

EXECUTIVE TURNOVER IN THE PRESENCE OF INTERNAL CONTROL WEAKNESSES

POST-SOX

By

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A Thesis Submitted to The Honors College

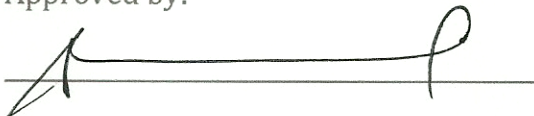
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Approved by:

A handwritten signature in black ink, appearing to read 'Dan Dhaliwal', is written over a horizontal line.

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ABSTRACT: This study tests the hypothesis that powerful CEOs are less likely to be fired than CFOs when internal control weaknesses are reported under Sarbanes-Oxley Section 404. This study uses four proxies for CEO power: Dual status as CEO and Chairman of the Board, CEO Pay Slice (compensation relative to other top firm executives), CEO tenure, and firm diversification (business and geographic). Controlling for prior year stock returns and ROA, and using a sample of 7,325 observed firm years, I document no significant relationship between CEO power and CFO scapegoating relating to SOX 404. Of the four proxies for CEO power, tenure had the strongest correlation with CFO scapegoating. My overall findings do not provide significant evidence as to the effect of CEO power on a board's decision to fire a CEO vs. a CFO in the wake of internal control weaknesses.

Executive Turnover in the Presence of Internal Control Weaknesses Post-SOX

I. INTRODUCTION

This study aims to answer the question: Why aren't CEOs fired along with CFOs when internal controls are found to be lacking post-SOX? Passed in 2002, the Sarbanes-Oxley Act (SOX) explicitly created dual responsibility in both a CEO and CFO for a company's internal controls. While prior studies have investigated trends in executive turnover and differing motivations of boards in the decisions to fire CEOs and CFOs, no study to date has examined whether the top two firm executives are held equally accountable for internal control weaknesses. Motivated by the stream of relevant prior literature, I investigate CEO power and ease of replacement as two important factors in a board's decision to retain or dismiss a CEO or CFO in the presence of internal control weaknesses.

In 2002, Congress passed the Sarbanes-Oxley Act (SOX) in response to a number of accounting and financial scandals that shook investor confidence. SOX was monumental legislation, passed largely to increase executive responsibility and accountability within companies so as to regenerate and maintain investor confidence in US markets. One of the sections of the Act is SOX 302, which pertains to "Corporate Responsibility in Financial Reports." This section states that both CEOs and CFOs are "responsible for establishing and maintaining internal controls" and that their certifications represent their evaluation of these internal controls.

This section clearly establishes dual liability between the CEO and CFO for internal controls.

Studies have since documented the effect of this policy as having increased both CEO and CFO turnover. Leone (2006) was one of the first studies done on the topic, and reported significant increases in CFO turnover in the three years immediately following the passage of SOX. Similarly, Kaplan & Minton (2011) showed an increase in CEO turnover in post-SOX years. These studies reflect the increased responsibility and accountability of the CEO and CFO under Sarbanes-Oxley. However, some recent studies have documented differences in how CEOs and CFOs are dismissed even in the context of SOX 302, which provides for dual responsibility and accountability. Burks (2007) showed that boards of directors disciplined and dismissed CEOs and CFOs differently in the post-SOX era. Additionally, Leone & Liu (2010) presented evidence that when CEOs are *firm founders*, boards will shift or direct blame to the CFO in the context of accounting irregularities. In discussing the results, the authors of the study even went so far as to use the term 'scapegoat' in reference to the CFO and how much more often CFOs were dismissed than CEOs.

Taken as a whole, these studies suggest that instances exist where a CEO is retained while the CFO is dismissed, and provide evidence of these top executives being treated differently by boards over the same issue. As boards appear to have different motivations when deciding to fire a CEO or CFO, these motivations could influence turnover decisions in the wake of reported internal control weaknesses. In

this study, I explain these differences using CEO power, tenure, and ease of replacement.

