

United States Department of Justice

For Immediate Release

April 21, 2010 **United States Attorney's Office**
Central District of California

Former CEO of KB Home Convicted of Federal Fraud Charges Related to Stock Option Backdating in Which He Awarded Himself Millions of Dollars in Compensation

LOS ANGELES—Bruce E. Karatz, a former CEO and chairman of the board of KB Home, was convicted today of four felony counts related to a stock option backdating scheme in which he awarded himself and other KB executives millions of dollars in undisclosed stock-based compensation.

Karatz, 64, of Bel Air Estates, was found guilty of two counts of mail fraud, one count of making false statements in a quarterly report filed with the Securities and Exchange Commission, and one count of making false statements to KB's outside accounting firm, Ernst & Young. The convictions stem from Karatz's attempts in 2006 to cover-up the fact that he had been backdating his own and other executive's stock options for the preceding seven years. The cover-up included failures to disclose the stock-option backdating in filings with the Securities and Exchange Commission and to KB's outside auditors.

As a result of today's guilty verdicts, Karatz faces a statutory maximum sentence of 80 years in federal prison. United States District Judge Otis D. Wright II, who presided over a six-week trial, is scheduled to sentence Karatz on September 8. Karatz was convicted of concealing a backdating scheme in which he participated, a scheme that hid the true nature and value of stock-based compensation KB had actually been awarding to Karatz and other KB executives through its stock-option granting practices. During the backdating scheme, Karatz caused below-market exercise prices to be selected for stock options granted to him and other KB executives by using hindsight to backdate the grant date of these options to the date with the lowest price point for KB's stock.

After KB commenced an internal investigation into its option-granting practice in May 2006, Karatz concealed that he had backdated KB's stock option grants during the preceding seven years. Among other things, Karatz caused a false and misleading internal report to be presented to KB's Audit Committee and to Ernst & Young. The false report said there was "no evidence of the backdating of options or other manipulation by management." KB's Audit Committee and other members of KB's management relied on this false and misleading internal report when filing a Form-10Q for the second quarter of 2006 that failed to disclose any irregularities in KB's past option-granting practices.

After KB discovered irregularities in its reporting, KB was unable to timely file its third quarter 10Q in October 2006. When KB ultimately filed its 2006 third quarter Form-10Q and its 2006

Form-10K in February 2007, the company was forced to recognize, for the first time, more than \$36 million in additional stock-based compensation expenses and a total increase of more than \$70 million in accrued liabilities arising from adjustments required to address the backdated stock options. The jury that convicted Karatz acquitted him on 16 other counts.

This case was investigated by the Federal Bureau of Investigation.