

Rubberstamping the Agents of Excess

How 20 large investment firms voted in director elections at four companies where executive pay abuses triggered high director withhold votes in 2006

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April 2, 2007
Updated: April 9, 2007

Executive Summary

Over the next two months, shareholders will vote in director elections at nearly 1000 U.S. public companies. Will this year's proxy season be a repeat of 2006, when even the most compliant directors at companies such as Home Depot received majority shareholder support? Or will investment managers, including those entrusted with some \$5 trillion in worker retirement savings, stand up for their clients by withholding votes from directors who fail to effectively represent shareholders?

In the following study, we analyze how twenty of the largest investment managers voted in 2006 on seventeen "problem" directors at four S&P 500 companies with egregious executive pay practices. Our objective is to identify which firms exercised their proxy votes responsibly in 2006 and which firms' behavior must change to make director elections meaningful. This window into investment manager proxy voting comes as withheld votes could, for the first time, make a real difference at the more than 180 companies that have adopted majority vote policies over the past year.¹

Our starting point is Home Depot's 2006 annual meeting, at which shareholders withheld at least 30 percent of their proxy votes from 10 of the board's 11 directors. By the standards of a typical board election, in which directors receive more than 95 percent of the vote, it was a striking display of no confidence. But it was nowhere near the majority withhold justified by Home Depot's excessive CEO pay and dismal share performance. One key reason: nine of the 20 investment managers with the most Home Depot shares voted to re-elect the entire board.

We then look at how these same firms voted at three other S&P 500 companies with very high CEO compensation and high director withhold votes: Clear Channel Communications, ExxonMobil, and UnitedHealth Group. At each of these companies, shareholders withheld at least 15 percent of their votes from at least one director, a distinction held by 17 directors at the four companies in the study, but relatively few other S&P 500 directors.

By using shareholder opinion—as expressed by their proxy votes—to identify the "problem" directors in our study, we intentionally set a low bar. In our view, if an investment manager did not withhold from these 17 directors, it is unlikely that it withheld from other unworthy directors, at least in response to executive compensation abuses.

Yet at each of the four companies, the majority of these 20 investment managers voted to re-elect every director. In fact, six firms voted for every director at all four companies, including Fidelity, the nation's largest mutual fund company. Only Barclays, the nation's largest money manager, and Grantham, Mayo, Van Otterloo, LLC ("GMO") withheld from all 17 "problem" directors.

These investment managers' failure is particularly troubling given that under ERISA, the Department of Labor has held that firms must cast proxy votes in the best interests of their private pension plan clients. Likewise, in adopting rules requiring mutual funds to disclose their

¹ Institutional Shareholder Services, "2006 Postseason Report: Spotlight on Executive Pay and Board Accountability," (Oct. 5, 2006).

proxy votes in 2003, the Securities and Exchange Commission confirmed that mutual fund managers have a fiduciary duty to cast votes in the best interests of their fund shareholders.²

Which 2007 director elections will determine whether this proxy season is a repeat of 2006? Directors at Home Depot, UnitedHealth and the more than 180 other companies under federal investigation for possible stock option backdating are certain to find themselves in the hot seat; directors who have *themselves* received suspiciously-timed options will likely come under especially sharp scrutiny.³ Likewise, shareholders may target directors at companies where new SEC disclosure rules concerning executive compensation help to expose abusive pay practices. Some specific upcoming elections likely to be a focus include:

- *CVS/Caremark* – Caremark’s directors signed off on a \$21 billion merger with CVS that provided plum jobs, massive personal windfalls and increased indemnification to Caremark directors and officers—but *no premium* to Caremark shareholders. When a competing bidder with a higher offer emerged, they refused even to negotiate. The board’s failed process prompted a shareholder lawsuit alleging the directors breached their fiduciary duties. Even as Caremark remains under investigation by the Department of Justice and SEC for possible stock option backdating, seven former Caremark directors are up for election to the merged CVS/Caremark board in May.
- *ExxonMobil* – ExxonMobil’s directors, already under pressure for the company’s outlandish executive pay, could face further investor backlash for repeatedly failing to respond to institutional investors—including public pension funds with over \$200 billion in assets—who have sought to discuss concerns with the company’s environmental practices.
- *Sunrise Senior Living* – The SEC launched an investigation of Sunrise after a shareholder, the SEIU Master Trust, raised concerns with possible insider trading and stock option backdating, lack of board independence, and poor handling of an internal accounting review. SEIU’s action prompted the company to appoint an independent counsel to review these issues. As a result of the accounting review, Sunrise disclosed a material weakness in internal controls over financial reporting and will restate previously filed financial statements for 2003 to 2005.
- *Clear Channel* – Last year, shareholders withheld 31 percent of their votes from John Williams, the chair of Clear Channel’s compensation committee and one of the 17 directors in this report. This year, the entire board is hoping that shareholders will approve a management buyout that allows them to avoid what would likely be a contentious director election. The deal has prompted such strong shareholder opposition that the board postponed the buyout vote from March 23 to April 19. If shareholders reject the deal, look for them to question the board’s independence at the 2007 annual meeting.

² U.S. Department of Labor, “Interpretive bulletin relating to written statements of investment policy, including proxy voting policy or guidelines,” 29 CFR § 2509.94-2 (2004); Securities and Exchange Commission, “Final Rule: Proxy Voting by Investment Advisers,” 17 CFR Part 275, Release No. IA-2106 (Mar. 10, 2003).

³ Eric Dash, “Study Finds Outside Directors Also Got Backdated Options,” THE NEW YORK TIMES, (Dec. 18, 2006).

Two important votes in March offer a possible preview of these meetings. On March 14, in response to initiatives led by the Laborers' International Union of North America and the Amalgamated Bank, Toll Brothers' shareholders withheld 25 percent of their votes from Carl Marbach, chair of the board's compensation committee. Like Home Depot last year, it was a strong vote of no confidence, especially considering that insiders control 26 percent of the company, but nonetheless short of the majority warranted by the homebuilder's outrageous CEO pay and plummeting profits.⁴

The very next day, the first proxy access resolution to ever come before shareholders received 39 percent of the votes at Hewlett Packard's annual meeting. By allowing shareholders to place their director nominees on the corporate proxy, the proposal—which was sponsored by the AFSCME Employee Pension Plan, the New York State Common Retirement Fund, the Connecticut Retirement Plans and Trust Funds and the North Carolina Equity Investment Fund Pooled Trust—offers shareholders a necessary alternative to withholding votes from directors.⁵

Following the 2007 proxy season, we look forward to reviewing how investment managers voted at Toll Brothers, Hewlett Packard and other illustrative companies. In the meantime, we hope that pension fund trustees find this report useful in helping them to fulfill their fiduciary obligations to monitor their investment managers' 2006 proxy voting performance.

