

**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-Q

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended December 28, 2002

Commission file number 000-49602

**SYNAPTICS INCORPORATED**

(Exact name of Registrant as specified in its charter)

**Delaware**

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(State or other jurisdiction  
of incorporation or organization)

**77-0118518**

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(I.R.S. Employer  
Identification No.)

**2381 Bering Drive**  
**San Jose, California 95131**  
(Address of principal executive offices)  
(Zip code)

**(408) 434-0110**  
(Registrant's telephone number, including area code)

Indicate by check whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes  No

Number of shares of Common Stock outstanding at February 5, 2003: 23,521,331

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**SYNAPTICS INCORPORATED**  
**QUARTERLY REPORT ON FORM 10-Q**  
**FOR THE QUARTER ENDED DECEMBER 31, 2002**

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## PART I — FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

SYNAPTICS INCORPORATED  
CONDENSED CONSOLIDATED BALANCE SHEETS  
(in thousands)

	December 31, 2002	June 30, 2002 (1)
	(unaudited)	
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 38,935	\$45,491
Short-term investments	30,743	19,689
Accounts receivable, net of allowances of \$210 and \$200 at December 31, 2002 and June 30, 2002, respectively	13,452	13,242
Inventories	6,103	5,867
Prepaid expenses and other current assets	3,401	2,964
Total current assets	92,634	87,253
Property and equipment, net	1,782	2,043
Goodwill	765	765
Other assets	236	320
Total assets	\$ 95,417	\$90,381
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 6,523	\$ 5,867
Accrued compensation	1,939	2,161
Accrued warranty	1,002	1,002
Income taxes payable	2,462	2,646
Other accrued liabilities	2,444	1,814
Capital leases and equipment financing obligations	346	445
Total current liabilities	14,716	13,935
Capital leases and equipment financing obligations, net of current portion	82	259
Note payable to a related party	1,500	1,500
Other liabilities	722	684
Commitments and contingencies		
Stockholders' equity:		
Common stock	23	23
Additional paid-in capital	76,666	75,013
Deferred stock compensation	(1,594)	(1,085)
Notes receivable from stockholders	(755)	(876)
Retained earnings	3,910	865
Accumulated other comprehensive income	147	63
Total stockholders' equity	78,397	74,003
Total liabilities and stockholders' equity	\$ 95,417	\$90,381

(1) Derived from our audited financial statements as of June 30, 2002, included in our Form 10-K filed with the Securities and Exchange Commission.

See notes to condensed consolidated financial statements.

**SYNAPTICS INCORPORATED**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
(in thousands, except per share data)  
(unaudited)

	Three Months Ended December 31,		Six Months Ended December 31,	
	2002	2001	2002	2001
Net revenue	\$24,199	\$26,402	\$46,376	\$49,971
Cost of revenue (1)	13,917	15,376	26,360	29,983
Gross margin	10,282	11,026	20,016	19,988
Operating expenses:				
Research and development (1)	4,812	4,117	10,135	7,808
Selling, general, and administrative (1)	2,638	2,426	5,242	5,101
Amortization of other acquired intangible assets	10	62	40	75
Amortization of deferred stock compensation	116	121	226	242
Total operating expenses	7,576	6,726	15,643	13,225
Operating income	2,706	4,300	4,373	6,763
Interest income	279	48	556	81
Interest expense	(47)	(49)	(86)	(113)
Income before income taxes	2,938	4,299	4,843	6,731
Provision for income taxes	1,093	1,497	1,798	2,342
Net income	\$ 1,845	\$ 2,802	\$ 3,045	\$ 4,389
Net income per share:				
Basic	\$ 0.08	\$ 0.42	\$ 0.13	\$ 0.66
Diluted	\$ 0.07	\$ 0.14	\$ 0.12	\$ 0.22
Shares used in computing net income per share:				
Basic	23,387	6,709	23,309	6,666
Diluted	25,083	20,376	24,957	20,369

(1) Cost of revenue excludes \$7,000, \$7,000, \$14,000, and \$14,000 of amortization of deferred stock compensation for the three months ended December 31, 2002 and 2001, and the six months ended December 31, 2002 and 2001, respectively. Research and development expense excludes \$38,000, \$49,000, \$77,000, and \$98,000 of amortization of deferred stock compensation for the three months ended December 31, 2002 and 2001, and the six months ended December 31, 2002 and 2001, respectively. Selling, general, and administrative expenses exclude \$71,000, \$65,000, \$135,000, and \$130,000 of amortization of deferred stock compensation for the three months ended December 31, 2002 and 2001, and the six months ended December 31, 2002 and 2001, respectively. These amounts have been aggregated and reflected as "Amortization of deferred stock compensation."

*See notes to condensed consolidated financial statements.*

**SYNAPTICS INCORPORATED**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(in thousands)  
(unaudited)

	Six Months Ended December 31,	
	2002	2001
<b>Operating activities</b>		
Net income	\$ 3,045	\$ 4,389
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization of property and equipment	696	609
Amortization of other acquired intangible assets	40	75
Amortization of deferred stock compensation	226	242
Fair value of options issued to consultants for services rendered	17	—
Changes in operating assets and liabilities:		
Accounts receivable	(210)	214
Inventories	(236)	2,284
Prepaid expenses and other current assets	(437)	37
Other assets	44	(776)
Accounts payable	656	(1,445)
Accrued compensation	(222)	476
Other accrued liabilities and income taxes payable	446	425
Accrued warranty	—	250
Other liabilities	38	44
Net cash provided by operating activities	4,103	6,824
<b>Investing activities</b>		
Purchases of short-term investments	(13,200)	—
Proceeds from sales and maturities of short-term investments	2,230	—
Purchase of property and equipment	(435)	(639)
Net cash used in investing activities	(11,405)	(639)
<b>Financing activities</b>		
Payments on capital leases and equipment financing obligations	(276)	(321)
Proceeds from equipment financing	—	308
Common stock issued under ESPP and stock option plans	902	642
Repayment of notes receivable from stockholders	120	30
Net cash provided by financing activities	746	659
Increase (decrease) in cash and cash equivalents	(6,556)	6,844
Cash and cash equivalents at beginning of period	45,491	3,766
Cash and cash equivalents at end of period	\$ 38,935	\$10,610
<b>Supplemental disclosures of cash flow information</b>		
Cash paid for interest	16	58
Cash paid for taxes	1,972	1,713

*See notes to condensed consolidated financial statements.*

**SYNAPTICS INCORPORATED**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
(unaudited)

**1. Basis of Presentation**

The accompanying unaudited condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission and generally accepted accounting principles. However, certain information or footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted pursuant to such rules and regulations. In our opinion, the statements include all adjustments (which are of a normal and recurring nature) necessary for the fair presentation of the results of the interim periods presented. The results of operations for the interim periods are not necessarily indicative of the operating results for the full fiscal year or any future period. These financial statements should be read in conjunction with the audited consolidated financial statements and related notes included in our annual report on Form 10-K for the year ended June 30, 2002.

The consolidated financial statements include our financial statements and our wholly owned subsidiaries. All significant intercompany balances and transactions have been eliminated upon consolidation.

Our fiscal year ends on the last Saturday in June. For ease of presentation, the accompanying financial statements have been shown as ending on June 30 and calendar quarter ends for all annual, interim, and quarterly financial statement captions.

**2. Net Income Per Share**

Basic net income per share amounts have been computed using the weighted-average number of shares of common stock outstanding during each period, less shares subject to repurchase. Diluted net income per share amounts also include the effect of potentially dilutive securities, including stock options, warrants, and convertible preferred stock, when dilutive.

The following table presents the computation of basic and diluted net income per share (in thousands, except per share amounts):

	Three Months Ended December 31,		Six Months Ended December 31,	
	2002	2001	2002	2001
Numerator for basic and diluted net income per share:				
Net income	\$ 1,845	\$ 2,802	\$ 3,045	\$ 4,389
Denominator for basic net income per share:				
Weighted average common shares outstanding	23,387	6,709	23,309	6,678
Less: Weighted average shares subject to repurchase	—	—	—	(12)
Denominator for basic net income per share	23,387	6,709	23,309	6,666
Denominator for diluted net income per share:				
Shares used above, basic	23,387	6,709	23,309	6,666
Dilutive stock options	1,696	2,533	1,648	2,569
Dilutive warrants	—	23	—	23
Dilutive preferred stock	—	11,074	—	11,074
Dilutive contingent shares	—	37	—	37
Denominator for diluted net income per share	25,083	20,376	24,957	20,369
Net income per share:				
Basic	\$ 0.08	\$ 0.42	\$ 0.13	\$ 0.66
Diluted	\$ 0.07	\$ 0.14	\$ 0.12	\$ 0.22

### 3. Cash Equivalents and Short-term Investments

Cash equivalents consist of highly liquid investments with original maturities of three months or less. Short-term investments consist of debt securities classified as available for sale and are carried at their market value as of the balance sheet date with approximated amortized cost. The amortized cost of securities is adjusted for amortization of premiums and accretion of discounts to maturity. Such amortization is included in investment income. Realized gains or losses are determined on the specific identification method and are reflected in income. Net unrealized gains or losses are recorded directly in stockholder's equity except those unrealized losses that are deemed to be other than temporary are reflected in income.

As of December 31, 2002, cash, cash equivalents, and short-term investments consisted of the following (in thousands):

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Cash and cash equivalents:				
Cash	\$ 4,341	\$ —	\$ —	\$ 4,341
Certificate of deposit	—	—	—	—
Money market	21,102	—	—	21,102
Municipal securities	13,492	—	—	13,492
	<u>\$38,935</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$38,935</u>
Short-term investments:				
Municipal securities	\$30,596	\$ 147	\$ —	\$30,743
	<u>\$30,596</u>	<u>\$ 147</u>	<u>\$ —</u>	<u>\$30,743</u>

### 4. Comprehensive Income

Comprehensive income includes all changes in stockholders' equity during a period except those resulting from investments by owners and distributions to owners. Other comprehensive income comprises unrealized gains and losses on available-for-sale securities. Total comprehensive income was \$1,927,000, \$2,802,000, \$3,129,000, and \$4,389,000 for the three months ended December 31, 2002 and 2001 and the six months ended December 31, 2002 and 2001, respectively. Accumulated other comprehensive income amounted to \$147,000 and \$63,000 as of December 31, 2002 and June 30, 2002, respectively. For the three months ended December 31, 2002 and 2001 and the six months ended December 31, 2002 and 2001, the change in unrealized gain on marketable equity securities was \$82,000, \$0, \$84,000 and \$0, respectively.

### 5. Inventories

Inventories are stated at the lower of cost (first-in, first-out method) or market (estimated net realizable value) and consisted of the following (in thousands):

	December 31, 2002	June 30, 2002
Raw materials and work-in-process	\$ 5,809	\$5,690
Finished goods	294	177
	<u>\$ 6,103</u>	<u>\$5,867</u>

### 6. Warranty

We generally warrant our products for a period of 12 months from the date of sale and estimate probable product warranty costs at the time revenue is recognized. Factors that affect our warranty liability include historical and anticipated rates of warranty claims, material usage, and service delivery costs. Warranty costs incurred have not been material in recent years. However, we assess the adequacy of our warranty obligations periodically and adjust the accrued warranty liability on the basis of our estimates.



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Changes in our warranty liability during the period are as follows (in thousands):

Balance, beginning of the period	\$1,002
Warranties issued during the period	9
Settlements made during the period	(9)
Changes in liability for pre-existing warranties during the period, including expirations	—
	<u>—</u>
Balance, end of the period	<u>\$1,002</u>

**7. Income Taxes**

The income tax provision for the three-month and six-month periods ended December 31, 2002 and 2001 reflects an effective income tax rate based on expected pre-tax income for the year and an expected research and development tax credit.

**8. Segment, Customers, and Geographic Information**

We operate in one segment, the development, marketing, and sale of interactive user interface solutions for intelligent electronic devices and products, and currently generate our revenue primarily from the personal computer ("PC") market.

The following is a summary of operations within geographic areas based on customer's location (in thousands):

	Three Months Ended December 31,		Six Months Ended December 31,	
	2002	2001	2002	2001
Revenue from sales to unaffiliated customers:				
Taiwan	\$12,051	\$21,044	\$26,934	\$39,186
China	7,620	694	10,786	1,092
Other	4,528	4,664	8,656	9,693
	<u>\$24,199</u>	<u>\$26,402</u>	<u>\$46,376</u>	<u>\$49,971</u>

Major customer data as a percentage of total revenue:

	Three Months Ended December 31,		Six Months Ended December 31,	
	2002	2001	2002	2001
Customer A	*	19%	*	18%
Customer B	*	17%	*	21%
Customer C	*	*	11%	*
Customer D	10%	*	*	*

Major customer data as a percentage of total accounts receivable:

	December 31, 2002	June 30, 2002
Customer A	*	14%
Customer B	15%	14%
Customer C	12%	*
Customer D	10%	*
Customer E	*	11%

\* Less than 10%

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

### Forward-Looking Statements and Factors That May Affect Results

You should read the following discussion and analysis in conjunction with our condensed consolidated financial statements and notes in Item 1 above and with our audited consolidated financial statements and notes for the year ended June 30, 2002, included in our Annual Report on Form 10-K.

In addition to the historical information contained herein, this report contains forward-looking statements, including those related to market penetration and market share gains in the notebook, iAppliance, and other electronic device markets, revenue from the notebook, iAppliance, and other electronic device markets, growth rates of these markets, average selling prices, product mix, cost improvement programs, gross margins, customer relationships, research and development expenses, selling, general, and administrative expenses, and liquidity and anticipated cash requirements, that involve risks and uncertainties that could cause actual results to differ materially.

We caution that these statements are qualified by various factors that may affect future results, including the following: changes in the market for our products and the success of our customers' products, our success in moving products from the design phase into the manufacturing phase, warranty failures, the failure of key technologies to deliver commercially acceptable performance, our dependence on the notebook market, penetration into new markets, the absence of both long-term purchase and supply commitments, and our lengthy development and product acceptance cycles. This report should be read in conjunction with the Risk Factors discussed in our Annual Report on Form 10-K for the year ended June 30, 2002.

### Overview

We are a leading worldwide developer and supplier of custom-designed user interface solutions that enable people to interact more easily and intuitively with a wide variety of electronic devices. We began shipping our proprietary TouchPad in fiscal 1996 and are now the world's leading supplier of interface solutions to the notebook computer market. Our interface solutions include our TouchPad, TouchStyk, and the combination of both a touchpad and pointing stick for dual pointing applications. We estimate that over half of all notebooks shipped during calendar year 2002 contained our products. We believe our market share results from the combination of our customer focus, the strength of our intellectual property, and our engineering know-how, which allow us to design products that meet the demanding design specifications of original equipment manufacturers, or OEMs. More than 95% of our revenue is generated through sales of our interface solutions to the notebook market.

Our manufacturing operations are based on a variable cost model in which we outsource all of our production requirements, eliminating the need for significant capital expenditures and allowing us to minimize our investment in inventories. This approach requires us to work closely with our manufacturing subcontractors to ensure adequate production capacity to meet our volume requirements. We provide our manufacturing subcontractors with six-month rolling forecasts and issue purchase orders based on our anticipated requirements for the next 90 days. We do not have any long-term supply contracts with any of our manufacturing subcontractors. Currently, we primarily use one third-party manufacturer to provide our proprietary capacitive-based application specific integrated circuits, or ASICs, and in certain cases we also rely on a single source or a limited number of suppliers to provide other key components of our products. Our cost of sales includes all costs associated with the production of our products, including materials, manufacturing, and assembly costs paid to third-party manufacturers and related overhead costs associated with our manufacturing operations personnel. Additionally, all warranty costs and any inventory provisions or write-downs are expensed as cost of sales.

