

Boardroom Brawls: An Empirical Analysis of Disputes Involving Directors

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Comments welcome

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Abstract

This paper examines the nature, incidence, and shareholder value implications of boardroom disputes involving directors. Using a comprehensive, hand-collected dataset of disputes in publicly traded U.S. companies over 1994-2006 that came to light upon the occurrence of director resignations, we find that such conflicts typically appear to be the result of power struggles between management and directors over corporate governance and control issues. We also find that disputes are more likely to occur in firms where CEOs are more powerful relative to board members, independent blockholdings are lower, or where the power structure between the CEO and directors is not clearly established. Within firms that experience a dispute, directors with shorter tenures, and directors who are more powerful or independent are more likely to be involved in a dispute. Firms experience large and significant stock price declines around the revelation of these disputes. In cross-sectional regressions, the stock price reaction is worse in larger firms, in firms where the CEO is more powerful relative to directors, and where board tenures of the CEO and directors are shorter. Finally, dispute firms display poor operating performance in the years surrounding the dispute episode, and experience significantly greater incidence of stock market delisting during the year following the dispute. These results are robust to alternative specifications. Our findings provide a rare glimpse into the internal functioning of corporate boards, and suggest that power struggles between directors and top management can lead to costly governance failures.

Keywords: Boards of directors, Corporate boards, Boardroom disputes, Board disputes, Director disputes, Director departures

JEL Classifications: G34, D23, D74, K22

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1. Introduction

In an influential review article, Shleifer and Vishny (1997) define corporate governance as “the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment.” Stated another way, a corporate governance system encompasses the set of control mechanisms that reduce agency problems among managers, shareholders, and other securityholders.¹ These mechanisms include boards of directors; managerial incentive contracts; institutional investors and blockholders; debtholders and banks; the market for corporate control; managerial labor markets; product market competition; stock market; auditors and security analysts; the media; investor rights; and the legal environment (see, e.g., Jensen and Meckling (1976), Fama (1980), Fama and Jensen (1983), Agrawal and Knoeber (1996), La Porta, et al. (2000), Dyck and Zingales (2002), and Gompers, Ishii and Metrick (2003)). Directors play a particularly important role in a firm’s governance, for they serve as fiduciaries of shareholders and are charged with hiring, monitoring, advising, compensating, and disciplining management.

Anecdotal evidence indicates that boards of directors do not always function smoothly, and they sometimes experience discord and strife. A recent example is the board dispute that came to light when prominent venture capitalist Thomas J. Perkins resigned abruptly from the board of Hewlett-Packard in May 2006 (see Murray (2006)). In subsequent letters and e-mails to the HP board, Perkins said that he had resigned because Chairman Patricia Dunn had targeted him and other board members with illegal and unethical ‘pretexting’ practices in order to uncover the source of a board leak. In the ensuing controversy, Dunn resigned from HP’s board in September 2006, and criminal felony charges were subsequently brought against her and other HP officials.

¹John and Senbet (1998) and Tirole (2001) define and analyze corporate governance more broadly to include conflicts between investors and other corporate stakeholders such as customers, suppliers, employees, government and society.

The HP incident, along with recent episodes at other prominent companies, suggests that a breakdown in board functioning can have adverse consequences for a company's operations, competitive position, and stock price.² At a minimum, internal board disputes that come to light can be highly embarrassing for a company and can tarnish its public image. Despite the importance of understanding internal board conflict, however, there has been little systematic evidence on this aspect of governance. Boards generally operate out of the public eye, making their internal functioning largely a 'black box' for financial economists. Extant economic analyses have focused mostly on board size, composition, and committee structure.³

In this paper, we provide the first systematic evidence on the nature, determinants, and consequences of major internal board disputes. Our study exploits a provision of U.S. securities rules requiring firms to disclose, in some circumstances, the details of internal disputes involving directors. Under the provision, when a director of a firm resigns or refuses to stand for re-election due to disagreements involving company operations, policies or practices, the firm must immediately disclose the circumstances surrounding such resignation or refusal in an 8-K filing with the SEC (see Plitch (2005)). In addition, the firm must disclose the director's letter describing the reasons for his resignation. We make use of these disclosure requirements to assemble a novel, hand-collected dataset consisting of 181 disputes over the 1994-2006 period that resulted in one or more director departures. The dataset enables us to empirically study the nature of internal board conflicts as well as the implications of such conflicts for corporate governance and shareholder value.

We start by examining the underlying nature of the internal disputes that lead to director resignations. We find that board disputes usually involve a firm's top management and only rarely occur among outside directors. Moreover, in most cases,

²Board disputes that become public often lead to large declines in share values (see, e.g., the case of General Motors in October 2006). Such episodes can also trigger changes in top management (e.g., Wal-Mart; see Zimmerman and Stringer (2005)) or even put a company in play (e.g., Janus Capital Group Inc.; see Dale (2005)).

³See, e.g., Hermalin and Weisbach (1988, 1998) for analyses of board composition, Yermack (1996) on board size, Agrawal and Knoeber (2001) and Kroszner and Strahan (2001) on the use of directors with different professional backgrounds, and Klein (1998) on the structure of board committees. John and Senbet (1998) and Hermalin and Weisbach (2003) provide excellent reviews of this literature.

board disputes are related to major rifts between the viewpoints of directors and management regarding management style, corporate governance, firm strategy, and specific corporate control or financing transactions. This suggests that board disputes are likely the result of power struggles between top management and certain board factions.

To gain a better understanding of why such disputes occur and which firms might be more predisposed to them, we examine the relationship between governance characteristics and dispute incidence. Using a matched control sample of firms that did not experience a dispute over the sample period, we find that the likelihood of a dispute is related to several measures of CEO and board power. First, we find that the dispute likelihood is greater when a CEO is more powerful relative to the board, such as when he belongs to the founding family or when the board has fewer independent directors or fewer independent committees. Second, dispute likelihood declines with CEO tenure, consistent with the notion that the power structure between management and directors evolves over a CEO's tenure, with CEOs generally gaining more power over time.

We then focus on firms that experience a dispute and investigate whether certain characteristics of individual directors make them more dispute-prone. We find that directors with shorter tenures, founders of other companies, venture capitalists, and investment bankers are more prone to dispute. Directors who are CEOs or chairmen of other companies are less likely to be engaged in a dispute, and outside directors with greater stock ownership are less likely to be involved in a dispute.

We also examine the shareholder value implications of the disclosure of boardroom conflict. Upon news of director departures stemming from internal disputes, stock prices decline significantly (both statistically and economically). The cumulative average abnormal return (CAAR) for our full sample of director departures amid disputes is -2.6% over days -1 to +1, and -6.1% over days -10 to +1. The CAAR is even more negative when the resigning director is an insider, averaging -3.9% and -10.3% over the [-1, +1] and [-10, +1] event windows. Moreover, we find that the decline in stock prices is particularly large for certain classes of disputes, such as those involving issues related to managerial employment contracts, corporate strategy and direction, management style, management hiring and succession, and conflicts of interest or possible fraud. Cross-sectional regressions reveal that the stock price reaction is significantly more negative

when the firm is large, when the CEO and the resigning directors have shorter tenures, when the CEO founded the company or effectively picks board members, and when other directors and officers own less stock. Finally, dispute firms display poor operating performance in the years surrounding the dispute episode, and experience significantly greater incidence of stock market delisting during the year following the dispute. These results are qualitatively similar before and after the tightening of the disclosure rules in 2004, and are robust to extreme stock price reactions to dispute disclosures.

Overall, our results imply that power struggles inside the boardroom can have consequences for a wide range of corporate decision-making. These struggles sometimes lead to governance failures and severe negative repercussions for shareholder value. Our findings indicate that the occurrence of this type of governance failure is not completely random but instead is related to measurable aspects of corporate governance, such as CEO power, board structure and ownership structure. Finally, our empirical analysis suggests that the inner workings of corporate boards are richer and more dynamic than has previously been recognized by financial economists.

The rest of the paper is organized as follows. Section 2 briefly describes the evolution of disclosure rules on director departures amid disputes. Section 3 details our sample and data. Section 4 examines the nature of these disputes and investigates the determinants of their incidence at the firm-level and at the level of the individual directors. Section 5 examines the stock price reaction, and the cross-sectional determinants of the reaction, to these incidents. Section 6 analyzes operating performance surrounding disputes and the aftermath of dispute episodes. Section 7 presents the results of several robustness checks, and the final section concludes.

2. Origin and Evolution of the Disclosure Rules

In April 1977, the SEC instituted a broad re-examination of its corporate governance rules and invited written comments from the public in response to expressions of concern about the efficacy of existing mechanisms of corporate accountability. It held public hearings on these issues in Fall 1977. On July 18, 1978, the SEC issued for public comment a rule proposal requiring a company to disclose under item 6 of Form 8-K and item 6(f) of schedule 14A (proxy statement) anytime a director

resigns or refuses to stand for re-election due to ‘differences involving company operations, policies or practices’. The proposal was aimed at providing information useful to investors in assessing management quality, consistent with the increasing emphasis on the monitoring function of corporate boards. On November 15, 1978, the SEC adopted a final rule on this issue that incorporated public comments on the proposed rule (see Wall Street Journal (1978) and Federal Register (1978)). The final rule required this disclosure only if the director provides the company with a letter describing the disagreement and requesting the matter to be disclosed. The company was then required to file a Form 8-K with the SEC within five business days of the receipt of the director’s letter. The filing was required to state the date of the director’s resignation or refusal to stand for re-election, summarize the director’s description of the disagreement, and file a copy of the director’s letter as an Exhibit to Form 8-K. If the company believed that the director’s description was inaccurate or incomplete, it could include in the filing a statement of its views of the disagreement. The rule became effective for 8-K and proxy statement filings made starting on January 15, 1979.

Following high-profile corporate scandals such as Enron, on June 17, 2002, the SEC proposed to expand the disclosure requirements under item 6 of Form 8-K. After reviewing public comments and holding public hearings, the SEC issued a revised rule on March 16, 2004 (see Bernstein (2004) and Federal Register (2004)). The new rule reduces the filing deadline to four business days after the triggering event and renumbers item 6 to item 5.02 (a). The new rule triggers disclosure if a director resigns or refuses to stand for re-election to the board due to a disagreement with the company, known to an executive officer of the company (as defined in Securities Exchange Act Rule 3b-7), on any matter relating to company operations, policies or practices, or if a director is removed for cause from the board.

Notice that disclosure is now triggered without the director having to write a letter to the company and having to request that the matter be publicly disclosed. The company must disclose: (1) the date of the director’s resignation, refusal to stand for re-election or removal, (2) membership of any board committees the director served on, and (3) a brief description of the management’s view of the nature and circumstances of the disagreement. In addition, if the director provides the company with any correspondence

describing the nature and circumstances surrounding her resignation, refusal or removal, the company must file the correspondence as an exhibit to Form 8-K, regardless of whether the director requests such disclosure. The company must provide the director with a copy of the disclosures it is making by the day of the SEC filing, and an opportunity to respond in writing indicating whether she agrees with the company's disclosures, and if not, why not. The company must file with the SEC any letter it receives from the director, within two days of its receipt, as an Exhibit that amends the previously filed Form 8-K. The revised rule became effective on August 23, 2004.

3. Sample and Data

We construct our sample of disputes from correspondence between companies and resigning directors that is disclosed in SEC 8-K filings. Each year, U.S. public companies make tens of thousands of 8-K filings with the SEC disclosing a range of material events. We use 10K Wizard, an online search engine, to identify all 8-Ks filed between January 1, 1994 and December 31, 2006⁴ that contain an Exhibit 17 (directors' resignation letters). Our search yields an initial group of over 1,000 8-K filings with associated resignation letters.

For each 8-K in the initial group, we read the director's resignation letters as well as the company's account of the director departure to determine whether the resignation was due to a dispute. We identify a total of 181 episodes at 168 companies in which one or more directors resigned amid dispute. We exercise no judgment in identifying the cases that involve a dispute; the letters and company descriptions clearly state whether the director is leaving due to 'differences involving company operations, policies or practices'. Of these 181 episodes, 13 are second occurrences that happen after a company has already experienced an earlier director resignation due to dispute. Since the time period between first and second occurrences is generally fairly short, we focus the

⁴We restrict our search to this time period because online availability of 8-Ks filed before 1994 is very limited.

analysis on the first occurrences of dispute-related departures.⁵ Our final sample thus consists of 168 disputes involving directors over the 1994-2006 period.

