AP Breaking News

Google creates new moneymaking option for employee stock options

By MICHAEL LIEDTKE, AP Business Writer

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(12-13) 00:09 PST San Francisco (AP) --

Google Inc. employs a lot of brilliant minds, but even smart people have trouble figuring out how much their stock options are really worth.

The Mountain View-based company hopes to simplify the task by creating a new online market that will show how much sophisticated investors are willing to pay for the company's options and enable rank-and-file workers to cash out at the prices being dangled.

"We think this will be very valuable in helping our employees understand what they own right from the beginning," said Dave Rolefson, Google's equity and executive compensation manager.

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The shift to transferable stock options, announced late Tuesday, is scheduled to occur during next year's second quarter.

Accounting for the change will lower Google's anticipated profit for next year, but the diminished earnings won't necessarily undercut the company's lofty market value because the analyst estimates that guide investor expectations already ignore stock compensation expenses.

With the switch, Google is hoping to make itself an even more appealing place to work than it already has become by feeding employees with free daily meals and ample opportunities to get rich off the company's high-flying stock.

"This should give Google something of an edge" over other employers,

said James Glassman, a senior fellow for the American Enterprise Institute, a think tank in Washington, D.C. "Google is going to get more bang for its buck by making its stock options more transparent."

Recruiting and retaining talented employees is a top priority for Google because it's in the midst of a hiring spree that is expected to continue for several more years. Since the end of 2004, Google has been hiring an average of about 10 new employees per day to expand its payroll to nearly 10,000 employees.

It marks the first time that a major U.S. company has established an ongoing market where employees will be able to sell their options to investors looking to hedge complex financial bets.

"Other companies are going to follow suit because it's a good idea," predicted Brian Hall, a Harvard University professor of business administration who has studied the advantages of transferable stock options.

Traditionally, workers make money off their stock options by cashing in on the spread between the exercise price and the current market price of the underlying shares.

For instance, a Google worker who owns 100 stock options with an exercise price of $200 would have a paper profit of just over $28,000, based on the company's Tuesday closing price of $481.78 on the Nasdaq Stock Market.

Google's new approach would offer that worker a chance to sell those 100 options at an even higher price to an investment bank or other institutional investor betting that Google's shares will be worth substantially more in the future. The buyer would have a maximum of two years to realize a gain from the options.

Even if they don't want to sell, Google employees should be able to get a better handle on the true value of their stock options.

"It's an exciting concept," agreed Arthur Levitt, a former chairman of the Securities and Exchange Commission who is now a senior adviser for the Carlyle Group.

Only stock options issued since Google's August 2004 initial public offering will be given access to an online market to be managed by Morgan Stanley. None of the options held by the company's top executives will become transferable.

The eligible pool covers about 6.6 million of Google's roughly 13 million employee stock options, according to company officials.

Accounting for the new system will crimp Google's profit next year because the change will extend the projected life of the affected employee stock options by about two years. That will raise the compensation expenses that recorded on Google's company books.

Google will absorb a second-quarter charge next year to recognize the expense for shifting to transferable options. The company doesn't expect to estimate the financial impact until the first quarter.

Accounting for the transferable stock options will continue to squeeze Google's earnings in subsequent quarters too, said Mark Fuchs, the company's chief accountant.

Investors may be largely unfazed by the projected drop in Google's earnings because Wall Street analysts discount the impact of stock compensation expenses.

Google's earnings, minus stock compensation expense, have exceeded analysts' estimates in all but one of the nine quarters that it has reported since its IPO. The stellar performance has propelled Google's stock price from $85 at the time of the IPO to a recent high of $513.

Excluding stock compensation expenses, analysts currently expect Google to earn $13.70 per share next year, a 33 percent increase from this year's projected $10.31 per share, according to Thomson Financial.

The transferable stock options are meant to address a challenge posed by Google's lofty stock price.

While hundreds of Google workers have already realized huge windfalls from their stock options, recently hired employees are more apt to feel shortchanged, said **Ted Buyniski**, a senior vice president with Radford Surveys + Consulting, a compensation specialist.

That's because the exercise price of stock options typically depend on a company's market value at the time an employee is hired.

The formula can create huge financial disparities among employees doing similar work. For instance, any Google worker hired this year would have received options with exercise prices ranging between $331.55 and $513. But workers hired between the completion of the company's IPO and January 2005 would have received options with exercise prices ranging between $95.96 and $201.60.

Despite the higher exercise prices, the stock options issued this year might be worth more than they appear because of Wall Street's ever-rising expectations for the company. Several analysts, for instance, believe Google's shares will hit $600 during 2007.

The transferable stock options will now give Google employees a way to take advantage of Wall Street's expectations before the shares actually rise.

"They have plucked the right tool out of their toolbox," **Buyniski** said.