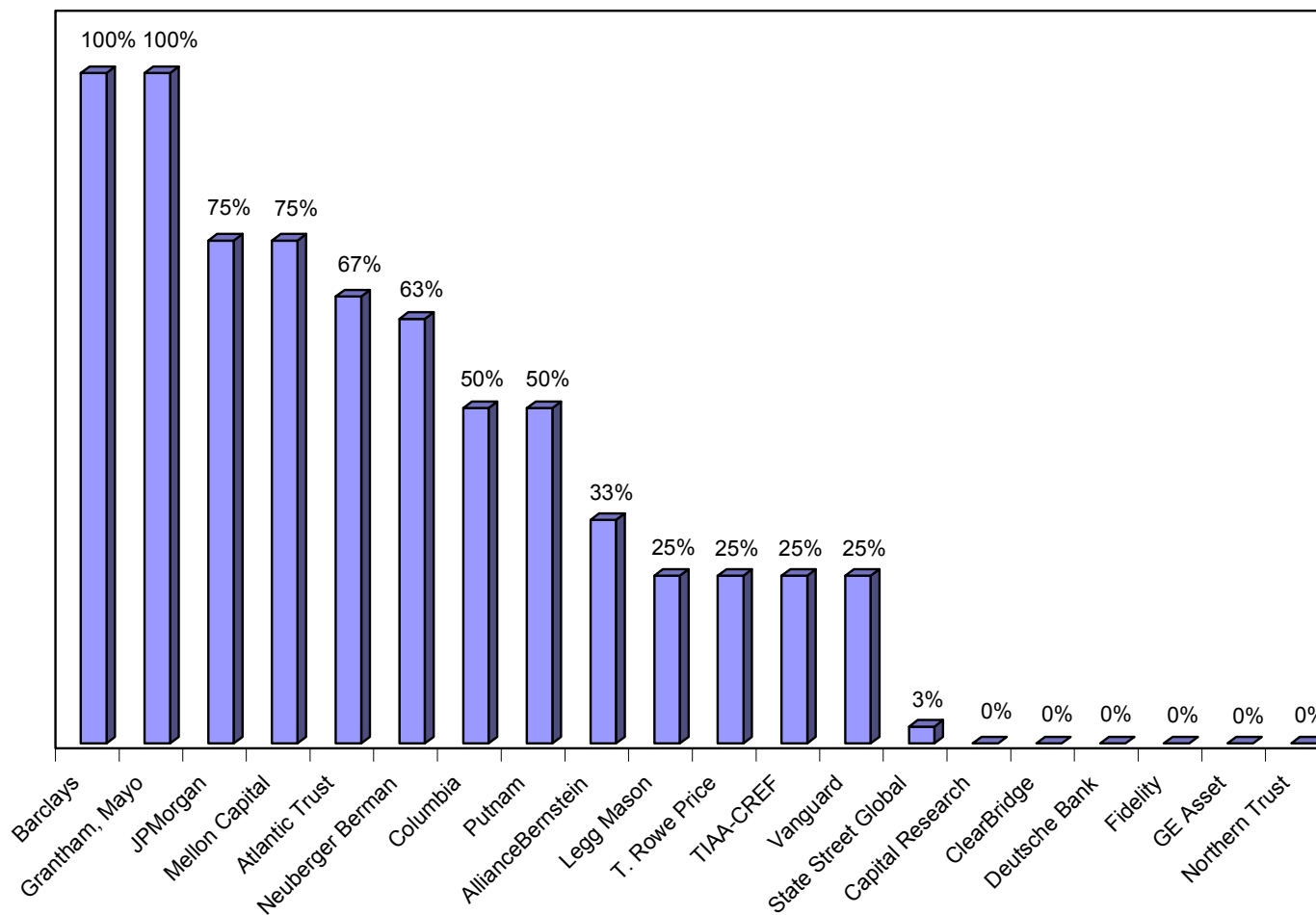
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⁴ Bob Fernandez, "Toll's bonus protested at shareholder meeting," THE PHILADELPHIA INQUIRER, (Mar. 15, 2007)

⁵ Benjamin Pimentel, "HP shareholders reject proposal on board election," THE SAN FRANCISCO CHRONICLE, (Mar. 15, 2007).

Weighted Investment Manager Withhold Ratings* in 2006 Based on Votes Cast on 17 Directors at Four Companies



*See Methodology below for a detailed description of ratings

Methodology

We selected four S&P 500 companies—Clear Channel Communications, ExxonMobil, Home Depot and UnitedHealth Group—at which shareholders withheld at least 15 percent of their votes from one or more directors in the 2006 proxy season due to executive compensation concerns. In total, this happened to 17 directors at the four companies. The four companies span the energy, media, retail, and healthcare industries.

We then identified the 20 institutional shareholders with the most Home Depot stock on September 30, 2006—the most current data available during the research phase of the project—using LionShares, which compiles data primarily from SEC Form 13-F and N-30D filings. We excluded the 12th largest, Citigroup Investment Research, since it did not file its proxy votes on SEC Form N-PX. (Note that Citigroup sold its asset management business to Legg Mason, which subsequently renamed it ClearBridge; both Legg Mason and ClearBridge are included in this report). We also excluded Hotchkis and Wiley Capital Management, the 13th largest holder, because it did not hold any of the other three companies in our survey. We replaced these two firms with Atlantic Trust Private Wealth Management (21st largest) and Deutsche Bank Investment Management (23rd largest), as Harris Associates, the 22nd largest shareholder, did not hold any of the other three companies.

