

CORPORATE LITIGATION, CORPORATE
GOVERNANCE RESTRUCTURING, AND
EXECUTIVE COMPENSATION

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ABSTRACT

This thesis examines corporate governance consequences within US publicly-listed companies, following encounters with litigation. Corporate litigation can impose significant wealth losses upon the sued companies, giving rise to both agency and reputational incentives to instigate changes. The thesis addresses the issue of whether, and to what extent, public companies undergo internal changes following litigation, and examines the various penalties incurred by the executive officers of the sued corporations. A large sample of lawsuits filed against the Standard and Poor's 1,500 companies during 2000-2007 is employed, comprising environmental violations, securities fraud, antitrust litigation, intellectual property infringements, and contractual disputes. The thesis further investigates the roles of lawsuit-specific characteristics, including the nature of allegations, their economic magnitudes, and their legal merits, in predicting the observed changes.

Chapter 2 summarizes the literature documenting a decline in market valuation upon the filing of lawsuits against public companies, and briefly outlines the issues pertaining to each type of litigation examined in this thesis. Chapter 3 details the procedures for collecting litigation data, and explores the characteristics of the lawsuits included in the dataset. Chapter 4 investigates executive turnover following litigation filings. By employing probit regressions and the Heckman Selection Model, this chapter produces evidence that the filing of lawsuits is associated with an increase in CEO turnover within the defendant companies. The nature of the allegations (particularly securities, intellectual property, and antitrust lawsuits) and their legal

merits (proxied by their manner of disposition) exhibit strong explanatory powers, indicating that agency concerns rather than reputational incentives appear to be driving the increased executive turnover. Chapter 5 investigates whether sued companies subsequently undergo restructurings in their boards of directors, by examining the change in board independence and size. Empirical evidence shows that board independence tends to increase, particularly following securities and contractual lawsuits. The changes are associated with the economic magnitudes of the lawsuits but not their legal merits. Chapter 6 focuses on the economic penalties imposed on the CEOs by a decrease in their remuneration. Empirical evidence shows that CEOs of sued companies tend to incur a reduction in cash and bonus compensation following litigation filings. The reduction is particularly associated with intellectual property and contractual lawsuits. Chapter 7 then examines the reputational penalties incurred by the CEOs following corporate lawsuit filings. It documents that, following securities lawsuits, CEOs are more likely to lose outside directorships held in other companies. Additionally, CEOs who depart from the sued companies during the period surrounding litigation filings tend to face an impaired prospect of finding comparative reemployment, especially following contractual lawsuits.

This thesis contributes to the literature by extending the realm of the existing investigations beyond the traditional focus upon securities and fraud allegations. It examines the public companies' responses to a diverse range of different types of corporate lawsuits. The findings shed light on corporate attitudes towards allegations of different natures. They also have implications for regulators, informing them of the non-legal penalties faced by managers of public companies for allegedly breaching the law.

DECLARATION

This work contains no material which has been accepted for the award of any other degree or diploma in any university or other tertiary institution and, to the best of my knowledge and belief, contains no material previously published or written by another person, except where due reference has been made in the text.

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