To obtain information on the individual directors of firms experiencing disputes, we read each board member's biographical profile in the latest proxy statement (or the latest Form 10KSB, in the case of small business issuers) prior to the director departure event. We gather information on individual director characteristics such as age, gender, occupation, tenure on the board, stock ownership, number of outside directorships, any executive positions held in the company, and whether or not the director belongs to the firm's founding family.

Panels A and B of Table 1 report annual frequencies of disputes, the incidence of disputes across industry groups, and the sizes of firms experiencing these events. Panel A shows that, except for a low of 2 events in 1995 (and none in 1994), the number of dispute events per year hovers around 10 until 2003, the last year before the August 23, 2004 tightening of the rules under which disputes must be disclosed. The number of dispute events increases modestly to 15 in 2004 and more substantially to 33 events in 2005 and 39 events in 2006. Out of the 168 total episodes in the sample, 137 involved departures of just one director, 18 involved departures of two directors, eight involved three departing directors, and five involved departures of four or more directors. The median firm in the sample is quite small, with total assets of about \$13 million. However, the sample contains some very large firms: the mean value of total assets is about \$3.5 billion. The asset size is under \$2 million for the bottom size quartile and above \$118 million for the top quartile. Panel B shows that the firms in the sample are distributed over a wide range of industries.

In Panel C of Table 1, statistics are reported for individual characteristics of the 214 departing and 873 non-departing directors in our sample of 168 firms. The median departing (remaining) director is 54 (56) years old, has served for 2 (3) years on the board, and owns 0.6% (0.4%) of the outstanding equity. On average, both departing and remaining directors hold about one-half of an additional outside board seat. About 2%

⁵Of the 13 companies experiencing two episodes, 9 have episodes less than two months apart; 2 have episodes between two to five months apart; and 2 have episodes between six to eleven months apart.

(5%) of the departing (remaining) directors are women, and about 2% (4%) belong to the company's founding family.

Panel D provides frequency breakdowns, by primary occupation, for departing and remaining directors. The panel also shows similar breakdowns for inside directors, gray directors, and independent directors. Among departing directors, corporate executives are well-represented (32%). Also represented are consultants (11%), lawyers (6%), investment bankers (6%), venture capitalists and private equity financiers (5%), engineers and scientists (4%), accountants (3%), and medical professionals (3%); the remaining 29% comprises a wide variety of professional backgrounds. The distribution of occupations for non-departing directors is roughly similar. Of the departing directors, about 36% are current or former CEOs of another company, 12% are current or former chairs of another board, and 23% are founders of another company. Compared to the departing directors, the remaining directors have more external CEO and board chairman experience in our sample.

We construct a control sample by matching each dispute firm to a COMPUSTAT firm in the same year and 2-digit SIC industry that (1) did not have a director dispute over the sample period; (2) used the same form type (either DEF 14A or 10-KSB) for proxy solicitation as the dispute firm; and (3) was closest in size (total assets) to the dispute firm at the end of the fiscal year preceding the dispute. For each firm in our dispute and control samples, we read the latest available proxy statements (or 10-KSBs), annual reports, and other SEC filings made prior to the director departure to obtain detailed information on the firm's board structure, ownership structure, CEO characteristics, and other governance arrangements. We also obtain data on other firm characteristics from Compustat, CRSP, 10-K or 10-KSB filings, securities registration filings and prospectuses, and other SEC filings.

Table 2 summarizes selected corporate governance and firm characteristics of the dispute and control firms. The average board of the dispute (control) firm has 6.6 (6.2) members, of whom about 39% (36%) are insiders, 12% (8%) are gray, and 50% (56%) are independent. Of the dispute (control) firms, 51% (61%) have independent audit committees, and 39% (49%) have independent compensation committees. Matched pairs t-tests and Wilcoxon signed-ranks tests show that dispute and control firms exhibit

statistically significant differences (at the 10% level or better) in board size, the fractions of gray or independent directors as well as in the incidence of independent audit or compensation committees.

The average age of CEOs at dispute (control) firms is about 53 (53) years, and about 20% (15%) of the CEOs belong to one of the founding families. CEOs of dispute (control) firms have served on the company's board for an average of 5.8 (8.4) years; this difference is statistically significant at the 1% level.⁶ Following Shivdasani and Yermack (1999), we say that a 'CEO picks board members' if the CEO serves on the nominating or corporate governance committee or if the board has no such committee. Accordingly, the CEO picks board members in 72% (80%) of the dispute (control) firms. The median stock ownership of the CEO is about 2.8% (4.8%) in dispute (control) firms; for all officers and directors, it is about 18% in each sample. Both groups of firms have a median of one independent blockholder. About 60% (54%) of the dispute (control) samples have an independent blockholder, and 38% (46%) have a Big 6 auditor. For each of the two groups, the CEO chairs the board about half of the time. None of these differences is statistically significant.

Although the median dispute firm is quite small, with total assets and market capitalization of \$13 million and \$52 million, respectively, mean values are substantially larger, at \$3.5 billion and \$3.3 billion, indicating that the sample includes some very large firms. The median value of total assets for the control sample is almost the same as that for the dispute sample. The median net income to firm value ratio for the dispute (control) firms is -4% (-3%); their cash flow to firm value ratio is -3% (0.4%). At the time of the dispute, about 7% of the dispute firms are listed on NYSE, 27% on Nasdaq, and 5% on AMEX; the rest are listed on regional exchanges or trade over-the-counter.

4. Nature and Incidence of the Disputes

Section 4.1 examines the nature of the disputes, and section 4.2 investigates the determinants of dispute incidence.

⁶A CEO's tenure on the board is likely an upper bound on his tenure as CEO, because appointment to the CEO position invariably comes with a board seat.

4.1 Nature of the Disputes

To shed some light on the nature of the conflicts that lead directors to resign, we identify the issues mentioned in directors' letters and companies' descriptions pertaining to each of the 168 episodes in our sample. The Appendix shows some excerpts from directors' letters to provide a sense for the types of issues that are at the heart of the disputes. We classify these issues into 11 key areas of disagreement. Table 3 summarizes the frequencies with which different categories of issues arise and gives some examples in each category. Three of the largest categories involve management style (e.g., management did not listen to the board's advice), board functioning (e.g., the resigning director was forced to vote upon unfamiliar matters without board discussion), and corporate governance (e.g., resigner opposed adoption of a shareholder rights plan or disagreed with the company's procedure for selecting an outside auditor). Other issues involve business matters such as corporate strategy and direction (e.g., company had moved away from its core focus) or specific financing or corporate control transactions (e.g., the board rejected a valuable takeover offer). The remaining issues pertain to diverse areas such as strife among board members, management conflicts of interest and possible fraud, corporate disclosure, management hiring and succession, and contract disputes. Two general observations can be drawn from Table 3. First, conflicts in the boardroom typically involve corporate governance and control issues. Second, these disputes usually occur between directors and management. These observations suggest that director departures amid disputes are often the result of power struggles between management and directors.

4.2 Determinants of Dispute Incidence

Section 4.2.1 analyzes the determinants of dispute incidence at the firm-level. Given that a firm experiences a dispute episode, section 4.2.2 examines which of the individual directors are more likely to be involved in the conflict.

4.2.1 Firm-level analysis

This section examines whether the incidence of boardroom disputes is systematically related to certain firm and governance characteristics. As discussed in the introduction, the public disclosure of a boardroom conflict is likely to be highly embarrassing for a company. Such a disclosure can compromise a firm's competitive position, harm its relations with various constituencies, and ultimately reduce firm value. So the public airing of a boardroom dispute represents a governance failure in a firm. To better understand what types of governance arrangements might precipitate such failure, we examine the relation between the occurrence of such episodes and three types of a firm's governance characteristics: CEO power, ownership structure, and the formal structure of the board.

If boardroom fights are merely random occurrences, we should not expect their incidence to be systematically related to governance and firm characteristics. But our findings in Table 3 suggest that such conflicts are usually manifestations of power struggles between management and directors. Thus, it is reasonable to expect the incidence of such disputes to be related to measures of CEO power. A priori, it is not clear whether greater CEO power should lead to more power struggles or less. On the one hand, a more powerful CEO is more likely to pursue his own views and to clash with directors. On the other hand, if a CEO is well-entrenched and board members are effectively hand-picked by the CEO, disputes are less likely. Therefore, we do not test for specific relationships between dispute incidence and measures of CEO power. Instead, we examine these relations empirically and use our results to interpret the forces at work.

We use four measures of CEO power. First, the longer a CEO's tenure on the board, the more power the CEO is likely to have in the boardroom (Hermalin and Weisbach (1998, 2003)). To allow for a decreasing effect of tenure on CEO power as tenure increases, and to convert tenure into a continuous variable, we use the natural logarithm of one plus tenure. Second, a CEO is likely to be more powerful if he founded the company or is a family member of the founder. Third, a CEO is likely to be less powerful if the board has a non-CEO chairman (Fama and Jensen (1983)). Finally, a CEO will enjoy more power over the board if he is involved in selecting new board members over time. Following Shivdasani and Yermack (1999), we define a binary variable called

‘CEO picks board members’ that equals 1 if the CEO serves on the board’s nominating or corporate governance committee (or the board has no such committee), and equals 0 otherwise.

We include the percentage of outstanding equity owned by the CEO, by other officers and directors, and by independent blockholders as measures of the relative powers and incentives of these groups. Here, too, the directional relationships between these variables and dispute incidence are not clear a priori. By reasoning similar to that for other measures of CEO power, disputes should be more likely if the CEO is more powerful relative to outside blockholders and other board members. But if the power structure among these groups is clearly established, disputes are less likely. In addition, with greater stockholdings, all parties have strong incentives to avoid public showdowns that will hurt firm value.

The structure of the board of directors is also likely to affect the balance of power between management and the board. A large literature suggests that independent directors are more effective monitors of management (see, e.g., Weisbach (1988), Byrd and Hickman (1992), and Brickley, Coles and Terry (1994)). We measure board structure by the proportions of inside, independent, and gray directors and include the latter two variables in our regressions as explanatory variables. Following prior literature, we define inside directors to be current employees of the firm. Gray directors are defined to be outsiders who are former employees of the firm, relatives of executive officers, founding family members, or persons having business dealings with the firm. Independent directors include all outside directors who are not gray directors. Yermack (1996) argues that smaller boards are more effective monitors of management. If small boards are better able to resolve disagreements through communication and compromise, then irreconcilable differences leading to director departure are more likely to be associated with larger boards. Hence, we include board size as another independent variable.

In addition, we include binary dummy variables that equal 1 if the board has independent audit or compensation committees, and equal 0 otherwise. We define a committee to be independent if it consists entirely of independent directors. Audit and compensation committees are important board committees that have been the focus of recent corporate governance reforms. When these committees are present and exclude

insiders, they can act as a significant check on the CEO's power over the board. Finally, we control for CEO age and firm characteristics such as size, operating performance, and financial leverage.

Table 4 shows pair-wise correlations among the variables in the regression. Dispute incidence is lower in firms with longer CEO tenures, a higher % of independent directors on the board, independent audit or compensation committees, and lower independent blockholdings. A number of explanatory variables are also significantly correlated among themselves. In particular, firm size is negatively correlated with 'CEO picks board members' and CEO shareholdings, and it is positively correlated with board size, the percentage of independent directors on the board, and the presence of independent audit or compensation committees. The latter two binary variables are correlated positively with board size and the percentage of independent directors, and negatively with the 'CEO picks board members' dummy. The latter dummy variable is negatively correlated with board size and the percentage of independent directors. Finally, the last two variables are positively correlated.

Table 5 presents the results from matched-pairs (conditional) logistic regressions of dispute incidence.⁷ Panel A reports the results for the full sample of all director departures, Panel B for the sub-sample where at least one of the departing directors is an insider, and Panel C for the sub-sample of outside director departures. Each panel presents four variants of our basic regression model.

As is apparent from Panel A, disputes are significantly more likely in firms where the CEO has had a shorter tenure on the board. This may capture two effects. First, when a CEO has been in office for a relatively short period of time, the power structure between directors and management is unlikely to have been firmly established, leading to greater incidence of disputes. Second, over a CEO's tenure, boards may become less effective monitors of the CEO (Hermalin and Weisbach (1988)). Thus, long-time CEOs are less likely to be challenged by directors, leading to lower dispute incidence.

⁷Since our sample consists of matched-pairs of dispute and control firms, and the dependent variable here is Dispute Firm, which equals 1 for a dispute firm and 0 for a control firm, the appropriate model is the matched-pairs logistic model. See Hosmer and Lemeshow (2000) for an excellent exposition of this model. Nevertheless, the results are very similar to those shown here when we estimate the regular logistic model.