This study contributes to the growing literature on executive turnover by examining the motivations of boards in executive termination decisions in the post-SOX period. Prior literature has documented that in the post-SOX period, CEO turnover has increased and CFOs are being dismissed for internal control weaknesses, but I am not aware of any research that combines these two topics for analysis. Prior studies have explored similar executive turnover phenomena in both the context of restatements (Burks, 2007) as well as accounting irregularities (Leone & Liu, 2010) and documented that CEOs are retained while CFOs are dismissed. This study, however, examines the unique question of why this phenomenon occurs in a context (SOX 302/404) that seemingly provides for dual and equal responsibility, examining why terminations and culpability are delivered and assigned seemingly *unequally* between the CEO and CFO. The findings of this study have the potential to provide indirect evidence as to the effectiveness of the Sarbanes-Oxley Act, specifically Section 302. The results of the study could show a failure among boards to properly hold CEOs accountable under SOX, illustrating the effect of the failure of an intermediary (boards of directors) on the overall effectiveness of the legislation.

II. PRIOR LITERATURE AND HYPOTHESIS DEVELOPMENT

CEO and CFO turnover is a particularly relevant and important topic because of the impact such high-level changes can have on a firm. The CEO leads a firm, and thus a change in the position can have a significant impact on firm strategy, relationships, and performance. The CFO, in addition to being responsible for managing a firm's financial risks, is also often expected to serve as a strategic advisor to the CEO. A change at the CFO position can greatly affect the accuracy and associated risks of a company's financial reporting. Financial reporting is an extremely important measure used to evaluate CEOs and CFOs, as evidenced by the results of Hennes et al. (2008), which found that either the CEO or CFO is terminated approximately 80% of the time following the disclosure of an accounting irregularity (which represents an inaccuracy in financial reporting). This finding illustrates the amount of pressure boards feel to hold either the CEO or CFO accountable, and supports the idea that this pressure (and thus, related turnover) increased following the passage of SOX.

As discussed, Leone (2006) documented increased CFO turnover immediately following SOX. The study showed CFO turnover rates of 13, 16, and 19 percent in the years 2003-2005 immediately following SOX. Li et al. (2010) directly linked the turnover to internal controls, finding that firms receiving adverse SOX 404 opinions tend to experience CFO turnover. These studies illustrate the point that when internal controls are found to be lacking post-SOX, the CFO is held more directly responsible (compared to pre-SOX) and is dismissed significantly more often.

Kaplan and Minton (2011) showed that CEO turnover has slightly increased between 2000 and 2007, which includes mostly post-SOX years. Their study reported an average annual CEO turnover rate of 15.8% between 1992 and 2007, but 16.8% more recently between 2000 and 2007. Together with the Leone (2006) study, these results provide evidence of increased executive turnover as a result of SOX.

More recent studies like Burks (2007) and Leone & Liu (2010) have begun to examine *why* turnover has increased, and their efforts have revealed that boards treat CEOs and CFOs differently. Specifically, Burks (2007) showed that in the context of restatements, boards are more likely to discipline CEOs by withholding bonuses rather than firing them, and more likely to fire CFOs than withhold bonuses for them. The study also documents a significant change in the strength and nature of CEO discipline in the post-SOX period. Leone & Liu (2010) documented the effect of a CEO's founder status in a board's decision to dismiss them, showing that non-founder CEOs were fired approximately 20% more often than founder CEOs. That finding is significant in that it provides evidence for founder status as having significant influence on the decision to terminate or retain a CEO, and supports the idea that other similar factors might exist that influence a board's turnover decision (in this paper, these factors are combined into a single comprehensive measure of CEO entrenchment, referred to hereafter as "CEO power"). While SOX 302 provides dual responsibility to the CEO and CFO regarding internal controls, I am motivated

to study other significant factors that could affect a board's decision on whether to fire the CEO, CFO or both in the presence of internal control weaknesses.