Our gross margin generally reflects the combination of the added value we bring to our customers' products in meeting their custom design requirements and our ongoing cost improvement programs. In the future, we plan to introduce additional new products, which may initially negatively impact our gross margin, as was the case with the introduction of our initial dual pointing solutions in fiscal year 2001.

Our research and development expenses include expenses related to product development, engineering, materials costs, patent expenses, and the costs incurred to design interface solutions for customers prior to the customers' commitment to incorporate those solutions into their products. These expenses have generally increased,

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reflecting our continuing commitment to the technological and design innovation required to maintain a leadership position in our existing markets and to develop new technologies for new markets.

Selling, general, and administrative expenses include expenses related to sales, marketing, and administrative personnel; internal sales and outside sales representatives' commissions; market research and consulting; and other marketing and sales activities. Increased sales staffing and additional management personnel in anticipation of our continued growth in our existing markets and penetration into new markets have generally caused selling, general, and administrative expenses to increase.

In connection with the grant of stock options to our employees and consultants, we have recorded deferred stock compensation of approximately \$3.0 million, representing the difference between the deemed fair value of our common stock for financial reporting purposes and the exercise price of these options at the date of grant. Deferred stock compensation is presented as a reduction of stockholders' equity and is amortized on a straight-line basis over the vesting period. Options granted are typically subject to a four-year vesting period. Restricted stock acquired through the exercise of unvested stock options is subject to our right to repurchase the unvested stock at the price paid, which right to repurchase lapses over the vesting period. We are amortizing the deferred stock compensation over the vesting periods of the applicable options and the repurchase periods for the restricted stock. As of December 31, 2002, there was \$1.6 million of deferred stock compensation remaining to be amortized in future periods.

### **Critical Accounting Policies and Estimates**

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue, expenses, and related disclosure of contingent assets and liabilities. We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our consolidated financial statements. Actual results may differ from these estimates under different assumptions or conditions.

#### *Revenue Recognition*

We recognize revenue from product sales when there is persuasive evidence that an arrangement exists, delivery has occurred and title has transferred, the price is fixed and determinable, and collectibility is reasonably assured. We accrue for estimated sales returns and other allowances at the time of recognition of revenue, which is typically upon shipment, based on historical experience. Contract revenue for research and development is recorded as earned based on the performance requirements of the contract. Non-refundable contract fees for which no further performance obligations exist, and for which there is no continuing involvement by us, are recognized on the earlier of when the payments are received or when collection is assured.

#### *Allowance for Doubtful Accounts*

We maintain allowances for doubtful accounts for estimated losses resulting from the inability of customers to meet their financial obligations. On an ongoing basis, we evaluate the collectibility of accounts receivable based on a combination of factors. In circumstances in which we are aware of a specific customer's inability to meet its financial obligation, we record a specific reserve of the bad debt against amounts due. In addition, we must make judgments and estimates of the collectibility of accounts receivable based on historical bad debt, customers' creditworthiness, current economic trends, recent changes in customer payment trends, and deterioration in the customers' operating results or financial position. If circumstances change adversely, additional allowances may be required.

#### *Inventory*

We are required to state our inventories at the lower of cost or market. Our assessment of the ultimate realization of inventories is based on our projections of future demand and market conditions. Any sudden decline in demand or rapid product improvements and technological changes, or both, can cause us to have excess or obsolete inventories. On an ongoing basis, we review for estimated obsolete or unmarketable inventories and write down our inventories to their net realizable value based upon our forecasts of future demand and market conditions. If actual market conditions are less favorable than our forecasts, additional inventory reserves may be required. Our estimates are influenced by the following considerations: sudden decline in demand due to economic downturn or customer

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demand, rapid product improvements and technological changes, and termination by our OEM customers of any product offerings incorporating our product solutions.

### *Warranty*

We generally warrant our products for a period of 12 months from the date of sale and estimate probable product warranty costs at the time revenue is recognized. While we engage in extensive product quality programs and processes, including actively monitoring and evaluating the quality of our materials and service suppliers, our warranty costs are affected by product failure rates, material usage, and service delivery costs incurred in correcting a product failure. We exercise judgment in determining the estimates underlying our accrued warranty liability. The actual results with regard to warranty expenditures could have a material adverse effect on our operating results if the actual rate of unit failure is greater than what we used in estimating the accrued warranty liability.

### **Results of Operations**

#### *Three months ended December 31, 2002 compared to three months ended December 31, 2001*

Net revenue was \$24.2 million for the three months ended December 31, 2002 compared to \$26.4 million for the three months ended December 31, 2001, a decrease of 8.3%. The decrease in revenue was primarily attributable to a reduction in overall average selling price, resulting from a change in product mix and general competitive pricing, and the absence of a one-time patent license fee that occurred in the comparable prior year period, partially offset by increased unit shipments. During the three months ended December 31, 2002, sales of higher priced dual pointing products decreased to approximately 37% of our revenue compared to 51% for the three months ended December 31, 2001. Increased unit shipments of touchpads, as well as revenue contributions from non-PC applications, partially offset the lower overall average selling price.

Gross margin as a percentage of revenue was 42.5% for the three months ended December 31, 2002 compared to 41.8% for the three months ended December 31, 2001. The improvement in gross margin as a percentage of revenue primarily reflected lower manufacturing costs, resulting from the combination of our ongoing design and process improvement programs and lower materials and assembly costs, partially offset by a shift in mix to lower margin products, a lower average selling price resulting from general competitive pricing, and the absence of a one-time patent license fee that occurred in the comparable prior year period.

Research and development expenses increased 16.9% to \$4.8 million, or 19.9% of revenue, for the three months ended December 31, 2002 from \$4.1 million, or 15.6% of revenue, for the three months ended December 31, 2001. The major contributors to the increase in spending were costs associated with our higher staffing levels, including compensation and facilities-related costs, additional new product development activities, which included outside services and materials costs, and higher patent-related costs.

Selling, general, and administrative expenses increased 8.7% to \$2.6 million, or 10.9% of revenue, for the three months ended December 31, 2002 from \$2.4 million, or 9.2% of revenue, for the three months ended December 31, 2001. The increase in spending resulted mainly from higher compensation costs associated with increased staffing levels, additional expenses related to generally higher operating levels, and additional costs related to our status as a public reporting company.

Amortization of other intangible assets related to our October 1999 acquisition of Absolute Sensors Limited, or ASL, a company located in Cambridge, United Kingdom. For the three months ended December 31, 2002, amortization of other intangible assets amounted to \$10,000 compared to \$62,000 for the three months ended December 31, 2001. As of December 31, 2002, these intangible assets were fully amortized.

The three months ended December 31, 2002 included amortization expense for deferred stock compensation of \$116,000 compared to \$121,000 for the three months ended December 31, 2001. We expect to record amortization expense for deferred stock compensation of \$282,000 in the remaining six months of fiscal 2003 and the balance of \$1.3 million in future years.

We generated operating income of \$2.7 million for the three months ended December 31, 2002 compared to \$4.3 million for the three months ended December 31, 2001. The major contributors to the decrease in operating

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income were the decrease in revenue, resulting primarily from a lower mix of higher margin products, lower average selling prices, and the absence of a one-time patent license fee that occurred in the comparable prior year period, and the increase in operating expenses, which primarily resulted from costs associated with our increased staffing levels, including higher compensation and facilities-related costs, higher research and development costs related to increased product development activities, and additional costs related to our status as a public reporting company. The decrease in revenue and increase in operating expenses were partially offset by an improvement in gross margin percentage, resulting primarily from lower manufacturing costs related to our ongoing design and process improvement programs and lower materials and assembly costs, and increased unit shipments.

Net interest income was \$232,000 for the three months ended December 31, 2002 compared to net interest expense of \$1,000 for the three months ended December 31, 2001, reflecting the benefit of higher cash balances available for investment activities from the net proceeds of our initial public offering of 5.0 million shares at \$11.00 per share, which closed on February 1, 2002.

The provision for income taxes for the three months ended December 31, 2002 was \$1.1 million compared to \$1.5 million for the three months ended December 31, 2001, a decrease of \$400,000, reflecting the lower pre-tax profit levels, partially offset by a higher effective tax rate of 37% for the three months ended December 31, 2002 compared to 35% for the three months ended December 31, 2001. The income tax provision represents the estimated federal and state taxes and the foreign taxes associated with our operations in the United Kingdom and Taiwan. The effective tax rates for the three-month periods ended December 31, 2002 and December 31, 2001 reflect the benefit of the federal research and development tax credit, partially offset by nondeductible deferred compensation.

### *Six months ended December 31, 2002 compared to six months ended December 31, 2001*

Net revenue was \$46.4 million for the six months ended December 31, 2002 compared to \$50.0 million for the six months ended December 31, 2001, a decrease of 7.2%. The decrease in revenue was primarily attributable to changes in product mix, general competitive pricing pressure, and lower non-recurring engineering and patent license fees, partially offset by increased unit shipments. During the six months ended December 31, 2002, sales of higher priced dual pointing products decreased to approximately 41% of our revenue compared to 50% for the six months ended December 31, 2001. Net revenue decreases caused by product mix changes and competitive pricing, resulting in a lower average selling price, were partially offset by increased unit shipments of touchpads as well as revenue contributions from non-PC applications.

Gross margin as a percentage of revenue was 43.2% for the six months ended December 31, 2002 compared to 40.0% for the six months ended December 31, 2001. The improvement in gross margin as a percentage of revenue primarily resulted from the benefit of manufacturing efficiencies gained from our ongoing design and process improvement programs and generally lower materials and assembly costs, partially offset by a decrease in mix of higher margin products, lower selling prices resulting from general competitive pricing, and lower non-recurring engineering and patent license revenue.

Research and development expenses increased 29.8% to \$10.1 million, or 21.9% of revenue, for the six months ended December 31, 2002 from \$7.8 million, or 15.6% of revenue, for the six months ended December 31, 2001. The major contributors to the increased spending were costs associated with our higher staffing levels, including compensation and facilities-related costs, higher product development activities, which included outside services and materials costs, and higher patent-related costs.

Selling, general, and administrative expenses increased slightly to \$5.2 million, or 11.3% of revenue, for the six months ended December 31, 2002 from \$5.1 million, or 10.2% of revenue, for the six months ended December 31, 2001. The increase in spending resulted mainly from higher compensation costs associated with increased staffing levels, higher expenses related to generally higher operating levels, and additional costs related to our status as a public reporting company, partially offset by significantly lower sales commissions, primarily resulting from the replacement of outside sales representatives with inside sales personnel for certain customer accounts that we implemented in October 2001, and to a lesser extent, the decrease in revenue.

Amortization of other intangible assets related to our October 1999 acquisition of ASL. For the six months ended December 31, 2002, the amount amortized was \$40,000 compared to \$75,000 for the six months ended December 31, 2001. As of December 31, 2002, these intangible assets were fully amortized.

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The six months ended December 31, 2002 included amortization expense for deferred stock compensation of \$226,000 compared to \$242,000 for the six months ended December 31, 2001. We expect to record amortization expense of \$282,000 in the remaining six months of fiscal 2003 and the balance of \$1.3 million in future years.

We generated operating income of \$4.4 million for the six months ended December 31, 2002 compared to \$6.8 million for the six months ended December 31, 2001. The major contributors to the lower operating income were the decrease in revenue, primarily reflecting the impact of a lower mix of higher margin products, lower average selling prices, lower non-recurring engineering and patent license fees, and the increase in operating expenses, which primarily resulted from higher costs associated with our increased staffing levels, including higher compensation and facilities-related costs, higher research and development costs related to increased product development activities, and additional costs related to our status as a public reporting company. The decrease in revenue and the increase in operating expenses were partially offset by an improvement in gross margin percentage, resulting from lower manufacturing costs related to improved manufacturing efficiencies from our ongoing design and process improvement programs and lower materials and assembly costs, increased unit shipments, and lower sales commissions.

Net interest income was \$470,000 for the six months ended December 31, 2002 compared to net interest expense of \$32,000 for the six months ended December 31, 2001, reflecting the benefit of higher cash balances available for investment activities from the net proceeds of our initial public offering of 5.0 million shares at \$11.00 per share, which closed on February 1, 2002.

The provision for income taxes for the six months ended December 31, 2002 was \$1.8 million compared to \$2.3 million for the six months ended December 31, 2001, reflecting the lower pre-tax profit levels, partially offset by a higher effective tax rate of 37% for the six months ended December 31, 2002 compared to 35% for the six months ended December 31, 2001. The income tax provision represents the estimated federal and state taxes and the foreign taxes associated with our operations in the United Kingdom and Taiwan. The effective tax rates for the six month periods ended December 31, 2002 and December 31, 2001, reflect the benefit of the federal research and development tax credit, partially offset by nondeductible deferred compensation.

### **Liquidity and Capital Resources**

Our cash, cash equivalents, and short-term investments were \$69.7 million as of December 31, 2002 compared to \$65.2 million as of June 30, 2002, an increase of \$4.5 million. During the six months ended December 31, 2002, cash and cash equivalents decreased by \$6.6 million, while short-term investments increased by \$11.1 million. The primary factors contributing to the changes in cash, cash equivalents, and short-term investments are described below.

During the six months ended December 31, 2002, operating activities generated cash of \$4.1 million compared to \$6.8 million during the six months ended December 31, 2001. For the six months ended December 31, 2002, increase in cash was mainly attributable to net income of \$3.0 million plus non-cash adjustments for depreciation and amortization of acquired intangible assets and deferred stock compensation. For the six months ended December 31, 2001, net income, adjusted for depreciation and amortization, contributed \$5.3 million, while a decrease in working capital contributed an additional \$1.5 million.

Our investing activities typically relate to purchases of government-backed securities and investment-grade fixed income instruments and capital assets. Investing activities during the six months ended December 31, 2002 used cash of \$11.4 million compared to \$639,000 used during the six months ended December 31, 2001. Cash used during the six months ended December 31, 2002 consisted of purchases of \$13.2 million of short-term investments and \$435,000 of capital equipment, partially offset by cash provided by the proceeds from sales and maturities of short-term investments of \$2.2 million. Cash used for investments during the six months ended December 31, 2001 consisted of capital equipment expenditures.

Financing activities for the six months ended December 31, 2002 were primarily related to proceeds from common stock issued under the Employee Stock Purchase Plan and stock option plans, and repayment of notes receivable from stockholders, less payments made on capital lease obligations. Net cash provided by financing activities during the six months ended December 31, 2002 was \$746,000 compared to \$659,000 during the six months ended December 31, 2001.

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Our principal sources of liquidity as of December 31, 2002 consisted of \$69.7 million in cash, cash equivalents, and short-term investments and a \$4.2 million working capital line of credit with Silicon Valley Bank, which renewed on November 25, 2002. The Silicon Valley Bank revolving line of credit expires on November 25, 2003 and has an interest rate equal to Silicon Valley Bank's prime lending rate, and provides for a security interest in substantially all of our assets. We had not borrowed any amounts under the line of credit as of December 31, 2002. The long-term note payable to National Semiconductor represents limited-recourse debt that is secured solely by a portion of our stockholdings in Foveon, Inc., in which National Semiconductor is also an investor. We do not anticipate making any payments under the limited-recourse loan with National Semiconductor, either prior to or at maturity, unless Foveon is participating in a liquidity event, such as an initial public offering of its equity securities or a merger, through which we would be able to receive amounts in excess of our \$1.5 million long-term note payable plus accrued interest expense.