Panel A shows that several other variables also are significantly related to dispute incidence. For instance, disputes are more likely when the CEO belongs to the founding family and when independent blockholdings are high. These findings suggest that boardroom fights are more apt to get out of hand when the CEO is more powerful or when the presence of large outside blockholders emboldens directors. In addition, larger boards are significantly more likely to experience disputes, consistent with the notion that larger boards are less effective at resolving disputes. In addition, having more individuals on the board naturally increases the odds that one of them will clash with the others or with the CEO. The regressions also show that the degree of board independence as measured by the fraction of independent directors or the presence of independent committees is negatively related to dispute likelihood. This finding suggests that a sizeable coalition of independent directors can be powerful enough to keep the CEO in check even if directors are not very powerful individually. Finally, there is weak evidence that boardroom conflicts are more likely during times of poor firm performance.

Most of the above relations hold for the insider and outsider sub-samples in Panels B and C, except that most of the coefficients for board and committee variables (except for the percentage of independent directors) hold only for outsider departures. In the latter sub-sample, dispute incidence is also lower in firms with greater financial leverage.

4.2.2 Director-level analysis

We next examine whether certain characteristics of individual directors make them more prone to getting involved in a boardroom conflict. In other words, given that a firm experiences a dispute, which of the director(s) are more likely to be embroiled in the dispute? If disputes are random occurrences, their incidence should not be systematically related to director characteristics. To address this issue, we estimate logistic regressions of dispute incidence. The dependent variable equals 1 if a director is involved in a dispute and 0 otherwise. The sample includes all individual directors of firms that experience a dispute. The independent variables are measures of power, independence, tenure, and incentives of directors, and the importance of the director position to them.

First, directors who are more powerful and independent are less likely to shy away from voicing their disagreements openly. Accordingly, we expect directors who are founders of other companies, venture capitalists, and investment bankers to be more assertive, and so more likely to be at the center of a boardroom conflict. Second, directors who are CEOs of other companies may be more sympathetic to the CEO's perspective, and so are less likely to clash with him. Third, disputes are more likely to involve directors who are relatively new to the board. Such directors may not understand the existing power structure in the boardroom and have not had time to establish themselves on the board. Fourth, directors with greater stock ownership in the firm have stronger incentives to avoid getting involved in public disputes that can harm firm value. Fifth, individuals for whom the directorship is more important are less likely to be embroiled in a dispute that can jeopardize their board seat. Accordingly, we expect academics, retirees, and directors with fewer outside directorships to be less likely to get involved in a board dispute. Finally, if women are on average less aggressive than men, we might expect women directors to be less likely to be involved in a dispute.

Table 6 shows the results of this analysis. Panel A shows the results for all directors, while Panel B focuses on outside directors. In both panels, directors with shorter tenures, founders of other companies, venture capitalists, and investment bankers are more prone to dispute. Directors who are CEOs or chairmen of other companies are less likely to be engaged in a dispute. In addition, in Panel B, outside directors with greater stock ownership are less likely to be involved in a dispute. All of these relations are statistically significant. While the coefficient estimate on women directors is negative in both panels, it is statistically insignificant.

5. Stock price reaction

Section 5.1 deals with the average stock price reaction to the revelation of director departures due to differences with the company, and section 5.2 provides a cross-sectional analysis of the stock price reaction.

5.1. Average stock price reaction

We define the announcement date (day 0) of the director departure as the earlier of the date of the 8-K filing with the SEC and the date of the first news story in the Factiva database, if any, about the director departure. Stock prices are drawn from CRSP and from Datastream. Daily abnormal returns are calculated as market-adjusted returns using the CRSP Equal-weighted index. Cumulative average abnormal returns (CAARs) are the sum of daily average abnormal returns over the relevant window. The t-statistics for CAARs are computed after adjusting for cross-sectional dependence, as in Brown and Warner (1985, equation (A.11)).

Panel A of Table 7 shows the CAARs for seven windows around the event day. Column 1 shows the CAARs for the sample of all disagreement events. The next four columns show CAARs for sub-samples by the highest executive position in the firm held by any of the resigning directors. Median values of cumulative abnormal returns are shown in parentheses below the means. Incidents of director departures amid disputes have large effects on stock prices. Over the 3 day period $[-1, +1]$, the abnormal return for the full sample is a statistically significant -2.6%. Over the longer $[-10, +1]$ day window, intended to capture possible leakage of information about the simmering boardroom dispute, the CAAR is as much as -6.1%. The abnormal return is substantially larger when the group of resigning directors includes at least one insider (i.e., executive) than when the group consists entirely of outsiders. Over the $[-10, +1]$ window, the mean (median) abnormal return for insider departures is -10.3% (-16.3%), while it is -4% (-3.4%) for outsider departures. While the t-test for the difference between the two means is insignificant, the Mann-Whitney test p-value for the difference is 0.09. For CEO departures, the mean (median) abnormal return over the $[-10, +1]$ window is as much as -17.6% (-20.7%).

Panel B of Table 7 partitions the sample based on whether at least one resigning director was a member of one of three board committees: audit, compensation, and nominating or corporate governance. Given the importance of these board committees, one might expect that departure of a committee member amid dispute would be worse news than departure of a non-member. While CAARs over days $[-1, +1]$ are more negative if at least one of the resigning director was a member for the audit or

compensation committees than if none of the directors was on these committees, the opposite results hold based on the CAARs over days [-10, +1]. In any case, the differences based on committee memberships are largely statistically insignificant.

Panel C of Table 7 subdivides the sample based on the nature of the departing director's disagreement with the company. The revelation of certain types of disputes has a more negative effect on stock prices. These include disputes over corporate strategy and direction (CAAR [-10, +1] = -14.1%), management style (CAAR = -21.1%), contract dispute (-20.6%), management hiring or succession (-19.8%), and conflicts of interest and possible fraud (-13.6%). All of these CAARs are statistically significant at the 1% level in two-tailed tests. Surprisingly, disputes over board functioning have a positive effect on stock prices.

5.2 Cross-sectional analysis

We next examine whether the cross-sectional reaction of stock prices to the revelation of these disputes is systematically related to characteristics of firms' governance, such as measures of CEO power discussed in section 4; stock ownership of the CEO, other officers and directors, and independent blockholders; board structure; characteristics of the group of resigning directors such as the number of resigners, their tenures on the board, memberships on important board committees, and whether the group includes the CEO of the company. In addition, we control for firm size and whether or not there was media coverage of the dispute. Table 8 shows pair-wise product-moment correlations between these variables, and Table 9 shows the regression results. To save space, we show results for abnormal returns over the [-10, +1] window, but results for the shorter [-1, +1] window are qualitatively similar.

Table 8 shows that the stock price reaction to the disputes is positively related to the average tenure of resigning directors and to CEO tenure, and is negative if the resigner is the company's CEO. A number of the explanatory variables are also correlated with each other. Notably, firm size and board size are highly correlated with many of the other variables, and the resigner's membership on the board and audit committees are positively correlated.

The first column of Table 9 shows the results of our basic regression model for the full sample. Column (2) adds dummy variables for whether any resigner is on the board's audit or compensation committee or is the company CEO, and column (3) adds a dummy variable for media coverage. Since the determinants of the stock price reaction to the disputes can differ according to whether the departing director is an insider or outsider, the next six columns report estimates of the corresponding regressions for two sub-samples: (1) where at least one resigner is an inside director, and (2) where all resigners are outsiders.

For the full sample of all director departures, the stock price reaction is more positive (or less negative) when the average tenures of the resigning directors, CEO tenure on the board, and stock ownership of other officers and directors excluding the CEO are higher; it is more negative when the CEO is company founder, the CEO picks board members, and the firm is larger. All of these relations are statistically significant. For the sub-sample of insider departures, the sign on the coefficient of average tenure of resigners reverses, although the coefficient is statistically insignificant. Other than that, the signs of the remaining relations for the sub-samples of insider and outsider departures are similar to those for the full sample, although the statistical significance declines (possibly due to the reduction in sample sizes), especially for the insider sub-sample. In addition, for outsider departures, the stock price reaction is less negative where independent blockholdings are greater. Overall, these findings suggest that disputes are more damaging for larger companies (perhaps because they receive more investor attention), and for companies where the CEO is the founder or picks board members, where the CEO and other resigners have shorter tenures on the board, and where non-CEO directors and officers own less stock. These results are consistent with the idea that these episodes are more damaging when the CEO has more power relative to other board members or when the power structure between the CEO and directors has yet to be clearly established.

6. Operating performance and dispute aftermath

Section 6.1 examines operating performance surrounding disputes and section 6.2 analyzes the aftermath of dispute episodes.

6.1 Operating performance

We next examine the operating performance of our samples of dispute and control firms from year -2 to year +3, where 0 is the fiscal year during which the 8-K filing on the dispute occurs. Table 10 shows median values of three operating performance measures for each sample: Return on assets (ROA), Cash flow to assets, and OIBD to assets. ROA is income before extraordinary items divided by total assets. Cash flow is income before extraordinary items plus depreciation. OIBD is operating income before depreciation. Total assets are end-of-year book value of assets. Financial data are obtained from Compustat and various SEC filings (including annual reports and 10-K, 10-KSB, and 10-Q filings). The table also reports absolute values of z-statistics from paired two-tailed Wilcoxon tests for differences in distributions.

Firms involved in director disputes have poor operating performance both before and after the dispute year. The median ROA of dispute (control) firms in years -2, -1, and 0 is -14.6% (-7.6%), -24.7% (-6.7%), and -29.9% (-2.6%). Dispute firms experience extremely poor performance by any yardstick; their performance is also significantly lower than the performance of control firms. Dispute firms continue to under-perform in year +1 (ROA = -18.8%). While their ROA improves somewhat in years +2 and +3, it remains negative, and is significantly lower than the performance of control firms in year +3. The results for cash flow to assets and OIBD to assets generally mirror those for ROA.

6.2 The aftermath of disputes

Finally, we examine whether firms involved in public episodes of director disputes experience greater incidence of acquisition, bankruptcy or delisting. Table 11 reports the frequency of different types of delisting events experienced by dispute and control firms within 6-month, 1-year, and 2-year periods following director disputes, as reported on CRSP. Each cell reports the number of delisted dispute (control) firms,

followed in parentheses by its frequency as a percentage of the total number of dispute (control) firms listed on CRSP at the time of the 8-K filing on the dispute. Delisting events are grouped into categories (not all mutually exclusive) based on CRSP delisting codes. The bankrupt category includes firms delisted due to insufficient assets or equity, or the stock price being too low. The table also shows p-values for the equality of proportions between the dispute and control samples.

Dispute firms suffer serious market consequences in the wake of the dispute episodes. While firms in the dispute sample are acquired or go bankrupt at frequencies that are not statistically distinguishable from their counterparts in the control sample, dispute firms experience significantly greater incidence of delisting than control firms over 6 or 12 months following the dispute. The overall incidence of all non-merger delistings and all delistings is also significantly higher in the dispute sample than in the control sample over this period.

7. Robustness checks

This section examines whether our Table 5 and 9 results differ before and after the 2004 change in disclosure rules, and whether our Table 9 results are affected by outliers in the stock price reaction to the revelation of the episode.

7.1 Change in disclosure rules

Starting on August 23, 2004, there has been a major change in disclosure rules on director departures due to differences with the company. As discussed in section 2, the new rules shift the onus of a disclosure trigger from the departing director to the company. The company is now required to disclose via an 8-K filing with the SEC any time a director resigns or refuses to stand for re-election due to differences with the company that are known to an executive officer of the company, or if a director is forced to resign for cause. The departing director no longer has to provide the company with a letter explaining the reasons for his resignation and request the company to disclose the reasons for his departure to trigger disclosure. The new rules thus lower the threshold for disclosing a dispute, suggesting that even less serious disputes may be revealed after 2004. Indeed, Panel A of Table 1 shows a marked increase in the number of disputes

reported after 2004. This suggests that the average stock price reaction to disputes revealed after the 2004 rule change should be lower in magnitude. Our findings do not support this conjecture. The differences between mean and median abnormal returns for the two sub-samples are statistically insignificant, as are differences between partitions based on board committee memberships within each sub-sample. To conserve space, these results are not reported in a table.