We then collected data on how these 20 investment managers voted on the 17 “problem” directors at the four companies in 2006 using the firms’ Form N-PX filed with the SEC.⁶ Because a particular company may be held by dozens of separate mutual funds managed by a single advisor, we looked at the specific mutual fund that held the largest share in each company and/or a minimum of two other mutual funds within the family. Our assumption is that mutual fund families generally vote as a block.

To determine the ratings, we assigned an equal weight to each company held by a particular investment manager, rather than to each of the directors. Thus, an investment manager that held all four companies and withheld only from Clear Channel’s one “problem” director would receive 25 percent, the same rating as an investment manager that held all four companies and only withheld from all 10 of Home Depot’s “problem” directors. An investment manager that did not hold Clear Channel, and that withheld from all of ExxonMobil’s “problem” directors, would receive a 33 percent rating.

⁶ In one instance, we clarified ambiguous vote disclosure on a firm’s Form N-PX by using proxy voting data provided to a pension fund client of that firm.

Key Findings

Investment Manager Votes on 17 “Problem Directors” at Four Companies

	Clear Channel	Exxon Mobil	Home Depot	United Health	<i>Rating</i>
# of “Problem” Directors	<i>1</i>	<i>4</i>	<i>10</i>	<i>2</i>	
%Withheld by all Shareholders	<i>31%</i>	<i>18-21%</i>	<i>30-36%</i>	<i>28-29%</i>	
AllianceBernstein	not held	0 of 4	10 of 10	0 of 2	33%
Atlantic Trust Private Wealth Management	0 of 1	not held	10 of 10	2 of 2	67%
Barclays Global Investors	1 of 1	4 of 4	10 of 10	2 of 2	100%
Capital Research & Management	0 of 1	0 of 4	0 of 10	0 of 2	0%
ClearBridge Advisors	not held	0 of 4	0 of 10	0 of 2	0%
Columbia Management Advisors	1 of 1	0 of 4	0 of 10	2 of 2	50%
Deutsche Bank Investment Management	0 of 1	0 of 4	0 of 10	0 of 2	0%
Fidelity Management & Research	0 of 1	0 of 4	0 of 10	0 of 2	0%
GE Asset Management	0 of 1	0 of 4	0 of 10	0 of 2	0%
Grantham, Mayo, Van Otterloo	1 of 1	4 of 4	10 of 10	2 of 2	100%
JPMorgan Asset Management	1 of 1	0 of 4	10 of 10	2 of 2	75%
Legg Mason Capital Management	1 of 1	0 of 4	0 of 10	0 of 2	25%
Mellon Capital Management	1 of 1	4 of 4	10 of 10	0 of 2	75%
Neuberger Berman	not held	0 of 4	9 of 10	2 of 2	63%
Northern Trust Global Investments	0 of 1	0 of 4	0 of 10	0 of 2	0%
Putnam Investment Management	not held	0 of 4	10 of 10	1 of 2	50%
State Street Global Advisors	0 of 1	0 of 4	1 of 10	0 of 2	3%
T. Rowe Price Associates	0 of 1	0 of 4	10 of 10	0 of 2	25%
TIAA-CREF Asset Management	0 of 1	0 of 4	10 of 10	0 of 2	25%
Vanguard Group	0 of 1	0 of 4	0 of 10	2 of 2	25%

As the table above illustrates, we found significant variation among the 20 investment managers. For example,

- Investment manager ratings ranged from 0 percent to 100 percent, with a median rating of 25 percent and a mean rating of 36 percent.
- 14 firms withheld their votes from at least one of the 17 “problem” directors at the four companies. Only two firms—Barclays and Grantham, Mayo, Van Otterloo—withheld from all 17 “problem” directors.
- Among the six firms that failed to withhold their votes from any of the 17 “problem” directors is Fidelity, the nation’s largest mutual fund company.
- State Street, a large pension fund manager, only withheld from one of Home Depot’s 10 “problem directors,” and voted for all seven “problem directors” at Clear Channel, Exxon Mobil and UnitedHealth.