We believe our existing cash, cash equivalents, and short-term investments will be sufficient to meet our cash requirements at least through the next 12 months. Our future capital requirements will depend on many factors, including our rate of revenue growth, our operating performance, our ability to maintain our gross margin as a percent of revenue, the timing and extent of spending to support product development efforts, the expansion of sales and marketing activities, the timing of introductions of new products and enhancements to existing products, the costs to ensure access to adequate manufacturing capacity, the continuing market acceptance of our product solutions, and the amount and timing of our investment in, or acquisition of, other technologies or companies. We cannot assure you that additional equity or debt financing, if needed, will be available to us on acceptable terms or at all.

The following table provides a summary of the effect on cash flows from our contractual obligations as of December 31, 2002:

Contractual Cash Obligations	Payments Due by Fiscal Year (in thousands)				
	2003	2004 to 2005	2006 to 2007	2008 and thereafter	Total
Note payable and interest	\$ —	\$ —	\$ 2,686	\$ —	\$2,686
Building leases	576	1,941	515	—	3,032
Capital leases	179	266	—	—	445
Total	\$755	\$ 2,207	\$ 3,201	\$ —	\$6,163

## Recent Accounting Pronouncements

In November 2002, the Financial Accounting Standards Board issued Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others" (the Interpretation, FIN 45). The Interpretation elaborates on the existing disclosure requirements for most guarantees. The Interpretation requires that at the time a company issues certain guarantees, the company must recognize an initial liability for the fair value, or market value, of the obligations it assumes under that guarantee and must disclose that information in its interim and annual financial statements. The initial recognition and initial measurement provisions of the Interpretation are applicable on a prospective basis to guarantees issued or modified after December 31, 2002. The Interpretation's disclosure requirements are effective for financial statements of interim or annual periods ending after December 15, 2002 and are applicable to all guarantees issued by the guarantor subject to the Interpretation's scope, including guarantees issued prior to the issuance of the Interpretation. The adoption of FIN 45 did not have any material impact on our financial position or results of operations.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Market risk for our company has not changed significantly from the interest rate and foreign currency risks disclosed in Item 7A of our Annual Report on Form 10-K for the fiscal year ended June 30, 2002.

### ITEM 4. CONTROLS AND PROCEDURES

As of a date within 90 days prior to the date of the filing of this report, our Chief Executive Officer and Chief Financial Officer have reviewed and evaluated the effectiveness of our disclosure controls and procedures, which included inquiries made to certain other of our employees. Based on their evaluation, our Chief Executive Officer and Chief Financial Officer have each concluded that our disclosure controls and procedures are effective and sufficient to ensure that we record, process, summarize, and report information required to be disclosed by us in our periodic reports filed under the Securities Exchange Act within the time periods specified by the Securities and Exchange Commission's rules and forms. Subsequent to the date of their evaluation, there have not been any significant changes in our internal controls or in other factors that could significantly affect these controls, including any corrective actions with regard to significant deficiencies and material weaknesses.

## PART II — OTHER INFORMATION

### ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

Our Annual Meeting of Stockholders was held on October 22, 2002. All of the nominees were elected to our Board of Directors as set forth in the Proxy Statement as follows:

Nominees	Votes in Favor	Votes Against
Federico Faggin	19,573,454	130,140
Francis F. Lee	18,596,035	1,107,559
Keith B. Geeslin	19,599,498	104,096
Richard L. Sanquini	19,597,494	106,100
W. Ronald Van Dell	19,632,898	70,696

An amendment to our Certificate of Incorporation to classify our board of directors into three classes with staggered terms of office was also voted upon and approved by our stockholders as follows:

Votes in Favor	Votes Against	Abstain
13,740,645	2,869,729	27,163

### ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits:

10.6(a) Amended and Restated 2001 Incentive Compensation Plan

10.6(b) Form of Grant Agreement for Amended and Restated 2001 Incentive Compensation Plan

99.1 Certification of the Chief Executive Officer of the Registrant, pursuant to 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

99.2 Certification of the Chief Financial Officer of the Registrant, pursuant to 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(b) Reports on Form 8-K:

None.



**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

Date: February 6, 2003

**SYNAPTICS INCORPORATED**

/s/ Francis F. Lee

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Francis F. Lee  
President and Chief Executive Officer

/s/ Russell J. Knittel

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Russell J. Knittel  
Senior Vice President and Chief  
Financial Officer

## CERTIFICATIONS

I, Francis F. Lee, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Synaptics Incorporated;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:
  - a) Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - c) Presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
  - a) All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: February 6, 2003

/s/ Francis F. Lee

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Francis F. Lee  
President and Chief Executive Officer

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I, Russell J. Knittel, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Synaptics Incorporated;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and have:
  - a) Designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
  - b) Evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this quarterly report (the "Evaluation Date"); and
  - c) Presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;
5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent function):
  - a) All significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and
6. The registrant's other certifying officers and I have indicated in this quarterly report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: February 6, 2003

/s/ Russell J. Knittel

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Russell J. Knittel  
Senior Vice President, Chief Financial  
Officer, Chief Administrative Officer,  
Secretary, and Treasurer

INDEX TO EXHIBITS

Exhibits:

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SYNAPTICS INCORPORATED

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 AMENDED AND RESTATED  
 2001 INCENTIVE COMPENSATION PLAN  
 (AS AMENDED THROUGH DECEMBER 10, 2002)

SYNAPTICS, INCORPORATED

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 AMENDED AND RESTATED  
 2001 INCENTIVE COMPENSATION PLAN  
 (AS AMENDED THROUGH DECEMBER 10, 2002)

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SYNAPTICS, INCORPORATED

AMENDED AND RESTATED  
2001 INCENTIVE COMPENSATION PLAN  
(AS AMENDED THROUGH DECEMBER 10, 2002)

1. Purpose. The purpose of this AMENDED AND RESTATED 2001 INCENTIVE COMPENSATION PLAN (the "Plan") is to assist SYNAPTICS INCORPORATED, a California corporation (the "Company") and its Related Entities in attracting, motivating, retaining and rewarding high-quality executives and other Employees, officers, Directors and independent Contractors by enabling such persons to acquire or increase a proprietary interest in the Company in order to strengthen the mutuality of interests between such persons and the Company's shareholders, and providing such persons with annual and long term performance incentives to expend their maximum efforts in the creation of shareholder value. In the event that the Company is or becomes a Publicly Held Corporation (as hereinafter defined), the Plan is intended to qualify certain compensation awarded under the Plan for tax deductibility under Section 162(m) of the Code (as hereafter defined) to the extent deemed appropriate by the Committee (or any successor committee) of the Board of Directors of the Company.

2. Definitions. For purposes of the Plan, the following terms shall be defined as set forth below, in addition to such terms defined in Section 1 hereof.

(a) "Annual Incentive Award" means a conditional right granted to a Participant under Section 8(c) hereof to receive a cash payment, Stock or other Award, unless otherwise determined by the Committee, after the end of a specified fiscal year.

(b) "Award" means any Option, Stock Appreciation Right (including Limited Stock Appreciation Right), Restricted Stock, Deferred Stock, Stock granted as a bonus or in lieu of another award, Dividend Equivalent, Other Stock-Based Award, Performance Award or Annual Incentive Award, together with any other right or interest, granted to a Participant under the Plan.

(c) "Beneficiary" means the person, persons, trust or trusts which have been designated by a Participant in his or her most recent written beneficiary designation filed with the Committee to receive the benefits specified under the Plan upon such Participant's death or to which Awards or other rights are transferred if and to the extent permitted under Section 10(b) hereof. If, upon a Participant's death, there is no designated Beneficiary or surviving designated Beneficiary, then the term Beneficiary means the person, persons, trust or trusts entitled by will or the laws of descent and distribution to receive such benefits.

(d) "Beneficial Owner", "Beneficially Owning" and "Beneficial Ownership" shall have the meanings ascribed to such terms in Rule 13d3 under the Exchange Act and any successor to such Rule.

(e) "Board" means the Company's Board of Directors.

(f) "Cause" shall, with respect to any Participant, have the equivalent meaning (or the same meaning as "cause" or "for cause") set forth in any employment agreement between the Participant and the Company or a Related Entity or, in the absence of any such agreement, such term shall mean (i) the

failure by the Participant to perform his or her duties as assigned by the Company (or a Related Entity) in a reasonable manner, (ii) any violation or breach by the Participant of his or her employment agreement with the Company (or a Related Entity), if any, (iii) any violation or breach by the Participant of his or her non-competition and/or non-disclosure agreement with the Company (or a Related Entity), if any, (iv) any act by the Participant of dishonesty or bad faith with respect to the Company (or a Related Entity), (v) chronic addiction to alcohol, drugs or other similar substances affecting the Participant's work performance, or (vi) the commission by the Participant of any act, misdemeanor, or crime reflecting unfavorably upon the Participant or the Company. The good faith determination by the Committee of whether the Participant's Continuous Service was terminated by the Company for "Cause" shall be final and binding for all purposes hereunder.

(g) "Change in Control" means a Change in Control as defined with related terms in Section 9 of the Plan.

(h) "Change in Control Price" means the amount calculated in accordance with Section 9(c) of the Plan.

(i) "Code" means the Internal Revenue Code of 1986, as amended from time to time, including regulations thereunder and successor provisions and regulations thereto.

(j) "Committee" means a committee designated by the Board to administer the Plan; provided, however, that the Committee shall consist of at least two directors, and, in the event the Company is or becomes a Publicly Held Corporation (as hereinafter defined), each member of which shall be (i) a "non-employee director" within the meaning of Rule 16b-3 under the Exchange Act, unless administration of the Plan by "non-employee directors" is not then required in order for exemptions under Rule 16b-3 to apply to transactions under the Plan, and (ii) an "outside director" within the meaning of Section 162(m) of the Code, unless administration of the Plan by "outside directors" is not then required in order to qualify for tax deductibility under Section 162(m) of the Code.

(k) "Consultant" means any person (other than an Employee or a Director, solely with respect to rendering services in such person's capacity as a director) who is engaged by the Company or any Related Entity to render consulting or advisory services to the Company or such Related Entity.

(l) "Continuous Service" means uninterrupted provision of services to the Company in any capacity of Employee, Director, or Consultant. Continuous Service shall not be considered to be interrupted in the case of (i) any approved leave of absence, (ii) transfers among the Company, any Related Entities, or any successor entities, in any capacity of Employee Director, or Consultant, or (iii) any change in status as long as the individual remains in the service of the Company or a Related Entity in any capacity of Employee, Director, or Consultant (except as otherwise provided in the Option Agreement). An approved leave of absence shall include sick leave, military leave, or any other authorized personal leave.

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(m) [Reserved]

(n) "Covered Employee" means an Eligible Person who is a Covered Employee as specified in Section 7(e) of the Plan.

(o) "Deferred Stock" means a right, granted to a Participant under Section 6(e) hereof, to receive Stock, cash or a combination thereof at the end of a specified deferral period.

(p) "Director" means a member of the Board or the board of directors of any Related Entity.

(q) "Disability" means a permanent and total disability (within the meaning of Section 22(e) of the Code), as determined by a medical doctor satisfactory to the Committee.

(r) "Dividend Equivalent" means a right, granted to a Participant under Section 6(g) hereof, to receive cash, Stock, other Awards or other property equal in value to dividends paid with respect to a specified

number of shares of Stock, or other periodic payments.

(s) "Effective Date" means the effective date of the Plan, which shall be March 7, 2001.

(t) "Eligible Person" means each Executive Officer of the Company (as defined under the Exchange Act) and other officers, Directors and Employees of the Company or of any Related Entity, and independent contractors with the Company or any Related Entity. The foregoing notwithstanding, only employees of the Company, the Parent, or any Subsidiary shall be Eligible Persons for purposes of receiving any Incentive Stock Options. An Employee on leave of absence may be considered as still in the employ of the Company or a Related Entity for purposes of eligibility for participation in the Plan.

(u) "Employee" means any person, including an officer or Director, who is an employee of the Company or any Related Entity. The Payment of a director's fee by the Company or a Related Entity shall not be sufficient to constitute "employment" by the Company.

(v) "Exchange Act" means the Securities Exchange Act of 1934, as amended from time to time, including rules thereunder and successor provisions and rules thereto.

(w) "Executive Officer" means an executive officer of the Company as defined under the Exchange Act.

(x) "Fair Market Value" means the fair market value of Stock, Awards or other property as determined by the Committee or the Board, or under procedures established by the Committee or the Board. Unless otherwise determined by the Committee or the Board, the Fair Market Value of Stock as of any given date after which the Company is a Publicly Held Corporation shall be the closing sale price per share reported on a consolidated basis for stock listed on the principal stock exchange or market on which Stock is traded on the date as of which such value is being determined or, if there is no sale on that date, then on the last previous day on which a sale was reported.

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(y) "Good Reason" shall, with respect to any Participant, have the equivalent meaning (or the same meaning as "good reason" or "for good reason") set forth in any employment agreement between the Participant and the Company or a Related Entity or, in the absence of any such agreement, such term shall mean (i) the assignment to the Participant of any duties inconsistent in any respect with the Participant's position (including status, offices, titles and reporting requirements), authority, duties or responsibilities as assigned by the Company (or a Related Entity), or any other action by the Company (or a Related Entity) which results in a diminution in such position, authority, duties or responsibilities, excluding for this purpose an isolated, insubstantial and inadvertent action not taken in bad faith and which is remedied by the Company (or a Related Entity) promptly after receipt of notice thereof given by the Participant; (ii) any failure by the Company (or a Related Entity) to comply with its obligations to the Participant as agreed upon, other than an isolated, insubstantial and inadvertent failure not occurring in bad faith and which is remedied by the Company (or a Related Entity) promptly after receipt of notice thereof given by the Participant; (iii) the Company's (or Related Entity's) requiring the Participant to be based at any office or location outside of fifty miles from the location of employment as of the date of Award, except for travel reasonably required in the performance of the Participant's responsibilities; (iv) any purported termination by the Company (or a Related Entity) of the Participant's Continuous Service otherwise than for Cause as defined in Section 2(f), or by reason of the Participant's Disability as defined in Section 2(o), prior to the Expiration Date. For purposes of this Section 2(v), any good faith determination of "Good Reason" made by the Company shall be conclusive.

(z) "Incentive Stock Option" means any Option intended to be designated as an incentive stock option within the meaning of Section 422 of the Code or any successor provision thereto.

(aa) [Reserved]

(bb) "Limited Stock Appreciation Right" means a right granted to a Participant under Section 6(c) hereof.



(cc) "Option" means a right granted to a Participant under Section 6(b) hereof, to purchase Stock or other Awards at a specified price during specified time periods.

(dd) "Optionee" means a person to whom an Option or Incentive Stock Option is granted under this Plan or any person who succeeds to the rights of such person under this Plan.

(ee) "Other Stock-Based Awards" means Awards granted to a Participant under Section 6(h) hereof.

(ff) "Parent" means any corporation (other than the Company), whether now or hereafter existing, in an unbroken chain of corporations ending with the Company, if each of the corporations in the chain (other than the Company) owns stock possessing 50 percent or more of the combined voting power of all classes of stock in one of the other corporations in the chain.