CEO Power - Dual Status as CEO/Chairman of the Board

Studies such as Morck et al. (1989) and Leone & Liu (2010) have found that more powerful CEOs are significantly less likely to be replaced by the board. Specifically, Morck et al. finds that CEOs have more power when no other person holds the title of president or chairman and no other person co-signs the letter to shareholders in the annual report. Leone & Liu, in turn, showed that CEOs use their power, proxied by their founder status, to entrench themselves as the head of a firm. That is, a CEO who is also a founder of the firm will use their human capital to develop firm-specific assets that make them less replaceable to their employing firm. When situations occur that warrant dismissal, empirical results show that these CEOs are then less likely to be dismissed. Specifically, in the presence of an accounting irregularity in the post-SOX period, founder CEOs were dismissed only 29% of the time compared to 49% for non-founder CEOs (Leone and Liu 2010). Finally, Adams et al. (2005), proxying for CEO power by their position as board chairman or the only insider on the board, find that stock returns are significantly more variable for firms run by more powerful CEOs.

CEO Power - Pay Slice

Bebchuk et al. (2011) provides another measure of CEO power, referred to as the "CEO Pay Slice" (CPS). CPS is defined as the fraction of the CEO's compensation

relative to the total compensation of the top five executives of the firm. Their paper examines the relationship between CPS and firm value, performance and behavior. The study found that CPS was negatively associated with firm value, and that CPS has significant effects on the behavior of a company and its board. This study suggests CPS is an important measure to be included in the measure of CEO power.

CEO Power - Tenure

Another factor in why a CFO might be fired but the CEO retained includes longer overall CEO tenure. This ties in to the idea of CEO power in that by having been with the firm for longer, it is assumed that a CEO has accumulated firm-specific knowledge and therefore made his/herself more difficult to dismiss from the firm. Studies such as Singh & Harianto (1989) and Wade et al. (1990) have hypothesized that the tenure of the CEO relative to the tenure of the board has a significant impact on each party's influence within the firm. Alderfer (1986) supports the idea that longer relative tenure provides a CEO with firm-specific knowledge through better understanding of firm methods and operations. This type of extra internal value to the firm entrenches the CEO, making him/her more difficult to replace.

CEO Turnover and Firm Diversification

A board's decision to replace a CEO vs. a CFO will consider the cost to hire an individual to lead the firm. Factors that could affect ease of replacement include the overall complexity of the firm as well as the business' diversification. Studies have shown that diversified firms have higher CEO succession costs, and that firm

complexity has a significant effect on CEO turnover/succession (Berry et al., 2006). Specifically, this study showed that diversified firms had less forced CEO turnover, and that turnover in diversified firms is much less sensitive to firm performance. A more complex firm could have steeper learning curves for new executives, and would thus be more hesitant to dismiss executives in place. This idea is supported by studies as early as Parrino (1997), which documented an inverse relationship between firm complexity and CEO turnover. This study finds evidence consistent with a highly diversified and/or geographically spread out firm being more reluctant to dismiss a CEO, indicating an increased value for a CEO's specific knowledge of the firm and its practices. Leone & Liu (2010) also support this notion. Their study showed that founder CEOs develop human capital, and that replacing them causes a decline in firm value, "since the next best CEO would not have an equivalent set of firm-specific skills."

On the whole, relevant prior literature strongly suggests that these four concepts are significant components of CEO power. Recognizing the link between CEO power and the likelihood of a board to dismiss or retain them, I hypothesize the following:

H1: CEO power will be higher in firms that retain the CEO but fire the CFO in the presence of internal control weaknesses, as compared to all other firms.

- a.* The CEO will more often have dual status as CEO and Board Chairman in firms that retain the CEO but fire the CFO in the presence of internal control weaknesses, as compared to all other firms.

- b. CEO Pay Slice (CPS) will be higher in firms that retain the CEO but fire the CFO in the presence of internal control weaknesses, as compared to all other firms.
- c. CEOs who are retained while their CFO counterparts are dismissed following internal control weaknesses will have, on average, longer tenures as CEO at the time the weakness is disclosed.
- d. Business and geographic diversification will be higher in firms that retain the CEO but fire the CFO in the presence of internal control weaknesses, as compared to all other firms.