 What follows is a detailed description, culled from press stories, independent proxy voting reports, and our own research, of the board failures at each company, and how the 20 investment managers voted on their “problem” directors.

Home Depot

If there was ever a board of directors that rewarded failure, it's Home Depot's. The home improvement company's directors awarded CEO Robert L. Nardelli with more than \$240 million in compensation since he joined the company in late 2000—even as the stock price went nowhere. Meanwhile, stockholders of chief rival Lowe's enjoyed a 177 percent gain.⁷

Our concern that Nardelli's extraordinary pay had undermined investor confidence led the CtW Investment Group to write Bonnie Hill, chair of the board's compensation committee, to ask that she personally step forward at the company's May 2006 shareholder meeting to account for the board's past executive comp decisions and describe the steps it would take to re-establish the link between executive pay and performance. Ms. Hill not only failed to step forward—she failed to even show up. At Nardelli's suggestion, all 10 outside directors boycotted the event, leaving Nardelli to run the show and curtly dismiss angry queries from shareholders.

The subsequent outcry finally led the board to oust Nardelli on January 3, 2007, but not before showering him with a stunning \$210 million in options, severance, and other goodies. Far from resigning in disgrace, the board also waived its mandatory retirement age of 72, thus leaving in place three directors who had played a key role in Nardelli's outsized compensation awards.⁸

It's easy to see why Nardelli's compensation triggered so much shareholder ire: he got paid staggering sums no matter how poorly he served shareholders. Nardelli's pay agreement gave him an annual base salary of not less than \$1.5 million and a guaranteed annual cash bonus of not less than and \$3 million. Despite Home Depot's subpar stock price performance—it fell 8 percent over his tenure—the four members of the board's compensation committee saw fit to pay him even more, granting a base salary and bonus of at least \$6.5 million a year in the fiscal years of 2003 to 2005, reaching a record high of \$9.5 million in the latter year.

In addition, Nardelli was guaranteed an annual stock option grant of not less than 450,000 shares, with an estimated Black-Scholes value of approximately \$6.8 million. In other words, he got a minimum of \$11 million in “not at risk” cash and equity-based compensation every year, in addition to other discretionary pay and perquisites.

Nor did Nardelli's riches end there. Beginning on his 62nd birthday or if his employment was terminated, he stood to receive an annual cash benefit equal to 50 percent of his base salary plus bonus at the time. Home Depot even forgave a \$10 million loan Nardelli received when he first became CEO—plus millions more to offset the taxes he had to pay for borrowing the money.

Nardelli's case so angered many that all directors but one received withhold totals of 30 percent or greater from all Home Depot shareholders in 2006. Only Angelo R. Mozilo, who was new to Home Depot's board in 2006, escaped much censure, although even he received a fairly high 8 percent withhold vote.⁹

⁷ Duhigg, “Investor Seeks Review of Home Depot's Management,” THE NEW YORK TIMES, (Dec. 19, 2006).

⁸ Clark, “Blame the Board,” FORBES.COM, (Jan. 3, 2007).

⁹ Institutional Shareholder Services, “Home Depot Inc.”, (May 12, 2006).

