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## CEO Stock Option Timing and the Positivity of Information Releases

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## CEO Stock Option Timing and the Positivity of Information Releases

CEO compensation plans such as stock option grants are put into place to align CEOs' interests with those of shareholders. Research to appear in the *Academy of Management Journal* examines times when granting stock options might instead present opportunities for CEOs to act in their own interests. Specifically, researchers examined whether CEOs might act to keep stock prices lower in the period leading up to a stock option grant. They found that firms' press releases had less positive language during the six weeks before CEO received stock options, especially for CEOs who were underpaid or in industries where CEOs have more discretion.

### Key Takeaways:

- In the weeks before stock options are granted, CEOs can gain from temporarily lower stock prices, resulting in a possible conflict of interest.
- CEOs may act to suppress stock prices before an option grant by releasing information that is less positive in tone. CEOs who were underpaid or had more discretion did so more.
- Simple remedies include issuing stock grants instead of options or issuing smaller grants more frequently.

The researchers studied option grants in large publicly traded U.S. firms between 2009 and 2013. They assessed the prevalence of positive words in company press releases, finding them to be less positive in the six weeks leading up to a grant. Understating positive news can suppress the stock market's positive response, keeping the price of options low. Positive information was even less prevalent during

those periods in firms whose CEOs were paid less than others with similar performance and firm characteristics, or in industries where the CEO has more discretion because of innovation, growth, or competitive factors. Returns on stock prices were 1.31% lower during the pre-grant periods compared to similar firms during the same periods.

The researchers emphasize that managers and owners often have different interests, and the mechanisms in place to align these motivations may not always be adequate. They suggest granting smaller options more often, or granting stock instead of options.

Source: Quigley, T. J., Hubbard, T. D., Ward, A., & Graffin, S. D. (in press). Unintended consequences: Information releases and CEO stock option grants. *Academy of Management Journal*. DOI: 10.5465/amj.2017.0455