III. MODELS AND SAMPLE

Models

To examine how CEO power affects a board's decision to retain the CEO while dismissing the CFO in the presence of internal control weaknesses, I estimate the following models and define the following variables:

$$\begin{aligned}
 CFO_NOCEO_TURNOVER = & \beta_0 + \beta_1 ICweak + \beta_2 Dual_status \\
 & + \beta_3 ICweak * Dual_status \\
 & + \beta_4 ROA + \beta_5 Compound_return + \varepsilon
 \end{aligned}
 \tag{1}$$

where:

$CFO_NOCEO_TURNOVER = 1$ if the CEO is retained but the CFO is dismissed within 13 months of the internal control weakness disclosure, and 0 otherwise;

ICweak = 1 if the firm has a disclosed internal control weakness, and 0 if it is a control firm;

Dual_status = 1 if the CEO has dual status as Chairman of the Board, and 0 otherwise;

ROA = ROA_{t-1} , income in the year prior to the control weakness divided by beginning of year assets;

Compound_return = Size-adjusted fiscal year stock return from CRSP.

Based on prior research, I expect the coefficient on *ICweak* (β_1) to be positive (+). I make no prediction as to the significance, as I have no reason to expect that a control weakness alone has a significant impact on how boards treat the CEO and CFO termination decisions. I predict the coefficient on *Dual_status* (β_2) to be positive (+) and significant, as relevant prior research shows that a CEO's dual status as Chairman of the Board indicates a CEO with more power and who is more difficult to dismiss. Hypothesis 1a predicts that the coefficient on *ICweak* * *Dual_status* in model (1) is positive (+).

$$\begin{aligned} CFO_NOCEO_TURNOVER = & \beta_0 + \beta_1 ICweak + \beta_2 Ceopayslice \\ & + \beta_3 ICweak * Ceopayslice \\ & + \beta_4 ROA + \beta_5 Compound_return + \varepsilon \end{aligned} \quad (2)$$

where:

Ceopayslice = The percentage of the total compensation to the top five firm executives that goes to the CEO.

Turning to model 2, I predict the coefficient on *Ceopayslice* (β_2) to be positive (+) and significant, as relevant prior research shows that a higher CEO Pay Slice indicates a CEO with more power and who is more difficult to dismiss. Hypothesis 1b predicts that the coefficient on *ICweak * Ceopayslice* in model (2) is positive (+).

$$\begin{aligned}
 CFO_NOCEO_TURNOVER = & \beta_0 + \beta_1 ICweak + \beta_2 Tenure_yrs \\
 & + \beta_3 ICweak * Tenure_yrs \\
 & + \beta_4 ROA + \beta_5 Compound_return + \varepsilon
 \end{aligned} \tag{3}$$

where:

Tenure_yrs = The number of years the CEO has served in their current position.

I predict the coefficient on *Tenure_yrs* (β_2) to be positive (+) and significant. Topical literature has demonstrated that longer CEO tenure generally leads to the accumulation of firm-specific capital. Hypothesis 1c predicts that the coefficient on *ICweak * Tenure_yrs* in model (3) is positive (+).

$$\begin{aligned}
 CFO_NOCEO_TURNOVER = & \beta_0 + \beta_1 ICweak + \beta_2 Biz_diverse + \beta_3 Geo_diverse \\
 & + \beta_4 ICweak * Biz_diverse \\
 & + \beta_5 ICweak * Geo_diverse \\
 & + \beta_6 ROA + \beta_7 Compound_return + \varepsilon
 \end{aligned} \tag{4}$$

where:

Biz_diverse = One minus the firm's segment-sales based

Herfindahl index, given by

$$1 - \sum_{i=1}^{\text{numseg}} \left[\frac{(\text{segment sales}_i)^2}{(\text{company sales})^2} \right];$$

Geo_diverse = The geographic diversity of the firm, measured as the number of business segments in a given year.

Looking at model 4, I predict the coefficients on *Biz_diverse* (β_2) and *Geo_diverse* (β_3) to be positive (+) and significant as relevant prior research shows that higher firm complexity and diversification is an indicator of less forced CEO turnover. Hypothesis 1d predicts that the coefficients on *ICweak * Biz_diverse* and *ICweak * Geo_diverse* in model (4) are positive (+).