Home Depot's 2006 Director Election

Investment Manager	Problem Directors									
	<i>Brenneman</i>	<i>Clendenin</i>	<i>Gonzalez</i>	<i>Hart</i>	<i>Hill</i>	<i>Jackson</i>	<i>Johnston</i>	<i>Langone</i>	<i>Nardelli</i>	<i>Ridge</i>
AllianceBernstein	W	W	W	W	W	W	W	W	W	W
Atlantic Trust	W	W	W	W	W	W	W	W	W	W
Barclays Global	W	W	W	W	W	W	W	W	W	W
Capital Research	F	F	F	F	F	F	F	F	F	F
ClearBridge Advisors	F	F	F	F	F	F	F	F	F	F
Columbia Management	F	F	F	F	F	F	F	F	F	F
Deutsche Bank	F	F	F	F	F	F	F	F	F	F
Fidelity	F	F	F	F	F	F	F	F	F	F
GE Asset Management	F	F	F	F	F	F	F	F	F	F
Grantham, Mayo, Van Otterloo	W	W	W	W	W	W	W	W	W	W
JPMorgan	W	W	W	W	W	W	W	W	W	W
Legg Mason	F	F	F	F	F	F	F	F	F	F
Mellon Capital	W	W	W	W	W	W	W	W	W	W
Neuberger Berman	W	W	W	W	W	W	W	W	W	F
Northern Trust	F	F	F	F	F	F	F	F	F	F
Putnam Investment	W	W	W	W	W	W	W	W	W	W
State Street Global	F	F	W	F	F	F	F	F	F	F
T. Rowe Price	W	W	W	W	W	W	W	W	W	W
TIAA-CREF	W	W	W	W	W	W	W	W	W	W
Vanguard Group	F	F	F	F	F	F	F	F	F	F
Shares Withheld by all Shareholders	31%	31%	36%	31%	32%	30%	32%	32%	32%	31%

F- voted for; W: votes withheld; "--": shares not held

Clear Channel Communications

The San Antonio-based radio giant, which owns 1,150 radio stations and one of the nation's largest outdoor-ad businesses, has never really broken out of the cozy, family-owned management style that began when the Mays family founded it in 1972. Even as the stock price lagged rivals for years, the nominally independent board overpaid the three Mays, who collectively control 7% of the stock¹⁰ and sit as its Chairman (co-founder L. Lowry Mays), CEO (Mark Mays), and President and CFO (Randall Mays).

For example, in 1999 the board's comp committee awarded all three extraordinarily generous severance "golden parachutes." If the company undergoes a change in control or if any is asked to reduce their pay, duties, or title, the Mays get a bonus of between \$1-3 million and a lump sum cash payment equal to three times their base salary and bonus. In addition, the executives are entitled to one million fully vested stock options as of the date of termination—or a grant of company stock of equal value—and may immediately exercise any unvested stock options.¹¹

Clear Channel stockholders have reason to doubt that the rest of the 11-member board will put their interests ahead of the Mays', even though they're officially independent. Three have been directors since the company went public 23 years ago. Attorney Alan Feld, for example, attended Highland Park High School in Dallas with one of the Mays and was an early partner at Akin Gump Strauss Hauer & Feld LLP, which has long done legal work for Clear Channel, including advising on the potential buyout. Another 23-year board member, Theodore H. Strauss, is the brother of Akin Gump partner Bob Strauss. Meanwhile, comp committee head John H. Williams, who was a Mays classmate at Harvard Business School, helped underwrite the company's IPO when he was a banker at Dallas-based Schneider, Bernet & Hickman.¹²

In mid-November 2006, Clear Channel concluded a search for a buyer that reinforced questions about the board's independence. The company agreed to be purchased by two private-equity groups, Thomas H. Lee Partners and Bain Capital Partners, for \$18.7 billion. According to the Wall Street Journal, if the deal goes through, Lowry Mays would step down as chairman and sell his 29 million shares for nearly \$1.1 billion; his sons Mark and Randall, meanwhile, would keep their posts, and would receive options for as much as 2.5% of the company. Such conflicts—and suspicions that the price is too low—now threaten to torpedo the deal.¹³

While this deal reinforced the Clear Channel board's credibility problem, unlike at Home Depot, shareholders withheld significant votes from only one Clear Channel director in 2006, John H. Williams, the head of the compensation committee who had recommended the Mays's original compensation contracts in 1999.¹⁴ Even so, most of the investment managers holding the stock stuck by Williams.

