



THE HIGH COST OF FLIGHT

Kobi Alexander's journey from hi-tech visionary to convicted felon

US DISTRICT Judge Nicholas Garaufis stared sternly at the defendant dressed in brown prison garb, in the dock of a Brooklyn courtroom, and said, "I really don't understand how someone as brilliant and accomplished and focused and respected as you could be so incredibly, abjectly foolish to make some of the decisions you made."

The 64-year-old defendant, Jacob "Kobi" Alexander, an Israeli hi-tech visionary and founder of the once market-leading company Comverse, replied, "I'm truly sorry for everything I have done wrong. I deeply regret running away instead of dealing with the justice system like I should have. All I ask is, when you sentence me today, you pay attention to the good in addition to the bad... For the majority of my life, I lived honestly and worked very hard."

On February 23, Judge Garaufis sentenced Alexander to 30 months in prison for securities fraud involving backdating of options. Alexander will serve his sentence at a Pennsylvania prison, though he may ask to serve part of it in Israel. The sentence was a bit more than the two years Alexander's lawyers sought but far less than the 10-year maximum the law specifies. He is eligible for a one-third reduction for good behavior.

The sentence brings to an end a decade-long saga.

In late June 2006, Alexander left the US

for a vacation in Israel. His lawyers had arranged with US authorities that he would return to face indictment on July 31 for securities fraud related to the backdating of options for himself and some senior employees from 1998 to 2001.

HOWEVER, RATHER than face trial, he fled with his wife and children to the desert nation of Namibia, on Africa's southwest coast, from where he felt he could not be extradited. (He fled Israel because Israel and the US have an extradition treaty.)

Namibia is a huge arid nation, mostly desert, 40 times the size of Israel with just two million people. It was first colonized by Germany, then ruled by South Africa, achieving full independence only in 1990.

Alexander and his family spent more than a decade in exile, in Windhoek, Namibia, and his wife and children stood by him the entire time. He voluntarily returned to the US in August 2016 and was at once arrested and jailed. At the time, he asked Garaufis to release him on a \$25 million bail bond but the judge refused so Alexander has been incarcerated since.

Why did Garaufis call Alexander "brilliant" and "accomplished"?

It was an understatement. In 1982, Alexander, then an investment banker, joined with engineer Boaz Misholi and Alexan-

der's brother-in-law Yechiam Yemini, a Columbia University computer science professor, to launch Efrat Future Technologies, the name of which later was changed to Comverse Technology – Comverse being a fusion of the words "communication" and "versatility."

The company became a market leader in voicemail hardware and software sold to telecom companies. It was the first Israeli company to be included in the prestigious Standard & Poor's 500 Index, and did a successful initial public offering of stock on NASDAQ in 1986. Alexander became the company's CEO and chairman in 1987, when he was only 35.

As mobile-phone use boomed, Comverse's revenues soared, passing \$1 billion in the late 1990s. Comverse dominated voicemail management and sold a popular short-message service-center product. Its headquarters were in the US, while R&D and manufacturing were done in Israel. At one point, Comverse was one of Israel's largest employers of software engineers. It benefited from numerous grants from the Office of Chief Scientist.

At the Technion Institute of Management, I recall working with Comverse on management development nearly 15 years ago. The daily newspapers Haaretz and The Jerusalem Post called Comverse a "flagship"



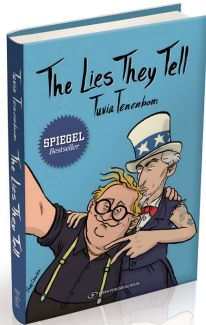
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Kobi Alexander stands outside the Windhoek Magistrates' Court in Namibia after an extradition hearing in 2008. Alexander won his battle against extradition and spent more than a decade in exile in Namibia before voluntarily returning to the US in 2016

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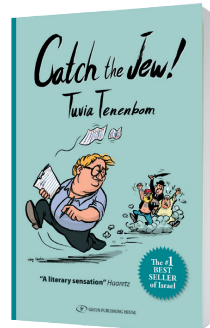
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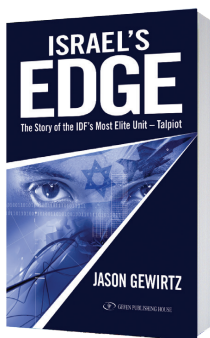
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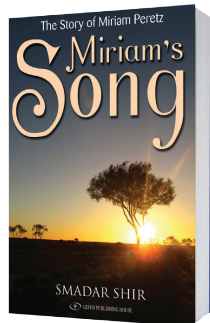
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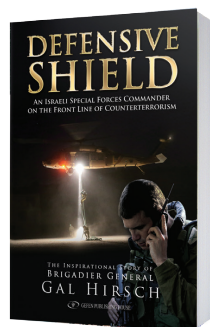
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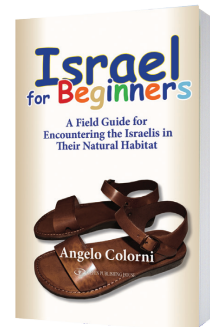
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company, and Bloomberg News called Alexander “the wizard of Israel’s technology boom.” I remember thinking, at the time, how well Comverse was run and led.

