CalPERS Leads Charge in Backdating Class Action

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The California Public Employees Retirement System ("CalPERS"), the largest U.S. public pension fund, was appointed lead plaintiff in the options backdating securities class action suit against UnitedHealth, Inc. on September 14. The action is currently pending in the Federal Court in Minnesota. Lerach Coughlin was also approved as lead class counsel.

The class action suit against UnitedHealth challenges the most significant and egregious example of executive malfeasance in what has become known as the “options backdating scandal.” CalPERS is seeking to recover billions in investor losses and disgorgement of hundreds of millions of dollars of insider trading profits – including over $136 million from William W. McGuire, UnitedHealth’s Chief Executive Officer, who allegedly orchestrated the options backdating scheme – and to void the prior election of UnitedHealth directors and other corporate reforms. While most of the options backdating cases filed thus far have been stockholder derivative actions to recover the damages sustained by the affected companies, CalPERS’ UnitedHealth case seeks class-action status due to the large damages sustained by investors in the company as a result of the actions of insiders. In addition, the suit seeks important non-monetary relief, including reforming corporate governance and forcing the corporate insiders to bear their own legal fees arising out of the stock option backdating scandal.

The CalPERS suit alleges that in late February 2006, amid a slew of articles about options backdating, McGuire learned that The Wall Street Journal was working on a story which would tie UnitedHealth and its executives to the scandal. McGuire then quickly sold 2.3 million of his UnitedHealth shares, which he had received via stock options, pocketing $136 million in sales proceeds.

On March 18, 2006, The Wall Street Journal published its article, raising questions about whether several public companies had been manipulating stock option grants to enrich executives by backdating these grants to lower prices. The article specifically mentioned UnitedHealth and McGuire. UnitedHealth immediately suspended all stock option grants to executives. The CalPERS suit also alleges that UnitedHealth’s 2002-2004 Proxy Statements were false and misleading, allowing the directors to be re-elected.

UnitedHealth’s common stock allegedly traded at artificially inflated prices during the class period, reaching a high of $64.61 on December 21, 2005. Certain defendants took advantage of the company’s inflated stock price by selling millions of shares of their UnitedHealth stock for illegal insider trading proceeds of more than $235 million. The value of these insider shares sold was further enhanced due to improper “backdating” and “spring-
loading” of the options.

On May 11, 2006, UnitedHealth revealed that the SEC was investigating the company. It admitted there had been “significant deficiencies” in its granting of and accounting for stock options to its executives, and that it would likely have to restate its financial results for the past three years to eliminate well over $450 million in profits.

On May 17, 2006, the company revealed a grand jury investigation of its stock option activities and a request from the IRS for years of documents. UnitedHealth stock collapsed to as low as $42.09 per share.

The suit alleges that the artificial inflation of UnitedHealth’s stock allowed its top officers to reap hundreds of millions of dollars via insider trading, and the falsification of its financial statements contributed to huge bonuses for insiders. By contrast, the purchasers and owners of UnitedHealth’s stock were damaged – the ownership of UnitedHealth by public stockholders was improperly diluted as the company’s executives received millions in stock options at lower option prices than they were entitled to.

In re UnitedHealth Group Inc. PSLRA Litig., No. 06-1691-JMR-FLN, Order (D. Minn. Sept. 14, 2006).