

Contractual Versus Actual Severance Pay Following CEO Departure

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Abstract

Using hand-collected data, we document the details of the ex-ante severance contract and the ex-post separation pay given to S&P500 CEOs upon departing from their company. We analyze for the determinants of whether or not a departing CEO receives separation pay in excess of her severance contract. This *excess* separation pay is on average, \$8 million, which amounts to close to 242% of a CEO's annual compensation. We investigate several potential explanations for this phenomenon and find evidence that in voluntary CEO departures, excess separation pay represents a governance problem. In contrast, we find evidence that in forced departures, excess separation pay represents a need to facilitate a quick and smooth transition from the failed ex-CEO to a new CEO. These results help to shed light on the dual role played by severance compensation and on bargaining games played between boards and departing executives.

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Executive compensation has been a topic of great interest for shareholders, government regulators and academic studies, mainly due to the fact that executive pay is a critical component of the corporate governance structure of a company.¹ While compensation contracts can alleviate agency problems, they can also serve as indicators of whether a board of directors is acting in the interest of shareholders, or whether it is simply rubber-stamping the demands of the CEO. Thus, we can learn much about the inner workings of a company by understanding the details of the bargaining game between the CEO and the board of directors, when determining executive pay.

In this paper we analyze this bargaining between the CEO and the board of directors at the point in time when the CEO is about to leave the firm. We do this by exploring the cross sectional determinants of the *difference* between the executive's promised (ex-ante) severance that is specified in the CEO's contract and the actual (ex-post) separation pay that the CEO receives upon departing from the firm.² We define this difference as *excess* separation pay. The analysis of the bargaining game at the time of CEO departure is especially intriguing as it provides us with information about the source of CEO power exactly at the point in time when the CEO is least likely to have any bargaining power.³ Thus, the goal of the paper is to explain why in some cases departing CEOs receive separation pay that is in excess of their existing severance agreement while in other cases they do not.

¹ See Murphy (1998) for a survey of the literature on executive compensation.

² Shareholder rights activists as well as the media argue in numerous articles that managers abuse separation agreements for their own benefits. They claim that CEOs receive millions of dollars and waltz out of the company even after poor firm performance. Moreover, they argue that the separation agreement does not seem to fit the pay-for-performance paradigm but is instead a "pay-for-failure" phenomenon.

³ Namely, this is the exact point in time where the concerns that CEOs control their pay (e.g., Bebchuk and Fried 2003), should no longer be present.

To fix ideas, consider the case of Mr. Jay Sidhu, CEO of Sovereign Bancorp between 1989 and 2006. According to a 2006 article in Forbes, "...Sovereign Bancorp's 12-member board is gearing up for a face-off with Sidhu... the board—led by activist shareholder Relational Investors—is unhappy with Sovereign's stock performance ...and plans to consider Sidhu's dismissal". In addition, a 2007 New York Times article points out that "...Despite the bank's poor performance, Mr. Sidhu left with a \$73.56 million platinum parachute lined with \$24.4 million in cash and stock options, five years of free health care, and a three-year, \$40,000-a-month consulting contract". The reported amount becomes even more peculiar when considering the actual severance contract between Sidhu and Sovereign. According to Sovereign's 2007 SEC filing, Sidhu was awarded an extra \$10 million in separation pay.⁴ This extra \$10 million amount is exactly what our paper focuses on.

More generally, we use hand-collected data to analyze 609 CEOs of S&P500 companies who left their companies between 1993 and 2007 and document the details of their severance agreements (signed at least one year prior to departure). We then compare the dollar award in each severance agreement with the reported actual severance pay given to each CEO upon her leaving her position. The data indicates that the above example of Sovereign is not an idiosyncratic event, but rather represents one of many such cases. Specifically, about 33% of S&P500 CEOs get more than what is pre-specified in their contracts. This is surprising given that even at a time when departing CEOs seemingly have no observed power over the board, those that do obtain excess separation pay, on average, receive a separation package that exceeds

⁴ See Appendix 1 for ex-ante and ex-post agreements between Sidhu and Sovereign.

their contractual severance amount by close to \$8 million. After documenting that this phenomenon is quite common in our sample, we turn to the central question of the paper, which is to explore why some executives receive excess separation pay while others do not.

The observation that executives sometimes receive separation payments in excess of what is specified in their contracts indicates that they have some form of bargaining power when negotiating with the board right before they leave the firm. The question we wish to explore is whether or not these excess payments represent CEO power due to poor corporate governance (i.e., represent something that is harmful to shareholders), or whether these excess separation payments represent an attempt by the board to respond to the incompleteness of contracts in a manner that increases the efficiency of the turnover process.

One hypothesis is that “excess” severance payments are given whenever the board is controlled by the CEO. This is the view in Bebchuk and Fried (2003), among others. The second hypothesis suggests that excess severance should not be explained by measures of the quality of the governance of the firm, but rather should be explained by variables that measure the extent to which the company will benefit from the quick and smooth departure of the incumbent CEO. The idea here is that the existing severance contract does not provide the CEO with enough incentive to leave the firm without disrupting the transition process.

The case of Dell’s firing of its CEO in 2007 illustrates this last point. It was reported that *“Former Dell CEO Kevin Rollins will receive a \$5 million severance package, according to documents filed by the computer maker, after Mr. Rollins was forced out by founder and*

*chairman Michael Dell. The filing also revealed that Mr. Rollins has agreed not to sue or compete with the company. In the Separation Agreements, Mr. Rollins provided a general release of claims against the company and agreed to certain non competition and non solicitation obligations for a period of 12 months following his termination...*⁵

In the empirical analysis we test these two hypotheses. Our main findings suggest that there is evidence for both the governance hypothesis and for the hypothesis that the board uses excess severance to facilitate a smooth and efficient transition from the previous CEO to a new one. Thus, while some cases of excess separation payment reflect agency problems, other cases seem to reflect the action of a board of directors who is focused on maximizing shareholder value. In particular, we find that excess separation payments made to CEOs whose departure is classified as voluntary represent weak internal corporate governance. In contrast, our findings suggest that excess separation payments to CEOs who are forced out represent an attempt by the board to facilitate an efficient transfer of power from a poorly performing CEO to a potentially better replacement.⁶

We first find that for the sample of CEOs that are identified as being forced out of their job, measures of governance do not explain the excess separation payment. In contrast, for the sample of CEOs who are classified as leaving voluntarily, we find that the worse the internal governance of the firm, the higher the excess separation pay.

⁵ Reported on www.redherring.com February 20, 2007.

⁶ In a slightly different context Broughman and Fried (2010) find evidence of this type of renegotiation between common shareholders and the controlling venture capitalist shareholder. In particular, they find that common shareholders that have the legal power to impede the sale of a company are able to receive additional payments from the venture capitalist.

Second, we find that for the subsample of CEOs who left voluntarily, past firm performance (as measured by past three-year abnormal stock return) does not explain excess separation pay. However, for the subsample of CEOs who were forced out, we find that the worse their past performance, the higher their excess separation pay.⁷ This result is consistent with the idea that CEOs have the ability to prolong the firing process and make it difficult for the company to move on in a different direction with a new hire. The cost of delaying the replacement process is larger for the companies with the worst-performing CEOs, and hence the board of directors in these companies has the greatest incentive to sweeten the deal in order to part ways with the CEO in a quick and amicable fashion.⁸

Third, we find that for the subsample of voluntary departures, leverage does not explain excess separation pay; but for the subsample of forced departures, higher leverage implies higher excess separation pay. This suggests that companies that are most concerned about the potential for bankruptcy, due to poor performance and high debt, are the ones who are highly motivated to make the replacement process go smoothly. Thus they award the departing CEO with a pay package that is above the promised severance.

Fourth, we find that CEOs with non-compete and/or non-solicitation clauses in their contracts are more likely to receive excess separation pay. This is true for both the subsample of CEOs who left voluntarily as well as the subsample of CEOs who were forced out. As the existence of these contractual features suggests that these companies are more susceptible to

⁷ Our result that poorly performing CEOs are being rewarded with larger pay is somewhat reminiscent of the finding in Garvey and Milbourn (2006) who show that CEO's are rewarded for good luck but not penalized for bad luck.

⁸ Further discussion of this hypothesis and additional anecdotal evidence of the ability of CEOs to prolong the separation process is provided by Dalton, Daily, and Kesner (1993).

harmful actions by the departing CEO, the results are in line with the hypothesis that excess separation pay is used to lower the risk of the departing CEO taking future actions that will lower the value of the company.