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(gg) "Participant" means a person who has been granted an Award under the Plan which remains outstanding, including a person who is no longer an Eligible Person.

(hh) "Performance Award" means a right, granted to an Eligible Person under Section 8 hereof, to receive Awards based upon performance criteria specified by the Committee or the Board.

(ii) "Person" shall have the meaning ascribed to such term in Section 3(a)(9) of the Exchange Act and used in Sections 13(d) and 14(d) thereof, and shall include a "group" as defined in Section 13(d) thereof.

(jj) "Publicly Held Corporation" shall mean a publicly held corporation as that term is used under Section 162(m)(2) of the Code.

(kk) "Related Entity" means any Parent, Subsidiary and any business, corporation, partnership, limited liability company or other entity in which the Company, a Parent or a Subsidiary holds a substantial ownership interest, directly or indirectly.

(ll) "Restricted Stock" means Stock granted to a Participant under Section 6(d) hereof, that is subject to certain restrictions and to a risk of forfeiture.

(mm) "Rule 16b-3" and "Rule 16a-1(c)(3)" means Rule 16b-3 and Rule 16a-1(c)(3), as from time to time in effect and applicable to the Plan and Participants, promulgated by the Securities and Exchange Commission under Section 16 of the Exchange Act.

(nn) "Stock" means the Company's Common Stock, and such other securities as may be substituted (or resubstituted) for Stock pursuant to Section 10(c) hereof.

(oo) "Stock Appreciation Right" means a right granted to a Participant under Section 6(c) hereof.

(pp) "Subsidiary" means any corporation (other than the Company), whether now or hereafter existing, in an unbroken chain of corporations beginning with the Company, if each of the corporations other than the last corporation in the unbroken chain owns stock possessing 50 percent or more of the total combined voting power of all classes of stock in one of the other corporations in such chain.

### 3. Administration.

(a) Authority of the Committee. The Plan shall be administered by the Committee; provided, however, that except as otherwise expressly provided in this Plan or, during the period that the Company is a Publicly Held Corporation, in order to comply with Code Section 162(m) or Rule 16b-3 under the Exchange Act, the Board may exercise any power or authority granted to the Committee under this Plan. The Committee or the Board shall have full and final authority, in each case subject to and consistent with the provisions of the Plan, to select Eligible Persons to become Participants, grant Awards, determine

the type, number and other terms and conditions of, and all other matters relating to, Awards, prescribe Award agreements (which need not be identical for each Participant) and rules and regulations for the

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administration of the Plan, construe and interpret the Plan and Award agreements and correct defects, supply omissions or reconcile inconsistencies therein, and to make all other decisions and determinations as the Committee or the Board may deem necessary or advisable for the administration of the Plan. In exercising any discretion granted to the Committee or the Board under the Plan or pursuant to any Award, the Committee or the Board shall not be required to follow past practices, act in a manner consistent with past practices, or treat any Eligible Person in a manner consistent with the treatment of other Eligible Persons.

(b) Manner of Exercise of Committee Authority. In the event that the Company is or becomes a Publicly Held Corporation, the Committee, and not the Board, shall exercise sole and exclusive discretion on any matter relating to a Participant then subject to Section 16 of the Exchange Act with respect to the Company to the extent necessary in order that transactions by such Participant shall be exempt under Rule 16b-3 under the Exchange Act. Any action of the Committee or the Board shall be final, conclusive and binding on all persons, including the Company, its Related Entities, Participants, Beneficiaries, transferees under Section 10(b) hereof or other persons claiming rights from or through a Participant, and shareholders. The express grant of any specific power to the Committee or the Board, and the taking of any action by the Committee or the Board, shall not be construed as limiting any power or authority of the Committee or the Board. The Committee or the Board may delegate to officers or managers of the Company or any Related Entity, or committees thereof, the authority, subject to such terms as the Committee or the Board shall determine, (i) to perform administrative functions, (ii) with respect to Participants not subject to Section 16 of the Exchange Act, to perform such other functions as the Committee or the Board may determine, and (iii) with respect to Participants subject to Section 16, to perform such other functions of the Committee or the Board as the Committee or the Board may determine to the extent performance of such functions will not result in the loss of an exemption under Rule 16b-3 otherwise available for transactions by such persons, in each case to the extent permitted under applicable law and subject to the requirements set forth in Section 7(d). The Committee or the Board may appoint agents to assist it in administering the Plan.

(c) Limitation of Liability. The Committee and the Board, and each member thereof, shall be entitled to, in good faith, rely or act upon any report or other information furnished to him or her by any Executive Officer, other officer or Employee, the Company's independent auditors, Consultants or any other agents assisting in the administration of the Plan. Members of the Committee and the Board, and any officer or Employee acting at the direction or on behalf of the Committee or the Board, shall not be personally liable for any action or determination taken or made in good faith with respect to the Plan, and shall, to the extent permitted by law, be fully indemnified and protected by the Company with respect to any such action or determination.

#### 4. Stock Subject to Plan.

(a) Limitation on Overall Number of Shares Subject to Awards. Subject to adjustment as provided in Section 10(c) hereof, the total number of shares of Stock reserved and available for delivery in connection with Awards under the Plan shall be the sum of (i) 1,000,000, plus (ii) the number of shares with respect to Awards previously granted under the Plan that terminate without being exercised, expire, are forfeited or canceled, and the number of

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shares of Stock that are surrendered in payment of any Awards or any tax withholding with regard thereto. In the event an Initial Public Offering ("IPO") of the shares of the Company's Stock occurs, the overall number of shares of the Company's Stock subject to Awards shall be further increased by 6% of the total number of shares of the Company's Stock outstanding immediately following the IPO, plus, on the first day of each subsequent calendar quarter, an additional 1.5% of the total number of shares of the Company's Stock outstanding on that day, provided, however, that at no time shall the number of shares of the

Company's Stock subject to Awards exceed 30% of the then outstanding shares of the Company's Stock (counting convertible preferred and convertible senior common shares as if converted), unless a greater percentage is approved by a vote of at least two-thirds of the securities entitled to vote, or a determination is made by counsel for the Company that such restriction is not required by applicable federal or state securities laws under the circumstances. Any shares of Stock delivered under the Plan may consist, in whole or in part, of authorized and unissued shares or treasury shares.

(b) Limitation on Number of Incentive Stock Option Shares.

Subject to adjustment as provided in Section 10(c) hereof, the number of shares of Stock which may be issued pursuant to Incentive Stock Options shall be the lesser of (i) the number of Shares that may be subject to Awards under Section 4(a), or (ii) 15,000,000.

(c) Application of Limitations. The limitation contained in this Section 4 shall apply not only to Awards that are settleable by the delivery of shares of Stock but also to Awards relating to shares of Stock but settleable only in cash (such as cash-only Stock Appreciation Rights). The Committee or the Board may adopt reasonable counting procedures to ensure appropriate counting, avoid double counting (as, for example, in the case of tandem or substitute awards) and make adjustments if the number of shares of Stock actually delivered differs from the number of shares previously counted in connection with an Award.

5. Eligibility; Per-Person Award Limitations. Awards may be granted under the Plan only to Eligible Persons. In each fiscal year during any part of which the Plan is in effect, an Eligible Person may not be granted Awards relating to more than 1,000,000 shares of Stock, subject to adjustment as provided in Section 10(c), under each of Sections 6(b), 6(c), 6(d), 6(e), 6(f), 6(g), 6(h), 7(b) and 7(c). In addition, the maximum amount that may be earned as an Annual Incentive Award or other cash Award in any fiscal year by any one Participant shall be \$2,000,000, and the maximum amount that may be earned as a Performance Award or other cash Award in respect of a performance period by any one Participant shall be \$5,000,000.

6. Specific Terms of Awards.

(a) General. Awards may be granted on the terms and conditions set forth in this Section 6. In addition, the Committee or the Board may impose on any Award or the exercise thereof, at the date of grant or thereafter (subject to Section 10(e)), such additional terms and conditions, not inconsistent with the provisions of the Plan, as the Committee or the Board shall determine, including terms requiring forfeiture of Awards in the event of termination of Continuous Service by the Participant and terms permitting a Participant to make elections relating to his or her Award. The Committee or the Board shall retain full power and discretion to accelerate, waive or modify, at any time, any term or condition of an Award that is not

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mandatory under the Plan. Except in cases in which the Committee or the Board is authorized to require other forms of consideration under the Plan, or to the extent other forms of consideration must be paid to satisfy the requirements of California law, no consideration other than services may be required for the grant (but not the exercise) of any Award.

(b) Options. The Committee and the Board each is authorized to grant Options to Participants on the following terms and conditions:

(i) Stock Option Agreement. Each grant of an Option under the Plan shall be evidenced by a Stock Option Agreement. Such Stock Option Agreement shall be subject to all applicable terms and conditions of the Plan and may be subject to any other terms and conditions which are not inconsistent with the Plan and which the Committee or the Board deems appropriate for inclusion in a Stock Option Agreement. The provisions of the various Stock Option Agreements entered into under the Plan need not be identical.

(ii) Number of Shares. Each Stock Option Agreement shall specify the number of shares of Stock that are subject to the Option and shall provide for the adjustment of such

number in accordance with Section 10(c) hereof. The Stock Option Agreement shall also specify whether the Stock Option is an Incentive Stock Option or a Non-Qualified Stock Option.

(iii) Exercise Price.

(A) In General. Each Stock Option Agreement shall state the price at which shares of Stock subject to the Option may be purchased (the "Exercise Price"), which shall be, with respect to Incentive Stock Options, not less than 100% of the Fair Market Value of the Stock on the date of grant. In the case of Non-Qualified Stock Options, the Exercise Price shall be determined in the sole discretion of the Committee or the Board; provided, however, that the Exercise Price shall be no less than 85% of the Fair Market Value of the shares of Stock on the date of grant of the Non-Qualified Stock Option.

(B) Ten Percent Shareholder. If an individual owns or is deemed to own (by reason of the attribution rules applicable under Section 424(d) of the Code) more than 10% of the combined voting power of all classes of stock of the Company or any Related Entity, any Option granted to such individual must comply with the following: (1) the Exercise Price of a Non-Qualified Stock Option must be at least 110% of the Fair Market Value of a share of Stock on the date of grant, or (2) in the case of an Incentive Stock Option, the Exercise Price must be at least 110% of the Fair Market Value of a share of Stock on the date of grant and such Incentive Stock Option by its terms is not exercisable after the expiration of five years from the date of grant.

(C) Non-Applicability. The Exercise Price restriction applicable to Non-Qualified Stock Options required by Sections 6(b)(iii)(A) and 6(b)(iii)(B) shall be inoperative if (1) the offer and sale of the shares of Stock to

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be issued upon payment of the Exercise Price have been registered under a then currently effective registration statement under applicable federal or state securities laws, or (2) a determination is made by counsel for the Company that such Exercise Price restrictions are not required in the circumstances under applicable federal or state securities laws.

(iv) Time and Method of Exercise. The Committee or the Board shall determine the time or times at which or the circumstances under which an Option may be exercised in whole or in part (including based on achievement of performance goals and/or future service requirements), provided that in the case of an Optionee who is not an officer, Director, or Consultant of the Company or a Related Entity, his or her Options shall become exercisable at least as rapidly as 20% per year, over a 5 year period commencing on the date of the grant, unless a determination is made by counsel for the Company that such vesting requirements are not required in the circumstances under applicable federal or state securities laws. The Board or the Committee may also determine the time or times at which Options shall cease to be or become exercisable following termination of Continuous Service or upon other conditions; provided, however, if the Optionee's Continuous Service is terminated for any reason other than Cause, that portion of the Option that is exercisable as of the date of termination shall remain exercisable for at least 6 months from the date of termination if by reason of death or Disability, and for at least 30 days from the date of termination if by reason other than the Optionee's death or Disability. The Board or the Committee may determine the methods by which such exercise price may be paid or deemed to be paid (including in the discretion of the Committee or the Board a cashless exercise procedure), the form of such

payment, including, without limitation, cash, Stock, other Awards or awards granted under other plans of the Company or a Related Entity, or other property (including notes or other contractual obligations of Participants to make payment on a deferred basis), and the methods by or forms in which Stock will be delivered or deemed to be delivered to Participants.

(v) Incentive Stock Options. The terms of any Incentive Stock Option granted under the Plan shall comply in all respects with the provisions of Section 422 of the Code. Anything in the Plan to the contrary notwithstanding, no term of the Plan relating to Incentive Stock Options (including any Stock Appreciation Rights in tandem therewith) shall be interpreted, amended or altered, nor shall any discretion or authority granted under the Plan be exercised, so as to disqualify either the Plan or any Incentive Stock Option under Section 422 of the Code, unless the Participant has first requested the change that will result in such disqualification. Thus, if and to the extent required to comply with Section 422 of the Code, Options granted as Incentive Stock Options shall be subject to the following special terms and conditions:

(A) the Option shall not be exercisable more than ten years after the date such Incentive Stock Option is granted; provided, however, that if a Participant owns or is deemed to own (by reason of the attribution rules of Section

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424(d) of the Code) more than 10% of the combined voting power of all classes of stock of the Company or any Parent Corporation and the Incentive Stock Option is granted to such Participant, the term of the Incentive Stock Option shall be (to the extent required by the Code at the time of the grant) for no more than five years from the date of grant; and

(B) The aggregate Fair Market Value (determined as of the date the Incentive Stock Option is granted) of the shares of stock with respect to which Incentive Stock Options granted under the Plan and all other option plans of the Company or its Parent Corporation during any calendar year exercisable for the first time by the Participant during any calendar year shall not (to the extent required by the Code at the time of the grant) exceed \$100,000.

(vi) Repurchase Rights. The Committee and the Board shall have the discretion to grant Options which are exercisable for unvested shares of Common Stock. Should the Optionee's Continuous Service cease while holding such unvested shares, the Company shall have the right to repurchase, at the exercise price paid per share, any or all of those unvested shares. The terms upon which such repurchase right shall be exercisable (including the period and procedure for exercise and the appropriate vesting schedule for the purchased shares) shall be established by the Committee or the Board and set forth in the document evidencing such repurchase right.

(c) Stock Appreciation Rights. The Committee and the Board each is authorized to grant Stock Appreciation Rights to Participants on the following terms and conditions:

(i) Right to Payment. A Stock Appreciation Right shall confer on the Participant to whom it is granted a right to receive, upon exercise thereof, the excess of (A) the Fair Market Value of one share of stock on the date of exercise (or, in the case of a "Limited Stock Appreciation Right" that may be exercised only in the event of a Change in Control, the Fair Market Value determined by reference to the Change in Control Price, as defined under Section 9(c) hereof), over (B) the grant price of the Stock Appreciation Right as determined

by the Committee or the Board. The grant price of a Stock Appreciation Right shall not be less than the Fair Market Value of a share of Stock on the date of grant except as provided under Section 8(a) hereof.

(ii) Other Terms. The Committee or the Board shall determine at the date of grant or thereafter, the time or times at which and the circumstances under which a Stock Appreciation Right may be exercised in whole or in part (including based on achievement of performance goals and/or future service requirements), the time or times at which Stock Appreciation Rights shall cease to be or become exercisable following termination of Continuous Service or upon other conditions, the method of exercise, method of settlement, form of consideration payable in settlement, method by or forms in which Stock will be delivered or deemed to be delivered to Participants, whether or not a Stock Appreciation Right shall be in

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tandem or in combination with any other Award, and any other terms and conditions of any Stock Appreciation Right. Limited Stock Appreciation Rights that may only be exercised in connection with a Change in Control or other event as specified by the Committee or the Board, may be granted on such terms, not inconsistent with this Section 6(c), as the Committee or the Board may determine. Stock Appreciation Rights and Limited Stock Appreciation Rights may be either freestanding or in tandem with other Awards.