Then came the options-backdating scandal. And it all fell apart.

I’m truly sorry for everything I have done wrong. I deeply regret running away instead of dealing with the justice system like I should have

What does “backdating options” mean?

Many hi-tech companies offer senior employees stock options – the right to buy the company’s shares at the price at which the shares trade on the day the options contract is signed. When the stock price rises, the workers can make a fortune, exercising their options by buying the stock at the lower price and selling it high. Companies do this because it does not require them to lay out scarce cash directly.

Sometimes, though, when the company’s stock price falls, those options lose value or even become worthless. Such options are called “out of the money” or “under water” in jargon. This can be a blow to employee morale, turning them from millionaires to paupers nearly overnight.

One solution has been to backdate the options – turn back the hands of time, to a date years earlier when the share price was much lower, to make the options more valuable. This is, in fact, legal provided the company reveals all the terms and conditions transparently and properly records the cost in its financial reports. If a company sells an employee 100 shares at \$5 and the share’s market price is \$10, it is giving up \$500 because it could have sold the shares for \$1,000. This is an expense and must be reported.

A study by Erik Lie of the University of Iowa’s Tippie School of Business found that more than 2,000 companies used options backdating to reward senior executives between 1996 and 2002.

So why is Alexander going to jail for doing something that is legal?

US prosecutors said Alexander backdated dates for options between 1998 and 2001 to make them more valuable but concealed this action. Concealment is what makes it illegal, because this inflates earnings. The law requires companies to take a financial charge for raising the value of options, and to report it. Alexander, as head of Comverse, apparently failed to do this – the transaction was hidden.

If you incur an expense, and backdating options does incur an expense, it must appear in the quarterly income statement. If it does not, it’s fraud. It is cheating and misleading the shareholders. To be legal, backdating options has to be clearly communicated to the company shareholders, accurately reflected in the financial statements, and clearly taken into account in tax returns. Alexander, according to the indictment, did not fulfill those terms.

STEVE JOBS received backdated stock options; in 2001, he won the right to buy 7.5 million Apple shares backdated to a price of \$18.30 when the current price was \$21.10. The taxable income of about \$20m. was not reported. Jobs returned the options without exercising them, and the Securities Exchange Commission said, in 2007, it would not file charges against Jobs, though it did charge two former Apple executives for their roles in backdating, even though Apple claimed the options deal was approved by a Board of Directors meeting that, in fact, never took place.

What was the result of Alexander’s flight?

A month after Alexander fled to Namibia, he was charged with securities fraud, along with two other Comverse executives – William Sorin, Comverse’s general counsel, and David Kreinberg, its finance chief. Sorin pleaded guilty and got a year in jail. Kreinberg pleaded guilty and was spared prison, probably because

of the information he provided.

Did Alexander pay compensation?

He did. While in Namibia, Alexander paid \$60m. to Comverse, in 2009, as well as \$6m. in penalties to the SEC to settle civil lawsuits against him. He also gave large sums to Namibia educational institutions.

Alexander and his family are far from poverty. Observers believe that he has retained some of his millions, even after generous philanthropy in Namibia.

What happened to Comverse?

Partly as a result of the options backdating, Comverse has ceased to exist. The law required Comverse to redo all its financial reports dating back to when the securities fraud occurred. This was costly, distracting and cast a pall on Comverse’s share price, and Comverse was delisted from the Nasdaq exchange because its stock price plummeted below the minimum. The 2008 financial crisis hurt Comverse, leading to large-scale layoffs. But mostly, I believe, it lacked the leadership Alexander had provided.

In 2012 and 2013, Comverse sold off all its holdings and ceased to exist. Two independent companies, Xuri and Verint Systems, carry on the company’s best-known product lines.

After Alexander serves his time, he will be expelled from the US and will return to Israel. Garaufis’s tongue-lashing of Alexander and sentence contrast sharply with what President Donald Trump’s chief strategist Steve Bannon, a far-right ideologue and former Wall Street tycoon, observed in 2014 about errant bank executives: “Think about it. Not one criminal charge has ever been brought to any bank executive associated with the 2008 crisis.”

As a strange sequel to this rather tragic story, the business daily *Globes* reported in 2006 that, according to ISSTA, a publicly traded tourist agency, “the Kobi Alexander affair has aroused Israelis’ interest in visiting Namibia.” Thanks to Kobi, perhaps Namibians can now say, “We’re on the map.” ■

The writer is senior research fellow at the S. Neaman Institute, Technion and blogs at www.timnovate.wordpress