Underwater stock options drive top executives turnover

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When the market price of company stock falls below the exercise price, the options are considered to be "out of the money" or underwater. Many publicly traded firms have become concerned about retaining highly valued executives who hold underwater stock options, fearing that they will voluntarily leave the firm for a better position elsewhere. A new study in *Personnel Psychology* reveals that voluntary top executive turnover was more likely to occur as executives' stock option portfolios fell further out of the money.

Benjamin Dunford, Ph.D., Derek Oler, Ph.D., and John Boudreau, Ph.D., examined a large sample of executives in publicly traded U.S. firms between 1996 and 2006.

Results show that not only were underwater options associated with voluntary executive turnover, but moreover, CEO turnover was significantly more sensitive to out of the money stock options than non-CEO turnover.

The study also found that the odds of voluntary executive turnover may be reduced substantially by increasing the value of out of the money stock option portfolios, even if they don't move the portfolio back in the money.

"Our findings suggest that firms should consider changes to their current retention policies and practices for valued top executives," the authors note. "Firms may not be doing enough to retain valued but underwater executives if they are relying solely on base pay, bonus pay, and restricted stock increases."

This study is published in the Winter 2008 issue of *Personnel Psychology.*

Source: Wiley

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