Fifth, if companies do not have in mind a suitable replacement for the CEO then there will be less of a need to incentivize the incumbent to leave. To test this aspect of the turnover process, we measure whether or not the new incoming CEO is from inside the company and see whether this correlates with excess severance. We find that if the new CEO is an insider, then the amount paid in excess of the contractual severance goes up. This result holds for the subsample of CEOs that are forced out, but not for the subsample of CEOs who leave voluntarily. This is, again, consistent with the hypothesis that excess separation pay is used by the board judiciously at a time when the board forces a CEO out.

Finally, we find some evidence that industry and market-wide conditions also play a role in determining excess separation pay. For example, we find that excess separation pay for voluntary departures is higher when the market is doing well as measured by the level of the market index.⁹ We also find that companies in more concentrated industries offer less excess separation payment. However, this result holds only for the forced subsample and not for the subsample of CEOs that departs voluntarily.

Several theoretical papers offer a rationale for the existence of severance contracts. Kahn (1985) suggests that severance pay is part of an optimal contract in which the worker gets partial

⁹ This result is reminiscent of Eissfeldt and Rampini (2008) who find that executive compensation depends on general market conditions and is procyclical in nature. Thus, CEOs that depart during good business conditions, as measured by the level of the market, may also require a larger severance pay.

insurance for the state in which he leaves the firm. More recently, Almazan and Suarez (2003) argue that severance contracts serve to reduce the incentive of strong boards to replace the CEO too frequently and also serve to reduce the incentive of a CEO working for a weak board to entrench herself. Thus, one interpretation of Almazan and Suarez (2003) is that severance contracts are a commitment mechanism that allows for a smoother process of replacing the CEO, which is what we find empirically. Ju, Leland, and Senbet (2002) and Van Wesep (2008) study the effect of severance contracts on firms' risk taking activity. While Ju, Leland, and Senbet (2002) show that severance agreements can be viewed as put options that induce managers to take more risks, Van Wesep (2008) shows that severance contracts will be awarded when managers are able to take excessive risk in order to hide information about their failed investments. Hence, severance pay provides the incentive to reveal unfavorable information about the firm.

Our study attempts to better understand the motives behind making payments to departing CEOs in excess of the contractual severance amount. Other recent empirical studies attempt to look at related questions. For example, Schwab and Thomas (2004), Zhao (2006), and Gillan, Hartzell and Parrino (2008) study features of CEO employment agreements focusing on whether or not CEOs have an explicit or implicit contract with the firm. While all CEOs with a severance contract will have an explicit employment contract with the firm, not all explicit employment contracts have severance agreements. Lambert and Larcker (1985) study the effect of golden parachutes on firms' M&A activities.

Papers that focus directly on severance pay include: Rusticus (2006), Rau and Xu (2008), Huang (2010), and Yermack (2006). Rusticus (2006) and Rau and Xu (2008) examine the firm level determinants of whether or not a CEO has a severance agreement as part of her contract. Huang (2010) looks at the impact of severance contracts on future firm performance and risk-taking activity of the CEO. Finally, Yermack (2006) studies separation pay levels and notes that some CEOs obtain separation pay even though they do not have severance agreements. In his analysis of separation pay he looks at the subsample of CEOs who are forced out and finds that separation pay levels are impacted by: years to retirement, leverage, and an index for anti-shareholder rights. When looking at the subsample of CEOs who leave voluntarily, he does not find any statistically significant results.

There are two key differences between our study and Yermack (2006). First, we focus on learning about the determinants of the *difference* between promised and contractual severance pay, while Yermack (2006) studies the determinants of the *level* of separation pay, which is most of the time equal to the initial severance contract. Thus, the analysis in Yermack (2006) likely explains why CEOs have severance contracts but does not explain the reasons for observing *excess* severance, which is exactly what we study here. Now, while *excess* separation pay and the *level* of separation pay are positively correlated, we conduct a robustness check and find that controlling for the level of separation pay leaves all of our results unchanged. This is an indication that the factors determining *excess* severance are not the same as those determining severance pay *levels*.

Second, perhaps because the two papers analyze a different dependent variable, our analysis shows that *excess* severance is explained by governance problems in the subsample of CEOs who depart voluntarily, while Yermack (2006) finds no variables which explain the level of separation pay for this subsample. In addition, the two studies find very different results for the sample of CEOs that are forced out. In fact, the *only* similar result in the two papers is that weak external governance increases both separation pay levels and excess severance pay.¹⁰

Overall, our study furthers our understanding of severance contracts, separation payments, and more importantly, the intricate bargaining game played between the CEO and the board upon the CEO's departure.¹¹

The remainder of the paper is organized as follows. In section I, we provide institutional background on CEO severance agreements as well as on their reported separation agreements. In section II, we describe the sample selection process, data and research design. The analysis is presented in section III. Finally, in section IV we conclude.

I. CEO Severance and Separation Agreements

A severance agreement is a contractual agreement between the CEO and the company which specifies the executive's benefits and obligations in the event that the executive leaves her

¹⁰ Specifically, Yermack (2006) finds that expected years to retirement increase the *level* of separation pay while we find that CEO tenure with the firm (probably negatively correlated with his measure) either has no effect on *excess* severance or might increase it. Yermack (2006) finds that high leverage lowers the *level* of severance pay while we show that leverage increases *excess* severance.

¹¹ In this sense, our paper also relates to Hanka (1998), Klasa et. al. (2009), and Matsa (2010), who show how corporate debt, cash holdings, and capital structure influence contract renegotiations at the firm.

position with the company.¹² Not all CEOs have severance contracts. In our sample, for example, we find that around 13% of CEOs have an effective severance contract in place at the time of their departure. In many cases, however, (around 33% of our sample) CEOs do receive severance pay even though they do not have a severance agreement. Whenever a CEO has a severance agreement, we find that it is signed an average of 6 years before the CEO ends up leaving the company.¹³

The separation agreement, which is signed within one year of the CEO turnover event, is a contract between the executive and the company that is signed during the separation process. Namely, it is part of the negotiation process that takes place right before the company and the CEO agree to part ways. Some departing CEOs, whether or not they have a severance contract in place, sign a separation agreement. In our sample, 287 of the 609 events have separation agreements.

Schwab and Thomas (2004) provide a summary of discussions with legal practitioners who are actively engaged in CEO employment/separation agreement negotiations. Based on their description, companies normally produce the initial drafts of employment agreements, many of which contain severance compensation. A standard severance contract contains specific payment amounts, such as a payment of multiple times the CEO's base salary and bonus, as well

¹² Note that we exclude all CEO departures that are related to change in control following a merger or a takeover. Thus, we exclude all golden parachute contracts.

¹³ In many cases contracts are renewed with unchanged severance agreements. This number represents the number of years since a severance contract with the existing features was last signed.

as continuing/immediate vesting of existing executive stocks and options. In return, CEOs usually agree not to compete with the company for a period of one to two years.

In order for the CEO to receive the promised severance amount, the termination event has to be either without “for cause” or due to “good reason”. The term “for cause” is specifically defined in the contract, and usually includes conditions such as willful misconduct or breach of fiduciary duties. However, the definition of “for cause” in the agreements does not normally include CEO incompetence or poor firm performance. Hence, based on these severance agreements, CEOs can still obtain the pre-specified severance amount in the event of termination due to poor firm performance. Similarly, “good reason” is narrowly defined in severance agreements. Examples of “good reason” include: involuntarily relocating CEOs or decreasing their base salary. Schwab and Thomas (2004) offer further detailed descriptions of CEO employment agreements from a legal perspective.

According to SEC regulations, companies are required to file severance and separation agreements with executives in their financial statements. Companies usually file the agreements as an attachment to the 10-K, 10-Q or 8-K. In addition, the proxy statement contains a brief summary of the principle terms of the severance and the separation contracts. We obtain the terms of severance agreements (ex-ante contracts) from 10-K, 10-Q, 8-K and proxy statements; the terms of separation agreements (ex-post contracts) are obtained from proxy statements by looking at agreement summaries.

Appendix 1 provides an example of a severance and a separation agreement summary obtained from a proxy statement.¹⁴ In this example we obtain information about the severance contract that was signed between Sovereign Bank and Mr. Sidhu. As indicated in Appendix 1, Sovereign Bank and Mr. Sidhu signed an employment contract in 1997 stating, among other things, the details of his severance contract. This severance includes things such as multiple times of salary and bonus, continued coverage of health benefits and gross tax payments by the company. The Appendix also details his actual separation pay following his dismissal in 2006.

II. Data Description

The analyses in this paper utilize two types of data. The main dataset consists of hand-collected information regarding the contractual (severance contract) and the actual (separation contract) payments made to CEO following her termination. We collect information for every CEO who left their position with an S&P500 company during the time period between 1993 and 2007. This sample is restricted to those firms with information on CRSP, Compustat, RiskMetrics, Thomson Reuters and ExecuComp.

