

## THE RICH GET RICHER -- AND SHAREHOLDERS ARE NOT AMONG THEM

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Forbes Magazine published a very interesting list in their October issue highlighting the \$100 million club. This list consisted of 31 companies whose CEO's each have in excess of \$100 million in VESTED options.

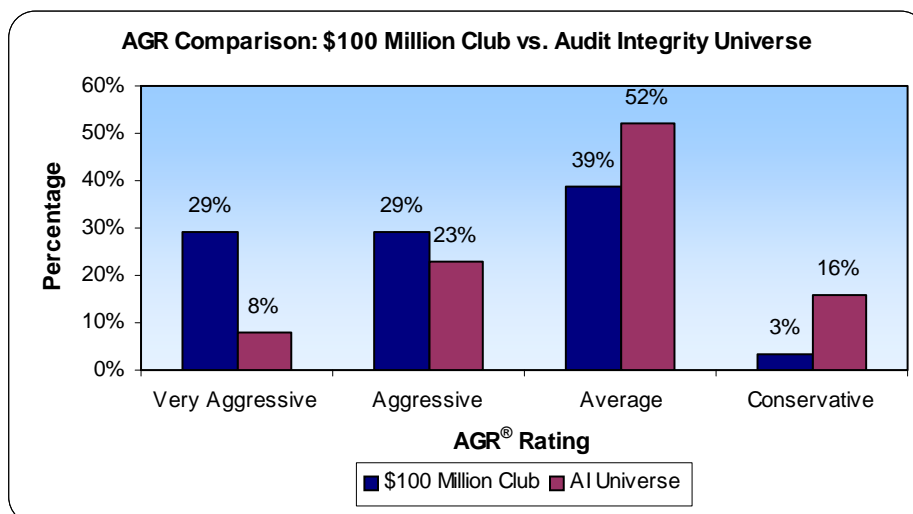
While this list ignores salary levels, bonus payments and unvested options, it makes a point: compensation for CEO's is absurdly high. However, the more important aspect of this exercise is the fact that these CEO's are raking in the dough while their shareholders are eating peanut butter sandwiches.

The New York Times published a set of interesting graphs in their October 20 edition. The graphs point out that over the last ten years, a time period that matches the acceleration of option grants to executives, the U.S. stock market's compound return was less than 4% per year (adjusted for inflation). This long-term return is far below historic real rates of return and comes nowhere near compensating shareholders for the risk they bear, nor does it justify the excessive awards lavished on management.

Company managers have argued that high compensation, particularly in the form of options, is a sure-fire motivation for executives to produce results for their shareholders. Unfortunately, the evidence supports a very contrary outcome. Why? Because over the short run, corporate management has substantial control over outcomes and information -- two ingredients that shareholders lack.

Management can, and often does manipulate the numbers to mask the true fundamentals of a company. Furthermore, they can – and frequently do - time the sale of their own holdings to occur in advance of the ultimate disclosure of problems they have concealed. The shareholders are left holding an investment that has suddenly become less desirable, which the market fixes by lowering the price of the stock.

This market response sometimes occurs quickly, but more often is seen over longer periods as hidden information comes to light. An examination of this phenomenon is ever so clear in the following graph.



How can shareholders determine whether their stock is vulnerable? Over 50% of the companies listed in the \$100 million dollar club are rated Very Aggressive or Aggressive by Audit Integrity, versus the overall population of only 31%, hardly a random sample. Furthermore the Audit Integrity Equity Model has identified a number of these companies to be substantial underperformers over the next three months to a year (see table below).

<b>The \$100 Million Club</b> (Ranked in order of Vested Options (\$))					
<b>Ticker</b>	<b>Company Name</b>	<b>5=Best, 1=Worst Equity Model Ranking</b>	<b>AGR® Ranking</b>	<b>100=Best, 0=Worst  AGR® Score</b>	<b>Insider Selling Flag*</b>
UNH	UnitedHealth Group Inc.	2	Aggressive	49	No
ORCL	Oracle Corporation	1	Very Aggressive	35	No
COF	Capital One Financial Corp.	1	Very Aggressive	18	No
TOL	Toll Brothers, Inc.	2	Very Aggressive	41	No
CMX	Caremark Rx, Inc.	4	Average	76	No
VNO	Vornado Realty Trust	2	Average	62	No
YHOO	Yahoo! Inc	2	Average	62	No
CFC	Countrywide Financial Corporation	1	Very Aggressive	27	No
OXY	Occidental Petroleum Corporation	4	Average	74	No
AET	Aetna Inc.	2	Aggressive	43	Yes
FDX	FedEx Corporation	4	Average	74	No
IACI	IAC/InterActiveCorp	2	Aggressive	44	No
COP	ConocoPhillips	4	Average	61	No
EBAY	eBay Inc.	1	Very Aggressive	22	No
AMTD	TD Ameritrade Holding Corp.	2	Aggressive	52	No
GILD	Gilead Sciences, Inc.	1	Very Aggressive	21	No
MAR	Marriott International Inc.	4	Average	77	No
BER	W.R. Berkley Corporation	5	Conservative	80	No
UTX	United Technologies Corporation	2	Aggressive	46	No
TGT	Target Corporation	2	Average	66	No
FNF	Fidelity National Financial	1	Very Aggressive	17	Yes
ERTS	Electronic Arts Inc.	2	Aggressive	50	No
SNDK	SanDisk Corporation	1	Very Aggressive	24	Yes
ASD	American Standard Companies Inc.	4	Average	67	No
FRX	Forest Laboratories, Inc.	4	Average	66	No
CSCO	Cisco Systems, Inc.	2	Aggressive	54	No
BBY	Best Buy Co., Inc.	2	Very Aggressive	36	No
OCR	Omnicare, Inc.	3	Average	62	No
KBH	KB Home	2	Aggressive	53	Yes
CTX	Centex Corporation	2	Average	61	No
MCK	McKesson Corporation	2	Aggressive	44	No

\* Flag represents the top 20% Directors and Officers selling within the industry over the trailing 12 months

Given Audit Integrity's ability to use forensic techniques to ferret out problems before they are generally recognized, I suggest that investors pay attention to the early warning signs before they are left with peanut butter on their hands.

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