In times of scandal, corporations are likely to use others' misconduct to justify their behavior

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Among corporations involved in the 2006 stock-option backdating scandal, those implicated earlier were more likely to dismiss their top executives than those that surfaced later on, according to new research from Rice University and the University of California at Irvine.

The study, "Executive Turnover in the Stock-Option Backdating Wave: The Impact of Social Context," will be published in an upcoming edition of the Strategic Management Journal.

The researchers examined the behavior of corporate boards following the 2006 stock-option backdating scandal, in which firms illegally manipulated stock-option grant dates. Researchers reviewed the 141 companies listed as having come under scrutiny for their stock-option practices in the Wall Street Journal Options Scorecard website to understand why corporations respond to the same kind of misconduct in different ways.

"When faced with scandal, it's critical for corporations to manage their images and maintain legitimacy with stakeholders and the general public," said Anthea Zhang, professor of strategic management at Rice University's Jones Graduate School of Business. "While it seems to be a natural choice to fire the executives/directors who should be responsible for option backdating, only one-third of the 141 firms we surveyed elected to do so."

Zhang and her co-author, Margarethe Wiersema at the University of California at Irvine, theorize that the decrease in executive/director turnover over the course of the scandal can be attributed to companies using other companies' similar misconduct to justify their own misconduct.

"Our findings suggest that corporate boards 'strategize' their response by calculating the reputation damage caused by scandal," Zhang said. "If accountability were the basis for their decision-making, we should have observed a more consistent pattern of companies choosing to dismiss their executives/directors over time."

Zhang said that attention from the media, as well as investigation by the Department of Justice and/or the Securities and Exchange Commission, plays an important role in pushing companies involved in the scandal to fire their executives and directors.

"This attention serves to counterbalance corporation boards' tendency to justify their misbehavior with others' misbehavior," she said.

Zhang hopes their research can help stakeholders and the general public better understand how corporate boards respond to scandal.

Provided by Rice University

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