(d) Restricted Stock. The Committee and the Board each is authorized to grant Restricted Stock to Participants on the following terms and conditions:

(i) Grant and Restrictions. Restricted Stock shall be subject to such restrictions on transferability, risk of forfeiture and other restrictions, if any, as the Committee or the Board may impose, or as otherwise provided in this Plan. The restrictions may lapse separately or in combination at such times, under such circumstances (including based on achievement of performance goals and/or future service requirements), in such installments or otherwise, as the Committee or the Board may determine at the date of grant or thereafter. Except to the extent restricted under the terms of the Plan and any Award agreement relating to the Restricted Stock, a Participant granted Restricted Stock shall have all of the rights of a shareholder, including the right to vote the Restricted Stock and the right to receive dividends thereon (subject to any mandatory reinvestment or other requirement imposed by the Committee or the Board). During the restricted period applicable to the Restricted Stock, subject to Section 10(b) below, the Restricted Stock may not be sold, transferred, pledged, hypothecated, margined or otherwise encumbered by the Participant.

(ii) Forfeiture. Except as otherwise determined by the Committee or the Board at the time of the Award, upon termination of a Participant's Continuous Service during the applicable restriction period, the Participant's Restricted Stock that is at that time subject to restrictions shall be forfeited and reacquired by the Company; provided that the Committee or the Board may provide, by rule or regulation or in any Award agreement, or may determine in any individual case, that restrictions or forfeiture conditions relating to Restricted Stock shall be waived in whole or in part in the event of terminations resulting from specified causes, and the Committee or the Board may in other cases waive in whole or in part the forfeiture of Restricted Stock.

(iii) Certificates for Stock. Restricted Stock granted under the Plan may be evidenced in such manner as the Committee or the Board shall determine. If certificates

representing Restricted Stock are registered in the name of the Participant, the Committee or the Board may require that such certificates bear an appropriate legend referring to the terms, conditions and restrictions applicable to such Restricted Stock, that the Company retain physical possession of the certificates, and that the Participant deliver a stock power to the Company, endorsed in blank, relating to the Restricted Stock.

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(iv) Dividends and Splits. As a condition to the grant of an Award of Restricted Stock, the Committee or the Board may require that any cash dividends paid on a share of Restricted Stock be automatically reinvested in additional shares of Restricted Stock or applied to the purchase of additional Awards under the Plan. Unless otherwise determined by the Committee or the Board, Stock distributed in connection with a Stock split or Stock dividend, and other property distributed as a dividend, shall be subject to restrictions and a risk of forfeiture to the same extent as the Restricted Stock with respect to which such Stock or other property has been distributed.

(e) Deferred Stock. The Committee and the Board each is authorized to grant Deferred Stock to Participants, which are rights to receive Stock, cash, or a combination thereof at the end of a specified deferral period, subject to the following terms and conditions:

(i) Award and Restrictions. Satisfaction of an Award of Deferred Stock shall occur upon expiration of the deferral period specified for such Deferred Stock by the Committee or the Board (or, if permitted by the Committee or the Board, as elected by the Participant). In addition, Deferred Stock shall be subject to such restrictions (which may include a risk of forfeiture) as the Committee or the Board may impose, if any, which restrictions may lapse at the expiration of the deferral period or at earlier specified times (including based on achievement of performance goals and/or future service requirements), separately or in combination, in installments or otherwise, as the Committee or the Board may determine. Deferred Stock may be satisfied by delivery of Stock, cash equal to the Fair Market Value of the specified number of shares of Stock covered by the Deferred Stock, or a combination thereof, as determined by the Committee or the Board at the date of grant or thereafter. Prior to satisfaction of an Award of Deferred Stock, an Award of Deferred Stock carries no voting or dividend or other rights associated with share ownership.

(ii) Forfeiture. Except as otherwise determined by the Committee or the Board, upon termination of a Participant's Continuous Service during the applicable deferral period thereof to which forfeiture conditions apply (as provided in the Award agreement evidencing the Deferred Stock), the Participant's Deferred Stock that is at that time subject to deferral (other than a deferral at the election of the Participant) shall be forfeited; provided that the Committee or the Board may provide, by rule or regulation or in any Award agreement, or may determine in any individual case, that restrictions or forfeiture conditions relating to Deferred Stock shall be waived in whole or in part in the event of terminations resulting from specified causes, and the Committee or the Board may in other cases waive in whole or in part the forfeiture of Deferred Stock.

(iii) Dividend Equivalents. Unless otherwise determined by the Committee or the Board at date of grant, any Dividend Equivalents that are granted with respect to any Award of Deferred Stock shall be either (A) paid with respect to such Deferred Stock at the dividend payment date in cash or in shares

of unrestricted Stock having a Fair Market Value equal to the amount of such dividends, or (B) deferred with respect to such Deferred Stock and the amount or value thereof automatically deemed reinvested in additional Deferred Stock, other Awards or other investment vehicles, as the Committee or the Board shall determine or permit the Participant to elect.

(f) Bonus Stock and Awards in Lieu of Obligations. The Committee and the Board each is authorized to grant Stock as a bonus, or to grant Stock or other Awards in lieu of Company obligations to pay cash or deliver other property under the Plan or under other plans or compensatory arrangements, provided that, in the case of Participants subject to Section 16 of the Exchange Act, the amount of such grants remains within the discretion of the Committee to the extent necessary to ensure that acquisitions of Stock or other Awards are exempt from liability under Section 16(b) of the Exchange Act. Stock or Awards granted hereunder shall be subject to such other terms as shall be determined by the Committee or the Board.

(g) Dividend Equivalents. The Committee and the Board each is authorized to grant Dividend Equivalents to a Participant entitling the Participant to receive cash, Stock, other Awards, or other property equal in value to dividends paid with respect to a specified number of shares of Stock, or other periodic payments. Dividend Equivalents may be awarded on a free-standing basis or in connection with another Award. The Committee or the Board may provide that Dividend Equivalents shall be paid or distributed when accrued or shall be deemed to have been reinvested in additional Stock, Awards, or other investment vehicles, and subject to such restrictions on transferability and risks of forfeiture, as the Committee or the Board may specify.

(h) Other Stock-Based Awards. The Committee and the Board each is authorized, subject to limitations under applicable law, to grant to Participants such other Awards that may be denominated or payable in, valued in whole or in part by reference to, or otherwise based on, or related to, Stock, as deemed by the Committee or the Board to be consistent with the purposes of the Plan, including, without limitation, convertible or exchangeable debt securities, other rights convertible or exchangeable into Stock, purchase rights for Stock, Awards with value and payment contingent upon performance of the Company or any other factors designated by the Committee or the Board, and Awards valued by reference to the book value of Stock or the value of securities of or the performance of specified Related Entities or business units. The Committee or the Board shall determine the terms and conditions of such Awards. Stock delivered pursuant to an Award in the nature of a purchase right granted under this Section 6(h) shall be purchased for such consideration (including without limitation loans from the Company or a Related Entity), paid for at such times, by such methods, and in such forms, including, without limitation, cash, Stock, other Awards or other property, as the Committee or the Board shall determine. The Committee and the Board shall have the discretion to grant such other Awards which are exercisable for unvested shares of Common Stock. Should the Optionee's Continuous Service cease while holding such unvested shares, the Company shall have the right to repurchase, at the exercise price paid per share, any or all of those unvested shares. The terms upon which such repurchase right shall be exercisable (including the period and procedure for exercise and the appropriate vesting schedule for the purchased shares) shall be established by the Committee or the Board and set forth in the document evidencing such repurchase right. Cash awards, as an element of or supplement to any other Award under the Plan, may also be granted pursuant to this Section 6(h).

## 7. Performance and Annual Incentive Awards.

(a) Performance Conditions. The right of a Participant to exercise or receive a grant or settlement of any Award, and the timing thereof, may be subject to such performance conditions as may be specified by the Committee or the Board. The Committee or the Board may use such business criteria and other measures of performance as it may deem appropriate in establishing any performance conditions, and may exercise its discretion to reduce the amounts payable under any Award subject to performance conditions,



except as limited under Sections 7(b) and 7(c) hereof in the case of a Performance Award or Annual Incentive Award intended to qualify under Code Section 162(m). At such times as the Company is a Publicly Held Corporation, if and to the extent required under Code Section 162(m), any power or authority relating to a Performance Award or Annual Incentive Award intended to qualify under Code Section 162(m), shall be exercised by the Committee and not the Board.

(b) Performance Awards Granted to Designated Covered Employees. If and to the extent that the Committee determines that a Performance Award to be granted to an Eligible Person who is designated by the Committee as likely to be a Covered Employee should qualify as "performance-based compensation" for purposes of Code Section 162(m), the grant, exercise and/or settlement of such Performance Award shall be contingent upon achievement of pre-established performance goals and other terms set forth in this Section 7(b).

(i) Performance Goals Generally. The performance goals for such Performance Awards shall consist of one or more business criteria and a targeted level or levels of performance with respect to each of such criteria, as specified by the Committee consistent with this Section 7(b). Performance goals shall be objective and shall otherwise meet the requirements of Code Section 162(m) and regulations thereunder including the requirement that the level or levels of performance targeted by the Committee result in the achievement of performance goals being "substantially uncertain." The Committee may determine that such Performance Awards shall be granted, exercised and/or settled upon achievement of any one performance goal or that two or more of the performance goals must be achieved as a condition to grant, exercise and/or settlement of such Performance Awards. Performance goals may differ for Performance Awards granted to any one Participant or to different Participants.

(ii) Business Criteria. One or more of the following business criteria for the Company, on a consolidated basis, and/or specified Related Entities or business units of the Company (except with respect to the total shareholder return and earnings per share criteria), shall be used exclusively by the Committee in establishing performance goals for such Performance Awards: (1) total shareholder return; (2) such total shareholder return as compared to total return (on a comparable basis) of a publicly available index such as, but not limited to, the Standard & Poor's 500 Stock Index or the S&P Specialty Retailer Index; (3) net income; (4) pretax earnings; (5) earnings before interest expense, taxes, depreciation and amortization; (6) pretax operating earnings after interest expense and before bonuses, service fees, and extraordinary or special items; (7) operating margin; (8) earnings per share; (9) return on equity; (10) return on capital; (11)

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return on investment; (12) operating earnings; (13) working capital or inventory; and (14) ratio of debt to shareholders' equity. One or more of the foregoing business criteria shall also be exclusively used in establishing performance goals for Annual Incentive Awards granted to a Covered Employee under Section 7(c) hereof that are intended to qualify as "performance-based compensation under Code Section 162(m).

(iii) Performance Period; Timing For Establishing Performance Goals. Achievement of performance goals in respect of such Performance Awards shall be measured over a performance period of up to ten years, as specified by the Committee. Performance goals shall be established not later than 90 days after the beginning of any performance period applicable to such Performance Awards, or at such other date as may be required or permitted for "performance-based compensation" under Code Section 162(m).

(iv) Performance Award Pool. The Committee may establish a Performance Award pool, which shall be an unfunded pool, for purposes of measuring Company performance in connection with Performance Awards. The amount of such Performance Award pool shall be based upon the achievement of a performance goal or goals based on one or more of the business criteria set forth in Section 7(b)(ii) hereof during the given performance period, as specified by the Committee in accordance with Section 7(b)(iii) hereof. The Committee may specify the amount of the Performance Award pool as a percentage of any of such business criteria, a percentage thereof in excess of a threshold amount, or as another amount which need not bear a strictly mathematical relationship to such business criteria.

(v) Settlement of Performance Awards; Other Terms. Settlement of such Performance Awards shall be in cash, Stock, other Awards or other property, in the discretion of the Committee. The Committee may, in its discretion, reduce the amount of a settlement otherwise to be made in connection with such Performance Awards. The Committee shall specify the circumstances in which such Performance Awards shall be paid or forfeited in the event of termination of Continuous Service by the Participant prior to the end of a performance period or settlement of Performance Awards.

(c) Annual Incentive Awards Granted to Designated Covered Employees. The Committee may, within its discretion, grant one or more Annual Incentive Awards to any Eligible Person, subject to the terms and conditions set forth in this Section 7(c).

(i) Annual Incentive Award Pool. The Committee may establish an Annual Incentive Award pool, which shall be an unfunded pool, for purposes of measuring Company performance in connection with Annual Incentive Awards. In the case of Annual Incentive Awards intended to qualify as "performance-based compensation" for purposes of Code Section 162(m), the amount of such Annual Incentive Award pool shall be based upon the achievement of a performance goal or goals based on one or more of the business criteria set forth

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in Section 7(b)(ii) hereof during the given performance period, as specified by the Committee in accordance with Section 7(b)(iii) hereof. The Committee may specify the amount of the Annual Incentive Award pool as a percentage of any such business criteria, a percentage thereof in excess of a threshold amount, or as another amount which need not bear a strictly mathematical relationship to such business criteria.

(ii) Potential Annual Incentive Awards. Not later than the end of the 90th day of each fiscal year, or at such other date as may be required or permitted in the case of Awards intended to be "performance-based compensation" under Code Section 162(m), the Committee shall determine the Eligible Persons who will potentially receive Annual Incentive Awards, and the amounts potentially payable thereunder, for that fiscal year, either out of an Annual Incentive Award pool established by such date under Section 7(c)(i) hereof or as individual Annual Incentive Awards. In the case of individual Annual Incentive Awards intended to qualify under Code Section 162(m), the amount potentially payable shall be based upon the achievement of a performance goal or goals based on one or more of the business criteria set forth in Section 7(b)(ii) hereof in the given performance year, as specified by the Committee; in other cases, such amount shall be based on such criteria as shall be established by the Committee. In all cases, the maximum Annual Incentive Award of any Participant shall be subject to the limitation set forth in Section 5 hereof.

(iii) Payout of Annual Incentive Awards. After the

end of each fiscal year, the Committee shall determine the amount, if any, of (A) the Annual Incentive Award pool, and the maximum amount of potential Annual Incentive Award payable to each Participant in the Annual Incentive Award pool, or (B) the amount of potential Annual Incentive Award otherwise payable to each Participant. The Committee may, in its discretion, determine that the amount payable to any Participant as an Annual Incentive Award shall be reduced from the amount of his or her potential Annual Incentive Award, including a determination to make no Award whatsoever. The Committee shall specify the circumstances in which an Annual Incentive Award shall be paid or forfeited in the event of termination of Continuous Service by the Participant prior to the end of a fiscal year or settlement of such Annual Incentive Award.

(d) Written Determinations. All determinations by the Committee as to the establishment of performance goals, the amount of any Performance Award pool or potential individual Performance Awards and as to the achievement of performance goals relating to Performance Awards under Section 7(b), and the amount of any Annual Incentive Award pool or potential individual Annual Incentive Awards and the amount of final Annual Incentive Awards under Section 7(c), shall be made in writing in the case of any Award intended to qualify under Code Section 162(m). The Committee may not delegate any responsibility relating to such Performance Awards or Annual Incentive Awards if and to the extent required to comply with Code Section 162(m).

