

Backdated Awards Added 10% to Executive Pay

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Hundreds of US company bosses inflated their pay by as much as 10 per cent by secretly backdating share options, according to new research that casts light on the scale of the latest scandal to hit corporate America.

A joint study by professors at Harvard Law School, Cornell University and Insead of France concludes that companies were systematically using manipulated options grants as a significant - and tax efficient - means of remuneration for their senior executives.

More than 130 companies are under investigation by the Wall Street watchdog, the Securities and Exchange Commission. At least 50 executives have lost their jobs as a result of the investigations, and five former executives have already been charged with fraud.

Apple Computer, inventor of the iPod; McAfee, the internet security software maker; and the jobs website Monster are among dozens of companies struggling to restate their financial results after uncovering deceptive accounting for stock options over several years.

Options allow executives to buy shares at a fixed price in the future, pocketing the difference between the share price on the date they are granted and the price at which the option is exercised. By pretending that the option was granted on a day when the share price was particularly low, executives artificially inflate profits.

Lucky CEOs, a paper by Lucian Bebchuk, Yaniv Grinstein and Urs Peyer, examined the effect of particularly suspicious, or "lucky", share options grants. The authors say it is wrong to assume that options backdating has been a technical or trivial issue. "We estimate the average gain to chief executives from grants that were backdated to the lowest price of the month to exceed 20 per cent of the reported value of the grant. The gain increases the CEO's total reported compensation for the year by more than 10 per cent."

The trio also found that "lucky" grants were more likely when the company did not have a majority of independent directors on the board and when the chief executives had longer tenure.

In contrast to impressions produced by cases under scrutiny thus far, grant manipulation has been wide-spread in old economy firms and was not concentrated in technology firms, they said.

The SEC has warned companies to expect more disciplinary action and predicted that there will be more individual prosecutions. So far charges have been filed only against executives from Brocade Communications Systems, a computer equipment maker, and Comverse Technology, a telecoms software company. The former chief executive of Comverse, Kobi Alexander, is fighting extradition from Namibia, where he fled with his family in the summer.