

## **Former Brocade CEO's trial begins / Reyes faces 10 felony counts, plus other charges, for alleged options backdating**

By **Jessica Guynn**, *Chronicle Staff Writer* June 19, 2007

Former Silicon Valley executive Gregory Reyes, who rose to prominence at the helm of Brocade Communications Systems Inc., found himself in a very different spotlight Monday, taking center stage in a San Francisco federal courtroom as the nation's first criminal trial in the stock-options scandal got under way.

With onlookers spilling out the courtroom doors into the hallway, Assistant U.S. Attorney Timothy Crudo and Reyes' lawyer, Richard Marmaro, used their opening arguments to wrestle over the case's central question. Did Reyes, who in 6 1/2 years took Brocade from a San Jose startup to a publicly traded market leader, intend to deceive investors by not disclosing compensation expenses associated with stock options granted to employees.

Reyes, a youthful looking man of 44 with graying hair in a dark suit, betrayed little emotion as Crudo portrayed him as a criminal mastermind, who for four years went to extraordinary lengths -- even altering board meeting minutes and company records -- to cover up a backdating scheme that made Brocade appear more profitable than it was. Crudo alleged that Reyes understood the accounting implications of his actions and that's why he concealed what he had done.

"This is a case about a person who misused a position of power, who misused the trust placed in him by shareholders," Crudo told the jury during his 25-minute opening argument. "It's about deception. It's about lies. And it's about fraud."

Marmaro cast his client as a superstar salesman who worked his way up through the corporate ranks to become a popular CEO. Marmaro said Reyes' only intention was to hire and keep the best employees in a bid to boost the success of his company which, far from being harmed, continues to thrive. Reyes never personally benefited from backdating, Marmaro added.

During his nearly two-hour opening statement, Marmaro said Reyes had a "good-faith belief" that his company's accounting practices were proper because they were well-known to the board of directors, senior executives and the company's accounting firm, Arthur Andersen. Further, Reyes, who was unfamiliar with a murky area of accounting, "surrounded himself with people who had knowledge and expertise that he did not have," namely former Brocade Chief Financial Officer Michael Byrd, who designed many of the company's early practices, Marmaro said. Byrd, who according to defense filings, struck an immunity deal with prosecutors this year, is scheduled as a prosecution witness.

"No one believed that the company was committing securities fraud," Marmaro said. "No one believed the company was deceiving investors."

Reyes, of Saratoga, who was ousted as CEO in January 2005 and indicted last summer, is charged with 10 felony counts of securities fraud and other offenses. He has pleaded not guilty to each count. If convicted, he could get a prison sentence and millions of dollars in fines.

Reyes is the first executive to stand trial for criminal charges in the government's stock-options probe. He is being tried separately from the other top Brocade executive charged in the case, Stephanie Jensen, Brocade's former vice president of human resources, who also has pleaded not guilty.

This was just the first day of testimony in a case expected to last up to two months with 1,600 items of evidence and many witnesses, some of whom will testify about arcane and confusing accounting issues. The case will delve deeply into backdating, the practice of changing the date of a grant to when stock prices were lower to potentially boost the windfall for employees and executives.

The practice is not necessarily illegal if companies properly account for and disclose what they are doing. But during heated competition for talent during the late 1990s, many Silicon Valley companies neglected to do so, putting them in the government crosshairs.

The stakes in this trial are high not just for Reyes, but for anyone implicated in the stock-options scandal. Proving criminal intent in a corporate fraud case can be difficult. Should prosecutors succeed, the outcome probably would determine how aggressively the government will pursue other executives.

It all hinges on one question: Will a jury decide such surreptitious backdating is a crime?

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