Do the new rules lead to changes in the determinants of dispute incidence or in the determinants of the cross-sectional reaction of stock prices to the dispute? We find no evidence of such changes. When we estimate our regressions in Tables 5 and 9 separately for sub-samples of dispute events revealed before and after the effective date of the rule change, the results are qualitatively similar for the two sub-samples. To save space, these results are not shown in a table.

7.2 The effect of outliers

Finally, we examine whether our Table 9 results are affected by outliers in the stock price reaction to the revelation of the dispute. We re-estimate the regressions in Table 9 using a 1% winsorization of the dependent variable at both tails. Our main results are qualitatively unaffected by this transformation.

8. Summary and conclusions

The internal functioning of corporate boards is largely invisible to outsiders such as financial economists. One instance that allows a peek into boards' internal functioning occurs when a director resigns or refuses to stand for re-election due to disagreements with the company, or if the director is removed for cause. U.S. securities rules then require companies to publicly report the circumstances surrounding the director's departure in an 8-K filing. In an Exhibit to the filing, companies also have to include any letters the director provides the company describing: (1) the reasons for his departure, and (2) commenting on the company's description of the events.

This paper addresses four main questions. First, what is the nature of the disputes that lead to director departures? Second, what firm and governance characteristics are related to the incidence of such episodes? Third, how do stock prices react to such

disclosures? And finally, what determines the stock price reaction to these incidents? To address these questions, we have put together a novel, hand-collected dataset that includes all 181 episodes of director departures amid disputes that occurred in 168 U.S. public companies over 1994-2006, and an industry-size matched sample of control firms. The dataset contains detailed information on firm and governance characteristics of these 168 matched-pairs of firms, assembled from a variety of SEC filings.

Our main findings are as follows. First, conflicts in the boardroom typically appear to be the result of power struggles between management and directors over corporate governance and control issues. Second, matched-pairs logistic regressions indicate that these episodes are more likely to occur in CEO-founded companies, companies with shorter CEO tenures, higher independent blockholdings, bigger or less independent boards, and non-independent audit or compensation committees. In addition, departures of inside directors are more likely in smaller firms, and in firms where the CEOs are older or own less stock, and where other directors and officers own more stock. Third, within firms that experience a dispute, directors with shorter tenures, and directors who are likely to be more powerful or independent are more prone to dispute; directors who are CEOs or chairmen of other companies are less likely to be engaged in a dispute, and outside directors with greater stock ownership are less likely to be involved in a dispute.

Fourth, stock prices decline significantly (both statistically and economically) upon news of these events. The cumulative average abnormal return (CAAR) for our full sample of director departures amid dispute is -2.6% over days [-1, +1], and -6.1% over days [-10, +1]. The CAAR is even larger, -3.9% and -10.3% over the two windows, respectively, when the resigning director is an insider. The decline in stock prices is greater in contract disputes and in disputes involving corporate strategy and direction, management style, management hiring and succession, conflicts of interest and possible fraud than in other types of disputes. In cross-sectional regressions, the stock price reaction is worse in larger firms and in firms where tenures of the CEO and the resigning directors are shorter, the CEO founded the company, the CEO picks board members, and other directors and officers own less stock. Finally, dispute firms have poor operating performance in the years surrounding the dispute episode, and experience significantly

greater incidence of stock market delisting in the year following the dispute. These results are generally similar before and after the 2004 tightening of disclosure rules, and are robust to extreme stock price reactions to dispute-revelation. These results provide a rare glimpse into the internal functioning of corporate boards, and suggest that power struggles between directors and top management can lead to costly governance failures.

Appendix

Excerpts from Directors' Resignation Letters

Robert D. Sanderson, Fair Isaac Corp., 6/1/2001

I am resigning because I disagree with the rest of the Board's willingness to grant 100,000 stock options to Tom Grudnowski in fiscal 2001. This was an incorrect decision for two principal reasons. First, the Company's 1992 Long-Term Incentive Plan limits the number of options which may be granted to any one employee to 50,000 a year. While it may be legal to grant Mr. Grudnowski 100,000 options, doing so would violate the spirit of the agreement among the Company, the Board and the shareholders embodied in the plan. Second, Mr. Grudnowski doesn't deserve the grant. He was hired to get the Company growing again and to develop Internet-based new business. During his tenure as CEO revenue growth has been below the Company's long-term record, and revenues from new business have been miniscule. He has not earned the reward of an extraordinary option grant. It is my hope that the Board will conclude, as I have, that the Company will not achieve long-term success with Mr. Grudnowski in charge and that the best way to increase shareholder value is to sell the Company.

James A. Miller, Surge Components, Inc., 8/1/2001

Since joining the board of directors of Surge, I have on numerous occasions expressed my belief that I have not been given appropriate and relevant information necessary for me to perform my duties. It has been difficult for me to receive requested information either in a timely manner or at all. Furthermore, it has come to my attention that there were significant events and actions taken which were not properly disclosed to me. Case in point: the company recently filed two 10-Qs without my advice, review or approval. This is particularly disturbing given the fact that I am chairman of the audit committee. As a result of these and other unacceptable circumstances, I do not believe I can discharge my responsibilities in the manner in which the shareholders deserve. This letter shall serve as my resignation from the Board of Directors of Surge Components Inc., effective as of today, July 25, 2001.

Jerome T. Osborne, GLB Bancorp, Inc., 9/8/2003

This resignation is prompted by my profound disagreement with the decision of the Board of Directors to approve the proposed merger with Sky Financial Group, Inc. Accordingly to the preliminary proxy statement/prospectus ("Preliminary Proxy Statement") relating to the special meeting of shareholders of GLB, filed with the Securities and Exchange Commission by Sky Financial Group, Inc. in its Registration Statement on Form S-4, filed August 22, 2003, the Board of Directors of GLB has also voted to recommend approval of the transaction, a recommendation I disagree with. The Board has abandoned the original vision of GLB as a financial institution with a community focus and a substantial community ownership base. In addition, once the decision was made to sell the Company, I do not believe that the GLB Board of Directors received adequate information regarding, or adequately considered, the community impact or value of alternative proposals described in the Preliminary Proxy Statement, which is why I voted against the proposed merger with Sky Financial Group, Inc. For example, I believe that the

transaction proposed by the institution described in the Preliminary Proxy Statement as "Bank X" would have provided a substantially greater value to the shareholders of GLB.

J. Peter Pierce, Iron Mountain Incorporated, 12/26/2002

My resignation from the Board will enable me to pursue shareholders' rights with other interested shareholders in seeing to it that Iron Mountain is governed and managed properly. Board meetings that are held in violation of the bylaws should not be countenanced. Actions taken by "rump" sessions of the Board without notice to all Board members should not be authorized. If there are issues that exist with any Board members, special committees should be formed and authorized to investigate. This did not happen at Iron Mountain at any time. No minutes were taken of the so-called surreptitious "Board meetings". The unauthorized nature of certain "Board actions" has been confirmed under oath by your general counsel Gary Watzke. It is also now clear that on March 27, 2002, the Executive Committee met and purported to authorize the lawsuit that was filed against me the next day in New Jersey state court, even though the Board had never given the Executive Committee this authority at a duly authorized meeting of which I received notice. Interestingly, even though the "Board," as of March 5th, had purported to authorize the lawsuit against me, no disclosure of that "fact" was made by you in your note to the shareholders in the 2001 Annual Report, dated March 20, 2002, nor was there any mention of my alleged secret investment in Sequedex in the description of me as a Board member, that was set forth therein. In addition, there was no disclosure in the legal proceeding section of the first quarter Form 10-Q concerning the litigation filed against me as a material proceeding adverse to Iron Mountain. I simply will not be a part of a Board that attempts to conduct business in such a surreptitious and improper manner.

James Schroeder, Streamedia Communications Inc., 10/12/2000

Given the recent events at Streamedia and the vast disagreement and disarray of the principal shareholders I feel that I no longer represent the views and interests of those shareholders. I serve at their discretion and I in good conscience do not agree with the proposed direction of this company as set forth by the Chairman. It is the right of the shareholders to have the company run the way they want whether I, as a board member, agree or not. I do not agree to the recent direction and management suggestions of the Chairman and feel there will be severe consequences to the corporation. Therefore, I feel that I must resign as a director and allow the shareholders to choose a board of their liking.

Clifford Wyatt, Electropure, Inc., 4/20/1999

I have become increasingly concerned by the fact that the Company is seemingly unable to finalize its audit with respect to its financial statements for Fiscal October 1998, and accordingly is unable to issue a 10-K in compliance with Federal securities laws. Since the end of the fiscal year, several months have passed, including the end of the first quarter of fiscal 1999, and I have yet to receive any financial statements for any period of the current year....It was only after repeated requests and having a call made to the Company's counsel for corporate matters that I finally received a draft 10-K....The draft 10-K contained numerous material misstatements and omissions which I found quite shocking. For example, it did not mention the cross-complaint filed by Wyatt Technology against the Company, although it did mention the action filed by the Company against Wyatt Technology. Further it appears that the Company had not informed its

auditors that Wyatt's position was that it was entitled to obtain rescission or termination of the technology license described at length in the draft 10-K.

Vaughan Shalson, Discovery Laboratories, Inc., 3/27/ 1998

In summary, I have serious reservations about the judgement of Dr. Capetola and feel deeply that the compensation proposed for the management team, and in particular for Dr. Capetola, involves an excessive use of cash. As I have stated repeatedly in our conference calls, I do not believe this to be in our shareholders' best interests....On the subject of Dr. Capetola's judgement, at our Board Meeting on December 5 we discussed a merger proposal from Dr. Capetola dated August 28, 1997. The compensation package included in this proposal was characterized by one of the other board members present at that meeting as egregious. I and others agreed with this sentiment....My own evaluation was that Capetola's proposal went so far beyond the pale of what could be considered negotiation posturing, as to lead any reasonable person to conclude that he exhibited either lack of experience or extremely poor judgement—neither of which should be acceptable qualities in the proposed CEO of the combined company....I regard this proposal as further evidence of Capetola's lack of judgement, by even proposing to expose the company to cash payments of such magnitude that they could severely strain the company's resources, and that are excessive by any reasonable standard for a development-stage company in such fragile financial condition.

Kenneth P. Weiss, RSA Security, Inc., 6/4/1996

In my opinion, you have surrounded yourself with a Board of Directors that does not, and perhaps is incapable, of providing you with independent objective guidance. To the contrary, from all of the actions that I have seen, these directors appear to be working for you, rather than you working for them. I have seen this time and time again under many circumstances. Illustrative is the way in which you are able to influence the Compensation Committee to pay you what you demand and to make decisions based upon on what you want, rather than on any objective policy. Recent events in this area have been consistent with a pattern of conduct that I have observed over the years. For example, contrary to the compensation consultant's recommendation for a consistent policy, you recently recommended that the vast majority of your bonus be calculated at "threshold" plan while the other executives had the majority of their bonus awarded at "stretch" plan. The Compensation Committee approved this unfair inconsistent treatment....On an individual basis, certain of these directors have performed particularly poorly for the company. In my opinion, one of them frequently disrupts meetings and appears to be motivated principally by self-aggrandizement and another appears to be inept and makes little or no positive contribution to the Board. Their continued participation on the Board is particularly glaring, especially in the light of your engineered forced departure of the most experienced director.

Nirmal Mulye, Ph.D., Synovics Pharmaceuticals, Inc., 9/21/2006

During the past several months, however, you, the other members of the Board and employees of the Company under your direction have acted in a manner designed to curtail meaningful participation by me in my role as a director of the Company....Specifically, I have been asked to vote on matters as a director of the Company while being denied access to the information needed by me to make informed decisions with respect to such matters....I have also

been denied the opportunity, on a number of occasions, to engage in full substantive deliberations with the other members of the Board with respect to matters on which I was then being asked to vote. For example, you as Chairman of the Board have severely restricted the ability of directors to discuss matters on which the Board was requested to act by either refusing to allow discussion of certain items at all or by abruptly and prematurely terminating discussions with respect to certain items and calling for an immediate vote on those items prior to all views of Board members being properly aired.

Stephen D. Moses, AcuNetx, Inc., 5/5/2006

As each of you knows, I have endeavored to coordinate and mediate consensus on the issues confronting us from time to time. That is my style. I believe it to be not only appropriate, but optimal. But that technique does not work at AcuNetx. It does not work with a C.E.O. who responds to suggestions with petulance....It does not work with a C.E.O. who declines to be open and forthcoming with his Board...It does not work when the Board decides that it will not and cannot yet be fully Sarbanes-Oxley compliant, but allows the C.E.O. to announce to its shareholders that it will be Sarbanes-Oxley compliant and then reacts angrily when the Chairman notes that paying consulting fees to the Compensation Committee Chairman would be a violation of Sarbanes-Oxley....It does not work when the C.E.O. responds to suggestions, or worse, criticism, with McCarthy-like investigations and mischaracterizations of his critic. It is unfortunate that the C.E.O. can stifle dissent and/or creative advice with tyrannical conduct.