In total we identify 609 events that meet these criteria. For each of these 609 events we read the 10-K, 10-Q, 8-K, and proxy statements and hand-collect details of any existing severance agreement as well as any separation agreement signed by the company and the CEO

¹⁴ In the example we present only the severance and separation agreement summary obtained from a proxy statement due to the length of the actual severance and separation contracts. In the analysis of the paper we read through the full contract to obtain all relevant details.

upon her leaving her position. We locate the severance and separation contracts by searching for such terms as “employment agreement”, “severance contract”, “severance agreement”, “separation agreement”, “termination of employment”, “severance”, “separation”, “contract”, “agreement”, “executive agreement”, “employee agreement”, and “termination arrangement”.¹⁵ We require that the severance contract is in place at least one year prior to the turnover event.¹⁶ For each severance contract, we record the terms of the agreement, such as one-time severance amount, multiples of salary and bonus, future consulting fees, immediate vesting of restricted shares and options, additional pension benefits, contract duration, reasons that can trigger the contracts to be effective, non-compete and/or non-solicit clauses, health care and life insurance benefits, gross tax payment, legal fees, access to private jet, office and secretarial supports.

For the separation agreement, which is signed within a year of the departure date, we collect similar information about the specific actual payments that will be made to the departing CEO. This separation agreement may be exactly the same as the previous severance contract or may be different.

For each CEO we calculate the dollar difference between the amounts paid to the CEO upon departure and the amounts that the severance contract specifies should have been paid to the CEO. We obtain the severance contractual dollar amount directly from the severance contract

¹⁵ In this paper, we specifically do not study change-in-control agreements which are agreements that become effective only when a “change-in-control” event occurs.

¹⁶ In a few cases new severance agreements were signed right before a departure. We ignore these contracts and record the details of the severance contract prior to that. This is because these new severance contracts appear to be written in order to justify ex-post what the board was planning to award the departing CEO.

if supplied by the firm; otherwise, we calculate the contractual dollar amount by employing the most recent year of CEO compensation data if the contractual terms involve certain multiples of salary and bonus. For instance, if the contract awards the CEO with five times her salary and bonus, then we obtain the dollar amount by multiplying the CEO's most recent year's salary and bonus by five. In addition, if the severance contract contains terms for immediate vesting of restricted options, we estimate the amount by using un-exercised un-exercisable option values, which is the estimation of the intrinsic value of the un-exercisable options at year end; and for restricted shares, we estimated it with unvested stock values.

As for the actual separation pay amount, we obtain this actual separation dollar amount directly from the separation contract, if provided by the company; otherwise, if a separation contract is absent, we search the proxy statement for any additional "good-bye" payment that the firm gave the CEO (usually the company specifies in the proxy statement when some additional payments have been made to the CEO as a "good-bye" bonus). Whenever a departing CEO is able to negotiate to have some or all of their unvested restricted stocks and options fully or partially vested, we obtain the estimated value of such stock and option grants from the separation agreement directly (if provided in the proxy statement); or else, we estimate the amount by using un-exercised un-exercisable option values and unvested stock values. Also, if the CEO stays with the firm as a chairman or consultant and receives a compensation that is the same or higher than the compensation she received as a CEO, we include that amount as well.

When calculating the dollar difference between the severance and separation amounts, we also consider the CEO's pension plan. For example, when the severance contract makes no mention of the CEO's pension, but later in the separation agreement, the firm allows for additional years of service credited toward the CEO's pension plan, then we obtain the present value of such additional benefits from searching the firm's proxy statement.

For both of our severance and separation dollar amount calculations, we do not include the gross tax payment, health insurance costs, legal fees, and fringe benefits, such as access to private jet, office and secretarial supports, due to the difficulty of valuing these benefits.

Finally, for each event we follow the methodology used in Parrino (1997) and classify whether the turnover event is a forced turnover or a voluntary turnover. We supplement the data with financial information about the company and the CEO from CRSP, Compustat, RiskMetrics, Thomson Reuters, and ExecuComp.

In Table I, we report the definition of variables used in the analyses. In Table II, we provide descriptive statistics on contract, company and CEO characteristics. For the full sample of 609 CEOs, we see that the average contractual severance payment for those 81 CEOs with a severance contract was 9.15 million dollars. In contrast, the actual amount specified in the final separation contract for those 287 CEOs that received a non-zero payment was 9.5 million dollars. The difference between the actual and promised pay for the full sample of 609 CEOs is, on average, 3.26 million dollars.

Out of the 609 CEOs, 287 received payment at departure while only 81 of the CEOs had explicit severance contracts prior to departing. Thus, separation pay is given many times even though the company is not required to provide any severance payment to the CEO. Whenever the CEO does have a severance contract, we observe that it is signed, on average, more than six years prior to termination.

The average tenure of the CEO (either as CEO or as an employee) at the time of departure is 24.79 years. Founder CEOs represent less than 10% of the sample, totaling 52. Out of the sample of 609, we are able to identify 112 CEOs (about 18%) who are forced out. This number is slightly lower than the 24% reported in Yermack (2006), but higher than the 12% reported in Parrino (1997). Our sample of CEOs tends to own around 3.66% of the firm's equity, which is close to the 3.7% reported in Griffith (1999). About 72% of the CEOs stay with the firm as chairman of the board after resigning from their position as CEO.

An average of 72% of board members for our sample companies are classified as independent.. This percentage is similar to the number reported in Sundaram and Yermack (2007), who found that 79.2% of directors are independent. As for the stock return prior to departure we see that the average abnormal return for the full sample is positive, again suggesting that we have many voluntary departures of CEOs whose wealth has recently gone up.

In Table II, we also separate out the sample into two subsamples according to whether or not the CEO ended up with an exit package that was larger than their severance agreement. Out of 609 observations, 246 CEOs had a difference in pay at the time of departure, with an average

difference in pay totaling more than 8 million dollars. In contrast, 363 CEOs received a separation pay that was in accordance with their severance contract. As can be seen from the table, there appear to be several differences between the two subsamples. For example, CEOs with excess severance appear more likely to have been founders and to stay at the firm after stepping down. These CEOs also tend to have non-compete and non-solicit clauses in their contracts and work for companies that have weaker internal governance. Finally, they appear to leave their positions during times when the market is doing well.

In Table III, we report some additional contract values when separating the sample based on whether or not the CEO left the firm voluntarily or whether she was forced out of her office. As will be seen shortly, this division of the data will be most informative about the reasons for excess severance. The first thing to notice is that the CEOs who were forced out are about equally likely to receive excess severance as those CEOs that leave voluntarily. Also, conditional on receiving excess severance, fired CEOs tend to get much more in excess severance than CEOs that depart voluntarily. For example, for the subsample of CEOs who had an initial severance agreement and were eventually forced out, the mean difference between actual and contractual pay is almost 17 million dollars. For CEOs that departed voluntarily, the mean difference is 7 million on average. Moreover, among those CEOs who receive excess separation pay, the excess amount is, on average, 2.4 times the CEOs' total annual compensation.

III. Results

Excess severance pay may be explained by different factors in the forced and voluntary subsamples. Thus, we conduct the multivariate analysis separately for these two groups. We start by defining the dependent variable as the *dollar value of the difference between the actual and contractual separation pay*, where the contractual pay is the pay that was specified in the severance agreement. We then regress this variable on several company, CEO, and market level variables. Because the dependent variable is zero for many of the observations and positive for others, we employ the Tobit model for the analyses. All CEO and firm characteristics are taken in the year prior to the CEO leaving her position.

The independent variables are chosen to measure the two alternative motives that firms have when awarding the CEO with an exit package. These variables measure the governance of the firm, the potential benefit to the firm from replacing the CEO, the extent to which the CEO has the ability to harm the firm after departing, and the economic conditions in the market at the time of CEO departure. Table IV provides summary statistics for these variables for the forced sample (Panel A) and for the voluntary sample (Panel B). In Tables VII and VIII, we provide the correlation matrix for the various independent variables for the two subsamples, respectively.

Table IV illustrates the univariate differences between CEOs with and without excess severance. While there are some differences between the CEOs with excess severance and the CEOs without excess severance, it is important to note that the univariate analysis conducted in the Table does not account for the excess amount being paid. Hence, the results should be taken as merely suggestive.

The main finding from Panel A of Table IV is that, for the subsample of executives that were forced out, excess severance pay is more likely to be offered to CEOs that have done particularly badly in the past three years and for those with non-compete or non-solicit clauses in their contract. For this subsample governance measures do not matter. Panel B of Table IV suggests that past performance does not explain excess severance for the subsample of executives who left voluntarily, while some measures of governance seem to matter. As is the case for the forced sample, here too non-compete and non-solicit clauses are associated with higher excess severance pay. In both panels, excess severance pay is more likely to happen when overall market conditions are good.