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(e) Status of Section 7(b) and Section 7(c) Awards Under Code Section 162(m). It is the intent of the Company that Performance Awards and Annual Incentive Awards under Section 7(b) and 7(c) hereof granted to persons who are designated by the Committee as likely to be Covered Employees within the meaning of Code Section 162(m) and regulations thereunder shall, if so designated by the Committee, constitute "qualified performance-based compensation" within the meaning of Code Section 162(m) and regulations thereunder. Accordingly, the terms of Sections 7(b), (c), (d) and (e), including the definitions of Covered Employee and other terms used therein, shall be interpreted in a manner consistent with Code Section 162(m) and regulations thereunder. The foregoing notwithstanding, because the Committee cannot determine with certainty whether a given Participant will be a Covered Employee with respect to a fiscal year that has not yet been completed, the term Covered Employee as used herein shall mean only a person designated by the Committee, at the time of grant of Performance Awards or an Annual Incentive Award, as likely to be a Covered Employee with respect to that fiscal year. If any provision of the Plan or any agreement relating to such Performance Awards or Annual Incentive Awards does not comply or is inconsistent with the requirements of Code Section 162(m) or regulations thereunder, such provision shall be construed or deemed amended to the extent necessary to conform to such requirements.

8. Certain Provisions Applicable to Awards or Sales.

(a) Stand-Alone, Additional, Tandem, and Substitute Awards. Awards granted under the Plan may, in the discretion of the Committee or the Board, be granted either alone or in addition to, in tandem with, or in substitution or exchange for, any other Award or any award granted under another plan of the Company, any Related Entity, or any business entity to be acquired by the Company or a Related Entity, or any other right of a Participant to receive payment from the Company or any Related Entity. Such additional, tandem, and substitute or exchange Awards may be granted at any time. If an Award is granted in substitution or exchange for another Award or award, the Committee or the Board shall require the surrender of such other Award or award in consideration for the grant of the new Award. In addition, Awards may be granted in lieu of cash compensation, including in lieu of cash amounts payable under other plans of the Company or any Related Entity, in which the value of Stock subject to the Award is equivalent in value to the cash compensation (for example, Deferred Stock or Restricted Stock), or in which the exercise price, grant price or purchase price of the Award in the nature of a right that may be exercised is equal to the Fair Market Value of the underlying Stock minus the value of the cash compensation surrendered (for example, Options granted with an exercise price "discounted" by the amount of the cash compensation surrendered).

(b) Term of Awards. The term of each Award shall be for such

period as may be determined by the Committee or the Board; provided that in no event shall the term of any Option or Stock Appreciation Right exceed a period of ten years (or such shorter term as may be required in respect of an Incentive Stock Option under Section 422 of the Code).

(c) Purchase Prices.

(i) In General. In the case of an Award under this Plan, other than an Option, which grants an Employee, Director, or Consultant of the Company the right to purchase Stock, the Board or the Committee shall have discretion to set

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the purchase price, provided that in no event shall the purchase price per share of Stock be less than 85% of the Fair Market Value of such share on the date of the Award or the date of the purchase, and in the case of an Award made to an Employee who owns or is deemed to own (by reason of the attribution rules applicable under Section 424(d) of the Code) more than 10% of the combined voting power of all classes of Stock of the Company, the Parent Corporation or a Subsidiary, the purchase price of such Stock shall be no less than 100% of the Fair Market Value of the Stock on the date of such award or the date of the purchase.

(ii) Non-Applicability of Restrictions. The Purchase Price restrictions contained in Section 8(c) (i) applicable to Awards under this Plan, other than Options, which grant an Employee, Director, or Consultant of the Company the right to purchase Stock, shall be inoperative if (A) the offer and sale of the shares of Stock to be issued upon payment of the Exercise Price have been registered under a then currently effective registration statement under applicable federal or state securities laws, or (B) a determination is made by counsel for the Company that such Exercise Price restrictions are not required in the circumstances under applicable federal or state securities laws.

(d) Form and Timing of Payment Under Awards; Deferrals.

Subject to the terms of the Plan and any applicable Award agreement, payments to be made by the Company or a Related Entity upon the exercise of an Option or other Award or settlement of an Award may be made in such forms as the Committee or the Board shall determine, including, without limitation, cash, other Awards or other property, and may be made in a single payment or transfer, in installments, or on a deferred basis. The settlement of any Award may be accelerated, and cash paid in lieu of Stock in connection with such settlement, in the discretion of the Committee or the Board or upon occurrence of one or more specified events (in addition to a Change in Control). Installment or deferred payments may be required by the Committee or the Board (subject to Section 10(e) of the Plan) or permitted at the election of the Participant on terms and conditions established by the Committee or the Board. Payments may include, without limitation, provisions for the payment or crediting of a reasonable interest rate on installment or deferred payments or the grant or crediting of Dividend Equivalents or other amounts in respect of installment or deferred payments denominated in Stock.

(e) Exemptions from Section 16(b) Liability. If and to the extent that the Company is or becomes a Publicly Held Corporation, it is the intent of the Company that this Plan comply in all respects with applicable provisions of Rule 16b-3 or Rule 16a-1(c) (3) to the extent necessary to ensure that neither the grant of any Awards to nor other transaction by a Participant who is subject to Section 16 of the Exchange Act is subject to liability under Section 16(b) thereof (except for transactions acknowledged in writing to be non-exempt by such Participant). Accordingly, if any provision of this Plan or any Award agreement does not comply with the requirements of Rule 16b-3 or Rule 16a-1(c) (3) as then applicable to any such transaction, such provision will be construed or deemed amended to the extent necessary to conform to the applicable requirements of Rule 16b-3 or Rule 16a-1(c) (3) so that such Participant shall avoid liability under Section 16(b). In addition, the purchase price of any Award conferring a right to purchase Stock shall be not less than any specified percentage of the

Fair Market Value of Stock at the date of grant of the Award then required in order to comply with Rule 16b-3.

9. Change in Control.

(a) Effect of "Change in Control." The effect of a "Change in Control," as defined in Section 9(b) below, shall be as provided, if at all, (1) in an employment, compensation, or severance agreement, if any, between the Company or any Related Entity and the Participant, relating to the Participant's employment, compensation, or severance with or from the Company or such Related Entity, or (2) in the agreement evidencing the Award.

(b) Definition of "Change in Control." A "Change in Control" shall be defined as it is defined, if at all, (1) in an employment, compensation, or severance agreement, if any, between the Company or any Related Entity and the Participant, relating to the Participant's employment, compensation, or severance with or from the Company or such Related Entity, or (2) in the agreement evidencing the Award to such Participant.

(c) Definition of "Change in Control Price." The "Change in Control Price" shall be defined as it is defined, if at all, (1) in an employment, compensation, or severance agreement, if any, between the Company or any Related Entity and the Participant, relating to the Participant's employment, compensation, or severance with or from the Company or such Related Entity, or (2) in the agreement evidencing the Award to such Participant."

10. General Provisions.

(a) Compliance With Legal and Other Requirements. The Company may, to the extent deemed necessary or advisable by the Committee or the Board, postpone the issuance or delivery of Stock or payment of other benefits under any Award until completion of such registration or qualification of such Stock or other required action under any federal or state law, rule or regulation, listing or other required action with respect to any stock exchange or automated quotation system upon which the Stock or other Company securities are listed or quoted, or compliance with any other obligation of the Company, as the Committee or the Board, may consider appropriate, and may require any Participant to make such representations, furnish such information and comply with or be subject to such other conditions as it may consider appropriate in connection with the issuance or delivery of Stock or payment of other benefits in compliance with applicable laws, rules, and regulations, listing requirements, or other obligations. The foregoing notwithstanding, in connection with a Change in Control, the Company shall take or cause to be taken no action, and shall undertake or permit to arise no legal or contractual obligation, that results or would result in any postponement of the issuance or delivery of Stock or payment of benefits under any Award or the imposition of any other conditions on such issuance, delivery or payment, to the extent that such postponement or other condition would represent a greater burden on a Participant than existed on the 90th day preceding the Change in Control.

(b) Limits on Transferability; Beneficiaries.

(i) General. Except as provided herein, a Participant may not assign, sell, transfer, or otherwise encumber or subject to any lien any Award or other

right or interest granted under this Plan, in whole or in part, including any Award or right which constitutes a derivative security as generally defined in Rule 16a1(c) under the Exchange Act, other than by will or by operation of the laws of descent and distribution, and such Awards or rights that may be exercisable shall be exercised during the lifetime of the Participant only by the Participant or his or her guardian or legal representative.

(ii) Permitted Transfer of Option. The Committee or Board, in its sole discretion, may permit the transfer of an

Option (but not an Incentive Stock Option, or any other right to purchase Stock other than an Option) as follows: (A) by gift to a member of the Participant's Immediate Family or (B) by transfer by instrument to a trust providing that the Option is to be passed to beneficiaries upon death of the Optionee. For purposes of this Section 10(b)(ii), "Immediate Family" shall mean the Optionee's spouse (including a former spouse subject to terms of a domestic relations order); child, stepchild, grandchild, child-in-law; parent, stepparent, grandparent, parent-in-law; sibling and sibling-in-law, and shall include adoptive relationships. If a determination is made by counsel for the Company that the restrictions contained in this Section 10(b)(ii) are not required by applicable federal or state securities laws under the circumstances, then the Committee or Board, in its sole discretion, may permit the transfer of Awards (other than Incentive Stock Options and Stock Appreciation Rights in tandem therewith) to one or more Beneficiaries or other transferees during the lifetime of the Participant, which may be exercised by such transferees in accordance with the terms of such Award, but only if and to the extent permitted by the Committee or the Board pursuant to the express terms of an Award agreement (subject to any terms and conditions which the Committee or the Board may impose thereon, and further subject to any prohibitions and restrictions on such transfers pursuant to Rule 16b-3). A Beneficiary, transferee, or other person claiming any rights under the Plan from or through any Participant shall be subject to all terms and conditions of the Plan and any Award agreement applicable to such Participant, except as otherwise determined by the Committee or the Board, and to any additional terms and conditions deemed necessary or appropriate by the Committee or the Board.

(c) Adjustments.

(i) Adjustments to Awards. In the event that any dividend or other distribution (whether in the form of cash, Stock, or other property), recapitalization, forward or reverse split, reorganization, merger, consolidation, spin-off, combination, repurchase, share exchange, liquidation, dissolution or other similar corporate transaction or event affects the Stock and/or such other securities of the Company or any other issuer such that a substitution, exchange, or adjustment is determined by the Committee or the Board to be appropriate, then the Committee or the Board shall, in such manner as it may deem equitable, substitute, exchange, or adjust any or all of (A) the number and kind of shares of Stock which may be delivered in connection with Awards granted thereafter, (B) the number and kind of shares of Stock by which annual per-person Award

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limitations are measured under Section 5 hereof, (C) the number and kind of shares of Stock subject to or deliverable in respect of outstanding Awards, (E) the exercise price, grant price or purchase price relating to any Award and/or make provision for payment of cash or other property in respect of any outstanding Award, and (F) any other aspect of any Award that the Committee or the Board determines to be appropriate.

(ii) Adjustments in Case of Certain Corporate Transactions. In the event of a proposed sale of all or substantially all of the Company's assets or any reorganization, merger, consolidation, or other form of corporate transaction in which the Company does not survive, or in which the shares of Stock are exchanged for or converted into securities issued by another entity, then the successor or acquiring entity or an affiliate thereof may, with the consent of the Committee or the Board, assume each outstanding Option or substitute an equivalent option or right. If the successor or acquiring entity or an affiliate thereof, does

not cause such an assumption or substitution, then each Option shall terminate upon the consummation of sale, merger, consolidation, or other corporate transaction. The Committee or the Board shall give written notice of any proposed transaction referred to in this Section 10(c)(ii) a reasonable period of time prior to the closing date for such transaction (which notice may be given either before or after the approval of such transaction), in order that Optionees may have a reasonable period of time prior to the closing date of such transaction within which to exercise any Options that are then exercisable (including any Options that may become exercisable upon the closing date of such transaction). An Optionee may condition his exercise of any Option upon the consummation of the transaction.

(iii) Other Adjustments. In addition, the Committee (and the Board if and only to the extent such authority is not required to be exercised by the Committee to comply with Code Section 162(m)) is authorized to make adjustments in the terms and conditions of, and the criteria included in, Awards (including Performance Awards and performance goals, and Annual Incentive Awards and any Annual Incentive Award pool or performance goals relating thereto) in recognition of unusual or nonrecurring events (including, without limitation, acquisitions and dispositions of businesses and assets) affecting the Company, any Related Entity or any business unit, or the financial statements of the Company or any Related Entity, or in response to changes in applicable laws, regulations, accounting principles, tax rates and regulations or business conditions or in view of the Committee's assessment of the business strategy of the Company, any Related Entity or business unit thereof, performance of comparable organizations, economic and business conditions, personal performance of a Participant, and any other circumstances deemed relevant; provided that no such adjustment shall be authorized or made if and to the extent that such authority or the making of such adjustment would cause Options, Stock Appreciation Rights, Performance Awards granted under Section 8(b) hereof or Annual Incentive Awards granted under Section 8(c) hereof to Participants designated by the Committee as Covered Employees and intended to qualify as "performance-based

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compensation" under Code Section 162(m) and the regulations thereunder to otherwise fail to qualify as "performance-based compensation" under Code Section 162(m) and regulations thereunder.

(d) Taxes. The Company and any Related Entity are authorized to withhold from any Award granted, any payment relating to an Award under the Plan, including from a distribution of Stock, or any payroll or other payment to a Participant, amounts of withholding and other taxes due or potentially payable in connection with any transaction involving an Award, and to take such other action as the Committee or the Board may deem advisable to enable the Company and Participants to satisfy obligations for the payment of withholding taxes and other tax obligations relating to any Award. This authority shall include authority to withhold or receive Stock or other property and to make cash payments in respect thereof in satisfaction of a Participant's tax obligations, either on a mandatory or elective basis in the discretion of the Committee.

(e) Changes to the Plan and Awards. The Board may amend, alter, suspend, discontinue or terminate the Plan, or the Committee's authority to grant Awards under the Plan, without the consent of shareholders or Participants, except that any amendment or alteration to the Plan shall be subject to the approval of the Company's shareholders not later than the annual meeting next following such Board action if such shareholder approval is required by any federal or state law or regulation (including, without limitation, Rule 16b-3 or Code Section 162(m)) or the rules of any stock exchange or automated quotation system on which the Stock may then be listed or quoted, and the Board may otherwise, in its discretion, determine to submit other such changes to the Plan to shareholders for approval; provided that,

without the consent of an affected Participant, no such Board action may materially and adversely affect the rights of such Participant under any previously granted and outstanding Award. The Committee or the Board may waive any conditions or rights under, or amend, alter, suspend, discontinue or terminate any Award theretofore granted and any Award agreement relating thereto, except as otherwise provided in the Plan; provided that, without the consent of an affected Participant, no such Committee or the Board action may materially and adversely affect the rights of such Participant under such Award. Notwithstanding anything in the Plan to the contrary, if any right under this Plan would cause a transaction to be ineligible for pooling of interest accounting that would, but for the right hereunder, be eligible for such accounting treatment, the Committee or the Board may modify or adjust the right so that pooling of interest accounting shall be available, including the substitution of Stock having a Fair Market Value equal to the cash otherwise payable hereunder for the right which caused the transaction to be ineligible for pooling of interest accounting.

(f) Reporting of Financial Information. The Company shall provide to the recipient of any Award under this Plan, no less frequently than annually, the financial statements of the Company, until such time as a determination is made by counsel for the Company that such reports are not required by applicable federal or state securities laws under the circumstances.