¹⁰ Mulligan, "Clear Channel to be sold for \$18.7 billion", LOS ANGELES TIMES (Nov. 17, 2006).

¹¹ Institutional Shareholder Services, "Clear Channel Communications," (Apr. 12, 2006).

¹² McBride and Berman, "Clear Channel Buyout Talks Fuel Concern of Management Conflicts," THE WALL STREET JOURNAL, (Nov. 14, 2006).

¹³ Berman and McBride, "Clear Channel Showdown Signals Investor Wariness of Privatizations," THE WALL STREET JOURNAL, (Jan. 27, 2007).

¹⁴ Institutional Shareholder Services, "Clear Channel Communications," (Apr. 12, 2006), at 7.

Clear Channel's 2006 Director Election

Investment Manager	Problem Director
	<i>Williams</i>
AllianceBernstein	-
Atlantic Trust	F
Barclays Global	W
Capital Research	F
ClearBridge Advisors	-
Columbia Management	W
Deutsche Bank	F
Fidelity	F
GE Asset Management	F
Grantham, Mayo, Van Otterloo	W
JPMorgan	W
Legg Mason	W
Mellon Capital	W
Neuberger Berman	-
Northern Trust	F
Putnam Investment	-
State Street Global	F
T. Rowe Price	F
TIAA-CREF	F
Vanguard Group	F
Shares Withheld by all Shareholders	31%

F- voted for; W: votes withheld; "-": shares not held

ExxonMobil Corp.

Former CEO Lee Raymond became a poster child for out-of-control executive pensions when he retired in December, 2005 with a \$98 million retirement payout. The princely sum, coming on top of his \$49 million pay package for that year, brought widespread criticism for its lack of connection to the company's performance under Raymond's tenure.

It's not just the amount that was objectionable but the contortions ExxonMobil directors allowed the company's compensation experts to go through to come up with it. To calculate Raymond's pension, the company included both his annual base salary and bonus, plus yet another payment based on how much the company's earnings had increased each year. In other words, Raymond was double-dipping, getting paid once in his annual compensation for ExxonMobil's earnings performance, and a second time for that same performance in his pension. This tactic hugely inflated his winnings. For example, Raymond's estimated lump-sum pension distribution jumped by \$17 million, to \$98.4 million, from February 2005 to February 2006 alone.¹⁵

Even though investors complained, the board's compensation committee did nothing to alter the practice. ExxonMobil shareholders meted out modest signs of displeasure in 2006, withholding roughly 20% from the committee's four existing members: James R. Houghton, William R. Howell, Reatha Clark King, and Walter V. Shipley. Most investment managers backed these four despite such questionable judgment.

Still, the excessive retirement package remains in effect for Raymond's successor, Rex W. Tillerson, and other top executives. "Thus, years from now, shareholders can expect another eye-popping pension distribution for Mr. Tillerson," concluded a scathing analysis from Institutional Shareholder Services, a leading proxy voting advisory firm.

¹⁵ Institutional Shareholder Services, "ExxonMobil Corp." (May 19, 2006).

Exxon Mobil's 2006 Director Election

Investment Manager	Problem Directors			
	<i>Houghton</i>	<i>Howell</i>	<i>King</i>	<i>Shipley</i>
AllianceBernstein	F	F	F	F
Atlantic Trust	-	-	-	-
Barclays Global	W	W	W	W
Capital Research	F	F	F	F
ClearBridge Advisors	F	F	F	F
Columbia Management	F	F	F	F
Deutsche Bank	F	F	F	F
Fidelity	F	F	F	F
GE Asset Management	F	F	F	F
Grantham, Mayo, Van Otterloo	W	W	W	W
JPMorgan	F	F	F	F
Legg Mason	F	F	F	F
Mellon Capital	W	W	W	W
Neuberger Berman	F	F	F	F
Northern Trust	F	F	F	F
Putnam Investment	F	F	F	F
State Street Global	F	F	F	F
T. Rowe Price	F	F	F	F
TIAA-CREF	F	F	F	F
Vanguard Group	F	F	F	F
Shares Withheld by all Shareholders	20%	21%	20%	18%