Richard A. Ajayi, Surgilight, Inc., 6/5/2001

Dr. Lin controls 70% of the voting shares of the company and I am convinced that he has repeatedly refused to accept, or simply ignored, some decisions and guidance of the Board regarding compliance with regulations of the Food and Drug Administration and the Securities and Exchange Commission. Therefore, after working diligently, but unsuccessfully, for several months to resolve these issues, I have come to the conclusion that there are no other alternatives for me but to resign from the board.

Peter G. Leighton, Intellect Communications Systems Limited, 5/5/1997

This letter also conveys my resignation as a Director of ICSL. Because of my complete objection to the Facility, and the course on which ICSL has been set by a majority of its Board members, it is impossible for me to continue as a Director of this Company....In my view and belief, the Facility is not in the interest of ICSL in its present form. As a Director I disassociate myself from it as a funding option. The Facility is being forced upon ICSL by Mr. Frietsch (and certain other ICSL Directors, namely Anton Liechtenstein and Phillip Sudan) over my repeated objections. I have repeatedly made clear to Mr. Frietsch that I regard the Facility as a unilateral and improper initiative. I consider that ICSL's entry into the Facility has been engineered by Mr. Frietsch, acting completely in excess of his executive authority as regards the Company's affairs.

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Table 1: Frequency of Disputes and Characteristics of Directors

Panel A reports frequencies and descriptive statistics for our sample of 168 disputes involving directors during 1995 to 2006. Disputes are identified from SEC 8-K filings containing directors' resignation letters. Data on total assets are obtained from COMPUSTAT and various SEC filings. Panel B shows the sample distribution by industry (primary 2-digit SIC code as reported in the SEC EDGAR database). Panels C and D summarize the professional backgrounds and other characteristics of departing and remaining directors. Data on firms and individual directors are obtained from proxy statements, annual reports, 10-K filings, 10-KSB filings, and other SEC filings. Inside directors are current firm employees. Gray directors are non-insiders who are relatives of executive officers, former employees of the firm, founding family members, or persons having business dealings with the firm. Independent directors include all non-employee directors who are not gray directors. A director's occupation is determined from his or her most recent professional experience at the time of the dispute as described in proxy statements or 10-KSB filings. Total assets are in inflation-adjusted 1995 dollars.

Panel A: Disputes, by Year and by Number of Departing Directors					
Year	Number of Dispute Episodes	Firm Size, Total Assets (\$ millions)			
		Mean	Median	Q1	Q3
1995	2	3,401.74	3,401.74	239.39	6,564.08
1996	8	1,295.67	34.08	19.31	162.33
1997	11	8,698.46	35.13	16.61	490.44
1998	13	77.80	10.92	0.64	149.19
1999	7	126.39	11.42	0.98	171.84
2000	9	22.63	4.17	0.84	12.37
2001	10	48.99	4.58	1.36	14.22
2002	12	252.35	18.52	2.07	56.98
2003	9	46.50	5.94	1.30	106.33
2004	15	48.64	10.48	4.05	37.99
2005	33	2,990.27	14.65	2.87	62.82
2006	39	9,570.03	18.09	4.50	227.30
Total	168				
One departing director	137	4,301.14	12.86	1.77	130.42
Two departing directors	18	36.35	10.98	6.90	33.43
Three departing directors	8	52.77	21.63	1.44	78.14
> Three departing directors	5	239.10	14.70	9.44	144.29
Total	168	3,521.00	13.25	2.10	118.11

Table 1 (cont.)
Panel B: Disputes, by Industry

Industry Groups	2-digit SIC Codes	# of firms	% of sample
Agriculture, mining, construction	01-19	10	5.95
Food, textiles, paper products, printing	20-27	2	1.19
Chemicals, petroleum, and coal	28-29	15	8.93
Rubber, plastic, leather, and metal goods	30-34	4	2.38
Industrial machinery, transport equipment	35-37	27	16.07
Instruments and miscellaneous manufacturing	38-39	14	8.33
Transport, communications, and utilities	40-49	18	10.71
Wholesale and retail trade	50-59	12	7.14
Finance, insurance, and real estate	60-69	19	11.31
Hotels, consumer services, business services	70-79	38	22.62
Health, legal, and social services	80-99	9	5.36
Total		168	

Panel C: Individual Director Characteristics

Characteristic	Departing directors (n = 214)			Remaining directors (n = 873)		
	Mean	Median	S.D.	Mean	Median	S.D.
Director age	53.90	54	10.97	55.47	56	10.63
Tenure on the board	4.11	2	4.85	5.01	3	5.35
Stock ownership per director (%)	3.97	0.61	7.79	4.03	0.42	9.70
# of outside directorships	0.46	0	0.98	0.57	0	1.18
# of outside chairmanships	0.06	0	0.29	0.15	0	0.48
Directors who are female	0.02	--	--	0.05	--	--
Directors who are CEO of the company	0.15	--	--	0.14	--	--
Directors who are former CEOs	0.04	--	--	0.03	--	--
Directors who are executive officers of the company	0.23	--	--	0.22	--	--
Directors who are Chairman	0.11	--	--	0.12	--	--
Directors who are former Chairman	0.02	--	--	0.02	--	--
Directors who belong to the founding family	0.02	--	--	0.04	--	--

Table 1 (cont.)
Panel D: Directors' Professional Experience

Experience	% of directors		All directors, % of total		
	Departing (n=214)	Remaining (n=873)	Inside (n=329)	Gray (n=116)	Independent (n=642)
<i>Occupation</i>					
Consultant	11	14	10	17	15
Accountant	3	4	4	2	4
Lawyer	6	7	4	9	7
Engineer/Scientist	4	5	6	4	4
Medical professional	3	3	2	3	4
VC/Private equity financier	5	3	2	2	5
Investment banker	6	3	3	7	3
Commercial banker	1	3	5	4	1
Corporate executives	32	37	45	31	32
Other	29	21	19	21	25
Total	100	100	100	100	100
<i>Corporate leadership / Entrepreneurship</i>					
Current CEO of another company	19	29	13	23	35
Former CEO of another company	17	24	22	28	23
Current chair of another board	5	12	4	14	13
Former chair of another board	7	9	4	10	10
Founder of another company	23	20	16	21	23

Table 2: Summary Statistics for Dispute and Control Firms

The table reports mean and median values for selected characteristics of 168 firms experiencing director disputes and 168 matched control firms. Dispute firms are identified from SEC 8-K filings over the 1995 to 2006 period that contain directors' resignation letters. We match each dispute firm to a control firm in the same year and 2-digit SIC industry that (1) was not involved in any director disagreements over the sample period; (2) used the same form type (either DEF 14A or 10-KSB) for proxy filing as the dispute firm; and (3) was the closest in size (total assets) at the end of the fiscal year preceding the relevant 8-K filing. Data are obtained from CRSP, COMPUSTAT, proxy filings, annual reports, 10-K filings, 10-KSB filings, securities registration filings, and other SEC filings. Company founders include family members of the founder or co-founders. The variable 'CEO picks board members' equals 1 if the CEO serves on the nominating or corporate governance committee or if the board has no such committee; it equals 0 otherwise. Inside directors are current employees of the firm. Gray directors are outsiders who are former firm employees, relatives of executive officers, founding family members, or persons having business dealings with the firm. Independent directors are all outside directors who are not gray directors. An audit or compensation committee is independent if all members of the committee are independent outside directors. Independent blockholders are owners of 5% or more of the outstanding common equity who have no business ties with the company. Big 6 auditors include Arthur Andersen, Price Waterhouse, Coopers & Lybrand, Ernst & Young, Deloitte and Touche, and KPMG Peat Marwick. Financial and market value data are as of the end of the latest fiscal year preceding the dispute episode. Firm value equals the market value of equity plus the book value of total liabilities. Cash flow equals operating income before depreciation minus income taxes minus interest expense. Net income equals income before extraordinary items. Dollar values are inflation-adjusted 1995 dollars using CPI data from the U.S. Bureau of Labor Statistics. The table reports p-values from two-tailed, matched pairs t-tests for differences in means and Wilcoxon signed-ranks test for differences in distributions.

Variable	Mean			Median			Number of Pairs
	Dispute Firms	Control Firms	p-value for diff.	Dispute Firms	Control Firms	p-value for diff.	
<i>Board structure</i>							
Board size	6.55	6.18	0.071	6	6	0.051	168
Inside directors on the board (%)	38.90	35.82	0.131	33.33	28.57	0.069	168
Gray directors on the board (%)	11.53	8.21	0.035	0	0	0.021	168
Independent directors on the board (%)	49.57	55.97	0.006	50.0	60.0	0.001	168
Independent audit committee	0.51	0.61	0.019	--	--	0.020	168
Independent compensation committee	0.39	0.49	0.018	--	--	0.018	168
Independent audit and compensation committees	0.36	0.46	0.035	--	--	0.036	168
<i>CEO characteristics</i>							
Age (years)	52.58	53.29	0.501	52	53	0.389	167
Tenure on the board (years)	5.79	8.40	0.0004	4	5	0.001	168
Company founder	0.20	0.15	0.181	--	--	0.180	166

CEO picks board members	0.72	0.80	0.206	--	--	0.345	167
<i>Ownership and governance</i>							
CEO stock ownership (%)	10.60	10.93	0.837	2.85	4.80	0.723	165
Directors and officers stock ownership (%)	23.91	23.80	0.954	18.44	18.05	0.861	164
Independent blockholdings (%)	14.25	10.99	0.083	7.30	5.22	0.289	164
Number of independent blockholders	1.29	1.07	0.164	1	1	0.345	164
Co. has an independent blockholder	0.60	0.54	0.212	--	--	0.211	168
CEO chairs the board	0.53	0.48	0.384	--	--	0.383	168
Big 6 auditor	0.38	0.46	0.033	--	--	0.034	147
<i>Firm characteristics</i>							
Total Assets (\$ millions)	3,521.00	2,149.71	0.180	13.25	13.23	0.186	168
Market Value of Equity (\$ millions)	3,295.09	747.99	0.140	52.74	20.35	0.158	105
Total Debt / Firm Value	0.29	0.36	0.037	0.17	0.31	0.035	99
Cash Flow / Firm Value	-0.14	-0.08	0.202	-0.03	0.004	0.034	97
Net income / Firm Value	-0.17	-0.11	0.194	-0.04	-0.03	0.073	99
Firm on CRSP at 8-K filing date	0.50	0.56	0.150	--	--	0.149	168
Firm on NYSE at 8-K filing date	0.07	0.11	0.109	--	--	0.109	168
Firm on AMEX at 8-K filing date	0.05	0.02	0.166	--	--	0.166	168
Firm on Nasdaq at 8-K filing date	0.27	0.35	0.069	--	--	0.069	168
Firm age from date of CRSP listing, in years	9.78	13.42	0.094	6	11	0.008	64

Table 3: Cited Causes of Disputes Involving Directors

The table shows the incidence of different types of issues cited by resigning directors as underlying causes of dispute for our sample of 168 firms. Dispute episodes are identified from SEC 8-K filings made over the 1995 to 2006 period that contain an Exhibit 17 (director's resignation letter) citing disagreement. The total frequency across all categories exceeds 168 because multiple issues are cited for some disputes.