(g) Limitation on Rights Conferred Under Plan. Neither the Plan nor any action taken hereunder shall be construed as (i) giving any Eligible Person or Participant the right to continue as an Eligible Person or Participant or in the employ of the Company or a

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Related Entity; (ii) interfering in any way with the right of the Company or a Related Entity to terminate any Eligible Person's or Participant's Continuous Service at any time, (iii) giving an Eligible Person or Participant any claim to be granted any Award under the Plan or to be treated uniformly with other Participants and Employees, or (iv) conferring on a Participant any of the rights of a shareholder of the Company unless and until the Participant is duly issued or transferred shares of Stock in accordance with the terms of an Award.

(h) Unfunded Status of Awards; Creation of Trusts. The Plan is intended to constitute an "unfunded" plan for incentive and deferred compensation. With respect to any payments not yet made to a Participant or obligation to deliver Stock pursuant to an Award, nothing contained in the Plan or any Award shall give any such Participant any rights that are greater than those of a general creditor of the Company; provided that the Committee may authorize the creation of trusts and deposit therein cash, Stock, other Awards or other property, or make other arrangements to meet the Company's obligations under the Plan. Such trusts or other arrangements shall be consistent with the "unfunded" status of the Plan unless the Committee otherwise determines with the consent of each affected Participant. The trustee of such trusts may be authorized to dispose of trust assets and reinvest the proceeds in alternative investments, subject to such terms and conditions as the Committee or the Board may specify and in accordance with applicable law.

(i) Nonexclusivity of the Plan. Neither the adoption of the Plan by the Board nor its submission to the shareholders of the Company for approval shall be construed as creating any limitations on the power of the Board or a committee thereof to adopt such other incentive arrangements as it may deem desirable including incentive arrangements and awards which do not qualify under Code Section 162(m).

(j) Payments in the Event of Forfeitures; Fractional Shares. Unless otherwise determined by the Committee or the Board, in the event of a forfeiture of an Award with respect to which a Participant paid cash or other consideration, the Participant shall be repaid the amount of such cash or other consideration. No fractional shares of Stock shall be issued or delivered pursuant to the Plan or any Award. The Committee or the Board shall determine whether cash, other Awards or other property shall be issued or paid in lieu of such fractional shares or whether such fractional shares or any rights thereto shall be forfeited or otherwise eliminated.

(k) Governing Law. The validity, construction and effect of the Plan, any rules and regulations under the Plan, and any Award agreement shall be determined in accordance with the laws of the State of California



without giving effect to principles of conflicts of laws, and applicable federal law.

(1) Plan Effective Date and Shareholder Approval; Termination of Plan. The Plan shall become effective on the Effective Date, subject to subsequent approval within 12 months of its adoption by the Board by shareholders of the Company eligible to vote in the election of directors, by a vote sufficient to meet the requirements of Code Sections 162(m) (if applicable) and 422, Rule 16b-3 under the Exchange Act (if applicable), applicable NASDAQ requirements, and other laws, regulations, and obligations of the Company applicable to the Plan. Awards may be granted subject to shareholder approval, but may not be exercised or otherwise

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settled in the event shareholder approval is not obtained. The Plan shall terminate no later than 10 years from the date the Plan is adopted by the Board or 10 years from the date the Plan is approved by the Shareholders, whichever is earlier.

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2001 INCENTIVE COMPENSATION PLAN  
SYNAPTICS INCORPORATED  
INCENTIVE STOCK OPTION AGREEMENT

1. Grant of Option. SYNAPTICS INCORPORATED (the "Company") hereby grants, as of the date of grant (the "Date of Grant") set forth in the attached Notice of Grant of Stock Options attached hereto and made a part hereof, to the person whose name is set forth in the Notice of Grant of Stock Options (the "Optionee") an option (the "Option") to purchase the total number of shares of the Company's Common Stock (the "Shares") set forth in the Notice of Grant of Stock Options, at the exercise price per share set forth in the Notice of Grant of Stock Options. The Option shall be subject to the terms and conditions set forth herein. The Option was issued pursuant to the Company's 2001 Incentive Compensation Plan (the "Plan"), which is incorporated herein for all purposes. The Option is an Incentive Stock Option, and not a nonqualified stock option. The Optionee hereby acknowledges receipt of a copy of the Plan and agrees to be bound by all of the terms and conditions hereof and thereof and all applicable laws and regulations.

2. Definitions. Unless otherwise provided herein, terms used herein that are defined in the Plan and not defined herein shall have the meanings attributed thereto in the Plan.

3. Exercise Schedule. Except as otherwise provided in Sections 6 or 10 of this Option Agreement, or in the Plan, the Option is exercisable in installments as provided in the Notice of Grant of Stock Options, which shall be cumulative. To the extent that the Option has become exercisable with respect to a percentage of Shares as provided in the Notice of Grant of Stock Options, the Option may thereafter be exercised by the Optionee, in whole or in part, at any time or from time to time prior to the expiration of the Option as provided herein. The Notice of Grant of Stock Options table indicates each date (the "Vesting Date") upon which the Optionee shall be entitled to exercise the Option with respect to the number of Shares granted as indicated beside the date, provided that the Continuous Service of the Optionee continues through and on the applicable Vesting Date. Except as otherwise specifically provided herein, there shall be no proportionate or partial vesting in the periods prior to each Vesting Date, and all vesting shall occur only on the appropriate Vesting Date. Upon the termination of an Optionee's Continuous Service, any unvested portion of the Option shall terminate and be null and void.

4. Method of Exercise. The vested portion of this Option shall be exercisable in whole or in part in accordance with the exercise schedule set forth in the Notice of Grant of Stock Options by written notice, which shall state the election to exercise the Option, the number of Shares in respect of which the Option is being exercised, and such other representations and agreements as to the holder's investment intent with respect to such Shares as may be required by the Company pursuant to the provisions of the Plan. Such written notice shall be signed by the Optionee and shall be delivered in person or by certified mail to the Secretary of the Company. The written notice shall be accompanied by payment of the exercise price. This Option shall be deemed to be exercised after both (a) receipt by the Company of such written notice accompanied by the exercise price and (b) arrangements that are satisfactory to the Committee or

the Board in its sole discretion have been made for Optionee's payment to the Company of the amount, if any, that is necessary to be withheld in accordance with applicable Federal or state withholding requirements. No Shares will be issued pursuant to the Option unless and until such issuance and such exercise shall comply with all relevant provisions of applicable law, including the requirements of any stock exchange upon which the Shares then may be traded.

5. Method of Payment. Payment of the exercise price shall be by any of the following, or a combination thereof, at the election of the Optionee: (a) cash; (b) check; or (c) such other consideration or in such other manner as may be determined by the Board or the Committee in its absolute discretion.

6. Termination of Option.

(a) Any unexercised portion of the Option shall automatically

and without notice terminate and become null and void at the time of the earliest to occur of the following:

(i) three months after the date on which the Optionee's Continuous Service is terminated other than by reason of (A) Cause, (B) a mental or physical disability (within the meaning of Internal Revenue Code Section 22(e)) of the Optionee as determined by a medical doctor satisfactory to the Committee or the Board, or (C) the death of the Optionee;

(ii) immediately upon the termination of the Optionee's Continuous Service for Cause;

(iii) twelve months after the date on which the Optionee's Continuous Service is terminated by reason of a mental or physical disability (within the meaning of Section 22(e) of the Code) as determined by a medical doctor satisfactory to the Committee or the Board;

(iv) (A) twelve months after the date of termination of the Optionee's Continuous Service by reason of the death of the Optionee, or, if later, (B) three months after the date on which the Optionee shall die if such death shall occur during the one year period specified in Subsection 6(a)(iii) hereof; or

(v) the tenth anniversary of the date as of which the Option is granted.

(b) To the extent not previously exercised, (i) the Option shall terminate immediately in the event of (1) the liquidation or dissolution of the Company, or (2) any reorganization, merger, consolidation or other form of corporate transaction in which the Company does not survive or the shares of Stock are converted into or exchanged for securities issued by another entity, unless the successor or acquiring entity, or an affiliate of such successor or acquiring entity, assumes the Option or substitutes an equivalent option or right pursuant to Section 10(c) of the Plan, and (ii) the Committee or the Board in its sole discretion may by written notice ("cancellation notice") cancel, effective upon the consummation of any corporate transaction in which the Company does survive whereby the stockholders of the Company prior to the transaction do not, immediately after, own more than 50% of the combined voting power, the Option (or portion thereof) that remains unexercised on such date. The Committee or the

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Board shall give written notice of any proposed transaction referred to in this Section 6(b) a reasonable period of time prior to the closing date for such transaction (which notice may be given either before or after approval of such transaction), in order that the Optionee may have a reasonable period of time prior to the closing date of such transaction within which to exercise the Option if and to the extent that it then is exercisable (including any portion of the Option that may become exercisable upon the closing date of such transaction). The Optionee may condition his exercise of the Option upon the consummation of a transaction referred to in this Section 6(b).

7. Transferability. The Option is not transferable otherwise than by will or the laws of descent and distribution, and during the lifetime of the Optionee the Option shall be exercisable only by the Optionee. The terms of this Option shall be binding upon the executors, administrators, heirs, successors and assigns of the Optionee.

8. No Rights of Stockholders. Neither the Optionee nor any personal representative (or beneficiary) shall be, or shall have any of the rights and privileges of, a stockholder of the Company with respect to any shares of Stock purchasable or issuable upon the exercise of the Option, in whole or in part, prior to the date of exercise of the Option.

9. Market Stand-Off Agreement. At the request of the Company or the underwriters managing any underwritten offering of the Company's securities, the Optionee agrees not to sell, make any short sale of, loan, grant any option for the purchase of, or otherwise dispose of any shares of Stock (other than those included in the registration) acquired pursuant to the exercise of the Option, without the prior written consent of the Company or such underwriters, as the case may be, for such period of time (not to exceed 180 days) from the effective date of such registration as may be requested by the Company or such managing

underwriters.

[Optional] 10. Acceleration of Exercisability of Option.

(a) This Option shall become exercisable to the extent set forth in an employment, compensation, or severance agreement with or from the Company in the event that, prior to the termination of the Option pursuant to Section 6 hereof, (i) there is a "Change in Control", as defined in such agreements, that occurs while the Optionee is employed by the Company or any of its subsidiaries, (ii) the Committee or the Board exercises its discretion to provide a cancellation notice with respect to the Option pursuant to Section 6(b)(ii) hereof, or (iii) the Option is terminated pursuant to Section 6(b)(i) hereof.

[ALTERNATE] (a) This Option shall become exercisable to the extent set forth in (b) below in the event that, prior to the termination of the Option pursuant to Section 6 hereof, (i) there is a "Change in Control", as defined in (b) below, that occurs while the Optionee is employed by the Company or any of its subsidiaries, (ii) the Committee or the Board exercises its discretion to provide a cancellation notice with respect to the Option pursuant to Section 6(b)(ii) hereof, or (iii) the Option is terminated pursuant to Section 6(b)(i) hereof.

(b) [Individual Change of Control Provisions]]

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11. No Right to Continued Employment. Optionee acknowledges and agrees that the vesting of shares pursuant to the Option granted is earned only by continuing employment or consultancy at the will of the Company (not through the act of being hired, being granted this Option or acquiring shares hereunder). Optionee further acknowledges and agrees that nothing in this Option Agreement, nor in the Plan, shall confer upon Optionee any right with respect to continuation of employment or consultancy by the Company, nor shall it interfere in any way with Optionee's right or the Company's right to terminate Optionee's employment or consultancy at any time, with or without Cause.

12. Law Governing. This Option Agreement shall be governed in accordance with and governed by the internal laws of the State of California.

13. Incentive Stock Option Treatment. The terms of this Option shall be interpreted in a manner consistent with the intent of the Company and the Optionee that the Option qualify as an Incentive Stock Option under Section 422 of the Code. If any provision of the Plan or this Option Agreement shall be impermissible in order for the Option to qualify as an Incentive Stock Option, then the Option shall be construed and enforced as if such provision had never been included in the Plan or the Option. If and to the extent that the number of Options granted pursuant to this Option Agreement exceeds the limitations contained in Section 4(b) of the Plan or the value of Shares with respect to which this Option may qualify as an Incentive Stock Option, this Option shall be a Non-Qualified Stock Option.

14. Interpretation / Provisions of Plan Control. This Option Agreement is subject to all the terms, conditions and provisions of the Plan, including, without limitation, the amendment provisions thereof, and to such rules, regulations and interpretations relating to the Plan adopted by the Committee or the Board as may be in effect from time to time. If and to the extent that this Option Agreement conflicts or is inconsistent with the terms, conditions and provisions of the Plan, the Plan shall control, and this Option Agreement shall be deemed to be modified accordingly. The Optionee accepts the Option subject to all the terms and provisions of the Plan and this Option Agreement. The undersigned Optionee hereby accepts as binding, conclusive and final all decisions or interpretations of the Committee or the Board upon any questions arising under the Plan and this Option Agreement.

15. Notices. Any notice under this Option Agreement shall be in writing and shall be deemed to have been duly given when delivered personally or when deposited in the United States mail, registered, postage prepaid, and addressed, in the case of the Company, to the Company's Secretary at:

Synaptics Incorporated  
2381 Bering Drive  
San Jose, California 95131

or if the Company should move its principal office, to such principal office, and, in the case of the Optionee, to the Optionee's last permanent address as shown on the Company's records,

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subject to the right of either party to designate some other address at any time hereafter in a notice satisfying the requirements of this Section.

16. Tax Consequences. Set forth below is a brief summary as of the date of this Option of some of the federal tax consequences of exercise of this Option and disposition of the Shares. THIS SUMMARY IS NECESSARILY INCOMPLETE, AND THE TAX LAWS AND REGULATIONS ARE SUBJECT TO CHANGE. OPTIONEE SHOULD CONSULT A TAX ADVISER BEFORE EXERCISING THIS OPTION OR DISPOSING OF THE SHARES.

(a) Exercise of Option. There will be no regular federal income tax liability upon the exercise of the Option, although the excess, if any, of the fair market value of the Shares on the date of exercise over the exercise price will be treated as an adjustment to the alternative minimum tax for federal tax purposes and may subject the Optionee to the alternative minimum tax in the year of exercise.

(b) Disposition of Shares. If Shares transferred pursuant to the Option are held for at least one year after exercise and are disposed of at least two years after the date of grant, any gain realized on disposition of the Shares will also be treated as long-term capital gain for federal income tax purposes. If Shares purchased under an Option are disposed of within such one-year period or within two years after the Date of Grant, any gain realized on such disposition will be treated as compensation income (taxable at ordinary income rates) to the extent of the difference between the exercise price and the lesser of (1) the fair market value of the Shares on the date of exercise, or (2) the sale price of the Shares.

(c) Notice of Disqualifying Disposition of Option Shares. If Optionee sells or otherwise disposes of any of the Shares acquired pursuant to the Option on or before the later of (1) the date two years after the date of grant, (2) the date one year after the date of exercise, the Optionee shall immediately notify the Company in writing of such disposition. Optionee agrees that Optionee may be subject to the income tax withholding by the Company on the compensation income recognized by the Optionee from the early disposition by payment in cash or out of the current earnings paid to the Optionee.

