-5 year amortization schedule has been struck from the recently issued 200410-K.

We think there is a curious dichotomy in that both the Company and the auditors are on record saying that the value of goodwill was such that a 4 to 5 year write-off was acceptable accounting treatment and not long thereafter taking the position that no diminution of value has occurred to warrant an impairment charge. If the 4 to 5 year treatment was acceptable, one wonders how close at hand an impairment charge might be. What breathed new, indefinite life into the goodwill?

Accounting: Noteworthy miscellaneous items

- **Deferred Revenue Growth:** It is well-known that Symantec's Deferred Revenue growth was aided significantly last year when it increased the on-line price of its consumer subscriptions by $5 per sale: Symantec's price increase left the up-front price (license price) unchanged and raised the subscription price (which is recognized ratably over a year). Consequently, the related Deferred Revenue growth in the Consumer Segment has made it difficult to assess whether the Company is experiencing less growth contribution from its critical Enterprise Segment than it had in earlier periods. Acquisitions have provided another important effect on Deferred Revenue in the last two years, contributing more than 14%, on average, to Deferred Revenue growth during the period. For the acquisitions to continue to contribute in this fashion, the availability of funds for making acquisitions will constitute a significant strategic aspect of the Company's planning, especially in light of conflicts imposed by the increases in share repurchases that lie ahead.

- **Allowance For Doubtful Receivables:** We also note that Symantec managed to decrease its receivable allowance by 42% (from $9.8 million to $5.7 million) between F/Y 2003 and F/Y 2004, this during a period where A/R's actually increased by 66%. Symantec made no mention as to whether the need for the smaller allowance was due to some housecleaning or an overall improvement in the quality of receivables. Nevertheless, the move contributed about a penny a share to EPS.