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ETHICS

CEOs Who Began Their Careers During Booms Tend to Be Less Ethical

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When Alan Greenspan addressed the Harvard University class of 1999, he shared a message of wealth and prosperity that was reflected in many aspects of American life. “You are being bequeathed the tools for achieving a material existence that neither my generation nor any that preceded it could have even remotely imagined as we began our life’s work,” he told the new graduates. The stock market had more than doubled in the previous five years, and the unemployment rate was at a 30-year low. The United States, Greenspan reminded graduates, was enjoying, “the greatest prosperity the world has ever experienced.”

Imagine you were sitting in the audience that day, about to begin constructing your career. What might you have expected the future to hold? Would these expectations have been different if you had entered the working world just 10 years later, during the Great Recession?

Young adulthood tends to be a particularly impressionable period of life. People often have a strong affinity for movies, music, and books that were popular during these formative years. It is also a time when people explore and solidify attitudes. The state of the economy can affect which values and concerns people champion for the rest of their lives. For instance, people who entered adulthood during economic depressions tend to be attuned to economic and national security throughout their adult lives, and particularly cautious with their personal and professional finances.

Entering adulthood in a boom or a bust can also have implications for your behavior at work, even decades later. CEOs who began their careers in prosperous times tend to use riskier financial strategies than CEOs who first entered the workforce in recessions. Those coming of age during booms tend to be more excessively confident in their own abilities, believe they are entitled to better outcomes, and pay themselves substantially more than other top executives.

Based on these previous findings, we wondered: Would CEOs who began their careers during boom times be less ethical?

Our question stemmed from the idea that prosperous times are often linked to ethical missteps. During booms, credit eases, conspicuous consumption proliferates, and fortunes swell. Speculation, swindling, and fraud often thrive as more people seek a piece of the expanding wealth, and wrongdoing is easier to hide under outsize profits. Moreover, risk appetite, optimism, and overconfidence increase during booms, any of which can increase the likelihood of someone traversing ethical lines. Indeed, social commentators have long noted that nearly every economic boom in United States history is associated with widespread unethical behavior, ranging from pervasive corruption during the Gilded Age to the sub-prime lending practices of the mid-2000s.

Given that early career conditions can leave an enduring mark on the work systems and mental models that people carry with them throughout their adult lives, we expected that CEOs who began their careers in good economic times would be more likely to cheat later on. For CEOs who began their careers when jobs were plentiful and ethical shortcuts were more prevalent, cutting corners or bending rules may become the template for how things are done and what it takes to succeed and survive. Once people become adept at rationalizing unethical actions (e.g., “I’m simply getting what I deserve”), these ways of thinking tend to be carried to other situations and domains.

We tested our hypothesis by examining the stock option backdating done by 2,012 American CEOs during a 10-year period, from 1996 to 2005. Backdating was a fairly common unethical, and almost always illegal, practice during this time period. Here’s how it worked: A CEO would receive a stock option grant on one date but report to the SEC that the grant was received on a different date, when the stock price was lower. This would allow a CEO to realize a larger financial gain when they sold the stock, by falsifying financial records and lying to the SEC. In March 2006 the Wall Street Journal published a story chronicling the suspiciously lucky timing of stock option awards at six large companies. After that, many CEOs were fired or forced to return ill-gotten gains, and reporting requirements were changed to make backdating much more difficult.

Backdating is very difficult to prove beyond a reasonable doubt, because there is always a chance that a CEO was simply extremely lucky. This is why so few executives were criminally convicted of backdating. But it is possible to identify CEOs who were repeatedly, suspiciously lucky. Drawing on a procedure developed by other scholars, we considered a stock likely to have been backdated if it was received on one of the most favorable days of the reporting period. While it’s probable that some CEOs were incredibly lucky, studies have repeatedly shown that CEOs were “lucky” much more often than chance alone would predict. Indeed, based on our procedure, 2.5% of grants should have been awarded on incredibly lucky dates by chance alone. In our sample, however, nearly 15% of grants were received on extremely lucky dates.

We then gathered information on the educational history of each CEO in our sample. We compiled information about where each CEO went to school, what degrees they earned, and the year they graduated (primarily in the 1960s, 1970s, and 1980s). We then examined whether CEOs who earned their highest degrees in best economic times, when the unemployment rate was particularly low, were more likely to backdate their stock options. They were. Even after adjusting for firm size, industry, number of options granted, and other factors, we found that CEOs who graduated in the best economic times were approximately 30% more likely to falsify the dates of their stock option grants than CEOs who graduated in the worst economic times. Quite simply, CEOs who began their careers in a boom were more likely to cheat.

There is no question that graduating during a recession has downsides. Recession graduates tend to earn less and hold less-prestigious positions than their boom-time peers. If they do become CEOs, research suggests they will probably lead smaller, less prestigious companies. Despite these disadvantages, recession graduates may make particularly good employees and executives. Other work has shown that these graduates are more satisfied workers, are less narcissistic, and tend to stay with their companies longer. Our work suggests that they may be more ethical, too.

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