Sample Selection

The sample began with 8,181 firm year observations in which a firm had the names of the CEO and Chairman of the Board available (to determine dual status CEOs) (see Table 1). The sample was then narrowed to only observations for which the prior year compound return was available, and then narrowed again to only include firms to which SOX 404 applies. Finally, the sample was again changed to include only firms for which prior year ROA was available, resulting in a total of 7,325 observations. As each of the empirical models measured different variables, the number of observations in the sample was different for each model and variable. The number of total observations available for each variable is visible in Table 2 below. Data collected was over a range of seven years (2004-2011) following the

passage of SOX. Relevant data for each variable of the empirical models was attained through the Center for Research in Security Prices (CRSP), the Compustat ExecuComp database, or the Compustat Audit Analytics database.

TABLE 1
Sample Selection – Common Variables

Beginning number of firm year observations	8,181
Observations for which dual-status info available	8,181
Less firms missing previous year compound return	-27
Less firms to which SOX 404 does not apply	-3
Less firms missing previous year ROA	-826
Total available firm observations	7,325

TABLE 2
Sample Selection – Model-Specific Variables

Variable	Available observations
CFO_NOCEO_TURNOVER	8,181
Dual_status	8,181
Compound_return	8,154
ICweak	8,151
ROA	7,325
Biz_diverse	6,695
Geo_diverse	5,933
Ceopayslice	3,474
Tenure_yrs	3,431

IV. DESCRIPTIVE STATISTICS AND RESULTS

Descriptive Statistics

Table 3 reports descriptive statistics for the sample and its variables. As it turns out, 39.4% of the available observations contained events where a CFO was fired while a CEO was retained at the same time, or approximately 3,219 instances. 11.1% of firm-year observations in the sample also contained reported internal control weaknesses. This is not an insignificant percentage, and highlights the importance of oversight legislation such as SOX in keeping financial statements as accurate as possible. Also, nearly a quarter of firms in the sample had CEOs also serving as the Chairman of the Board (22.5%). Other notable characteristics of the sample include an average ROA of -8.8% (reflects economic conditions during sample period), average CEO tenure of just over 7 years, and average CEO Pay Slice of 37%. This means that for the firms in this sample, the average CEO earned 37% of the total compensation distributed to their firm's top 5 executives, nearly double what they would earn if the money were split equally.

TABLE 3
Descriptive Statistics

Variable	N	Mean	Median	Lower Quartile	Upper Quartile
CFO_NOCEO_TURNOVER	8181	0.3934727	0	0	1
ICweak	8151	0.1116427	0	0	0
dual_status	8181	0.2254003	0	0	0
ROA	7325	-0.0883504	0.0115082	-0.070458	0.0609319
Compound_return	8154	0.0194274	-0.0432859	-0.3460411	0.2407292
ceopayslice	3474	37.0134175	37.3775637	29.7926017	44.5747554
tenure_yrs	3431	7.0385699	5.0833333	2.5	9.3333333
Biz_diverse	6695	0.2243926	0	0	0.4862709
Geo_diverse	5933	0.2764076	0.1946174	0	0.5377382

Table 4 describes the correlations and relationships between each of the variables used in the empirical models. The figures in bold represent significant relationships at the $p = .05$ level. As discussed previously, the models were run using interactions of variables with the *ICweak* variable, such as *ICweak * Ceopayslice*. However, there are interesting relationships to note between the variables themselves. For example, there is an interesting lack of correlation between *ICweak* and *Tenure_yrs*. One might think that as a CEO gained longer tenure with a single firm, that the probability of significant control weakness would diminish as the CEO gained familiarity with the financials of the company. However, the p-value of .81 illustrates a significant *lack* of correlative relationship between these two items. Also interesting to note is that every variable except *Dual_status* and *Geo_diverse* had a significant relationship with the dependent variable *CFO_NOCEO_TURNOVER*.

