

**EXECUTIVE TURNOVER IN THE STOCK OPTION BACKDATING WAVE:
WHEN A FIRM GETS IMPLICATED MAKES A DIFFERENCE**

By

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ABSTRACT

Corporate misconduct can inflict damage to a firm's image and reputation, as well as undermine its legitimacy. Prior research has found that a firm involved in misconduct seeks to restore or repair damage to its legitimacy. However, previous research has largely examined corporate misconduct in isolation; therefore we know little about the role of the firm's social context. In this study, we argue that the social context surrounding corporate misconduct is likely to be influenced by the pervasiveness of the activity; thus the perceived severity of the transgression diminishes as the incidence of the activity increases, which in turn reduces the need for the implicated firm to take decisive action to repair or restore its legitimacy. We utilize the 2006 stock option backdating scandal, in which firms illegally manipulated stock options' grant dates, to test this argument. Our paper proposes and finds that firms implicated earlier in the stock option backdating scandal were more likely to remove the executives responsible for the misconduct than were firms implicated later. Our study contributes to our understanding of how a firm's response to its misconduct can be influenced by an important aspect of the firm's social context – namely the pervasiveness of corporate misconduct.