The results from the Tobit regressions are provided in Table V for the sample of CEOs that were forced out and in Table VI for the sample of CEOs who left voluntarily. From Model 1 of Table V, we see that the lower the stock return prior to the dismissal event, the higher the excess severance. This result implies that excess severance is given to those CEOs who have done the most damage to the firm. This may seem counterintuitive at first. Our interpretation of the result is that the worst CEOs are the ones who the firm needs to get rid of the quickest. Thus, as long as the incumbent CEO has an ability to delay their departure (via such actions as law suits or derailing the hiring and search process for the new CEO), then we would expect the board to provide them with additional incentives to leave the firm. The second result, from Model 1 and Model 2, is that governance measures do not matter in the sample of executives that are forced out. Namely, excess severance does not seem to be explained by the poor internal or external governance of the firm.

Models 3 and 4 of Table V indicate that existence of non-compete or non-solicit clauses in the CEOs' contracts are also correlated with excess severance. In particular, the existence of either of these clauses implies a larger amount of excess severance. The intuition for this result is that non-solicit or non-compete clauses will only be put in the contract when the company fears that the CEO can harm the firm by leaving it and going to competitors. Hence, these are also the situations where ex-post, the board wants to make sure that the departing CEO is (relatively) happy by giving her additional severance.

In Models 5, 6, 7 and 8 of Table V we control for whether or not the incoming CEO is from outside the company. The idea is that if the board already has a candidate from inside the firm, it will be important to have a quick transition.¹⁷ We find a negative coefficient consistent with the above argument. In Models 6, 7, and 8 of the table we include a measure of industry competition. The results show that CEOs that are forced out receive more excess pay in less concentrated industries. The intuition here is that in less concentrated industries there are more outside options for a replacement CEO, which means that the company will have a greater incentive to replace the incumbent without delay. This is somewhat similar to Parrino's (1997) argument, which states that CEO termination is more likely in industries that have many similar companies.

Finally, in all specifications, we find leverage to be positively correlated with excess severance. This is consistent with the idea that more levered firms are at a higher risk of

¹⁷ Parrino (1997) provides a comprehensive analysis of the choice between hiring the new CEO from within the firm or from the outside.

bankruptcy, given their poor performance in the past, and hence are in great need of a quick turnaround to recovery. This increases the pressure on the board to ensure a smooth replacement process.

The results for the subsample of CEOs who leave voluntarily are given in Table VI. These results are very different than those obtained in the analysis of the sample of executives who were forced out. In Models 1, 2, 3, and 4 of Table VI we find that past returns do not explain excess severance. Therefore, for the voluntary subsample it does not appear that severance is used as a tool to hasten the departure of the CEO. In addition, these models indicate that governance plays an important role. A less independent board tends to award the departing CEO with larger excess severance. A founder CEO is likely to receive larger excess severance. However, companies with weaker external governance (as measured by the G-index) tend to award lower excess severance. The fact that weaker external governance is associated with lower excess pay is consistent with the argument made in Yermack (2006), who suggests that “a company at a low risk of takeover may feel a diminished need to use severance pay to deter ex-CEO from participating in a hostile raid”.

Models 5 and 6 show that the existence of non-compete or non-solicit clauses increases the likelihood of getting higher excess pay (as was the case for the forced-out subsample). This is consistent with the idea that firms are willing to pay extra good-bye payment to ensure departing CEOs will not compete against the firm in the future. Model 7 looks at the additional factor of whether the new CEO is hired from outside the firm and finds no statistical impact on excess

severance. This is consistent with our argument that excess severance in this subsample is not related to the turnover process. Namely, for voluntary CEO departures the board does not need to offer further incentive for the CEO to leave, even when they have a suitable (internal) candidate waiting.

Model 8 shows that industry competition does not impact the amount of excess severance. Model 9 shows that all our main results continue to hold, even after controlling for CEOs staying as either a chairman or a consultant after stepping down from the CEO position. Model 10 indicates that CEOs departing during periods where the market is doing well (as measured by the level of the S&P500 index) tend to receive higher excess exit packages. If shareholders engage in less monitoring during periods when the economy is doing well, then the CEO will be able to extract more rents from a friendly board. This result is consistent with Eisfeldt and Rampini (2008), who show that executives tend to obtain higher compensation when the market is doing well.

Finally, we see that for the voluntary departure sample, leverage does not explain excess severance. This again is consistent with the argument that the importance of replacing the CEO to avoid the costs of financial distress is critical in the cases when the CEO is forced out and not in those where the CEO leaves for other reasons.

A. Robustness

In order to ensure the robustness of our results, we conduct several additional tests. These tests are reported in Table IX for the sample of CEOs who were forced out and in Table X for the sample of CEOs who left voluntarily.

In Models 1 and 2 of both tables we include alternative measures of the governance of the company. In Model 1 we measure how busy the independent directors of the board are (see Peyer and Perry (2005), Fich and Shivdasani (2006)). We define the variable of “Busy Board” as the percentage of independent directors who sit on three or more boards. The results indicate that for the forced sample this measure does not explain excess severance, but for the voluntary sample it does. Essentially, for voluntary turnover CEOs, the busier the board, the higher the excess severance awarded to the departing CEO. In Model 2 of the two tables, we control for the shares owned by active large shareholders. Similar to Almazan, Hartzell and Starks (2005), we define the institutions that are active monitors as investment advisors and investment companies. We then compute the percentage of the firm’s total shares outstanding that are held by these shareholders. The results indicate that higher ownership by active institutions lowers excess severance payments in the sample of voluntary departures, but not in the sample of forced departures, again consistent with our main results in the paper. Models 3 and 4 repeat the analysis with additional control variables. In Model 5 of Table IX we control for the level of separation payment studied in Yermack (2006). The model shows that the results remain unchanged (although one variable loses significance), which highlights the point that our measure of interest (*excess severance*) is not the same as severance *level* and is not determined by the same factors.

Finally, in table IX, Models 6 to 10, and table X, Models 5 to 8, we repeat the multivariate analysis with a scaled dependent variable that measures the excess severance paid divided by the total salary of the departing CEO. We find that the results remain the same using this specification.

IV. Conclusion

In this paper we document the phenomenon that CEO exit packages are sometimes larger than what is contractually specified in their severance agreement. Our analysis of the dollar difference in actual versus contractual exit pay shows that the cross section of this difference can not only be explained by weak internal corporate governance, but also by boards acting in the interest of shareholders. In particular, we find that weak corporate governance explains the existence of excess severance pay for the subsample of CEOs who depart voluntarily. In contrast, excess severance pay is not related to weak governance in those events where the CEO is forced out. For these forced-out CEOs, excess pay is given in order to assure that the company moves forward in a way that is most beneficial to the shareholders.

The results overall indicate that severance pay and excess severance pay, while seemingly reflecting poor governance, may actually play a critical role in the efficient replacement process of poorly-performing CEOs. This aspect of executive compensation, which

has received limited attention to date, can provide interesting details about how the board and the CEO interact.

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Appendix 1: Sidhu and Sovereign Bank Severance and Separation Agreements

Ex-ante severance agreement:

Sovereign Bank entered into an employment agreement, dated March 1, 1997, with Jay S. Sidhu, which superseded, in its entirety, Mr. Sidhu's then existing employment agreement. Mr. Sidhu's agreement has an initial term of five years and, unless terminated as set forth therein, is automatically extended annually to provide a new term of five years except that, at certain times, notice of nonextension may be given, in which case the agreement will expire at the end of its then-current term. No such notice has been given.

The agreement provides a base salary, which, if increased by action of the Board, becomes the new base salary provided thereafter by the agreement. In addition, the agreement provides, among other things, a right to participate in any bonus plan approved by the Board and insurance, vacation, pension and other fringe benefits for Mr. Sidhu.