Key Areas of Dispute	Examples of Issues Cited	Frequency
Management style	<ul style="list-style-type: none">• Poor working relationship with CEO• Management did not listen to board's legal and strategic advice• Loss of confidence in management's ability to increase shareholder value• Chairman ignored directors and was hostile to them• Insubordination of the company's management team	45
Board functioning	<ul style="list-style-type: none">• Directors were not given sufficient information on financials and operations• Resigner was forced to vote upon unfamiliar matters without board discussion• Special board meetings were called on short notice regarding important matters• Resigner was not given notice of board meetings• Directors were not independent under Sarbanes-Oxley• CEO exerted undue influence over Compensation Committee to pay him what he liked• Other board members sided with management rather than with shareholders• CEO/Chairman attempted to remove resigner from the board• Management appeared to pursue their own interests, unconstrained by the board	43
Corporate strategy and direction	<ul style="list-style-type: none">• Co. has moved away from its R&D focus, to the detriment of shareholders• Disagreement over direction of the company• Lack of clarity in business, marketing, and financial plans	39
Corporate governance	<ul style="list-style-type: none">• Disagreement with board practices, including adoption of shareholder rights plan• Disagreement over recent changing of the audit committee chair• No review of corporate disclosures and executive employment contracts• Board's governance practices, especially CEO compensation and succession• Disagreement over procedure for selecting outside auditor	33

Specific financing or control transaction	<ul style="list-style-type: none"> • Board rejected takeover offer that would have added to shareholder value • Company did not receive full value on its recent sale of key assets • Terms of going-private offer were inadequate • 112 million shares issued to outside consultants 	32
Dispute among board members	<ul style="list-style-type: none"> • Disagreement over process and decisions related to development of the company • Other board members accused the resigner of misconduct • Board was controlled by blockholders, to the detriment of other shareholders • Board faction seized control in a hostile manner 	24
Conflicts of interest and possible fraud	<ul style="list-style-type: none"> • CEO purchased company stock one day before the board approved a stock buyback • CEO used pseudonym to post misleading messages on Internet stock message boards • Company delayed return of excess funds to IPO subscribers • Excessive options grant was made to the CEO 	23
Corporate disclosure	<ul style="list-style-type: none"> • Letter to shareholders made misrepresentations about shareholder proposals • Misstatements were made in SEC filing about newly-acquired technology • Proxy statement reported misleading executive compensation amounts • Co. made inappropriate use of resigner's name as signatory in 10-K filing • Registration statement was not reviewed by the board prior to SEC filing 	22
Management hiring or succession	<ul style="list-style-type: none"> • Disagreement over appointment of the newly-hired CEO as Chairman • Calls for resignation of CEO/Chairman were ignored • CEO's re-election to the board • Other directors unwilling to effect a change in leadership • Other board members repeatedly refused to hire full-time CEO 	16
Contract dispute	<ul style="list-style-type: none"> • Dispute over money (cash or stock) owed to resigner • D&O insurance coverage not renewed 	12
Miscellaneous	<ul style="list-style-type: none"> • CEO withheld wages from line employees • Disagreement over Management's position on a confidential matter • Workplace environment was counterproductive • Management did not foster diversity in the workplace • Payroll taxes were delinquent 	13

Table 4: Correlations

The table shows pair-wise correlations for the sample and variables in Table 5. ^{a,b,c} indicate statistical significance at the 10%, 5%, and 1% levels, respectively.

	Dispute Firm	CEO Age > 63	Ln (1 + CEO tenure)	CEO is founder	Non-CEO chairman	CEO picks board members	CEO Shareholdings (%)	D&O shareholdings (%), excl. CEO	Independent blockholdings (%)	Ln (1 + board size)	Independent directors on the board (%)	Gray directors on the board (%)	Independent audit committee	Independent compensation committee	Avg. ROA, past two years	Total debt/total assets
CEO Age > 63	0.024															
Ln (1 + CEO tenure)	-0.174 ^c	0.257 ^c														
CEO is founder	0.071	0.026	0.247 ^c													
Non-CEO chairman	-0.031	-0.183 ^c	-0.180 ^c	-0.192 ^c												
CEO picks board members	-0.032	-0.034	-0.115 ^b	0.069	-0.038											
CEO shareholdings (%)	-0.013	0.149 ^e	0.116 ^b	0.273 ^c	-0.215 ^c	0.210 ^e										
D&O shareholdings (%), excl. CEO	0.008	-0.146 ^c	-0.150 ^c	-0.036	0.289 ^c	0.159 ^c	-0.093 ^a									
Independent blockholdings (%)	0.102 ^a	0.018	-0.063	-0.082	0.051	-0.203 ^c	-0.148 ^c	-0.049								
Ln (1 + board size)	0.077	-0.104 ^a	0.107 ^b	-0.059	0.219 ^c	-0.314 ^c	-0.281 ^c	0.034	0.087							
Independent directors on the board (%)	-0.129 ^b	-0.011	0.142 ^c	-0.058	0.124 ^b	-0.367 ^c	-0.246 ^c	-0.131 ^b	0.194 ^c	0.559 ^c						
Gray directors on the board (%)	0.117 ^b	-0.135 ^b	-0.119 ^b	-0.056	0.138 ^b	0.064	-0.024	0.196 ^c	0.028	0.104 ^a	-0.356 ^c					
Independent audit committee	-0.105 ^a	-0.029	0.112 ^b	-0.064	0.112 ^b	-0.416 ^c	-0.148 ^c	-0.174 ^c	0.129 ^b	0.382 ^c	0.577 ^c	-0.236 ^c				
Independent compensation committee	-0.110 ^b	-0.095 ^a	0.102 ^a	-0.081	0.069	-0.452 ^c	-0.249 ^c	-0.229 ^c	0.136 ^b	0.387 ^c	0.525 ^c	-0.183 ^c	0.673 ^c			
Avg. ROA, past two years	-0.026	0.014	0.047	-0.041	-0.002	-0.081	-0.072	0.007	0.067	0.241 ^c	0.249 ^c	-0.001	0.145 ^b	0.122 ^b		
Total debt/total assets	0.056	0.151 ^c	0.001	-0.012	-0.051	0.046	0.045	-0.046	-0.052	-0.042	-0.081	-0.036	-0.089	-0.071	-0.286 ^c	
Ln (1+total assets)	-0.003	-0.044	0.149 ^c	-0.037	0.129 ^b	-0.408 ^c	-0.244 ^c	-0.074	-0.130 ^b	0.652 ^c	0.476 ^c	0.059	0.338 ^e	0.377 ^c	0.170 ^c	-0.104 ^a

Table 5: Probability of Dispute Involving Directors: Firm-level Analysis

The table reports the results of matched-pairs (conditional) logistic regressions explaining the occurrence of disputes involving directors. The dependent variable in each regression equals 1 if a firm experienced a dispute and 0 otherwise. The base sample consists of 168 dispute firms over the 1995 to 2006 period and 168 matching control firms. The number of observations varies across regressions due to missing data for some variables. Data are obtained from COMPUSTAT, proxy filings, annual reports, 10-K and 10-KSB filings, securities registration filings, and other SEC filings. Company founders include family members of the founder or co-founders. The variable ‘CEO picks board members’ equals 1 if the CEO serves on the nominating or corporate governance committee or if the board has no such committee; it equals 0 otherwise. Inside directors are current employees of the firm. Gray directors are outsiders who are former employees of the firm, relatives of executive officers, founding family members, or persons having business dealings with the firm. Independent directors include all outside directors who are not gray directors. An audit or compensation committee is independent if all members of the committee are independent outside directors. Independent blockholders are owners of 5% or more of common stock who have no business ties with the company. Financial and market value data are as of the end of the most recent fiscal year preceding the dispute episode. Return on assets is income before extraordinary items divided by total book assets. Panel A includes all pairs of observations; Panel B includes only observation pairs in which at least one inside director resigned; and Panel C includes only observation pairs in which all resigning directors are outsiders. Z-statistics are computed using a robust variance estimator and are reported in parentheses below coefficient estimates. *, **, and *** denote estimates significantly different from zero at the 10%, 5%, and 1% levels, respectively, in two-tailed tests.

Panel A: All Director Departures				
Explanatory Variable	(1)	(2)	(3)	(4)
CEO Age > 63 years	0.360 (0.87)	0.449 (1.09)	0.444 (1.06)	0.538 (1.14)
Ln (1 + CEO tenure on the board in years)	-0.745*** (-3.87)	-0.766*** (-4.11)	-0.750*** (-4.06)	-0.719*** (-3.10)
CEO is company founder	0.907** (2.11)	0.874** (2.02)	0.862** (2.04)	0.871 (1.54)
Board has a non-CEO chairman	-0.407 (-1.26)	-0.370 (-1.18)	-0.418 (-1.33)	-0.443 (-1.29)
CEO picks board members	-0.365 (-1.04)	-0.399 (-1.16)	-0.398 (-1.14)	-0.372 (-0.89)
CEO stock ownership (%)	-0.007 (-0.76)	-0.004 (-0.40)	-0.007 (-0.82)	-0.009 (-0.53)
D&O stock ownership, excluding CEO (%)	-0.005 (-0.48)	-0.005 (-0.55)	-0.007 (-0.67)	-0.005 (-0.36)
Independent blockholdings (%)	0.021** (2.25)	0.014 (1.70)	0.014* (1.67)	0.024*** (2.78)
Ln (1 + board size)	1.561*** (3.02)	0.982* (1.93)	0.946* (1.94)	2.128*** (3.46)
Gray directors (%)	-0.153 (-0.14)	1.459* (1.66)	1.562* (1.75)	0.710 (0.53)

Independent directors (%)	-2.922*** (-3.13)			-2.440** (-2.20)
Independent audit committee		-0.820** (-2.05)		
Independent compensation committee			-0.777** (-2.43)	
Avg. return on assets, past two years				-0.020* (-1.76)
Total debt/total assets				-0.015 (-0.68)
Ln (1 + total assets in \$ millions)	-0.263 (-0.81)	-0.192 (-0.40)	-0.216 (-0.47)	0.077 (0.17)
P-value, Likelihood Ratio Test	0.002	0.021	0.004	0.0005
Pseudo R-Squared	0.203	0.173	0.173	0.245
Number of observations	324	324	324	256

Panel B: At Least One Inside Director Departure

Explanatory Variable	(1)	(2)	(3)	(4)
CEO Age > 63	0.889 (1.08)	0.401 (0.57)	0.403 (0.56)	3.986* (1.87)
Ln (1 + CEO tenure on the board in years)	-0.445 (-1.15)	-0.741** (-2.09)	-0.739** (-2.10)	-0.232 (-0.22)
CEO is company founder	1.103* (1.71)	1.400** (2.42)	1.375** (2.28)	6.085** (2.23)
Board has a non-CEO chairman	-0.604 (-0.87)	-0.955 (-1.35)	-1.001 (-1.53)	0.963 (0.73)
CEO picks board members	1.016 (1.01)	0.744 (0.85)	0.727 (0.83)	2.554 (1.51)
CEO stock ownership (%)	-0.022 (-0.93)	-0.015 (-0.89)	-0.017 (-1.04)	-0.181** (-2.06)
D&O stock ownership, excluding CEO (%)	0.013 (0.65)	0.007 (0.43)	0.003 (0.23)	0.115** (2.44)
Independent blockholdings (%)	0.030** (2.06)	0.015 (1.38)	0.014 (1.29)	0.051* (1.67)

Ln (1 + board size)	1.422 (1.37)	-0.113 (-0.13)	-0.056 (-0.07)	-4.963 (-1.41)
Gray directors (%)	-3.740* (-1.76)	1.389 (0.70)	0.690 (0.40)	1.180 (0.22)
Independent directors (%)	-5.544*** (-3.42)			-11.608 (-1.40)
Independent audit committee		0.052 (0.07)		
Independent compensation committee			-0.466 (-0.82)	
Avg. return on assets, past two years				-0.054* (-1.86)
Total debt/total assets				1.004 (0.56)
Ln (1 + total assets in \$ millions)	-0.605 (-0.57)	-0.920 (-1.45)	-1.002 (-1.53)	2.059 (1.27)
P-value, Likelihood Ratio Test	0.028	0.276	0.275	0.553
Pseudo R-Squared	0.340	0.186	0.192	0.578
Number of observations	116	116	116	82

Panel C: Outside Director Departures

Explanatory Variable	(1)	(2)	(3)	(4)
CEO Age > 63	0.719 (1.19)	0.691 (1.18)	0.705 (1.19)	0.948 (1.34)
Ln (1 + CEO tenure on the board in years)	-0.802*** (-2.86)	-0.927*** (-3.29)	-0.878*** (-2.95)	-0.803** (-2.11)
CEO is company founder	0.799 (1.33)	0.823 (1.08)	0.722 (1.23)	0.174 (0.22)
Board has a non-CEO chairman	-0.253 (-0.60)	-0.282 (-0.69)	-0.205 (-0.46)	-0.442 (-0.94)
CEO picks board members	-0.763 (-1.51)	-1.369** (-2.52)	-1.064** (-2.30)	-0.715 (-1.21)

CEO stock ownership (%)	-0.005 (-0.43)	0.003 (0.18)	-0.005 (-0.44)	0.005 (0.29)
D&O stock ownership, excluding CEO (%)	-0.005 (-0.41)	-0.010 (-0.65)	-0.014 (-0.84)	-0.006 (-0.33)
Independent blockholdings (%)	0.012 (0.85)	0.011 (0.82)	0.014 (0.93)	0.017 (1.25)
Ln (1 + board size)	1.922*** (3.06)	2.060*** (2.89)	1.979*** (2.94)	2.857*** (3.78)
Gray directors (%)	2.103 (1.39)	1.908 (1.51)	2.052* (1.77)	3.084 (1.36)
Independent directors (%)	-0.933 (-0.80)			-0.077 (-0.05)
Independent audit committee		-2.064*** (-2.49)		
Independent compensation committee			-1.488*** (-2.95)	
Avg. return on assets, past two years				-0.051*** (-2.84)
Total debt/total assets				-1.942** (-2.56)
Ln (1 + total assets in \$ millions)	-0.126 (-0.31)	0.621 (1.09)	0.412 (0.83)	-0.173 (-0.32)
P-value, Likelihood Ratio Test	0.047	0.033	0.006	0.0003
Pseudo R-Squared	0.232	0.311	0.295	0.349
Number of observations	208	208	208	174

Table 6: Probability of Dispute: Director-level Analysis

This table reports the results of logistic regressions explaining the likelihood of individual director departures at companies experiencing board disputes. The dependent variable equals 1 if a director resigns due to a dispute and 0 otherwise. Regressions in Panel A include all individual directors of dispute firms; those in Panel B include only outside directors of dispute firms. A director is considered to be a founder of a company if he/she founded or co-founded the company or is a member of the founding family. Only public companies are included in the number of outside directorships. A director's profession (academic, VC, investment banker, or retired) is determined from the most recent career information provided in biographical sketches disclosed in proxy statements. Z-statistics are computed using a robust variance estimator and are reported in parentheses below coefficient estimates. *, **, and *** denote estimates significantly different from zero at the 10%, 5%, and 1% levels, respectively, in two-tailed tests.

