



#### This 3DAdvisors Report Covers:

- ✓ **Insider Trading:** Insider Trading Behavior
- Accounting:** Quality of Earnings Issues
- Governance:** Corporate Governance Issues

## Disclosure of Forward Sales Meant to Avoid Detection Jabil Circuit, Inc. (NYSE:JBL)

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Jabil Circuit, Inc. is a worldwide independent provider of electronic manufacturing services (EMS). The Company designs and manufactures electronic circuit board assemblies and systems for original equipment manufacturers (OEMs) in the networking, telecommunications, computing and storage, instrumentation and medical, computer, peripherals, automotive and consumer products industries. Jabil serves its OEM customers with work cell business units that combine high-volume, highly automated, continuous-flow manufacturing with advanced electronic design and design for manufacturability technologies. The Company's customers include Cisco Systems, Inc., Dell Computer Corporation, Hewlett-Packard Company, Johnson Controls, Inc., Intel Corporation, Valeo, Lucent Technologies, Nokia Corporation, Marconi Communications plc (Marconi) and Royal Philips Electronics (Philips).

### Summary of 3DAdvisors Findings for JBL

- **Insider Trading:** Disclosure of forward sales meant to avoid detection

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### Discussion of 3DAdvisors Findings

#### Insider Trading: Disclosure of forward sales meant to avoid detection

It's one thing when we see an anomalous convergence of insiders selling, it's another thing when they do it in a way that seems meant to avoid detection. Recently, we have spotted both occurring at Jabil Circuit. This situation gets our attention due to the unusual insider trading behavior, but one could also argue that the manner in which the disclosure takes place makes this a governance story as well.

In June and July, four Jabil insiders entered into Prepaid Variable Forward Contracts with brokerage firms. This type of contract should be well known by now. For those not familiar with them, suffice it to say that these contracts allow for an individual to monetize a position by committing to the delivery of the underlying shares, at a later

date, at the market price of the shares at the contract's expiration date. The insiders involved receive cash up front in consideration for the deal.

This type of insider sale frequently slips detection from the public eye. A particular matter catching our attention, with regards to these forward sales, was the fact that their filings were submitted in a way that would suggest, to the untrained eye, that the individuals involved may be actually picking up contracts to buy shares, not sell them. We say this because in each case, the derivative transaction being reported, on each individual's filing (remember, these forward sales are derivatives) was made to look like a "purchase" of a derivative contract. This is an unusual and highly deceptive way to present this sort of transaction. Make no mistake about it; thorough reading of the related footnotes presents no doubt about the fact that the derivative contracts involved the forward sales of the insiders involved.

Another interesting aspect of these sales is the "hit and run" nature of their disclosure. By this we mean that, once the disclosure of a forward sale shows up on a Jabil insider's Form 4 filing, it is not seen again on that person's future Form 4's. Over the years, we have become accustomed to seeing evidence of Forward Sales repeated, on an individual's subsequent Form 4's. In Jabil's case, if you missed it on the first round, you're out of luck. We view this as another deceptive filing practice.

Perhaps the most interesting nature of forward sales is that those involved are willing to take in cash now, and bet that their shares will be lower at the expiration of the contract.

**Thomas Samsone (53)** – Vice Chairman and former Jabil President. Samsone, a regular seller during the 1999 – 2000 peak period, began selling again in December of 2002, clearing out of 47,330 shares in the \$17.75 range. In April of 2003, he got out of 100,000 in the same price range. On June 25<sup>th</sup>, though, with Jabil shares trading in the \$22 to \$23 range, Samsone entered into a forward contract to deliver another 250,000 Jabil shares (delivery date, June 25, 2006).

**Mel Lavitt (65)** – Director. Lavitt was a bit early when, in September of 2002, he entered into a Forward Contract to sell 208,000 Jabil shares one-year later (September of 2003). This transaction represented about 69% of his position at the time. On June 24, 2003, Lavitt managed to alter the agreement to extend the delivery of 60,000 of the shares out to January 24, 2005. Prior to this, Lavitt had not sold a share since July of 2000.

**Chris Lewis (42)** – CFO. Prior to recent activity, CFO Chris Lewis hadn't sold a share since April of 2000. His profile changed in July, however, when on the 7<sup>th</sup> he entered into a forward contract to sell 20,000 shares on the contract expiration date of July 7, 2005.

**Forbes Alexander (42)** – Treasurer. On June 4<sup>th</sup>, Alexander entered into a forward contract to sell 10,000 shares three years out. On June 18<sup>th</sup> he acted again, entering into a separate contract to sell another 10,000 shares on June 18<sup>th</sup>, 2005. Prior to these, he had not sold a share since July of 2000. Interestingly enough, just one month later, Alexander exercised his total amount of two long-vested options series, series that were not set to expire until at least 2006. In selling the underlying shares, he

cleared out of an additional 20,498 shares of his holdings. His Form 4's, relating to the July sales, bore no mention of his June forward sale contracts.

**John Patrick Redmond (42)** – Controller. On June 4th, Redmond cleared out of two separate, long-vested, options series and sold the underlying shares. These options had been vested since at least early 1999 and were not set to expire until 2008. These transactions resulted in his sale of 29,600 shares, by far his largest sales on record.

While some may focus on the 1.2 million shares sold by Chairman William Morean, between March and July, we find his sales to lose significance when compared to those mentioned above. After all, Morean held about 33.5 million shares prior to his sales. In all, between March and early July, a total of eleven insiders have sold 1.4 million Jabil shares in the open market. This does not count the forward sales. Taking Morean's sales out of the number, the Company could point to the 200,000 shares sold by the rest as a normal event, normal that is, unless they want to add those 498,000 shares, pledged to forward sales, back into the equation.

It is interesting to us how the transactions we are focusing on occurred both before and after the June 18th Q3 release. One of the key points, emerging from the release, and subsequent conference call, was the fact that the consumer business (expected to be driven by new acquisitions from Philips) was up only 7% vs. expectations of 13% to 15%. There were a number of questions concerning this, and the Philips acquisitions in general, fielded during the call.

One of the insiders mentioned above, the Company Treasurer, entered into a forward sale contract (his second of the month) on the day of the release and subsequent conference call. In that light, we also find it extremely interesting that the list of insiders, whose selling have caught our attention, include so many members of the financial team (CFO, Treasurer and Controller). This convergence of so many long-dormant sellers, during the same time frame, seems less-than-coincidental. Consequently, we will be monitoring this issue closely in the near-term.

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