If Mr. Sidhu's employment is terminated without cause (as defined therein), or if Mr. Sidhu voluntarily terminates employment for good reason (as defined therein), Mr. Sidhu becomes entitled to severance benefits under the agreement. The term good reason includes the assignment of duties and responsibilities inconsistent with Mr. Sidhu's status as President and Chief Executive Officer of Sovereign, a reduction in salary or benefits or a reassignment which requires Mr. Sidhu to move his principal residence more than 100 miles from Sovereign's principal executive office. If any such termination occurs, Mr. Sidhu will be paid an amount equal to five times the sum of (i) his highest annual base salary under the agreement, and (ii) the average of his annual bonuses with respect to the three calendar years immediately preceding his termination. Such amount will be payable in sixty equal monthly installments. In addition, in the event of such termination, Mr. Sidhu will be entitled to continuation of certain insurance and other specified benefits for sixty months or until he secures substantially similar benefits through other employment, whichever shall first occur. Further, Mr. Sidhu will be entitled to additional retirement benefits to which he would have been entitled had his employment continued through the then remaining term of the agreement, including increased benefits under Sovereign's long-term incentive plans. If the payments and benefits under the agreement, when aggregated with other amounts received from Sovereign and Sovereign Bank, are such that Mr. Sidhu becomes subject to excise tax on excess parachute payments under Code Sections 4999 and 280G he will receive additional payments equal to such excise tax and any incremental income taxes he may be required to pay by reason of the receipt of additional amounts under the agreement. Sovereign estimates that, if Mr. Sidhu had terminated employment as of August 1, 2006 under circumstances entitling him to the above-described severance benefits, he would have been entitled to receive approximately \$13 million, exclusive of the non-cash benefits, additional retirement benefits, and any potential excise tax-related payments.

If Mr. Sidhu's employment terminates by reason of his disability, he will be entitled to continuation of 80% of the annual base salary and bonus described above, less amounts payable under any disability plan of Sovereign, until the earliest of (i) his return to employment, (ii) his attainment of age 65, or (iii) his death. Provision is also made generally for the continuation of insurance and other specified benefits for such period, as well as additional credits for retirement benefit purposes.

The agreement contains provisions restricting Mr. Sidhu's right to compete with Sovereign and Sovereign Bank during the period he is receiving severance or disability benefits thereunder, except under certain circumstances.

Ex-post separation agreement:

On October 10, 2006, we entered into a Retirement-Resignation and Transition Agreement with Jay S. Sidhu, our former President, Chairman, and Chief Executive Officer and the former Chairman and Chief Executive Officer of Sovereign Bank, in connection with Mr. Sidhu's resignation and retirement. The resignation and retirement came in the face of our threatened termination of Mr. Sidhu's employment without cause and, therefore, we viewed the termination as an exercise by Mr. Sidhu of his right to resign for good reason under the terms of his employment agreement. The Retirement-Resignation and Transition Agreement provided, among other things, that:

- Mr. Sidhu resigned as President and Chief Executive Officer of Sovereign and Sovereign Bank effective on October 10, 2006.
- Mr. Sidhu continued to serve as Chairman, with Board-related responsibilities, and as a director of Sovereign and Sovereign Bank through December 31, 2006; and
- Mr. Sidhu will provide consulting services as special advisor to our Board for three years from October 10, 2006.

Under the Retirement-Resignation and Transition Agreement, we have agreed to honor Mr. Sidhu's employment agreement and Mr. Sidhu received or will receive:

- a lump-sum cash payment of approximately \$10.5 million, representing the present value of payments due under his employment agreement;
- continuation, for 60 months from October 10, 2006, of life, disability, and medical insurance, also due under his employment agreement; and
- a lump-sum payment of \$22,448,671 in cash, which represents the present value of amounts earned by and due to him under the terms of the Enhanced Retirement Plan and the Supplemental Retirement Plan. In 2006, we paid the amounts under the plans that vested before January 1, 2005 (approximately \$3.4 million) and we will pay the balance in April 2007.

In addition, consistent with past practice with respect to senior executive officers who have resigned and retired, we **accelerated, as of October 10, 2006, the vesting of equity awards made as part of Mr. Sidhu's annual compensation package from 2003 through February 2006, which equity awards would have otherwise terminated. These awards have a net value to Mr. Sidhu of about \$9.0 million based on a price of \$24.00 per share for our common stock of which Mr. Sidhu recognized approximately \$6.3 million as income in 2006 due to restricted stock and performance unit vesting. Mr. Sidhu will generally have the lesser of 24 months from the effective date of his resignation or the grants' original expiration date to exercise outstanding stock options. In addition, we made Mr. Sidhu a one-time special payment of \$1.0 million. We approved the one-time special payment and the acceleration of the vesting of the equity awards in consideration for Mr. Sidhu's resignation from the Board and the boards of Sovereign Bank and Santander on December 31, 2006, an accord and satisfaction of his employment agreement, delivery of a release of claims, and for a number of other concessions and accommodations.**

Mr. Sidhu will also receive payments of \$40,000 per month for 36 months for providing the consulting services described above. Mr. Sidhu is not entitled to any perquisites in connection with providing the consulting services or otherwise under the Retirement-Resignation and Transition Agreement. Mr. Sidhu also received fees totaling \$36,000 for service as a non-employee director of Sovereign and Sovereign Bank through December 31, 2006. Mr. Sidhu also participated in our deferred compensation plans, including our Retirement Plan, which is applicable to all of our team members, and our Bonus Recognition and Retention Program, which is applicable to certain of our senior executive officers. Under these plans, Mr. Sidhu is entitled to his earned and vested account balances which will be paid in accordance with the terms of such plans. Under the Retirement-Resignation and Transition Agreement, Mr. Sidhu forfeited approximately \$640,000 in value of certain existing unvested restricted stock awards, based on a \$24.00 stock price.

Table I: Variable Definitions

Variable	Definition
# of CEO with a severance contract at time of departure	Total number of CEOs with active severance agreements at the time of turnover and the CEOs are eligible for severance payments
% of independent directors	Percentage of independent directors on the board
3 YR Market-adjusted return	The return on the firm's stock, adjusted using the CRSP value-weighted index over the three year proceeding the CEO turnover event date
Actual-Contractual pay (Mill\$)	Dollar differences between what CEOs are promised to receive and what they actually obtain
Actual pay (Mill\$)	Separation payments are amounts CEOs actually received
Assets	Book value of total assets at the end of the fiscal year ending immediately before the CEO turnover event
Contractual pay (Mill\$)	The amount specified in the severance contract that a CEO is entitled to and we only consider contracts that are signed at least one year prior to the departure event
CEO ownership	Percentage of the firm's common stock beneficially owned by the CEO as of the CEO turnover event
CEO tenure	Number of years CEOs stay with the firm
CEO with non-compete clause (=1)	Has an indicator of 1 if the CEO has non-compete clause in the separation agreement and 0 otherwise
CEO with non-solicit clause (=1)	Has an indicator of 1 if the CEO has non-solicit clause in the separation agreement and 0 otherwise
Excess severance to Total compensation (%)	(Actual-contractual pay)/CEO's last year total compensation
Existence of severance contract	Has an indicator of 1 if the CEO and the firm has a severance agreement at least one year before the CEO turnover event and 0 otherwise
Family Firm	Has an indicator of 1 if the firm is a family firm and 0 otherwise
Forced	Has an indicator of 1 if the CEO is forced out of the firm and 0 otherwise
Founder	Has an indicator of 1 if the CEO is the founder or co-founder of the firm and 0 otherwise
HHI (%)	Herfindahl Index for that firm's two-digit SIC industry. This index is computed as the sum of the squares of the market shares of the firms in the industry, where market share is defined as firm sales divided by total industry sales.
Leverage	Long term and short term debt to market value of equity
Next CEO from outside (=1)	Has an indicator of 1 If the following new CEO is hired from outside and has not been with the firm for more than 1 year and 0 otherwise
S&P index level	The level of the Standard & Poor's 500 Composite Index
Severance contract duration (yr)	Average term of severance agreements, if exist
Stay at the firm after step down (=1)	Has an indicator of 1 if the CEO stays at the firm after stepping down the CEO position and 0 otherwise

Table II: Descriptive Statistics

This table provides descriptive statistics for the sample of 609 S&P500 CEOs who left their position as CEO between the year 1993 and 2007. The table describes contract, CEO, and company characteristics for all 609 events. The statistics are provided for the whole sample as well as for the subsamples of turnover events in which the CEO received (did not receive) severance pay in excess of their contractual severance. Variable definitions are given in Table 1. CEO and firm characteristics are from the year of CEOs turnover events. The notation of *, **, *** denotes significance at the 10%, 5% and 1% level respectively.