Panel A: All Directors		
Explanatory Variable	(1)	(2)
Intercept	-1.117*** (-5.55)	-1.154*** (-5.81)
Ln(1 + director tenure on the board in years)	-0.277** (-2.31)	-0.264** (-2.21)
Director stock ownership (%)	0.214 (0.28)	0.368 (0.49)
Director is CEO of another firm	-0.857*** (-3.02)	
Director is Chairman of another firm's board		-1.000*** (-2.92)
Female	-0.657 (-1.33)	-0.662 (-1.33)
Company founder	-0.421 (-0.85)	-0.467 (-0.92)
Retired	0.108 (0.31)	0.119 (0.34)
Number of outside directorships	0.012 (0.15)	0.024 (0.31)
Founder of another firm	0.399** (2.14)	0.346 (1.85)
Academic	-0.111 (-0.22)	-0.084 (-0.17)
VC	1.159*** (2.66)	1.079** (2.43)
Investment banker	0.668* (1.88)	0.746** (2.05)
P-value, Likelihood Ratio Test	0.005	0.008
Pseudo R-Squared	0.030	0.030
Number of observations	1,071	1,071

Table 6 (cont'd.)

Panel B: Outside Directors		
Explanatory Variable	(1)	(2)
Intercept	-1.236*** (-4.80)	-1.269*** (-5.02)
Ln(1 + director tenure on the board in years)	-0.226 (-1.54)	-0.215 (1.48)
Director stock ownership (%)	-3.304*** (-2.71)	-3.198*** (-2.58)
Director is CEO of another firm	-0.680** (-2.01)	
Director is Chairman of another firm's board		-0.658* (-1.72)
Female	-0.640 (-1.15)	-0.655 (-1.16)
Company founder	-1.179 (-1.09)	-1.246 (-1.15)
Retired	0.162 (0.40)	0.161 (0.40)
Number of outside directorships	0.040 (0.48)	0.046 (0.55)
Founder of another firm	0.463** (1.99)	0.429* (1.83)
Academic	0.228 (0.43)	0.254 (0.48)
VC	1.095** (1.98)	1.062* (1.91)
Investment banker	1.077*** (2.63)	1.152*** (2.79)
P-value, Likelihood Ratio Test	0.002	0.007
Pseudo R-Squared	0.044	0.043
Number of observations	748	748

Table 7: Abnormal Returns Surrounding Director Disputes

The table shows cumulative abnormal returns (CARs) computed from daily market-adjusted returns using the CRSP equal-weighted index. The sample consists of 123 disputes involving directors that led to director departure. Disputes are identified from SEC 8-K filings made over the 1995 to 2006 period that contained an Exhibit 17 (director's resignation letter). The event date is defined as the earlier of the 8-K filing date and the date of the first Factiva news story, if any, reporting the director departure. Stock price data are from CRSP and Datastream. Panel A reports CARs for the full sample and for subsamples defined according to the highest executive officer position held by any of the departing directors. The rightmost column in this panel reports p-values from tests for differences in means (distributions) between columns (4) and (5) based on a t-test (Mann-Whitney test). Panel B reports CARs for subsamples defined according to whether at least one resigning director was a member of a particular board committee. P-values for differences in means (distributions) based on a t-test (Mann-Whitney test) are also reported. Panel C shows results partitioned by the type of dispute. The table reports mean CARs and median CARs (in parentheses). *, **, and *** denote CARs significantly different from zero at the 10%, 5%, and 1% significance levels, respectively, using two-tailed Brown and Warner (1985) t-tests for means and two-tailed Wilcoxon tests for medians. Statistics for the Brown and Warner t-tests are computed using daily price data over a 50-day estimation period ending 21 days before the event date.

Panel A: By Resigning Directors' Executive Positions						
	All Disagreement Events	Positions of Resigning Director(s)				P-value of diff, (4) vs. (5)
		CEO	Non-CEO Executive Officer	Any Executive Officer	Outsider	
	(1)	(2)	(3)	(4)	(5)	
CAR [0,0]	-2.15*** (-0.71)***	-2.01* (-0.66)	-2.14 (-0.11)	-2.07** (-0.32)	-2.19* (-0.95)**	0.96 (0.84)
CAR [-1,0]	-0.88 (-0.98)*	-0.23 (-3.70)	-3.18* (-0.25)	-1.53* (-1.15)	-0.56 (-0.98)	0.68 (0.42)
CAR [-1,1]	-2.58** (-2.08)***	-2.43 (-3.88)	-5.69*** (-2.44)**	-3.86*** (-3.16)**	-1.94 (-1.73)**	0.47 (0.30)
CAR [-5,1]	-2.28* (-1.55)**	-7.83* (-10.53)	-0.75 (-0.50)	-4.72* (-2.26)*	-1.04 (-1.54)*	0.48 (0.44)
CAR [-5,5]	-1.58 (-1.65)*	-11.47** (-13.41)	2.77 (-0.52)	-5.22 (-6.78)	0.27 (-1.09)	0.34 (0.21)
CAR [-10,1]	-6.11*** (-6.06)***	-17.61*** (-20.74)**	-0.86 (-1.99)	-10.26*** (-16.31)**	-4.01* (-3.40)**	0.29 (0.09)
CAR [-10,10]	-5.14** (-5.69)**	-25.10*** (-28.33)**	1.43 (3.69)	-13.45*** (-14.85)**	-0.93 (-4.61)	0.09 (0.07)
<i>N</i>	123	23	18	41	82	

Table 7 (cont.)

Panel B: By Resigning Directors' Committee Membership									
	Audit Committee member			Compensation Committee member			Nominating Committee Member		
	Yes (1)	No (2)	p-value, diff.	Yes (3)	No (4)	p-value, diff.	Yes (5)	No (6)	p-value, diff.
CAR [0,0]	-2.94*** (-1.56)***	-1.78* (-0.34)	0.60 (0.16)	-2.24*** (-1.73)**	-2.10 (-0.50)*	0.95 (0.34)	-1.12 (-1.00)*	-2.49*** (-0.69)**	0.57 (0.82)
CAR [-1,0]	-2.46 (-1.24)*	-0.15 (-0.48)	0.32 (0.55)	-1.65* (-1.12)	-0.53 (-0.82)	0.63 (0.98)	0.66 (-1.11)	-1.40* (-0.75)	0.41 (0.73)
CAR [-1,1]	-4.04** (-3.42)**	-1.90 (-1.62)**	0.43 (0.52)	-2.72** (-2.60)*	-2.52 (-1.90)**	0.94 (0.97)	-1.24 (-1.95)	-3.03*** (-2.16)**	0.54 (0.62)
CAR [-5,1]	-4.15 (-2.29)*	-1.40* (-1.54)	0.60 (0.95)	-4.56** (-2.39)**	-1.21 (-1.08)	0.52 (0.76)	-2.65 (-2.26)	-2.15** (-1.26)**	0.93 (0.83)
CAR [-5,5]	-3.37 (-1.71)	-0.73 (-1.58)	0.65 (0.99)	-3.37 (-3.48)	-0.73 (-1.40)	0.65 (0.97)	-1.54 (-0.90)	-1.59 (-2.23)	0.99 (0.47)
CAR [-10,1]	-3.78 (-2.60)	-7.20*** (-7.92)***	0.56 (0.22)	-4.92 (-2.78)*	-6.67*** (-7.92)**	0.77 (0.34)	-0.56 (-1.36)	-7.99*** (-7.80)***	0.24 (0.06)
CAR [-10,10]	0.83 (-4.13)	-7.94*** (-5.95)**	0.24 (0.42)	2.39 (-3.02)	-8.67*** (-6.84)**	0.14 (0.24)	-1.22 (-5.64)	-6.47*** (-5.73)**	0.51 (0.44)
<i>N</i>	39	84		39	84		31	92	

Table 7 (cont.)

Panel C: By Type of Dispute			
	Event Window		
	[-1,1]	[-5,1]	[-10,1]
Corporate strategy and direction (n = 31)	-6.38*** (-6.30)**	-10.13*** (-7.10)***	-14.08*** (-16.31)***
Specific financing or control transaction (n = 22)	0.30 (-1.16)	-0.71 (-1.97)	-3.88 (-3.60)
Management style (n = 35)	-8.22*** (-5.79)***	-15.92*** (-8.68)***	-21.08*** (-20.44)***
Contract dispute (n = 8)	-8.43*** (-6.97)**	-7.39 (-0.24)	-20.60*** (-21.93)**
Corporate disclosure (n = 14)	6.20*** (2.84)	7.10* (7.20)*	5.74* (3.49)
Management hiring or succession (n = 10)	-5.87*** (-5.40)***	-11.16*** (-2.33)	-19.76*** (-5.20)*
Dispute among board members (n = 18)	-2.11*** (-1.80)	-5.53*** (-1.67)	-9.45*** (-11.77)
Conflicts of interest and possible fraud (n = 15)	-1.54* (-0.16)	-11.89*** (-7.39)	-13.63*** (-7.92)*
Board functioning (n = 32)	2.27** (-0.87)	9.54** (4.57)	10.03*** (6.41)
Corporate governance (n = 26)	-0.33 (-1.29)	-0.75** (-1.00)	-1.86*** (-1.18)
Miscellaneous (n = 5)	-5.72 (-3.01)*	-24.03*** (-4.11)**	-23.06*** (-0.81)

Table 8: Correlations

This table shows pair-wise correlations for the sample and variables used in Table 9. ^{a,b,c} indicate statistical significance at the 10%, 5%, and 1% levels, respectively.