TABLE 4
Variable Correlations

	CFO_NOCEO_TURNOVER	ICweak	dual_status	ROA	Compound_return	ceopayslice	tenure_yrs	Biz_diverse
CFO_NOCEO_TURNOVER	1							
ICweak	0.03337	1						
	0.0026							
dual_status	-0.01112	-0.08909	1					
	0.3147	<.0001						
ROA	0.05399	-0.04737	0.13635	1				
	<.0001	<.0001	<.0001					
Compound_return	0.0581	-0.06089	0.05044	0.1722	1			
	<.0001	<.0001	<.0001	<.0001				
ceopayslice	0.0694	-0.04256	0.09678	0.05112	0.04217	1		
	<.0001	0.0122	<.0001	0.0049	0.013			
tenure_yrs	-0.05399	0.00413	0.31444	0.06731	0.00174	-0.04285	1	
	0.0016	0.8088	<.0001	0.0002	0.9187	0.0121		
Biz_diverse	-0.02903	-0.00029	0.21734	0.14928	0.02926	0.07342	-0.00841	1
	0.0175	0.9813	<.0001	<.0001	0.0168	<.0001	0.6529	
Geo_diverse	0.01532	0.02982	0.12163	0.03391	0.00984	-0.00651	0.007	0.12856
	0.2381	0.0218	<.0001	0.0128	0.4491	0.7278	0.7095	<.0001

Univariate Tests

Tables 5-8 report the results of the regressions run on each of the models for CFO 'scapegoating' (represented by *CFO_NOCEO_TURNOVER*). The yellow highlights indicate a significant relationship with the dependent variable. Unfortunately, the results for CEO Dual status were not consistent with the applicable H1(a), which predicted the coefficient of the interaction term would be positive and the relationship would be significant. The coefficient of the interaction term *ICweak * Dual_status* is negative (-0.15) and not significant ($p=0.88$), suggesting that in the presence of an internal control weakness, a CEO's dual status as Chairman of the Board does not have any significant effect on whether the CFO is scapegoated. As illustrated in Table 6 below, the coefficient on *ICweak * Ceopayslice* is also not significant. While the positive sign of the relationship between *ICweak* and *Ceopayslice* is consistent with H1(b), the insignificance of the relationship is not, as illustrated by the p-value of 0.68. This result suggests that a CEO's compensation relative to other top firm executives does not have a significant influence on whether the same firm's CFO is scapegoated in the presence of an internal control weakness.

Tests on the third variable (CEO tenure) produced results similar to those of the second. Consistent with H1(c), the coefficient on *ICweak * Tenure_yrs* is positive (1.16). However, the relationship is not statistically significant ($p = 0.24$), inconsistent with H1(c). Interestingly, *Tenure_yrs* has a significant negative relationship with *CFO_NOCEO_TURNOVER*, suggesting that longer CEO tenure

actually *decreases* the overall likelihood that a firm will fire the CFO but not the CEO. However, also important to note is that the relationship between *ICweak * Tenure_yrs* is not only positive, but also the strongest (lowest p-value) of the interaction terms tested thus far. These conflicting relationships may be caused by the varied effects that increased tenure can have. In some cases, as these results illustrate, increased tenure doesn't necessitate the CEO getting better at his/her job. The CEO with increased tenure might have the power to produce sub-optimally, and more years experience does not always lead to better performance. It is also possible that tenure correlates with age, in which case the effect of retirement (forced and voluntary) must be taken into account. The effect of age and retirement may on their own affect the likelihood of CEO and/or CFO turnover.

The results of the tests for firm diversification were again inconsistent with hypotheses. Contrary to H1(d), the coefficients on both interaction terms *ICweak * Biz_diverse* and *ICweak * Geo_diverse* were negative and not significant. The p-values of 0.71 and 0.85 suggest that business and geographic firm diversification have no significant effect on CFO scapegoating in the presence of an internal control weakness.

The lack of consistency between my hypotheses and the results could be attributed to a number of causes. For one, SOX 404 might be effectively serving its purpose in providing a dual responsibility for internal controls that firms are employing in their executive turnover decisions. While CEO power is a significant

documented effect, it might be that SOX is effective and powerful enough that CEO power cannot have the same impact on turnover decisions as it has historically. Another possibility is that the most diverse firms are also some of the largest, most mature, and/or longest-existing firms. In this case, an enduring history of success could make a Board of Directors less afraid of making big decisions like firing the CEO. Based on the negative sign of the relationship between *ICweak * Dual_status* and *CFO_NOCEO_TURNOVER*, it appears that a dual-status CEO could actually be *more* likely to be terminated in the presence of internal control weaknesses compared to CEOs who do not have dual status. One possible explanation for this is that boards hold dual-status CEOs even more responsible for financial statement irregularities (including internal controls) when they hold the extra responsibility and power of also serving as the Chairman of the Board.