	Total sample (609)		CEO w/o a difference in exit package (363)		CEO with a difference in exit package (246)		t-value
	Mean	STD	Mean	STD	Mean	STD	
Panel A: Contract characteristics							
Actual-Contractual pay (Mill\$)	3.26 (N=609)	9.69	0 (N=363)	0.00	8.08 (N=246)	13.93	
# of CEO with a separation contract at time of departure	287		41		246		
# of CEO with a severance contract at time of departure	81		41		40		
Actual pay (Mill\$)	9.50 (N=287)	16.67	9.11 (N=41)	11.98	9.57 (N=246)	17.34	
Contractual pay (Mill\$)	9.15 (N=81)	16.16	9.11(N=41)	11.98	9.19 (N=40)	19.72	
Severance contract duration (yr)	6.23 (N=61)	4.15	5.46 (N=30)	2.91	6.98 (N=31)	5.01	
Panel B: CEO characteristics							
Founder (N)	52	0.28	23	0.24	29	0.32	-2.25 **
CEO tenure	24.79	10.82	24.92	10.95	24.60	10.65	0.36
CEO ownership	3.66	6.64	3.51	6.56	3.89	6.76	-0.70
Stay at the firm after step down (=1)	0.72	0.45	0.65	0.48	0.83	0.38	-5.02 ***
Forced (N)	112	0.39	65	0.38	47	0.39	-0.37
CEO with non-compete clause (=1)	0.082	0.275	0.039	0.193	0.146	0.354	-4.36 ***
CEO with non-solicit clause (=1)	0.077	0.267	0.036	0.186	0.138	0.346	-4.25 ***
Panel C: Firm characteristics							
% of independent directors	0.72	0.14	0.73	0.13	0.71	0.15	1.33
G-index	9.57	2.48	9.74	2.44	9.33	2.54	1.96 *
Next CEO from outside (=1)	0.22	0.41	0.21	0.41	0.23	0.42	-0.45
3 YR Market-adjusted return	0.10	28.56	1.53	29.72	-2.01	26.69	1.53
HHI	0.02	0.01	0.02	0.01	0.01	0.01	0.78
S&P index level	1094	291	1060	309	1145	253	-3.74 ***

Table III: Agreement Characteristics for Voluntary vs. Forced Turnover

This table provides the dollar value of the actual and contractual severance pay amounts for the sample of 609 S&P500 CEOs who departed their company between the years 1993 and 2007. The left column shows actual and contractual exit pay for 363 CEOs who do not receive excess severance pay while the right column shows both the actual and contractual exit payments for 246 CEOs who receive excess severance. All variable definitions are given in Table 1.

	CEO w/o a difference in exit package (363)	CEO with a difference in exit package (246)
Voluntary		
CEOs w/o severance contract		
Actual payment mean	0	7,379,558
Excess severance to Total compensation (%)		224
N	278	176
CEOs with severance contract		
Actual payment mean	9,780,126	12,612,653
Contractual payment mean	9,780,126	4,794,750
Actual-Contractual payment mean	0	7,817,904
Excess severance to Total compensation (%)		73
N	20	23
Forced		
CEOs w/o severance contract		
Actual payment mean	0	6,937,700
Excess severance to Total compensation (%)		160
N	44	30
CEOs with severance contract		
Actual payment mean	8,477,588	32,853,819
Contractual payment mean	8,477,588	15,137,017
Actual-Contractual payment mean	0	17,716,802
Excess severance to Total compensation (%)		811
N	21	17

Table IV: Summary Statistics for Forced vs. Voluntary Turnover CEOs

Descriptive statistics for a sample of 609 S&P500 CEOs who left their position as CEO between year 1993 and 2007. Left panel shows contract, CEO and firm characteristics for a subset of CEOs whose actual pay upon departure was the same as their contractual exit package. Right panel shows contract, CEO and firm characteristics for a sub-sample of CEOs with a difference in pay between actual and contractual exit packages. The variables are defined in table 1. CEO and firm characteristics are from the year of CEOs turnover events. The notation of *, **, *** denotes significance at the 10%, 5% and 1% level respectively.

	CEO w/o a difference in exit package (363)		CEO with a difference in exit package (246)		
	Mean	STD	Mean	STD	t-value
Panel A: Forced					
3 YR Market-adjusted return	-5.09	27.48	-18.13	16.31	3.14 ***
% of independent directors	0.75	0.13	0.73	0.17	0.68
G-index	9.63	2.59	9.42	2.62	0.42
Next CEO from outside (=1)	0.43	0.50	0.38	0.49	0.50
HHI	0.02	0.02	0.01	0.01	0.91
CEO with non-compete clause (=1)	0.09	0.29	0.30	0.46	-2.69 ***
CEO with non-solicit clause (=1)	0.06	0.24	0.30	0.46	-3.20 ***
CEO Tenure	19.61	9.51	21.16	9.12	-0.87
Existence of severance agreement (=1)	0.32	0.47	0.36	0.49	-0.42
S&P index level	1133.03	266.24	1222.17	220.35	-1.93 *
N	65.00		47.00		
Panel B: Voluntary					
3 YR Market-adjusted return	2.97	30.03	1.80	27.26	0.45
% of independent directors	0.72	0.13	0.71	0.14	1.18
Founder (=1)	0.07	0.26	0.14	0.34	-2.16 **
G-index	9.76	2.41	9.31	2.53	1.97 **
Next CEO from outside (=1)	0.16	0.37	0.19	0.39	-0.75
HHI	0.02	0.01	0.02	0.01	0.46
Stay at the firm after step down (=1)	0.67	0.47	0.86	0.35	-5.03 ***
CEO with non-compete clause (=1)	0.03	0.16	0.11	0.31	-3.46 ***
CEO with non-solicit clause (=1)	0.03	0.17	0.10	0.30	-2.98 ***
CEO Tenure	26.08	10.91	25.41	10.85	0.67
Existence of severance agreement (=1)	0.07	0.25	0.12	0.32	-1.80 *
S&P index level	1043.72	315.36	1127.08	257.84	-3.23 ***
N	298.00		199.00		

Table V: Tobit Models Predicting Differences between Actual and Contractual Payments for Forced Turnover CEOs

The sample includes 112 CEOs between year 1993 and 2007. The dependent variable is a difference between actual and contractual exit packages (in million dollars). The variables are defined in table 1. CEO and firm characteristics are from the year of CEOs turnover events. (t-statistics in parentheses). The symbols *, **, *** denote significance at the 10%, 5% and 1% level respectively.

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7	Model 8
Constant	-19.6548 (-1.20)	-19.8673 (-1.21)	-17.8172 (-1.12)	-17.8984 (-1.11)	-14.3198 (-0.89)	-13.4335 (-0.74)	-15.7593 (-0.88)	-15.5503 (-0.87)
<u>Firm characteristics</u>								
3 YR Market-adjusted return	-0.2479 ** (-2.55)	-0.2498 ** (-2.55)	-0.2478 ** (-2.55)	-0.2406 ** (-2.47)	-0.2683 *** (-2.71)	-0.2562 *** (-2.71)	-0.2423 ** (-2.57)	-0.2336 ** (-2.46)
% of independent directors		-8.9739 (-0.76)	-5.8746 (-0.51)	-5.5075 (-0.47)	-5.2677 (-0.46)	-4.4934 (-0.41)	-2.0695 (-0.19)	-2.2082 (-0.21)
G-index	-0.5467 (-0.77)							
Next CEO from outside (=1)					-6.0382 (-1.63)	-5.5534 (-1.58)	-5.8308 * (-1.70)	-5.8528 * (-1.72)
HHI (%)						-4.4089 ** (-2.01)	-4.8581 ** (-2.24)	-4.7223 ** (-2.18)
CEO tenure							0.3084 (1.63)	0.3226 * (1.70)
<u>Contract characteristics</u>								
CEO with non-compete clause (=1)				11.1947 ** (2.55)	11.7427 *** (2.70)	10.6287 *** (2.60)	11.3775 *** (2.81)	10.9839 *** (2.69)
CEO with non-solicit clause (=1)			14.1022 *** (3.17)					
Existence of severance agreement (=1)								1.8901 (0.53)
<u>Business cycle</u>								
S&P index level (000)						8.5948 (1.13)	7.7816 (1.05)	7.4188 (1.00)
<u>Control variables</u>								
Log of Assets	1.2195 (0.77)	1.3887 (0.86)	0.6151 (0.39)	0.6411 (0.40)	0.4651 (0.29)	-0.0915 (-0.06)	-0.5594 (-0.36)	-0.6146 (-0.40)
Leverage	7.7953 *** (6.77)	7.8028 *** (6.77)	8.4470 *** (7.49)	8.3523 *** (7.27)	8.2884 *** (7.34)	8.5978 *** (7.98)	9.0667 *** (8.23)	9.0444 *** (8.26)
Total observation	112	112	112	112	112	112	112	112
Log likelihood	-231	-231	-226	-228	-226	-223	-222	-222

Table VI: Tobit Models Predicting Differences between Actual and Contractual Payments for Voluntary Turnover CEOs

The sample includes 497 CEOs between year 1993 and 2007. The dependent variable is a difference between actual and contractual exit packages (in million dollars). The variables are defined in table 1. CEO and firm characteristics are from the year of CEOs turnover events. (t-statistics in parentheses). The symbols *, **, *** denote significance at the 10%, 5% and 1% level respectively.