F- voted for; W: votes withheld; “-“: shares not held

UnitedHealth Group Incorporated

Although Home Depot directors made fools of themselves by refusing to face shareholders, in some respects their counterparts at UnitedHealth may have committed even worse omissions. For years, a group dubbed “one of America’s most pliant boards” by the Wall Street Journal allowed former CEO William McGuire the right to pick the grant date for his own stock options. Even though UnitedHealth’s stock had soared 5-fold during his 15-year reign, McGuire decided that this didn’t give him enough. So he backdated his options, according to an investigation directors finally commissioned after the practice was exposed in the press. The result: McGuire collected close to \$2 billion. (After he was forced out in October, 2006, he agreed to surrender about \$200 million of his ill-gotten gains, but the company wants to take back hundreds of millions more).

UnitedHealth’s experience offers a case study in why even wildly successful corporate leaders need somebody watching to make sure they don’t cheat. As McGuire built the insurer into one of the nation’s powerhouse health providers, awed directors behaved more like cheerleaders than watchdogs. He helped the process in imperial fashion, using his power as CEO to benefit and co-opt them. McGuire made sure that both the company and his own family foundation gave generously to charities some directors were involved with. McGuire also invested \$500,000 in a business run by William Spears, the head of the company’s Compensation Committee, and placed over \$55 million in McGuire family assets under Spears’ management.¹⁶

The upshot was that no one was watching when McGuire chose the dates on which he would take his options. Although he vigorously denied back-dating them, several grants were dated just before runups in UnitedHealth’s stock. And three times, McGuire took his options at the lowest closing price of the year. The odds of hitting all these low points by pure luck were on the order of one in 300 billion. UnitedHealth’s star struck board compounded the problem by awarding McGuire a guaranteed minimum of 2.6 million options annually, regardless of how the company performed. Although the stock did in fact do spectacularly well, directors made sure that he would rake in millions even if it had just crawled upward.¹⁷

Many of McGuire’s board buddies stuck by him even after the law firm they brought in found clear evidence to support the backdating allegations, and finally dumped him only after their lawyer told them federal regulators appeared likely to charge the UnitedHealth chief. Their vigorous neglect has left a mess, including a formal SEC investigation and a \$1.53 billion charge to earnings to fix the improper accounting for backdated stock options.¹⁸

Investors didn’t register strenuous displeasure in 2006, only withholding votes from the two directors on the compensation committee who were up for election (UnitedHealth’s board is staggered, so only four members faced election last year). These two were James A. Johnson and Mary O. Mundinger, who racked up withholds of 29% and 28%, respectively.

¹⁶ Bandler and Forelle, “How a Giant Insurer Decided To Oust Hugely Successful CEO,” THE WALL STREET JOURNAL, (Dec. 7, 2006).

¹⁷ Institutional Shareholder Services, “UnitedHealth Group Incorporated,” (Apr. 27, 2006).

¹⁸ “United’s Stock-Option Tab: \$1.53 Billion,” STAR TRIBUNE (Mar. 7, 2007).

UnitedHealth's 2006 Director Election

Investment Managers	Problem Directors	
	<i>Johnson</i>	<i>Mundinger</i>
AllianceBernstein	F	F
Atlantic Trust	W	W
Barclays Global	W	W
Capital Research	F	F
ClearBridge Advisors	F	F
Columbia Management	W	W
Deutsche Bank	F	F
Fidelity	F	F
GE Asset Management	F	F
Grantham, Mayo, Van Otterloo	W	W
JPMorgan	W	W
Legg Mason	F	F
Mellon Capital	F	F
Neuberger Berman	W	W
Northern Trust	F	F
Putnam Investment	W	F
State Street Global	F	F
T. Rowe Price	F	F
TIAA-CREF	F	F
Vanguard Group	W	W
Shares withheld by all Shareholders	29%	28%

F- voted for; W: votes withheld; “-“: shares not held