TABLE 5
The Relation Between CEO Dual Status and CFO Scapegoating

Dependent Variable: CFO_NOCEO_TURNOVER					
Parameter Estimates					
Variable	DF	Parameter Estimate	Standard Error	t Value	P-value
Intercept	1	0.39495	0.00709	55.71	<.0001
ICweak	1	0.05934	0.01936	3.07	0.0022
dual_status	1	-0.01456	0.01452	-1	0.316
ICWeak_x_Dual_Status	1	-0.00845	0.05484	-0.15	0.8776
ROA	1	0.05125	0.01297	3.95	<.0001
Compound_return	1	0.03126	0.00799	3.91	<.0001

TABLE 6
The Relation Between CEO Pay Slice and CFO Scapegoating

Dependent Variable: CFO_NOCEO_TURNOVER					
Parameter Estimates					
Variable	DF	Parameter	Standard	t Value	P-value
		Estimate	Error		
Intercept	1	0.29242	0.02927	9.99	<.0001
ICweak	1	0.0317	0.10508	0.3	0.7629
ceopayslice	1	0.00278	0.0007506	3.7	0.0002
ICweak_x_CPS	1	0.00114	0.00279	0.41	0.6822
ROA	1	0.13295	0.05478	2.43	0.0153
Compound_return	1	0.02643	0.01725	1.53	0.1256

TABLE 7
The Relation Between CEO Tenure and CFO Scapegoating

Dependent Variable: CFO_NOCEO_TURNOVER					
Parameter Estimates					
Variable	DF	Parameter	Standard	t Value	P-value
		Estimate	Error		
Intercept	1	0.43014	0.01365	31.52	<.0001
ICweak	1	0.03855	0.04745	0.81	0.4166
tenure_yrs	1	-0.0049	0.00143	-3.43	0.0006
ICweak_x_tenure	1	0.00504	0.00434	1.16	0.2462
ROA	1	0.14419	0.0552	2.61	0.009
Compound_return	1	0.0261	0.01732	1.51	0.132

TABLE 8
The Relation Between Firm Diversification and CFO Scapegoating

Dependent Variable: CFO_NOCEO_TURNOVER					
Parameter Estimates					
Variable	DF	Parameter	Standard	t Value	P-value
		Estimate	Error		
Intercept	1	0.39646	0.0115	34.42	<.0001
ICweak	1	0.08109	0.0336	2.41	0.0159
Biz_diverse	1	-0.05858	0.0274	-2.14	0.0328
Geo_diverse	1	0.03245	0.0262	1.24	0.2161
ICweak_x_biz_diverse	1	-0.03007	0.082	-0.37	0.7139
ICweak_x_geo_diverse	1	-0.01409	0.0745	-0.19	0.85
ROA	1	0.10945	0.0213	5.15	<.0001
Compound_return	1	0.02699	0.0097	2.79	0.0053

V. CONCLUSION

In this study, I examine whether firms are more likely to use CFOs as ‘scapegoats’ while retaining CEOs when internal control weaknesses are reported under SOX 404. My findings suggest that the presence of an internal control weakness in itself significantly increases the likelihood that a firm fires their CFO but retains their CEO. However, given the presence of a control weakness, it does not appear that CEO power (as proxied by dual status as board chairman, pay slice, tenure, and firm diversification) significantly affects the same turnover decision. Rather, it appears that the “traditional” measures of firm performance (such as ROA and compound stock returns) often used in turnover decisions have a more significant effect.

My findings suggest CEO tenure as a potential factor influencing a board's turnover decision in the presence of an internal control weakness. One idea for further study involves including CEO age as a control variable, with the idea being that tenure can correlate with age, and thus including age as a control would help reduce the effect of age and retirement factors that may make a long-tenured older CEO already more likely to leave the firm than an otherwise similar CEO of younger age.

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