	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7	Model 8	Model 9	Model 10
Constant	-2.1061 (-0.37)	-2.9487 (-0.51)	-12.4624 ** (-2.56)	-6.1137 (-1.06)	-5.6749 (-0.98)	-4.9780 (-0.86)	-4.8892 (-0.84)	-6.1030 (-1.01)	-12.3402 ** (-2.00)	-16.5645 ** (-2.49)
<u>Firm characteristics</u>										
3 YR Market-adjusted return	0.0061 (0.23)	-0.0003 (-0.01)	-0.0005 (-0.02)	-0.0057 (-0.21)	-0.0060 (-0.22)	-0.0052 (-0.19)	-0.0063 (-0.23)	-0.0072 (-0.27)	-0.0228 (-0.83)	-0.0281 (-1.04)
G-Index	-0.7770 ** (-2.54)									
% of independent directors		-12.3701 ** (-2.23)		-10.7385 * (-1.96)	-11.8226 ** (-2.14)	-12.4631 ** (-2.26)	-12.2844 ** (-2.22)	-12.1844 ** (-2.20)	-13.7810 ** (-2.52)	-14.3844 *** (-2.67)
Founder (=1)			7.8648 *** (3.31)	7.4182 *** (3.13)	7.2090 *** (3.04)	7.1022 *** (3.00)	7.0899 *** (3.00)	7.2003 *** (3.04)	5.5526 ** (2.38)	5.2892 ** (2.29)
Next CEO from outside (=1)							-0.5493 (-0.28)	-0.4831 (-0.24)	-0.4001 (-0.20)	-0.8180 (-0.42)
HHI (%)								0.3782 (0.67)	0.4253	0.7141 (1.26)
Stay (=1)									9.2265 *** (4.75)	9.3553 *** (4.84)
CEO tenure										-0.1021 (-1.45)
<u>Contract characteristics</u>										
CEO with non-compete clause (=1)						7.9150 *** (2.79)	7.9470 *** (2.80)	8.0805 *** (2.85)	8.6760 *** (3.12)	6.9875 ** (2.39)
CEO with non-solicit clause (=1)					5.6151 * (1.92)					
Existence of severance agreement (=1)										2.0988 (0.80)
<u>Business cycle</u>										
S&P index level										7.9481 *** (2.91)
<u>Control variables</u>										
Log of Assets	0.5607 (1.03)	0.8113 (1.48)	0.7941 (1.47)	0.9499 * (1.75)	0.9413 * (1.73)	0.8975 * (1.66)	0.8863 (1.63)	0.9468 * (1.72)	0.9953 * (1.83)	0.7730 (1.39)
Leverage	-1.3862 (-1.26)	-1.3198 (-1.21)	-1.1935 (-1.11)	-1.1538 (-1.08)	-1.0692 (-1.00)	-1.0457 (-0.98)	-1.0657 (-1.00)	-1.0764 (-1.01)	-1.2727 (-1.21)	-0.9095 (-0.88)
Total observation	497	497	497	497	497	497	497	497	497	497
Log likelihood	-974	-975	-972	-970	-969	-966	-966	-966	-954	-947

Table VII: Correlation Coefficients for Forced Turnover CEOs

Correlation coefficients for contract, CEO and firm characteristics from a sample of 112 S&P500 CEOs between year 1993 and 2007. The variables are defined in table 1.

Variables	3 YR Market- adjusted return	% of independ directors	G-index	Next CEO from outside (=1)	HHI	CEO with non- compete clause (=1)	CEO with non-solicit clause (=1)	CEO Tenure	Existence of sever agreement (=1)	S&P index level (000)	Log (Assets)	Leverage
3 YR Market-adjusted return	1.0000	0.0306	0.0449	-0.2318	0.0073	-0.0570	-0.0256	-0.1413	-0.1155	-0.0067	0.1741	-0.0356
% of independent directors	0.0306	1.0000	0.1990	0.0686	-0.1145	-0.0155	0.0015	-0.0404	0.0713	-0.1182	0.1225	0.1186
G-index	0.0449	0.1990	1.0000	0.0886	-0.1267	-0.0460	-0.0310	0.0263	-0.0516	-0.0264	0.0450	0.1363
Next CEO from outside (=1)	-0.2318	0.0686	0.0886	1.0000	0.0559	0.0846	0.0300	0.0852	0.0534	-0.1125	-0.1111	0.0630
HHI	0.0073	-0.1145	-0.1267	0.0559	1.0000	-0.0014	0.0248	0.0485	-0.1129	-0.2142	-0.2088	-0.0629
CEO with non-compete clause (=1)	-0.0570	-0.0155	-0.0460	0.0846	-0.0014	1.0000	0.9385	-0.0337	0.2075	0.1405	0.0973	-0.1106
CEO with non-solicit clause (=1)	-0.0256	0.0015	-0.0310	0.0300	0.0248	0.9385	1.0000	0.0219	0.1999	0.0982	0.0662	-0.1802
CEO Tenure	-0.1413	-0.0404	0.0263	0.0852	0.0485	-0.0337	0.0219	1.0000	-0.0921	0.0333	0.0495	-0.1189
Existence of severance agreement (=1)	-0.1155	0.0713	-0.0516	0.0534	-0.1129	0.2075	0.1999	-0.0921	1.0000	0.0902	0.1114	0.0585
S&P index level (000)	-0.0067	-0.1182	-0.0264	-0.1125	-0.2142	0.1405	0.0982	0.0333	0.0902	1.0000	0.0119	-0.3594
Log (Assets)	0.1741	0.1225	0.0450	-0.1111	-0.2088	0.0973	0.0662	0.0495	0.1114	0.0119	1.0000	0.2569
Leverage	-0.0356	0.1186	0.1363	0.0630	-0.0629	-0.1106	-0.1802	-0.1189	0.0585	-0.3594	0.2569	1.0000

Table VIII: Correlation Coefficients for Voluntary Turnover CEOs

Correlation coefficients for contract, CEO and firm characteristics from a sample of 497 S&P500 CEOs between year 1993 and 2007. The variables are defined in table 1.

Variables	3 YR Market- adjusted return	% of independ directors	G-index	Next CEO from outside (=1)	HHI	Stay at the firm after step down (=1)	CEO with non- compete clause (=1)	CEO with non- solicit clause (=1)	CEO Tenure	Existen of severan agreeme nt (=1)	Founder (=1)	S&P index level (000)	Log (Assets)	Leverage
3 YR Market-adjusted return	1.0000	-0.1308	-0.0144	-0.1404	-0.0015	0.1113	-0.0313	-0.0215	0.0266	0.0288	0.0634	0.0575	-0.0110	-0.1892
% of independent directors	-0.1308	1.0000	0.1712	0.1289	-0.1660	0.0206	0.0986	0.0748	-0.1514	0.0885	-0.1242	0.1069	0.1846	0.0677
G-index	-0.0144	0.1712	1.0000	0.0636	-0.0152	-0.0281	-0.0428	-0.0439	0.0344	0.0102	-0.0988	-0.0098	-0.0331	0.0160
Next CEO from outside (=1)	-0.1404	0.1289	0.0636	1.0000	0.0170	-0.0259	0.0611	0.0434	-0.1818	-0.0099	-0.0103	-0.0043	-0.0691	-0.1010
HHI	-0.0015	-0.1660	-0.0152	0.0170	1.0000	0.0115	-0.0929	-0.0664	0.0549	-0.0580	0.0048	-0.1986	-0.2899	-0.1309
Stay at the firm after step down (=1)	0.1113	0.0206	-0.0281	-0.0259	0.0115	1.0000	-0.0089	0.0058	0.0400	0.0134	0.1450	0.0322	0.0051	-0.0804
CEO with non-compete clause (=1)	-0.0313	0.0986	-0.0428	0.0611	-0.0929	-0.0089	1.0000	0.9461	-0.1150	0.3728	0.0295	0.0736	0.0234	-0.0345
CEO with non-solicit clause (=1)	-0.0215	0.0748	-0.0439	0.0434	-0.0664	0.0058	0.9461	1.0000	-0.0872	0.3509	0.0328	0.0779	0.0101	-0.0534
CEO Tenure	0.0266	-0.1514	0.0344	-0.1818	0.0549	0.0400	-0.1150	-0.0872	1.0000	-0.1614	-0.0299	-0.0975	0.1223	0.0295
Existence of severance agreement (=1)	0.0288	0.0885	0.0102	-0.0099	-0.0580	0.0134	0.3728	0.3509	-0.1614	1.0000	-0.0538	0.0308	0.0332	-0.0391
Founder (=1)	0.0634	-0.1242	-0.0988	-0.0103	0.0048	0.1450	0.0295	0.0328	-0.0299	-0.0538	1.0000	0.0621	-0.1114	-0.1744
S&P index level (000)	0.0575	0.1069	-0.0098	-0.0043	-0.1986	0.0322	0.0736	0.0779	-0.0975	0.0308	0.0621	1.0000	0.1725	-0.3094
Log (Assets)	-0.0110	0.1846	-0.0331	-0.0691	-0.2899	0.0051	0.0234	0.0101	0.1223	0.0332	-0.1114	0.1725	1.0000	0.2665
Leverage	-0.1892	0.0677	0.0160	-0.1010	-0.1309	-0.0804	-0.0345	-0.0534	0.0295	-0.0391	-0.1744	-0.3094	0.2665	1.0000