	11-day CAR, [-10, +1]	Ln(1 + avg. tenure of resigners)	Ln (1 + number of resigners)	Ln (1 + CEO tenure)	CEO is founder	Non-CEO chairman on the board	CEO picks board members	CEO Share-Holdings (%)	D&O share-holdings (%), excl. CEO	Independent blockholdings (%)	ln (1 + board size)	Independent directors (%)	Gray directors (%)	Resigner on audit committee	Resigner on compensation committee	Resigner is CEO	Media Coverage
Ln(1 + avg. tenure of resigners)	0.255 ^c																
Ln (1 + number of resigners)	0.023	-0.041															
Ln (1 + CEO tenure)	0.247 ^c	0.297 ^c	0.046														
CEO is founder	-0.042	-0.048	0.096	0.270 ^c													
Non-CEO chairman on the board	-0.135	0.078	-0.008	-0.166 ^b	-0.107												
CEO picks board members	-0.123	-0.198 ^b	-0.018	-0.152 ^b	0.052	-0.172 ^b											
CEO shareholdings (%)	-0.036	-0.150 ^a	0.071	0.113	0.288 ^c	-0.246 ^c	0.175 ^b										
D&O shareholdings (%), excl. CEO	0.076	0.005	-0.065	-0.145 ^a	0.054	0.278 ^c	0.152 ^a	-0.132 ^a									
Independent blockholdings (%)	0.079	0.026	-0.124	-0.088	-0.088	0.112	-0.163 ^b	-0.140 ^a	-0.138 ^a								
ln (1 + board size)	0.002	0.250 ^c	0.073	0.277 ^c	-0.073	0.229 ^c	-0.387 ^c	-0.266 ^c	0.105	0.020							
Independent directors (%)	0.084	0.175 ^b	0.113	0.182 ^b	-0.078	0.102	-0.357 ^c	-0.207 ^c	-0.165 ^b	0.182 ^b	0.511 ^c						
Gray directors (%)	0.078	0.093	-0.136 ^a	-0.027	-0.050	0.195 ^b	-0.021	-0.016	0.163 ^b	0.008	0.155 ^b	-0.346 ^c					
Resigner on Audit committee	-0.024	-0.080	0.198 ^c	-0.104	-0.003	-0.132 ^a	0.106	0.099	-0.089	-0.122	-0.305 ^c	-0.199 ^c	-0.078				
Resigner on compensation cmte.	-0.066	-0.093	0.152 ^b	-0.090	-0.003	-0.074	0.091	0.084	-0.058	-0.050	-0.372 ^c	-0.202 ^c	-0.123	0.589 ^c			
Resigner is CEO	-0.183 ^b	-0.054	0.044	-0.140 ^a	0.056	0.039	0.204 ^c	0.004	-0.045	0.035	-0.227 ^c	-0.149 ^a	-0.134 ^a	-0.186 ^b	-0.124		
Media coverage	0.011	0.197 ^b	0.084	0.191 ^b	0.032	0.128 ^a	-0.225 ^c	-0.159 ^b	-0.021	0.144 ^a	0.248 ^c	0.256 ^c	-0.039	-0.090	-0.026	0.022	
ln (1+total assets)	0.007	0.337 ^c	-0.042	0.248 ^c	-0.101	0.137 ^a	-0.451 ^c	-0.256 ^c	-0.036	0.179 ^b	0.639 ^c	0.442 ^c	0.125	-0.178 ^b	-0.301 ^c	-0.194 ^b	0.335 ^c

Table 9: Cross-sectional Analysis of Abnormal Returns

The sample consists of disputes that were disclosed upon resignation of a director. Disputes are identified from SEC 8-K filings made over the 1995 to 2006 period that contained an Exhibit 17 (director's resignation letter) detailing the dispute. The table shows estimates of ordinary least squares regressions of the cumulative abnormal return over the [-10,+1] window surrounding the event date. The event date is the earlier of (1) the date of the SEC 8-K filing that revealed the dispute and departure or (2) the first Factiva news story, if any, reporting the director departure. Stock price data are from CRSP and Datastream. Cumulative abnormal returns (CARs) are computed from daily market-adjusted returns using the CRSP equal-weighted index. Company founders include family members of the founder or co-founders. The variable 'CEO picks board members' equals 1 if the CEO serves on the nominating or corporate governance committee or if the board has no such committee; it equals 0 otherwise. Independent blockholders are owners of 5% or more of common stock who have no business ties with the company. Media coverage equals 1 if the director departure was reported in at least one Factiva news story; it equals 0 otherwise. Inside directors are current firm employees. Gray directors are outsiders who are relatives of executive officers, former firm employees, founding family members, or persons having business dealings with the firm. Total assets are measured as of the end of the latest fiscal year preceding the dispute episode. Committee membership is defined according to whether a director belonged to a particular board committee or, when no such committee exists, whether the board consists of five or fewer directors. Each regression includes industry dummies (1-digit SIC). All regressions use a robust variance estimator. T-statistics are reported in parentheses below coefficient estimates. *, **, and *** denote significantly different from zero at the 10%, 5%, and 1% levels, respectively, in two-tailed tests.

	All Director Departures			At least One Inside Director Departure			Outside Director Departures		
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Intercept	0.173 (0.71)	0.364 (1.39)	0.362 (1.35)	0.419 (0.81)	0.550 (1.12)	0.451 (0.65)	0.487 (1.44)	0.667* (1.92)	0.661* (1.85)
Ln (1+Avg. tenure of resigning directors)	0.091** (2.26)	0.099** (2.39)	0.100** (2.30)	0.052 (0.48)	-0.009 (-0.08)	-0.019 (-0.15)	0.128** (2.53)	0.139** (2.54)	0.141** (2.46)
Ln (1+number of directors resigning)	0.037 (0.33)	0.079 (0.67)	0.079 (0.67)	-0.143 (-0.37)	-0.212 (-0.47)	-0.263 (-0.56)	0.038 (0.32)	0.099 (0.84)	0.092 (0.79)
Ln (1+CEO tenure on the board in years)	0.122** (2.53)	0.111** (2.33)	0.112** (2.31)	0.245 (1.62)	0.332* (1.90)	0.335* (1.89)	0.054 (1.31)	0.061 (1.54)	0.061 (1.49)
CEO is company founder	-0.112* (-1.73)	-0.115* (-1.74)	-0.113* (-1.68)	-0.168 (-1.00)	-0.117 (-0.55)	-0.118 (-0.56)	-0.008 (-0.11)	-0.003 (-0.04)	0.003 (0.04)
Board has a non-CEO chairman	-0.113* (-1.75)	-0.095 (-1.45)	-0.094 (-1.42)	-0.281 (-1.23)	-0.272 (-1.03)	-0.273 (-1.01)	-0.007 (-0.08)	0.003 (0.03)	0.003 (0.04)
CEO picks board members	-0.146** (-2.57)	-0.158*** (-2.74)	-0.158*** (-2.71)	-0.338* (-1.68)	-0.399* (-1.90)	-0.383 (-1.53)	-0.109** (-2.03)	-0.117** (-2.04)	-0.117** (-2.01)
CEO stock ownership (%)	-0.001 (-0.60)	-0.001 (-0.75)	-0.001 (-0.73)	-0.004 (-0.79)	-0.005 (-1.16)	-0.004 (-0.80)	-0.002 (-1.28)	-0.002 (-1.37)	-0.002 (-1.31)

D&O stock ownership, excl. CEO (%)	0.007*** (3.59)	0.006*** (3.44)	0.006*** (3.44)	0.014*** (3.74)	0.016*** (3.93)	0.016*** (3.12)	0.003 (1.04)	0.002 (1.05)	0.003 (1.05)
Independent blockholdings (%)	0.002 (1.43)	0.003 (1.50)	0.003 (1.50)	0.005 (1.18)	0.005 (1.05)	0.005 (0.79)	0.004** (2.02)	0.004** (2.08)	0.004** (2.05)
Ln (1+board size)	-0.117 (-0.81)	-0.156 (-1.13)	-0.156 (-1.13)	-0.071 (-0.29)	-0.080 (-0.31)	-0.063 (-0.21)	-0.170 (-0.71)	-0.214 (-0.99)	-0.216 (-0.99)
Independent directors (%)	0.116 (0.70)	0.045 (0.24)	0.053 (0.29)	0.246 (0.69)	0.146 (0.32)	0.219 (0.36)	-0.239 (-0.93)	-0.264 (-0.97)	-0.241 (-0.90)
Gray directors (%)	0.255 (1.00)	0.179 (0.66)	0.180 (0.66)	0.186 (0.41)	0.068 (0.14)	0.119 (0.22)	-0.169 (-0.54)	-0.186 (-0.56)	-0.178 (-0.54)
Any resigner on audit committee		-0.005 (-0.09)	-0.005 (-0.09)		0.070 (0.28)	0.104 (0.37)		-0.042 (-0.68)	-0.040 (-0.64)
Any resigner on compensation committee		-0.101 (-1.60)	-0.099 (-1.56)		-0.120 (-0.49)	-0.091 (-0.32)		-0.106 (-1.49)	-0.101 (-1.39)
Any resigner is CEO		-0.101 (-1.02)	-0.099 (-1.02)		0.176 (1.01)	0.191 (1.03)			
Media coverage			-0.016 (-0.20)			0.072 (0.26)			-0.027 (-0.33)
Ln (1+total assets in \$ millions)	-0.032* (-1.75)	-0.037* (-1.92)	-0.036* (-1.86)	-0.092*** (-2.69)	-0.092** (-2.42)	-0.093** (-2.39)	-0.017 (-0.76)	-0.024 (-0.98)	-0.021 (-0.90)
p-value of F-test	.001	.003	.005	.008	.017	.002	.095	.166	.199
Adjusted R ²	0.260	0.266	0.258	0.441	0.415	0.392	0.205	0.234	0.222
Number of observations	118	118	118	40	40	40	78	78	78

Table 10: Operating Performance of Sample and Control Firms Surrounding Disputes

This table shows median values of operating performance measures for firms experiencing director disputes and for matched control firms. Return on Assets is income before extraordinary items divided by total assets. Cash flow is income before extraordinary items plus depreciation. OIBD is operating income before depreciation. Total assets are end-of-year book value of assets. Accounting data are obtained from COMPUSTAT and various SEC filings (including annual reports and 10-K, 10-KSB, and 10-Q filings). The table reports absolute values of z-statistics from paired two-tailed Wilcoxon tests for differences in distributions. The sample sizes shown are for cash flow/assets and OIBD/assets. The sample sizes for return on assets are slightly higher, ranging from three more pairs in year -2 to one more pair in year +3.

Year relative to dispute	Sample size (# of pairs)	Return on Assets			Cash Flow/Assets			OIBD/Assets		
		Dispute Firms	Control Firms	z-statistic for difference	Dispute Firms	Control Firms	z-statistic for difference	Dispute Firms	Control Firms	z-statistic for difference
-2	140	-0.146	-0.076	1.713*	-0.130	-0.020	1.533	-0.086	0.007	1.593
-1	148	-0.247	-0.067	3.069***	-0.175	-0.009	3.130***	-0.114	0.006	2.538**
0	125	-0.299	-0.026	3.270***	-0.219	0.009	3.335***	-0.119	0.027	3.825***
1	80	-0.188	0.008	0.990	-0.159	0.014	0.868	-0.152	0.027	1.626
2	47	-0.030	0.011	1.129	0.003	0.035	1.111	-0.046	0.069	2.942***
3	27	-0.057	0.020	1.981**	0.012	0.060	2.042**	-0.023	0.087	2.763***

Table 11: Aftermath of Director Disputes

The table reports the frequency of different types of delisting events experienced by dispute and control firms within 6-month, 1-year, and 2-year periods following director disputes, as reported on CRSP. Each cell reports the number of delisted dispute (control) firms, followed in parentheses by its frequency as a percentage of the total number of dispute (control) firms listed on CRSP at the time of the 8-K filing on the dispute. Delisting events are grouped into categories (not all mutually exclusive) based on CRSP delisting codes. The bankrupt category includes firms delisted due to insufficient assets or equity, or the stock price being too low. The p-values are for the equality of proportions between the dispute and control samples.

Delisting Category (CRSP Delisting Codes)	Number (Percent) of Delistings								
	Within 6 months			Within 1 year			Within 2 years		
	Dispute Firms	Control Firms	p-value	Dispute Firms	Control Firms	p-value	Dispute Firms	Control Firms	p-value
Acquired (231, 233, 241)	2 (2.4)	1 (1.1)	0.496	2 (2.4)	6 (6.4)	0.198	3 (4.7)	8 (11.1)	0.170
Bankrupt (552, 560, 561, 574)	1 (1.2)	0 (0)	0.289	2 (2.4)	1 (1.1)	0.496	5 (7.8)	4 (5.6)	0.597
Delisted (580, 582, 584, 585, 550, 551, 570)	6 (7.1)	0 (0)	0.008	8 (9.5)	2 (2.1)	0.032	9 (14.1)	7 (9.7)	0.433
All non-merger delistings (500, 520, 550, 551, 552, 560, 561, 570, 574, 580, 582, 584, 585)	8 (9.5)	0 (0)	0.002	12 (14.3)	3 (3.2)	0.008	16 (25.0)	11 (15.3)	0.156
All delistings (231, 233, 241, 500, 520, 550, 551, 552, 560, 561, 570, 574, 580, 582, 584, 585)	10 (11.9)	1 (1.1)	0.003	14 (16.7)	9 (9.6)	0.159	19 (29.7)	19 (26.4)	0.669
# of sample firms listed on CRSP at the 8-K filing date	84	94		84	94		64	72	