If and to the extent that the number of Options granted hereunder exceeds the limitations contained in Section 4(b) of the Plan or the value of Shares with respect to which this Option may qualify as an Incentive Stock Option, this Option shall be a Non-Qualified Stock Option. The holder of a Non-Qualified Stock Option will be treated as having received compensation income (taxable at ordinary income tax rates) at the time the Option is exercised equal to the excess, if any, of the fair market value of the shares of Stock on the date of exercise over the exercise price. If the shares of Stock transferred pursuant to the Non-Qualified Stock Option are held for at least one year after the Option is exercised, any gain realized on disposition of the shares of Stock will be treated as long-term capital gain for federal income tax purposes.

The foregoing discussion assumes that, and only is applicable if, the fair market value of the Shares as of the date on which the Option is granted is not less than the exercise price. The Company believes that it has made a good faith effort to determine the fair market value of the Shares and does not believe that the exercise price is less than the fair market value of the Shares

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on the Date of Grant. No assurances can be given, however, that the Internal Revenue Service would not take a contrary position, or that the Internal Revenue Service would not treat the Option as an Incentive Stock Option for some other reason. If the exercise price is determined to be less than the fair market value of a Share on the Date of Grant, then the Option may be taxable as a Non-Qualified Stock Option. It is also possible that if the fair market value is determined to be significantly greater than the exercise price, the Internal

Revenue Service may take the position that the Option is not in effect a stock option but should be treated as a restricted stock for tax purposes. The Optionee should consult with his or her own tax advisors as to whether any action should be taken to minimize these risks.

17. Execution. This Option Agreement is executed by the parties hereto on the Notice of Grant of Stock Options, which is attached hereto and made a part hereof.

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EXHIBIT 10.6(B)

2001 INCENTIVE COMPENSATION PLAN  
SYNAPTICS INCORPORATED  
NON-QUALIFIED STOCK OPTION AGREEMENT

1. Grant of Option. SYNAPTICS INCORPORATED (the "Company") hereby grants, as of the date of grant ("Date of Grant") set forth in the attached Notice of Grant of Stock Options attached hereto and made a part hereof, to the person whose name is set forth in the Notice of Grant of Stock Options (the "Optionee") an option (the "Option") to purchase the total number of shares of the Company's Common Stock (the "Shares") set forth in the Notice of Grant of Stock Options, at the exercise price per share set forth in the Notice of Grant of Stock Options. The Option shall be subject to the terms and conditions set forth herein. The Option was issued pursuant to the Company's 2001 Incentive Compensation Plan (the "Plan"), which is incorporated herein for all purposes. The Option is a nonqualified stock option, and not an Incentive Stock Option. The Optionee hereby acknowledges receipt of a copy of the Plan and agrees to be bound by all of the terms and conditions hereof and thereof and all applicable laws and regulations.

2. Definitions. Unless otherwise provided herein, terms used herein that are defined in the Plan and not defined herein shall have the meanings attributed thereto in the Plan.

3. Exercise Schedule. Except as otherwise provided in Sections 6 or 8 of this Option Agreement, or in the Plan, the Option is exercisable in installments as provided in the Notice of Grant of Stock Options, which shall be cumulative. To the extent that the Option has become exercisable with respect to a percentage of Shares as provided in the Notice of Grant of Stock Options, the Option may thereafter be exercised by the Optionee, in whole or in part, at any time or from time to time prior to the expiration of the Option as provided herein. The Notice of Grant of Stock Options table indicates each date (the "Vesting Date") upon which the Optionee shall be entitled to exercise the Option with respect to the number of Shares granted as indicated beside the date, provided that the Continuous Service of the Optionee continues through and on the applicable Vesting Date. Except as otherwise specifically provided herein, there shall be no proportionate or partial vesting in the periods prior to each Vesting Date, and all vesting shall occur only on the appropriate Vesting Date. Upon the termination of an Optionee's Continuous Service, any unvested portion of the Option shall terminate and be null and void.

4. Method of Exercise. The vested portion of this Option shall be exercisable in whole or in part in accordance with the exercise schedule set forth in the Notice of Grant of Stock Options by written notice, which shall state the election to exercise the Option, the number of Shares in respect of which the Option is being exercised, and such other representations and agreements as to the holder's investment intent with respect to such Shares as may be required by the Company pursuant to the provisions of the Plan. Such written notice shall be signed by the Optionee and shall be delivered in person or by certified mail to the Secretary of the Company. The written notice shall be accompanied by payment of the exercise price. This Option shall be deemed to be exercised after both (a) receipt by the Company of such written notice accompanied by the exercise price and (b) arrangements that are satisfactory to the Committee or the Board in its sole discretion have been made for Optionee's payment to the Company of the

amount that is necessary to be withheld in accordance with applicable Federal or state withholding requirements. No Shares will be issued pursuant to the Option

unless and until such issuance and such exercise shall comply with all relevant provisions of applicable law, including the requirements of any stock exchange upon which the Shares then may be traded.

5. Method of Payment. Payment of the exercise price shall be by any of the following, or a combination thereof, at the election of the Optionee: (a) cash; (b) check; or (c) such other consideration or in such other manner as may be determined by the Board or the Committee in its absolute discretion.

6. Termination of Option.

(a) Any unexercised portion of the Option shall automatically and without notice terminate and become null and void at the time of the earliest to occur of:

(i) three months after the date on which the Optionee's Continuous Service is terminated other than by reason of (A) Cause, (B) a mental or physical disability (within the meaning of Internal Revenue Code Section 22(e)) of the Optionee as determined by a medical doctor satisfactory to the Committee or the Board, or (C) the death of the Optionee;

(ii) immediately upon the termination of the Optionee's Continuous Service for Cause;

(iii) twelve months after the date on which the Optionee's Continuous Service is terminated by reason of a mental or physical disability (within the meaning of Section 22(e) of the Code) as determined by a medical doctor satisfactory to the Committee or the Board;

(iv) (A) twelve months after the date of termination of the Optionee's Continuous Service by reason of the death of the Optionee, or, if later, (B) three months after the date on which the Optionee shall die if such death shall occur during the one year period specified in Subsection 6(a)(iii) hereof; or

(v) the tenth anniversary of the date as of which the Option is granted.

(b) To the extent not previously exercised, (i) the Option shall terminate immediately in the event of (1) the liquidation or dissolution of the Company, or (2) any reorganization, merger, consolidation or other form of corporate transaction in which the Company does not survive or the shares of Stock are converted into or exchanged for securities issued by another entity, unless the successor or acquiring entity, or an affiliate of such successor or acquiring entity, assumes the Option or substitutes an equivalent option or right pursuant to Section 10(c) of the Plan, and (ii) the Committee or the Board in its sole discretion may by written notice ("cancellation notice") cancel, effective upon the consummation of any corporate transaction in which the Company does survive whereby the stockholders of the Company prior to the transaction do not, immediately after, own more than 50% of the combined voting power, the Option (or portion thereof) that remains unexercised on such date. The Committee or the Board shall give written notice of any proposed transaction referred to in this Section 6(b) a reasonable period of time prior to the closing date for such transaction (which notice may be

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given either before or after approval of such transaction), in order that the Optionee may have a reasonable period of time prior to the closing date of such transaction within which to exercise the Option if and to the extent that it then is exercisable (including any portion of the Option that may become exercisable upon the closing date of such transaction). The Optionee may condition his exercise of the Option upon the consummation of a transaction referred to in this Section 6(b).

7. Transferability

(a) General. Except as provided herein, a Participant may not assign, sell, transfer, or otherwise encumber or subject to any lien any Award or other right or interest granted under this Plan, in whole or in part, including any Award or right which constitutes a derivative security as generally defined in Rule 16a-1(c) under the Exchange Act, other than by will or by operation of the laws of descent and distribution, and such Awards or rights

that may be exercisable shall be exercised during the lifetime of the Participant only by the Participant or his or her guardian or legal representative.

(b) Permitted Transfer of Option. The Committee or Board, in its sole discretion, may permit the transfer of an Option granted under this Option Agreement as follows: (A) by gift to a member of the Participant's Immediate Family or (B) by transfer by instrument to a trust providing that the Option is to be passed to beneficiaries upon death of the Optionee. For purposes of this Section 7(b), "Immediate Family" shall mean the Optionee's spouse (including a former spouse subject to terms of a domestic relations order); child, stepchild, grandchild, child-in-law; parent, stepparent, grandparent, parent-in-law; sibling and sibling-in-law, and shall include adoptive relationships. If a determination is made by counsel for the Company that the restrictions contained in this Section 7(b) are not required by applicable federal or state securities laws under the circumstances, then the Committee or Board, in its sole discretion, may permit the transfer of Options granted under this Option Agreement to one or more Beneficiaries or other transferees during the lifetime of the Participant, which may be exercised by such transferees in accordance with the terms of this Option Agreement, but only if and to the extent permitted by the Committee or the Board pursuant to the express terms of this Option Agreement (subject to any terms and conditions which the Committee or the Board may impose thereon, and further subject to any prohibitions and restrictions on such transfers pursuant to Rule 16b-3). A Beneficiary, transferee, or other person claiming any rights under the Plan from or through any Participant shall be subject to all terms and conditions of the Plan and any Award agreement applicable to such Participant, except as otherwise determined by the Committee or the Board, and to any additional terms and conditions deemed necessary or appropriate by the Committee or the Board.

[Optional] 8. Acceleration of Exercisability of Option.

(a) This Option shall become exercisable to the extent set forth in an employment, compensation, or severance agreement with or from the Company in the event that, prior to the termination of the Option pursuant to Section 6 hereof, (i) there is a "Change in Control", as defined in such agreements, that occurs while the Optionee is employed by the Company or any of its subsidiaries, (ii) the Committee or the Board exercises its discretion to

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provide a cancellation notice with respect to the Option pursuant to Section 6(b)(ii) hereof, or (iii) the Option is terminated pursuant to Section 6(b)(i) hereof.

[ALTERNATE] (a) This Option shall become exercisable to the extent set forth in (b) below in the event that, prior to the termination of the Option pursuant to Section 6 hereof, (i) there is a "Change in Control", as defined in (b) below, that occurs while the Optionee is employed by the Company or any of its subsidiaries, (ii) the Committee or the Board exercises its discretion to provide a cancellation notice with respect to the Option pursuant to Section 6(b)(ii) hereof, or (iii) the Option is terminated pursuant to Section 6(b)(i) hereof.

(b) [Individual Change of Control Provisions]

9. No Rights of Stockholders. Neither the Optionee nor any personal representative (or beneficiary) shall be, or shall have any of the rights and privileges of, a stockholder of the Company with respect to any shares of Stock purchasable or issuable upon the exercise of the Option, in whole or in part, prior to the date of exercise of the Option.

10. Market Stand-Off Agreement. At the request of the Company or the underwriters managing any underwritten offering of the Company's securities, the Optionee agrees not to sell, make any short sale of, loan, grant any option for the purchase of, or otherwise dispose of any shares of Stock (other than those included in the registration) acquired pursuant to the exercise of the Option, without the prior written consent of the Company or such underwriters, as the case may be, for such period of time (not to exceed 180 days) from the effective date of such registration as may be requested by the Company or such managing underwriters.

11. No Right to Continued Employment. Neither the Option nor this



Option Agreement shall confer upon the Optionee any right to continued employment or service with the Company.

12. Law Governing. Optionee acknowledges and agrees that the vesting of shares pursuant to the Option granted is earned only by continuing employment or consultancy at the will of the Company (not through the act of being hired, being granted this Option or acquiring shares hereunder). Optionee further acknowledges and agrees that nothing in this Option Agreement, nor in the Plan, shall confer upon Optionee any right with respect to continuation of employment or consultancy by the Company, nor shall it interfere in any way with Optionee's right or the Company's right to terminate Optionee's employment or consultancy at any time, with or without Cause.

13. Interpretation / Provisions of Plan Control. This Option Agreement is subject to all the terms, conditions and provisions of the Plan, including, without limitation, the amendment provisions thereof, and to such rules, regulations and interpretations relating to the Plan adopted by the Committee or the Board as may be in effect from time to time. If and to the extent that this Option Agreement conflicts or is inconsistent with the terms, conditions and provisions of the Plan, the Plan shall control, and this Option Agreement shall be deemed to be modified accordingly. The Optionee accepts the Option subject to all the terms and provisions of the Plan and this Option Agreement. The undersigned Optionee hereby accepts as binding, conclusive and

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final all decisions or interpretations of the Committee or the Board upon any questions arising under the Plan and this Option Agreement.

14. Notices. Any notice under this Option Agreement shall be in writing and shall be deemed to have been duly given when delivered personally or when deposited in the United States mail, registered, postage prepaid, and addressed, in the case of the Company, to the Company's Secretary at:

Synaptics Incorporated  
2381 Bering Drive  
San Jose, California 95131

or if the Company should move its principal office, to such principal office, and, in the case of the Optionee, to the Optionee's last permanent address as shown on the Company's records, subject to the right of either party to designate some other address at any time hereafter in a notice satisfying the requirements of this Section.

15. Tax Consequences. Set forth below is a brief summary as of the date of this Option of some of the federal tax consequences of exercise of this Option and disposition of the Shares. THIS SUMMARY IS NECESSARILY INCOMPLETE, AND THE TAX LAWS AND REGULATIONS ARE SUBJECT TO CHANGE. OPTIONEE SHOULD CONSULT A TAX ADVISER BEFORE EXERCISING THIS OPTION OR DISPOSING OF THE SHARES.

(a) Exercise of Option. There may be a regular federal income tax liability upon the exercise of the Option. The Optionee will be treated as having received compensation income (taxable at ordinary income tax rates) equal to the excess, if any, of the fair market value of the Shares on the date of exercise over the exercise price. If Optionee is an employee, the Company will be required to withhold from Optionee's compensation or collect from Optionee and pay to the applicable taxing authorities an amount equal to a percentage of this compensation income at the time of exercise.

(b) Disposition of Shares. If Shares are held for at least one year, any gain realized on disposition of the Shares will be treated as long-term capital gain for federal income tax purposes.

The foregoing discussion assumes that, and only is applicable if, the fair market value of the Shares as of the date on which the Option is granted is not significantly less than the exercise price. The Company believes that it has made a good faith effort to determine the fair market value of the Shares and does not believe that the exercise price is significantly less than the fair market value of the Shares on the Date of Grant. No assurances can be given, however, that the Internal Revenue Service would not take a contrary position. It is possible that if the fair market value is determined to be significantly greater than the exercise price, the Internal Revenue Service may take the position that the Option is not in effect a stock option but should be treated

as a restricted stock for tax purposes. The Optionee should consult with his or her own tax advisors as to whether any action should be taken to minimize these risks.

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16. Execution. This Option Agreement is executed by the parties hereto on the Notice of Grant of Stock Options, which is attached hereto and made a part hereof.

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**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-Q of Synaptics Incorporated (the "Company") for the quarterly period ended December 31, 2002 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Francis F. Lee, President, Chief Executive Officer and Director of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m(a) or 78o(d)); and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Francis F. Lee

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Francis F. Lee  
President, Chief Executive Officer, and Director  
February 6, 2003

**CERTIFICATION PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Quarterly Report on Form 10-Q of Synaptics Incorporated (the "Company") for the quarterly period ended December 31, 2002 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Russell J. Knittel, President, Senior Vice President, Chief Financial Officer, Chief Administrative Officer, Secretary and Treasurer of the Company, certify, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m(a) or 78o(d)); and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Russell J. Knittel

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Russell J. Knittel  
Senior Vice President, Chief Financial Officer,  
Chief Administrative Officer, Secretary and Treasurer  
February 6, 2003