Table IX: Robustness Test Using Tobit Models for Forced Turnover CEOs

The sample includes 112 CEOs between year 1993 and 2007. For panel A, the dependent variable is a difference between actual and contractual exit packages (in million dollars). For panel B, the dependent variable is a difference between actual and contractual exit packages scaled by the total compensation of the CEO (in %). The variables are defined in table 1. Busy Board is defined as the percentage of independent directors who sit on three or more boards. Active institutional ownership is defined as the percentage of the firm's total shares outstanding that are held by investment advisers and investment companies. CEO and firm characteristics are from the year of CEOs turnover events. (t-statistics in parentheses). The symbols *, **, *** denote significance at the 10%, 5% and 1% level respectively.

	Panel A: Actual-Contractual pay (Mill\$)					Panel B: (Actual-Contractual pay)/Total Compensation				
	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7	Model 8	Model 9	Model 10
Constant	-24.2894	-22.9208	-16.6704	-18.4720	2.6762	-16.2283	-0.7036	-1.7462	-0.2889	83.6236
<u>Firm characteristics</u>										
3 YR Market-adjusted return	-0.2516 **	-0.2496 **	-0.2323 **	-0.2326 **	-0.1321 **	-1.5551 **	-1.5473 **	-1.4839 **	-1.3996 **	-1.0102 *
	(-2.57)	(-2.55)	(-2.49)	(-2.48)	(-2.13)	(-2.54)	(-2.53)	(-2.38)	(-2.23)	(-1.94)
% of independent directors			-1.4953	-1.9913			-89.6916	-42.9282	-43.9897	
			(-0.14)	(-0.19)			(-1.21)	(-0.61)	(-0.63)	
Busy Board (%)	-4.2021		-14.3273	-13.9195	-3.5119					-17.2475
	(-0.34)		(-1.23)	(-1.20)	(-0.47)					(-0.27)
Active institutional ownership (%)		-13.5784		8.9497	3.6607					
		(-0.65)		(0.46)	(0.30)					
G-Index						-3.6564				
						(-0.81)				
Next CEO from outside (=1)			-5.2985	-5.3769	-2.5413			-19.0518	-19.2259 *	-3.0437
			(-1.57)	(-1.59)	(-1.14)			(-0.84)	(-0.86)	(-0.16)
HHI (%)			-4.8766 **	-4.8195 **	-3.3458 **			-22.5769	-21.3906	-14.8303
			(-2.27)	(-2.25)	(-2.34)			(-1.57)	(-1.49)	(-1.21)
CEO tenure			0.3321 *	0.3390 *	0.3459 ***			2.1459 *	2.2665 *	2.6034 **
			(1.77)	(1.80)	(2.78)			(1.71)	(1.80)	(2.46)
<u>Contract characteristics</u>										
Non-compete (post-sep)			11.2589 ***	11.5033 ***	4.5426 *			69.1752 ***	65.6291 **	38.9269 *
			(2.79)	(2.82)	(1.65)			(2.58)	(2.44)	(1.71)
Existence of separation agreement (=1)			1.3899	1.6693					17.1031	
			(0.39)	(0.47)					(0.73)	
Separation Pay (Mill)					0.4332 ***					2.3900 ***
					(7.83)					(5.16)
<u>Business cycle</u>										
S&P index level (000)			10.3007	11.1223				50.6710	46.7868	
			(1.34)	(1.41)				(1.06)	(0.98)	
<u>Control variables</u>										
Log of Assets	1.2206	1.1551	-0.6611	-0.6810	-1.7070 *	-5.1662	-3.4044	-15.9964	-16.3430	-23.5885 **
	(0.76)	(0.72)	(-0.44)	(-0.45)	(-1.73)	(-0.52)	(-0.34)	(-1.54)	(-1.60)	(-2.78)
Leverage	7.9161 ***	7.9058 ***	9.2149 ***	9.2266 ***	6.1078 ***	47.7247 ***	47.4341 ***	56.0669 ***	55.7855 ***	41.0380 ***
	(6.89)	(6.89)	(8.44)	(8.46)	(7.78)	(6.61)	(6.61)	(7.67)	(7.71)	(6.17)
Total observation	112	112	112	112	112	112	112	112	112	112
Log likelihood	-231	-231	-221	-221	-201	-313	-313	-306	-306	-295

Table X: Robustness Tests Using Tobit Models for Voluntary Turnover CEOs

The sample includes 497 CEOs between year 1993 and 2007. For panel A, the dependent variable is a difference between actual and contractual exit packages (in million dollars). For panel B, the dependent variable is a difference between actual and contractual exit packages scaled by the total compensation of the CEO (in %). The variables are defined in table I and IX. Busy Board is defined as the percentage of independent directors who sit on three or more boards. Active institutional ownership is defined as the percentage of the firm's total shares outstanding that are held by investment advisers and investment companies. CEO and firm characteristics are from the year of CEOs turnover events. (t-statistics in parentheses). The symbols *, **, *** denote significance at the 10%, 5% and 1% level respectively.

	Panel A: Actual-Contractual pay (Mill\$)				Panel B: (Actual-Contractual pay)/Total Compensation			
	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6	Model 7	Model 8
Constant	-2.2863	0.5069	-9.1001	-6.7073	34.4496	33.7029	19.4392	2.7923
<u>Firm characteristics</u>								
3 YR Market-adjusted return	-0.0006	-0.0027	-0.0273	-0.0298	-0.0952	-0.1202	-0.1476	-0.1601
	(-0.02)	(-0.10)	(-1.01)	(-1.10)	(-0.79)	(-0.99)	(-1.22)	(-1.33)
G-Index					-2.4888 *			
					(-1.84)			
% of independent directors	-13.0445 **	-13.0009 **	-15.2683 ***	-15.1054 ***		-42.6526 *	-40.9901 *	-42.4642 **
	(-2.36)	(-13.00)	(-2.81)	(-2.77)		(-1.73)	(-1.66)	(-1.74)
Busy Board (%)	8.9851 **		8.0060 *					
	(2.06)		(1.91)					
Active institutional ownership (%)		-19.2089 *		-18.8437 *				
		(-1.85)		(-1.86)				
Founder (=1)			5.7115 **	5.9448 **			35.8517 ***	34.0924 ***
			(2.47)	(2.56)			(3.44)	(3.29)
Next CEO from outside (=1)			-0.9844	-1.1170			0.4305	-1.2131
			(-0.50)	(-0.57)			(0.05)	(-0.14)
HHI (%)			0.5554	0.5364			1.0519	2.1439
			(0.98)	(0.95)			(0.42)	(0.84)
Stay (=1)			9.2675 ***	9.3952 ***				
			(4.79)	(4.85)				
CEO tenure			-0.1355 *	-0.1262 *				-0.3795
			(-1.93)	(-1.80)				(-1.20)
<u>Contract characteristics</u>								
Non-compete (post-sep)			7.0949 **	7.0743 **			30.7999 **	28.5697 **
			(2.41)	(2.40)			(2.45)	(2.15)
Existence of separation agreement (=1)			1.9963	1.9737				-2.1802
			(0.76)	(0.74)				(-0.18)
<u>Business cycle</u>								
S&P index level (000)								32.6696 ***
								(2.66)
<u>Control variables</u>								
Log of Assets	0.6187	0.6835	0.9796 *	1.0219 *	-4.3945 *	-3.5629	-2.9710	-4.0479
	(1.11)	(1.24)	(1.78)	(1.86)	(-1.81)	(-1.45)	(-1.21)	(-1.59)
Leverage	-1.1529	-1.1102	-1.3267	-1.2473	-0.0167	0.2200	1.5094	3.2862
	(-1.07)	(-1.02)	(-1.28)	(-1.19)	(0.00)	(0.05)	(0.32)	(0.70)
Total observation	497	497	497	497	497	497	497	497
Log likelihood	-973	-973	-950	-950	-1257	-1257	-1248	-1243